

# **An Examination of the Degree of Management Control Used by American and Japanese Multinational Corporations on their Subsidiaries in Thailand**

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## **ABSTRACT**

As businesses continue to expand internationally, Multinational corporations (MNCs) have experienced a dramatic change in their global business environment. With subsidiaries operating in various countries, MNCs find themselves surrounded by the complexity and cultural diversity that are different from those they have faced by domestic corporations. Control and coordination issues become increasingly more complex as the MNCs focus on identifying mechanisms to ensure effectiveness of the different types of subsidiaries within their global networks. In order to compete with others in a global environment, MNCs need to develop and choose the appropriate degree of management control to exert in their subsidiaries.

This research has identified the importance and difficulties in considering various factors and the degree of management control for MNCs in the global economy. The research uses a survey-based method to examine American and Japanese subsidiaries operating in Thailand. It investigates the significant relationship between various contextual variables and the degree of input control and output control.

The results indicate that the degree of MNC ownership, MNC nationality, cultural distance, decision-making structure, and industry characteristics affect the choice of degree of particular types of control in different manners. The findings also indicate that American companies use both input control and output control more than do Japanese companies. Regarding the effectiveness of MNC's subsidiaries, cultural distance is the only contextual factor found to play an important role in achieving the effectiveness of the subsidiary. In addition, the degree of input control used by American and Japanese MNCs over their subsidiaries in Thailand does not play an important role in determining the effectiveness of the subsidiary. On the other hand, output control will influence the subsidiary effectiveness when considered with other contextual factors. In summary, the subsidiaries will achieve high or low effectiveness when the degree of output control used over it are considered or examined with other contextual variables.

In order for an MNC to compete successfully and achieve high effectiveness, it needs to successfully implement a comprehensive strategy. Because a

control system is the critical linkage to ensure the efficiency and effectiveness in the organization, senior management needs to develop the appropriate parent-subsidiary control system that fits each individual country. This can eventually lead to the achievement of long-term viability, and significantly improve performance at both the subsidiary and headquarters levels.

## **RATIONALE**

International trade and investment have increased dramatically and businesses are now becoming more competitive in the modern world. Global business has grown significantly and currently is expanding its presence, customer base, partnerships and joint ventures in Asia, Latin America and, Europe (Fishman, 1996). Most companies are doing business abroad and make the world become smaller and smaller in every aspect of life (Chang, 1993). This increasing integration in the world economy has been brought about largely by multinational corporations (termed MNCs, hereafter) (Hong, Gibbons & Schoch, 1999).

The issue of management control is a very important concern in a multinational setting (Beldona, 1997). This dissertation attempts to investigate the mechanisms used by MNCs to obtain control over the uncertainty surrounding the management of their foreign subsidiaries. This research develops predictions about the degree of control MNCs use over their subsidiaries, using basic propositions from agency theory and strategic management, while, at the same time, this research also investigates how the nationality of the MNC owners and cultural distances between the parent company and subsidiaries may affect the degree of management control over an MNC's performance in Thailand.

## **PURPOSE OF STUDY**

The purpose of this research is to conduct a theoretically based examination of the degree of control exerted by American and Japanese MNCs on their subsidiaries operating in Thailand. The study uses agency theory and the literature of various

contextual factors to help explain how MNC ownership, the nationality of MNC headquarters, national cultural distance, decision-making structure, and industry characteristics determine the degree of control exerted.

The following research questions will be the focus of this study:

- 1) What factors influence the degree of management control used by parent companies on their subsidiaries in Thailand?
- 2) What differences are there between American and Japanese MNCs in the degree of management control used on their subsidiaries in Thailand?
- 3) What factors influence the effectiveness of subsidiaries?
- 4) Will the types of control used by American and Japanese MNCs affect subsidiary effectiveness?

