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Reexamining the relationship between control mechanisms and international joint venture performance: The mediating roles of perceived value gap and information asymmetry

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ABSTRACT

According to transaction cost theory, the risk of opportunism is a major obstacle to cooperative relationships, such that multinational corporations need to exert control over their international joint ventures (IJVs). However, inconsistent findings indicate that the control–performance linkage is complex and poorly understood. This study develops a mediating framework and suggests that perceived value gap and information asymmetry have a direct effect on IJV performance. Perceived value gap and information asymmetry can also mediate the relationship between control mechanisms (e.g., centralization, formalization, and socialization) and IJV performance. A sample of 152 Taiwanese IJVs in China showed that the direct effects of formalization and socialization on IJV performance satisfaction were significant. The empirical results showed that information asymmetry and perceived value gap mediated the formalization–performance and socialization–performance relationships. However, neither the direct effect of centralization nor the indirect effect through information asymmetry mediation on IJV performance was significant.

1. Introduction

The formation of an international joint venture (IJV) is an important market entry strategy that has been adopted by many multinational corporations (MNCs) in the course of their global expansions (Gong, Shenkar, Luo, & Nyaw, 2007; Makino, Chan, Isobe, & Beamish, 2007). To realize the potential for joint value creation, partners must exchange information, share knowledge, and make investments. Due to the possibility of opportunism, however, investing valuable assets and sharing proprietary knowledge with the other partner(s) may expose each party to a certain degree of risk (Parkhe, 1993; Zeng & Chen, 2003). Luo (2007a) defined opportunism in the context of IJVs as acts or patterns of behavior performed by specific parties from specific countries to obtain unilateral gains to the substantial detriment of other parties from other countries. When entering into a voluntary interorganizational arrangement such as an IJV, assets are located overseas, a focal parent becomes vulnerable to the actions of the other partner, and the risk of expropriation or opportunism is greater than it would be in a domestic context (Ertug, Cuypers, Noorderhaven, & Bensaou, 2013; Pangarkar & Klein, 2004). There is therefore a need for control mechanisms, which can be classified as centralization, formalization, and socialization according to their objective of control over actions, results, and personnel/culture (Li, Tang, Okano, & Gao, 2013). There is also a need to reduce transaction costs and enhance parent satisfaction by decreasing the likelihood of opportunism (Deitz, Tokman, Richey, & Morgan, 2010; Fryxell, Dooley, & Vryza, 2002; Luo, Shenkar, & Nyaw, 2001; Mesquita & Brush, 2008; Pangarkar & Klein, 2004). The purpose of control is to protect an MNC's own interests while simultaneously trying to overcome a partner's opportunistic behavior (Calantone & Zhao, 2000; Ren, Gray, & Kim, 2009), which can be considered as an antecedent of IJV performance (Christoffersen, 2013; Reus & Rottig, 2009; Selekler-Gökşen & Uysal-Tezölmez, 2007). IJV control is very important to explaining IJV performance and to IJV success (Liu, Vredenburg, & Steel, 2014).

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There are many studies of—and numerous efforts to explore—the relationships between control mechanisms and IJV outcomes that enhance our understanding and knowledge of international alliances, the causes and consequences of the MNC-subsidiary relationship, and the organizational design of international business. However, the theoretical arguments and empirical findings remain incongruent. For example, Newburry, Zeira, and Yeheskel (2003) showed that IJVs located in China with authority are more effective in the formulation and implementation of strategic plans. Zhang and Li (2001) indicated that autonomy and success are related to IJV performance. However, Lu and Lee (2005) reported that the impact of centralization on IJV performance satisfaction is insignificant. The meta-analysis of Reus and Rottig (2009) indicated that hierarchical control may theoretically have positive or negative effects on performance. In mainland China, Calantone and Zhao (2000) indicated that the control–performance relationship is insignificant for Japanese IJVs in China; however, for Korea and the USA IJVs, it is positive. Reus and Rottig (2009) report that hierarchical control has an insignificant direct effect on performance in the Chinese sample but a significant effect in the non-Chinese sample. Some studies indicate that formal control mechanisms can enhance IJV performance (Gong et al., 2007; Perrone, Zaheer, & McEvily, 2003), while other studies report inconsistent results (Fryxell et al., 2002; Inkpen & Currall, 2004; Nohria & Ghoshal, 1994). Luo and Park (2004) confirm the positive relationship between socialization and IJV performance. However, the empirical results of Fryxell et al. (2002) show only a marginally significant positive relationship between socialization and IJV performance. These studies provide important insights and syntheses, but they do not provide conclusive evidence of control–performance relationship (Liu et al., 2014). These inconsistent findings indicate that the control–performance linkage is complex and poorly understood. The relationship between control mechanisms and IJV performance remains unclear (Pangarkar & Klein, 2004). We still have only a limited understanding of the process by which specific control mechanisms function.

