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MNEs and FSAs: Network knowledge, strategic orientation and performance

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ABSTRACT

The objective of this research is to empirically investigate the contribution of network knowledge and strategic orientation to firm-specific advantages (FSAs). Using a unique firm-level dataset of the largest multinational enterprise (MNE) units across six small advanced economies, we find significant and positive relationships between different types of FSAs and (1) knowledge of the focal unit, and from internal corporate and external business networks; (2) unit role (headquarters and subsidiaries); (3) strategic orientation (local and global) and; (4) firm performance.

1. Introduction

Knowledge is a fundamental driver of value creation in the firm (Barney, 1991; McEvily & Chakravarthy, 2002; Porter, 1986, 1990). The literature suggests knowledge from various sources and locations leads to strong competitive advantages (Almeida, Song, & Grant, 2002; Gupta & Govindarajan, 2000; Mudambi, 2002; Regner & Zander, 2011; Zaheer & Nachum, 2011), and knowledge flows from both internal and external sources enhance firm performance (Fang, Wade, Delios, & Beamish, 2013; Holm & Sharma, 2006; Nguyen, 2011; Tsai, 2002). Thus, multinational enterprises (MNEs), by virtue of their global scope and strategy, can derive further advantage from their ability to tap into global and local networks of knowledge (Gupta & Govindarajan, 1991, 2000). Indeed, MNEs are recognized as one of the most efficient and effective mechanisms for transferring knowledge, through their ability to span both internal (corporate) and external business (industry) networks across national boundaries (Feinberg & Gupta, 2004; Hansen & Løvås, 2004; Kogut & Zander, 1993/2003).

Despite its importance to MNEs, there are research gaps in our understanding of how network knowledge influences firm-specific advantages (FSAs) of various units across borders. The extent to which different sources of knowledge underpin FSA remains a central question about the nature and evolution of the firm, and the question deserves attention. On the one hand, subsidiary-centered work has demonstrated that both internal and external network knowledge enhance subsidiaries' ability to recombine and generate new advantages (see for instance Andersson, Forsgren, & Holm, 2002; Birkinshaw, Hood, & Jonsson, 1998; Birkinshaw, 2000; Cantwell & Mudambi, 2005; Frost, Birkinshaw, & Ensign, 2002; Rugman, Verbeke, & Yuan, 2011). Such advantages, in turn, can also contribute to headquarters through reverse transfers from foreign subsidiaries for internal knowledge (Ambos, Ambos, & Schlegelmilch, 2006; Najafi-Tavani, Giroud, & Sinkovics, 2012) or inter-firm interactions for external knowledge (Andersson et al., 2002; Andersson, Bjorkman, & Forsgren, 2005; Giroud & Scott-Kennel, 2009). Studies of FSAs focus either on headquarters or, more recently, subsidiaries, in limited contextual settings (Rugman, Verbeke, & Nguyen, 2011) – typically a single country or MNE (Michailova & Mustaffa, 2012, p. 9). This does not allow the comparison of the role of network knowledge in explaining FSAs for both headquarters and subsidiaries across countries. In this paper, we address this gap by analyzing FSAs in both headquarters and subsidiary units, doing so in a number of country contexts, thereby addressing calls for analysis of firms' advantages within a cross-comparative research methodology (Grant, 1996; Khalid & Larimo, 2012).

Within the MNE network context, we further suggest that distinguishing sources of knowledge and strategic orientation is

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important. Although knowledge and strategy are the focus of studies on firm performance, they have neither been linked with different types of FSA, nor to different types of unit (i.e. headquarters and subsidiaries) (Birkinshaw et al., 1998; Rugman & Collinson, 2012; Rugman, Verbeke, & Nguyen, 2011; Verbeke, 2009). Yet the potential for these factors to vary widely suggests a need to explore these relationships in more depth. We do so by including internal and external network sources of knowledge; unit role and strategic orientation; and FSAs for both headquarters and subsidiary units of MNEs. Finally, we analyze the relationship between FSAs (relating to innovation, marketing capability, product differentiation, human-resource efficiency and managerial routines) and performance, extending previous research focusing on innovation and marketing (Kirca et al., 2011; Lee & Rugman, 2012).

The contributions of this paper are fourfold. First, the paper contributes by exploring the relationships between network knowledge sources, strategy and FSAs, which to date have been largely assumed rather than empirically tested. Secondly, the paper enhances our understanding of the differences between FSAs across unit roles. Thirdly, using a unique dataset, the paper contributes through cross-country analysis. The research context is the small, open, advanced economy, highly active, due to its small domestic market, in international trading and investment activities, and highly dependent on knowledge developed both at home and abroad (Benito, Larimo, Narula, & Pedersen, 2002; Ghauri, 1992; Scott-Kennel, 2008; van den Bulcke, Verbeke, & Yuan, 2009). Finally, this paper adds to the literature by providing support for the notion that some FSAs – but not all – do matter for the performance of MNE units.

Our findings reveal that knowledge derived from both internal and external firm networks, as well as the activities of the focal unit itself, are associated with FSAs, but this differs by type of advantage, unit role (whether headquarters or subsidiary) and strategic orientation. Our results also confirm a positive association between marketing- and innovation- related FSAs and unit profitability, productivity and sales growth.