Multinational corporations (MNCs) have experienced a dramatic shift in their global business environment in the last couple of decades (Kim & Campbell, 1995). Multinational corporations are defined as "enterprises that have a network of wholly or partially (jointly with one or more foreign partners) owned producing, marketing or R&D affiliates located in a number of countries" (Chang & Taylor, 1999). MNCs can also be characterized as a group of geographically dispersed and goal-disparate organizations (Ghosal & Bartlett, 1990). Significantly, they are workplaces where different ethnicities and cultural values are intertwined. Usually, three types of employees compose multinational corporations: (1) parent-country nationals (expatriates)—employees who have the same nationality as the parent company; (2) host-country nationals—employees whose nationality is the same as the host company; and (3) third-country nationals—employees whose nationality is different from either the parent or the host company. In the multinational workplace, these three types of workers often bring different attitudes, values and goals to share among each other, thereby causing some interpersonal conflicts (Chang, 1993). MNCs have to face cultural differences that strongly affect their ability to deploy and manage business-critical applications. Now, MNCs have been plagued by the problem of premature return of expatriates due to their inability to adapt to the culture of the host country. Therefore, multinationalization has increased the demand for individuals who can manage effectively in a foreign environment (Katz & Seifer, 1996).

The reason that this research studies two nations is because, by studying MNCs in one country, the researcher will be able to control other environmental variables, such as degree of cultural differences among foreign subsidiaries, and differences in legal restraints of host countries, which, left uncontrolled, might have obscured the relationship between agency control and owners (Chang, 1993).

## **THEORETICAL BACKGROUND**

As a general concept, control is defined as any process that a firm determines or intentionally affects what others will do (Sohn, 1994). Control is also described as the process that regulates organizational activities so that they are in accordance with the organization's stated objectives (Muralidharan & Hamilton, 1999). Fisher (1998) proposes that control is used to create conditions and motivate the organization to achieve the desirable outcomes. Teall (1992) defines management control as the means by which senior managers ensure that subordinate managers, efficiently and effectively, strive to attain the company's strategy. When the company expands, it is impossible to maintain an efficient management control check on each subordinate manager. A management control system is imperative to every multiple-manager organization.

In the international environment, MNCs are characterized as a group of geographically dispersed and goal-disparate organizations (Ghoshal & Bartlett, 1990). Focusing on the flows of knowledge between MNC subsidiaries, Gupta and Govindarajan (1991) suggest that different subsidiaries play different roles in implementing corporate strategy. This variety of roles complicates the selection of an appropriate control system. Since subsidiaries are workplaces where different ethnicities and cultural values are intertwined, the complexity of the various external-operating environments in the host country have the potential to significantly alter country-specific results and are beyond the control of the subsidiary managers. Therefore, MNCs headquarters have to create and develop their management control systems carefully in order to use them as significant tools in controlling the performance of their overseas subsidiaries. A MNC must internally differentiate its various headquarter relationships based on host country antecedent conditions and local resources (Ghoshal & Nohria, 1989). This will ensure that their management control systems will be compatible and support the common goals (Chang & Taylor, 1999).

### **Agency Theory**

Agency theory is presented as the theoretical background of this research. Agency theory is related to the control system of the operations from an ownership or stockholder perspective (Huse & Eide, 1996). It was developed in the 1960s as an attempt to model the relationship between the principal and the agent. The agent is the one who acts on behalf of the principal or being undertaken to benefit the principal (Chang & Taylor, 1999). The relationship between two parties in this theory is useful to investigate any type of situation where one individual depends on the actions of another. The agents are supposed to behave and act on behalf of the principals (Pratt & Zeckhauser, 1991). Agency theory is used to investigate the

survival of organizations when there is a separation of ownership and control in a multinational company (Beldona, 1997). Agents and principals entered into these relationships because of the benefits of specialization and because of the ability to control agency problems by the separation of decision making

and risk bearing parties. This theory investigates the agency problem that occurs when two parties have different goals or desires (Logan, 2000). Table 1 illustrates how the three different types of control systems differ.

