Journal of International Management xxx (2017) xxx–xxx

Contents lists available at ScienceDirect

Journal of International Management
Fox School of Business
TEMPLE UNIVERSITY®

Trojan Horses or Local Allies: Host-country National Managers in Developing Market Subsidiaries

Jakob Muellner [a], Patricia Klopf [a], Phillip C. Nell [a,b,*]

[a] WU Vienna, Vienna University of Economics and Business, Austria
[b] CBS, Copenhagen Business School, Denmark

ARTICLE INFO

Article history:
Received 11 July 2016
Received in revised form 22 December 2016
Accepted 23 December 2016
Available online xxxx

Keywords:
Multinational corporations
Subsidiary staffing
Institutional theory
Corruption
Institutional distance

ABSTRACT

We investigate a multinational corporation's (MNC) decision to appoint host-country national (HCN) managers to foreign subsidiaries based on the institutional context of and familiarity with the host country. HCN managers are commonly associated with specialized knowledge, superior responsiveness, and higher legitimacy. Yet, we argue that local familiarity of HCNs can also be perceived as risky or harmful by MNC parents. We analyze how formal and informal institutions affect the trade-off between positive effects and potential costs associated with HCN managers ("*Local allies*" vs. "*Trojan horses*"). We find that legal institutions protect foreign MNCs from potential costs, encourage the use of HCNs and reinforce their benefits. Corruption and corruption distance, however, increase perceived costs associated with HCN managers up to a point at which they outweigh their perceived benefits.

1. Introduction

Multinational corporations (MNC) operate in countries that differ in their external institutional environments and often require specialized, local knowledge. At the same time they need to organize the internal institutional environment and manage their foreign subsidiaries across country borders (e.g. Kostova and Zaheer, 1999; Roth and Kostova, 2003b). Subsidiary staffing is one important strategic instrument for MNCs to cope with the different environments. Ideally, subsidiary managers implement MNC strategies and act in the MNC's interests, while they are also responsive to and knowledgeable about the external host-country environment. Unlike domestic staffing in independent firms, however, foreign subsidiary staffing is complicated by institutional duality (Kostova and Roth, 2002). A foreign subsidiary has to comply with strategic decisions of the MNC parent (i.e. within organization domain), and is exposed to the host-country institutional context (Kostova and Roth, 2002). Hence, foreign subsidiary managers face isomorphic pressures from two potentially competing domains.

Researchers have found that expatriates can support MNC-internal integration. However, these managers may not be as knowledgeable about the host-country institutional context as host-country national (HCN) managers (Gaur et al., 2007; Gong, 2003a, 2003b). They do not possess contacts or legitimacy to an equal extent (Athanassiou and Nigh, 2000; Tan and Mahoney, 2006). As a result, literature has widely agreed on the overall benefits of hiring HCNs (Mezias and Mezias, 2010), describing them as "*a unique nonmarket strategic advantage*" (White et al., 2015, p. 343).

Nevertheless, it is also widely acknowledged that the goals of individual managers and the MNC can be misaligned, and managers might act opportunistically (Kostova et al., 2016). Institutional duality can aggravate conflicts between the MNC, subsidiary

* Corresponding author.
E-mail addresses: jakob.muellner@wu.ac.at (J. Muellner), patricia.klopf@wu.ac.at (P. Klopf), phillip.nell@wu.ac.at (P.C. Nell).

http://dx.doi.org/10.1016/j.intman.2016.12.001
1075-4253/

managers and external stakeholders (e.g. cheap labor vs. well-paid jobs) (Kostova and Roth, 2002). Hence, institutional duality puts MNCs in a situation in which they are dependent on HCNs' knowledge, while at the same time facing higher information asymmetry about their behavior. This can be even more problematic for the MNC, when the host-country context does not protect from opportunistic behavior sufficiently (Dieleman and Boddewyn, 2012; Hearn, 2015; Marquis and Raynard, 2015). In such a situation of institutional duality, HCNs may be perceived as more risky or more likely to engage in opportunistic behavior by the MNC. As a result, MNCs may forego the benefits of HCNs in their foreign subsidiaries.

MNC subsidiary staffing of top management teams and boards has attracted considerable scholarly interest. Yet, we believe the topic needs to be revisited for a number of reasons. First, subsidiary staffing literature has focused predominantly on the potential benefits of HCN subsidiary managers (Gaur et al., 2007; Tan and Mahoney, 2006) and board members (Du et al., 2015; Oxelheim et al., 2013). Little research has accounted for potential costs of HCN subsidiary managers as perceived by the MNC parent (notable exceptions being Shin et al., 2016; Tan and Mahoney, 2006). In doing so, existing studies have oversimplified subsidiary staffing, hypothesizing unidirectional average effects, where, in fact, there are theoretically compelling arguments for higher-order relationships, i.e. trade-offs and curvilinear effects (Alcácer et al., 2013). In particular, research has failed to acknowledge the fact that HCNs may be perceived as more risky by the MNC, because they may use their superior knowledge and local contacts to the detriment of the MNC (Gong, 2003a).

