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Intra-MNE advantage transfer and subsidiary innovativeness: The moderating effect of international diversification☆

Fang-Yi Lo *

Department of International Trade, Feng Chia University, 100 Wenhwa Rd., Seatwen, Taichung, Taiwan

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ABSTRACT

This study focuses on multinational enterprise (MNE) advantage transfer and focuses on the new trend about subsidiary innovativeness. This study explores the intra-MNE advantage transfer from parent companies to their subsidiaries and the effect on innovativeness and performance of foreign subsidiaries, and further examines the moderating effect of the international diversification. The empirical results support the existence of an invert-U relationship between intra-MNE advantage transfer and subsidiary performance. In addition, findings support the moderating effect of international diversification of intra-MNE advantage transfer on subsidiary innovativeness and performance.

1. Introduction

Previous strategy and management scholars focus mainly on the subsidiary networks all around the world (Eden, 2009) and widely agree that these networks constitute a potentially important source of competitive advantage for MNEs (Birkinshaw & Hood, 1998; Bjorkaman, Barner-Rasmussen, & Li, 2004; Frost, 2001; Rugman & Verbeke, 2001). By accessing the knowledge residing in these networks, MNEs can exploit existing repositories of knowledge and combine these sources of knowledge to explore new issues (Frost, 2001). For MNEs, the transfer of monopoly advantages (Kindleberger, 1969; Lall & Siddharthan, 1982) can stimulate the initial foreign explore, subsidiaries can also link up with local knowledge to develop the local distinctive advantages. This advantage can become the main source of MNEs competitive advantages (Minbaeva, Pedersen, Bjorkman, Fey, & Park, 2003). According to Mudambi and Navarra (2004), innovation is the main advantage for MNEs, and among subsidiaries, innovation is also increasingly important (Huston & Sakkab, 2004; Kuemmerle, 2004; Lewin, Massini, & Peeters, 2009).

Previous research explores the advantages of transfer form parent companies (Buckley & Carter, 1999; Iwasa & Odagiri, 2004; Kotabe, Dunlap-Hinkler, Parente, & Mishra, 2007), but overlooks the innovation continuous and ignores subsidiary innovation (Kotabe et al., 2007). Therefore, this study focuses on subsidiaries and explores the advantages of internal transfer from parent companies to their foreign subsidiaries to further observe the effect of this transfer on the subsidiaries' operation.

Growth-triggering innovations emerge in foreign subsidiaries because employees are closer to customers and do not follow so much the procedures and politesse of the home market (Birkenshaw & Hood, 2004). Through strategical independency and obtaining a wider variety of ideas, products, processes, and technologies (Hakanson & Nobel, 2001), subsidiaries can integrate local competences and develop operation systems which are close to local needs and can benefit the entire MNEs (Mudambi & Navarra, 2004). Thus, the first research objective is to explore the intra-MNE advantage transfer from the parent companies to their subsidiaries to examine the influence on subsidiary innovativeness.

The resource-based view (RBV) theory suggests that resources are important antecedents for performance, unique competitive advantages that create excess profit for firms (Barney, 1991), and have positive effects on firm performance (Delios & Beamish, 1999; Gulati, 1999; Morck & Yeung, 1991; Powell, 2001). Most of the existing studies further support the existence of this the positive relationships between advantages and performance, whereas traditional RBV focuses on the domestic context. Therefore, the second research objective is to explore the intra-MNE advantage transfer from the parent company to their subsidiaries to examine the influence of this transfer on the subsidiary's performance.

In international operations, MNEs can arbitrage in different markets (Bartlett & Ghoshal, 1989) and extend the market power to control the output market (Kogut, 1985). Diversification also affects the firm's operation by increasing the governance cost (Conner, 1991), management cost (Jones & Hill, 1988), or the international investment strategy (Davidson & McFetridge, 1985). Nevertheless, international diversification is an important issue that further influences RBV. Tallman and Li (1996) argue that in larger territories, product diversification and

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* Corresponding author. Tel.: +886 4 24517250x4184.
E-mail address: fylo@fcu.edu.tw.

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performance can be non-linear relationship. When diversification exceeds the viable economic scope, firms cannot produce more economic rent with the existing resources. International diversification between parent company and subsidiary thus moderates the RBV with the applicability of intra-MNE advantage transfer. The third research objective is to explore the moderating effect of international diversification.

Following this introduction, Section 2 contains a literature review and the research hypotheses. Section 3 describes the method and the findings. Section 4 presents the concluding remarks.

2. Literature review and hypotheses

2.1. Subsidiary innovativeness

Foreign subsidiaries can either exploit the existing technology from the parent company or self-innovate new technologies. Previous studies mainly focus on the transfer of mature technology that parent companies develop and subsidiaries' application of this existing technology. Nevertheless, a new stream of scholars suggest that MNEs need to reconsider subsidiaries as a peninsula rather than as island – as extensions of the MNE's strategic domain rather than as isolate outputs – to create a flow of innovative ideas that goes from the periphery to the corporate center (Birkenshaw & Hood, 2004). This idea reveals the importance of subsidiary innovativeness for the entire MNE.