Table 1: Three Types of Control Systems (Muralidharan, R. and Hamilton III, R.)

<b>Output Control</b>	<b>Behavior Control</b>	<b>Input Control</b>
1.) Sales targets such as sales growth, and sales per product categories.	1.) General operating procedures	1.) Controlling the recruitment and training process to promote desired organizational culture.
2.) Cost-based targets such as annual unit cost reduction, unit cost reduction over cumulative volume, and budgetary control.	2.) Decision-making routines.	2.) Repeated and extensive communication of organizational values and beliefs within the MNC.
3.) Productivity targets such as sales per person and operating margins per person.	3.) Procurement norms such as supplier firm size, reputation, and contracting period.	3.) Extensive socialization of managers across country markets within MNC.
4.) Performance targets such as ROA, ROI and profit margins.	4.) Sales-related procedures such as dealer selection criteria and advertising media policies	4.) Staffing country operations with third and home country MNC managers.
		5.) Country market rotation and transfer of key managers.

Snell (1992) and Hamilton & Kashlak (1999) also describe the three types of control in different aspects as follows:

**Output Control** - This type of control can be measured by analyzing a MNC along the following dimensions: the degree to which a firm uses evaluations with significant weightings on results, pay is based on performance, pre-established targets are used for evaluating personnel; numerical records are used as indices of effectiveness, performance is linked to concrete results, and appraisals are based on achieving goals with lack of achievement resulting in low ratings.

**Behavior Control**-This type of control can be measured by analyzing the following organizational attributes: the degree to which a firm weighs evaluations based on behaviors, whether an employee is held accountable regardless of the outcome, the degree to which there is concern for procedures or methods, the degree to which performance programs are imposed from the top down, and the frequency in which employees receive feedback or performance information.

**Input Control** - This type of control can be measured by assessing the degree to which a MNC: provides substantial training before assuming responsibility, establishes the best staffing procedures available, becomes involved in the skill development of an employee, performs multiple evaluations before hiring an individual, provides opportunities for broadening a skill set of an employee takes pride in hiring the best employees possible, and has an overall commitment of the firm to training and development.

A review of literature on agency theory indicates that output-based incentives are probably the primary

method used by principals to reduce agency costs. Corporate headquarters more actively influence a subsidiary's decision making when the decisions involve compensation and benefits, than when they involve other issues such as training and development (Chang, 1993). Eisenhardt (1989) proposes that the agent is more likely to behave in the interest of the principal when the contract is output-based and when the principal has more information about the activities of the agent. Hence output control is utilized in MNCs to avoid perceived compensation risk, or a CEO's perceived risk regarding his or her pay package. Another component of output control in MNCs is the performance reporting system. It is a formal control style that includes frequent performance reporting of financial, marketing, and manufacturing results (Hong et al, 1999). Frequent performance reporting is important because it attempts to monitor outputs of the agency and allows evaluation and feedback about the outcome (Egelhoff, 1984).

Another type of agency control is input control (defined as staffing control by Finkelstein and Hambrick, 1989 or cultural control by Chang, 1993). Chang (1993) proposes that cultural control is accomplished by staffing parent company nationals (PCNs) to the top position of a foreign subsidiary while Finkelstein and Hambrick (1989) define staffing control as the control of selection and retention mechanisms. The major component of input control is to control the CEO's selection and retention mechanisms rather than strictly linking their pay to performance. The headquarters will put PCNs

(parent country nationals) into key positions within the foreign subsidiary because the president position of a foreign subsidiary is undoubtedly a key position (Chang, 1993).

In this research, American and Japanese MNC's headquarters are considered as the principals and the foreign subsidiaries in Thailand are considered as the agents. As the principal, the MNC's headquarters can not effectively make all decisions in the foreign subsidiary since the local interests of subsidiaries may not always be aligned with those of the MNC's headquarters as a whole (Roth & O'Donnell, 1996). The relationship between principal (headquarters) and agent (subsidiary) may lead to agency problems since subsidiaries operate in environments that are very different from those of the headquarters (Beldona, 1997).