The following sections review FSA literature, sources of network knowledge, unit role, strategic orientation and performance. Hypotheses are developed, our conceptual model and method outlined, and then the results presented, followed by discussion and conclusions.

2. Theory and propositions

2.1. Firm-specific advantages in the MNE

Hymer (1970, 1976) was the first to acknowledge the importance of firm-specific advantages (FSAs) to firms engaging in international production to overcome liabilities of foreignness (Zaheer, 1995). Hymer explained the nature of multinationality, emphasizing power and deployment within MNEs, with a particular focus on strategic planning at the top of multinationals and control considerations. He saw the ''development of a global outlook as closely associated with the ascent of marketing and product development in the strategic thinking of large corporations'' (Yamin & Forsgren, 2006, p. 168). Hymer suggested that FSAs were the basis of monopolistic behavior in foreign markets (though arguably few MNEs nowadays truly benefit from monopolies). His seminal work remains important in the study of MNE advantages because of the centrality of the headquarters, both in terms of initial determination of what constitute MNEs' core advantages, and also in terms of corporate control and power dimensions, thereby differentiating headquarters from individual subsidiaries (Dörrenbacher & Geppert, 2011).

Firm-specific advantages are defined as unique assets or capability proprietary to the firm that determine its competitive advantage (Caves, 1982; Hymer, 1970, 1976; Rugman & Collinson, 2012; Rugman, 2005). FSAs may arise from upstream research and development (R&D) expenditures that lead to innovation such as new products, production processes or proprietary technology, or innovation which occurs at more downstream levels, in marketing or distribution leading to differentiated product lines, distinct branding or specific marketing capabilities (Verbeke, 2009). FSAs can also arise from unique organizational structure or managerial routines (Rugman & Collinson, 2012; Rugman & McIlveen, 1985), and from the recombinative capability of the MNE (Verbeke, 2009). Recombination capability is the MNE's highest-order FSA, by which a firm can ''not only transfer abroad its existing set of FSAs, but also create new knowledge, integrate it with the existing knowledge base and exploit the resulting new knowledge bundles across geographic space'' (Verbeke, 2009, p. 39). Because recombination capabilities refer to the capacity to augment existing resources productively, they may also confer FSA, and imply a link to multiple sources of knowledge. This idea is closely related to that of subsidiary initiative (Birkinshaw, 2000; Birkinshaw et al., 1998), where the focus is on innovatively recombining both home- and host-country-specific advantages (CSAs), as well as both headquarters and subsidiary advantages to strengthen overall competitive advantage (Rugman & Collinson, 2012; Rugman, Verbeke, & Nguyen, 2011).

FSAs are, therefore, location- and unit-specific by nature. They may be either location-bound (LB) or non-location-bound (NLB) (Prahalad & Doz, 1981, 1987; Rugman & Verbeke, 1992). LB, or non-transferable FSAs, include stand-alone resources linked to location advantages or locality (e.g. networks, marketing knowledge, reputational resources, local best practices and routines, and domestic recombination capability) (Verbeke, 2009). NLB FSAs are those which are transferable, thus helping to overcome the additional costs of business abroad, and are embodied in products or include technological, marketing and administrative resources. It is important to distinguish LB and NLB FSAs, as they relate to the international transferability of FSAs within the MNE network, and the ability to share and use knowledge across different units of an organization is critical in developing organizational-wide advantage (Nahapiet & Ghoshal, 1998). As FSAs are also unit-specific, however, they are generally difficult to deploy and exploit beyond the location where they were developed; hence, recombination capability may not be achieved (Rugman & Verbeke, 2007).

Thus, it is also important to recognize that FSAs can be developed by both parent firms (headquarters) (headquarter-specific advantages or HQSAs) in the home-country context or by subsidiaries (subsidiary-specific advantages or SSAs) in the host-country context (Birkinshaw, 2000; Rugman & Verbeke, 2001, 2003). Most studies examine FSAs through one of these two lenses. Early studies focused on home-country factors providing advantages to the MNE (headquarters) that explained outward FDI (Rugman, Verbeke, & Nguyen, 2011), whilst more recent studies have focused on subsidiaries as units of analysis and pointed to their ability to engage in innovative recombination of knowledge in host-country settings (Birkinshaw et al., 1998; Cantwell & Mudambi, 2005; Frost et al., 2002). It is because of the growing dispersal of knowledge creation within MNEs and the rise of subsidiary-specific advantages (Mudambi & Navarra, 2004; Rugman & Verbeke, 2001) that this study focuses on both HQSAs and SSAs.

The shift in focus from headquarters to subsidiaries has occurred because the modern MNE is presented as a complex integrated network (Bartlett & Ghoshal, 1989; Buckley, 2009; Ghoshal & Bartlett, 1990; Rugman, Verbeke, & Nguyen, 2011), with dispersed and concentrated knowledge systems (Nohria & Ghoshal, 1997). In this context, an MNE's global strategy influences the development and exploitation of FSAs, as well as internal