Through a careful review of the literature, this study identifies three research gaps. First, opportunism is a critical assumption of human behavior in transaction cost theory, and the potential for opportunism plays an important role in IJV success (Geringer & Hebert, 1989). Opportunism creates a need for *ex ante* and *ex post* safeguarding, including formal and social governance structure (Nakos & Brouthers, 2008; Subramani & Venkatrman, 2003). However, potentially opportunistic partners do not necessarily behave opportunistically. This observation raises the question of why opportunistic behavior occurs. We contend that *the perceived value gap* and *information asymmetry* are two critical conditions that may induce opportunistic behaviors (Williamson, 1985). Seetoo and Hsiung (2004) refer to the perceived value gap as the extent to which common goals or shared values diverge among partners, and they identify information asymmetry as the level of information distribution asymmetry throughout the alliance. Control mechanisms must overcome these two antecedents to prevent opportunistic behavior. Little systematic empirical research has been conducted to test the effects of control mechanisms on the perceived value gaps and information asymmetry. Second, many studies assume that if a value gap and information asymmetry exist among partners, control mechanisms will have direct positive effects on IJV performance. The indirect effects of control mechanisms on an IJV's outcome through a reduction in the value gap and information asymmetry are treated as given and ignored. Therefore, few studies have precisely measured the extent of value gap incongruence and information asymmetry or clarified the way in which the control– performance relationship of an IJV is affected by the value gap and information asymmetry among partners. Given the importance of control mechanisms in IJVs, how they function should be addressed systematically. However, there is little research on how control mechanisms have been executed in practice (Li et al., 2013). Finally, the definitions of control mechanisms differ such that the empirical results are difficult to compare. Ren et al. (2009) suggested that making distinctions among control mechanisms and understanding the impact of each mechanism on IJV performance to enrich our understanding could be necessary for future studies.

To answer the question of how MNCs can effectively coordinate and control IJVs, we suggest that the underlying reasons for opportunism should be taken into account. Based on transaction cost theory and the information process perspective, this study proposes a conceptual model to examine whether parent companies' control mechanisms could enhance the performance of an IJV by reducing the perceived value gap and information asymmetry among partners. In our view, information asymmetry and the perceived value gap have a significant mediating effect on the relationship between control mechanisms and IJV performance. The IJV approach is particularly prevalent among MNCs in the Chinese market (Chan, Luk, & Wang, 2005; Li et al., 2013). A sample of 152 IJVs in China involving a Taiwanese parent company confirmed the mediating effects of a perceived value gap and information asymmetry on the relationships between control mechanisms and IJV performance. This paper proposes a theoretical model and contributes to the literature on the control–performance relationship of IJVs in the following ways: (1) testing the effects of control mechanisms on value gap and information asymmetry reduction, which allowed us to address the issues of opportunistic behavior and IJV management; (2) clarifying the direct and indirect relationships between control mechanisms and IJV performance through this theoretical framework to enhance our understanding of the control–performance link.

The remainder of this paper is organized as follows. In the next section, we review the relevant literature, discuss the main study concepts, and explain the theoretical basis for the hypothesized relationships. In the methodology section, we describe the sample, the measures used, and the statistical methods. In the results section, we present the statistical relationships that were observed among the control mechanisms, perceived value gap, information asymmetry, and IJV performance. Finally, we present the conclusions, explain the theoretical implications, and discuss the practical implications of our findings.

2. Theoretical background and hypotheses

2.1. Facilitating conditions of opportunistic behavior

Transaction cost theory defines opportunism as seeking self-interest with guile (Williamson, 1985), with decision-makers showing a tendency to exploit their positions to advance their own self-interest (Das & Rahman, 2010; Rindfleish & Heide, 1997; Tsang, 2006). This phenomenon provides a foundation for IJV control theory (Deitz et al., 2010). The potential for opportunism arises when one party is vulnerable to the actions of another, whose behavior is not under its control (Parkhe, 1993). The formation of a joint venture naturally gives rise to many opportunities for opportunism (Morris & Cadogan, 2001). While opportunism is the cause and antecedent of a partner's opportunistic behavior (Rindfleish & Heide, 1997), opportunism *per se* is not a sufficient condition for opportunistic behavior. Certain critical conditions or facilitators should exist for the actual occurrence of this behavior. Opportunistic behavior is most likely to appear in two situations. The first such situation occurs when the partners lack common objectives or shared values. The larger a partner perceives a value