## **HYPOTHESES DEVELOPMENT**

With subsidiaries operating in various countries, MNCs find themselves surrounded by the complexity and cultural diversity that are different from those faced by domestic corporations. The complexity of the various external operating environments in the host country has the potential to significantly alter country-specific results and is beyond the control of the subsidiary managers. The different subsidiaries play different roles in implementing corporate strategy. This variety of roles complicates the selection of an appropriate control system. Hence in order to compete successfully in the global business and to sustain a competitive advantage in the international scene, MNCs need a comprehensive strategy that is successfully implemented. They need to develop an effective and appropriate parent-subsidiary control system that is appropriate for both host and home countries. However, designing the appropriate control system becomes more difficult because MNCs increasingly compete around the world in countries with different environments and nationalities. Therefore, MNCs must internally differentiate their various headquarter relationships based on host country antecedent conditions and local resources (Hamilton III & Kashlak, 1999).

### **Degree of Ownership and Control Systems**

Chang (1993) noted in his research about agency theory that the ownership structure affects the choice of control in MNCs. He found that as the ownership of a MNC's subsidiary increases, the degree of control exerted by the parent company of the subsidiary also increases. In order for managers to be able to directly control a foreign subsidiary, theoretically they are supposed to have more ownership of the subsidiary.

Using the studies of Chang (1993) and Beldona (1997), the degree of ownership owned by the parent company is expected to influence the degree of control used in MNC subsidiaries. With a higher degree of ownership, managers can reduce their risks by directly controlling the activities of the

subsidiaries. The more they own, the more control they have. Therefore, the degree of agency control used by the parent company is predicted by the degree of ownership of headquarters in the foreign subsidiaries. With a high degree of ownership in the foreign subsidiary, the degree of either input control or output control is expected to increase.

Moreover, when the degree of ownership by the parent is high, output control used by the parent should be higher than input control. This is because output control is the way to control its subsidiaries in the form of more frequent reporting to the head-quarters whereas input control requires performance reporting less frequently from the subsidiaries (Chang, 1993). Accordingly, the hypotheses of the relationship between the degree of ownership and control systems would be expressed as follows:

Hypothesis 1: The degree of MNC ownership of a subsidiary will influence the degree of control over its subsidiary.

H1a) The higher the degree of ownership by the parent company of a subsidiary, the higher the degree of input control used by the parent.

H1b) The higher the degree of ownership by the parent company of a subsidiary, the higher the degree of output control used by the parent.

H1c) The higher the degree of ownership by the parent company of a subsidiary, the higher the degree of output control vs input control used by the parent.

### **Nationality of MNC Headquarters and Control Systems**

There have been many studies about management practices in the U.S and Japan. They show the different styles of management practices between the two nations. Hence it might be hypothesized that the degree of agency control exerted by American and Japanese MNCs would differ greatly because of the cultural differences.

Chang (1993) explains that American companies focus on output control while Japanese companies focus on input control. American companies' utilization of output control may be explained by considering their management systems, which emphasizes the concept of efficiency (Chang, 1993). Hodgetts & Luthans (1997) explain that control in American MNCs focuses more on the quantifiable, objective aspects of a foreign subsidiary. The MNCs require more precise plans and budgets in generating suitable standards for comparison. Moreover, Kreder and Zeller (1988) also suggested that there is less participation and employee-orientation in American companies because employees' personal problems are rarely discussed. American managers emphasize employee relative independence. Since American systems pursue efficiency and high performance through the application of quantifiable measures and need less participation of the employees, managers are likely to focus heavily on outcomes (Chang, 1993).