The intra-MNE advantage transfer allows the subsidiary to learn the parent company's advantages, apply the existing skills on the local market, and limit subsidiaries time and space to innovate the subsidiary's own technology. Subsidiaries that focus on applying the parent companies' technology are less prone to create new technology themselves. Although, absorbing local knowledge can help subsidiary innovativeness (Phene & Almeida, 2008), abundant advantage transfer from the parent company can lower the subsidiary's willingness to develop their own technology because they lack the urgent need for innovation. The advantage transfer can also hinder the subsidiaries' inherent innovation ability.

H1. Intra-MNE advantage transfer negatively relates to subsidiary's innovativeness.

2.2. Subsidiary performance

Previous literature defends the positive effect of advantage transfer on subsidiary's performance (Delios & Beamish, 2001; Isobe, Makino, & Montgomery, 2000). However, some of the advantage from parent companies may not be suitable for use in a local context and may hinder subsidiary's performance instead because the parent company is unable to get closer to customers and unable to respond to local needs (Bartlett, Ghoshal, & Birkinshaw, 2004).

At first, the advantage transfer from the parent company can help the subsidiaries' operation because subsidiaries gain a better competitive position (Isobe et al., 2000), overcome the liability of foreignness, and increase performance (Isobe et al., 2000). However, too much advantage transfer becomes a disadvantage because some MNE's advantages are location-specific and need adjustment to the local culture to function properly in the host environment. The advantage transfer from parent company will enhance subsidiary performance outcome up to a certain point, and then the benefits will start to diminish, which becomes an invert-U relationship.

H2. An invert-U relationship exists between intra-MNE advantage transfer and subsidiary performance.

2.3. Moderating effect of international diversification

Diversification influences RBV (Geringer, Tallman, & Olsen, 2000). In low international diversification, the linkage of parent-subsidiaries advantage, shares information, and advantages let the parent companies advantage transfer effectively to the subsidiary (Davidson & McFetridge, 1985) and induce the subsidiary's low ability and willingness to innovate. In high international diversification, the subsidiaries' industry domain, or main product is different from the parent company's domain or product. Subsidiaries can transfer advantage from the parent company, but the low applicability of parent companies' advantage forces subsidiaries to invest resources in innovating their own advantages. Therefore, high international diversification reduces the negative impact of intra-MNE advantage transfer on subsidiaries' innovativeness.

H3. International diversification positively moderates the relationship between intra-MNE advantage transfer and subsidiary innovativeness.

In low international diversification, the familiarity of the same industry lowers the international management and operation costs (Rumelt, 1974), helps to apply the internal factors of a firm to gain better economic rent in larger markets (Geringer et al., 2000), and also increases the positive effect of parent companies' advantage transfer on subsidiary performance. This effect also intensifies the subsequent negative effect on subsidiary performance. Conversely, in high international diversification, irrelative operation territories between parent companies and subsidiaries reduce the first positive effect of the advantage transfer on subsidiary performance, and for the second stage, receive less negative effect of the performance attack.

H4. International diversification diminishes the invert-U relationship between intra-MNE advantage transfer and subsidiary performance.

Fig. 1 presents the research framework for this study: advantage transfer between MNE and subsidiaries negatively affects the subsidiaries' innovativeness, and an invert-U relationship exists with subsidiary performance. In addition, Fig. 1 presents the moderating effect of international diversification.

3. Method

3.1. Data and sample

This research explores the intra-MNE advantage transfer and the effect on subsidiary operation. To test the hypotheses, this study uses data from two databases. The sample for this study includes US-based MNEs and their foreign (non-US) subsidiaries. The first part of the data comes from the OSIRIS database by Bureau van Dijk Electronic Publishing (BvDEP). OSIRIS is a database of financial information, ratings, stock data, and news on global companies around the world, with coverage of over 125 countries. The population of this study includes 1609 US-based manufacturing companies that are listed on stock market. This study focuses on international operations, therefore selects MNEs that have at least 1 foreign subsidiary. This study thus uses a sample of 1200 parent companies.

The second part of the data comes from the WIPS database. The study uses US patent data and the patent citation analysis. US patent data are representative of global inventive activities because most significant innovations have a US-based patent (Kotabe et al., 2007; Patel & Pavitt, 1991). Because US firms patent extensively using the US patent system for innovations from both the US and abroad (Phene & Almeida, 2008), this study combines OSIRIS data and WIPS patent data to test the hypotheses. After comparing those two databases, the final sample consists of 283 subsidiaries.

3.2. Measurement

3.2.1. Intra-MNE advantage transfer

Patent data measures advantage transfer. Literature reports the use of patents as measures of knowledge flows (Almeida & Kogut, 1997;