Second, some recent studies have used institutional theory to hypothesize about subsidiary staffing with HCNs or expatriates (Baik and Park, 2015; Gaur et al., 2007). These studies have examined the effects of differences between the MNC home- and subsidiary host-country institutional context. The effect of specific host-country institutions that potentially facilitate or protect from opportunistic behavior, however, remains under-examined (Kostova and Zaheer, 1999; van Hoorn and Maseland, 2016).

We aim to address these gaps integrating institutional theory (Doh et al., 2012; Henisz, 2000; Kostova and Roth, 2002; Kostova et al., 2008; Peng et al., 2008). Following Granovetter (1978, 1985) and Granovetter and Soong (1983), we contend that MNC subsidiary staffing with HCNs is characterized by a trade-off between their benefits of knowledge (local allies) and their costs resulting from potential opportunistic behavior, as perceived by the MNC parent (Trojan horse cost). By separating benefits and costs conceptually, we theorize about and empirically measure a trade-off in subsidiary staffing with HCN managers.

However, empirical verification of potential cost associated with HCNs is of little value without understanding boundary conditions of variations in the cost (Alcácer et al., 2013). Hence, we hypothesize how the specific host-country institutional context in terms of corruption, corruption distance, property rights and contracting institutions, affects the cost of HCN managers as perceived by the MNC parent, and ultimately their net probability to be appointed (i.e. benefits minus cost) (Acemoglu and Johnson, 2005; La Porta et al., 1998; North, 1981; van Veen et al., 2014). Our study extends institutional subsidiary staffing literature by integrating the potential cost of HCNs and theorizing about institutional boundary conditions. By investigating host-country institutional mechanisms that can restrict the potential misappropriation of value from an MNC, our study also offers important managerial implications (Casciaro and Piskorski, 2005; Dieleman and Boddewyn, 2012; Siegel, 2007).

We use a unique dataset covering 4,029 developing market subsidiaries to test our hypotheses on subsidiary staffing with HCNs. We identify non-linear effects, which are consistent with our trade-off argument and the hypothesized potential costs of HCN managers in environments with high corruption, low familiarity of the MNC and weak legal protection from opportunism.

2. Literature background

Researchers have widely enhanced our understanding of the composition and diversity of top management teams and boards. They have theorized about aspects such as size (Carpenter et al., 2004; de Andres et al., 2005), gender (Terjesen and Singh, 2008; Westphal and Milton, 2000), and professional background or experience (Geletkanycz and Black, 2001; Kor and Misangyi, 2008; Papadakis and Barwise, 2002; Yoo and Reed, 2015) in general firm staffing, as well as nationality (Gong, 2006; Masulis et al., 2012; Oxelheim et al., 2013; van Veen and Marsman, 2008; van Veen et al., 2014) in the context of MNC staffing in particular. Other studies have focused on consequences, finding evidence for a link between board or top management team composition and company performance (Carpenter et al., 2004; Certo et al., 2006; Dalton et al., 1998), diversification (Greve et al., 2015; Sanders and Carpenter, 1998; Tihanyi et al., 2000) and market entry strategies (Nielsen and Nielsen, 2011) in MNCs. Such studies have clearly identified staffing as a key strategic instrument. However, they have often looked into domestic staffing in independent firms in the absence of institutional duality. While scholars have emphasized the potential to transfer insights from research on domestic independent firms to MNC subsidiaries, they attest a need for theoretical adaptations (Alpay et al., 2005; Reuer et al., 2014). We claim that nationality of subsidiary managers (i.e. top management team and board members), in particular, is one such field that requires theoretical adaptations due to institutional duality.

2.1. MNC subsidiary management staffing and institutional theory

It is widely acknowledged that "*multinational organizations are substantially different from domestic firms*" (Kostova et al., 2008, p. 997), and more complex. Their organizational units are spread across institutional and country contexts, which often require local responsiveness and knowledge (e.g. Kostova and Zaheer, 1999; Roth and Kostova, 2003a). After all, one of the most important roles of subsidiary managers is to connect to and bargain with host-country stakeholders, and thereby pursue the goals of the MNC (Barringer and Harrison, 2000; Peng et al., 2008; Young et al., 2008). At the same time, however, the MNC needs to strive for integration of subsidiaries within the organization. For subsidiaries, this complexity implies a need to react to host-country