Some studies show Japanese MNCs rely more heavily on the use of input control than American MNCs. Japanese MNCs assigned parent country nationals (PCNs) more extensively to their CEO positions than American MNC's did (Chang, 1993). Fukuda (1992) noted the differences of staffing strategies between American and Japanese MNCs in that the American style prefers selecting and promoting able individuals regardless of their nationalities while Japanese MNCs have the tendency of filling a high percentage of senior management positions with PCNs sent from the home country. Similarly, Hofstede (1993) found that the core of Japanese companies is the permanent worker group; workers who for all practical purposes are tenured and who aspire to life-long employment. The Japanese management styles of life employment and seniority are thought to generate a psychological reluctance to hire foreigners. Home country attitudes, management practices, knowledge, and managers are superior to those of host countries (Chang, 1993). These explanations regarding Japanese management styles show that Japanese MNCs focus heavily on the input basis of control.

The assumptions based on the above arguments lead to the following hypotheses:

Hypothesis 2: The nationality of the parent company will influence the degree of control over its subsidiaries.

H2a) For American subsidiaries operating in Thailand, the degree of input control used by the parent company will be relatively low.

H2b) For American subsidiaries operating in Thailand, the degree of output control used by the parent company will be relatively high.

H2c) For Japanese subsidiaries operating in Thailand, the degree of input control used by the parent company will be relatively high.

H2d) For Japanese subsidiaries operating in Thailand, the degree of output control used by the parent company will be relatively low.

### **Cultural Distance and Control Systems**

There have been many researches of how cultural distance affects work values, managerial decisions, patterns of negotiations, overseas entry modes, and the degree of partner reciprocity, etc. (Hamilton & Kashlak, 1999). The greater the extent to which an organization's headquarters and subsidiaries are culturally distant, the more difficult it becomes to effectively supervise the various agents (Gomez-Meija & Palich, 1997). According to the agency theory perspective, agency costs will increase relative to cultural distance (Roth & O'Donnell (1996). When the degree of cultural distance decreases, the cost of adapting an MNC's control system to the host country subsidiary will also decrease (Gomez-Meija & Palich, 1997). Since the distance between national cultures significantly influences decision-making and strategies, it is proposed that the degree of cultural distance is an

antecedent condition affecting the MNC selection of a control system. When cultural distance between the home country and the host country is high, the probability of using an input control system should increase because of the higher transaction costs associated with output or behavior control. The probability of using input control should increase as the parent company's ability to effectively employ output control declines (Hamilton & Kashlak, 1999). For example, cultural training may be required for expatriates when the culture between the home country and the host country is distant. Conversely, we can propose that when cultural distance between the home country and the host country is close, the probability of using output control system should increase. The preceding arguments lead to the following hypotheses:

Hypothesis 3: The cultural distance between the home country and the host country will influence the degree of control over its subsidiaries.

H3a) The greater the cultural distance between the home country and the host country, the higher the degree of input control that will be used by the parent company.

H3b) The smaller the cultural distance between the home country and the host country, the higher the degree of output control that will be used by the parent company.

### **Decision Making Structure and Control Systems**

In addition to the degree of MNC ownership, nationality, and cultural distance, the effect of various contextual dimensions like the decision-making structure of the subsidiary is also examined in this research study. According to agency theory, the agency relationship consists of a contract under which principals engage agents to perform some services on their behalf (Eisenhardt, 1989). This includes delegating decision-making authority to the agent. Decision-making authority in a subsidiary should be centralized or decentralized depending on the subsidiary's strategy (Beldona, 1997). Principals always bear uncertainty and risk about what the agents are normally doing (Chang & Taylor, 1999). Determining the performance of the agent by evaluating the agent on the basis of output will be costly to the headquarters because they can be affected by several factors in uncertain environments such as economic conditions and competitors' actions. Therefore, in high uncertainty situations, such as decentralized firms, input control is more appropriate (Beldona, 1997). This implies that the degree of input control used by the parent will be high and the degree of output control used by the parent will be low in decentralized firms. Conversely, when uncertainty is low, as in the centralized firms, the degree of output control used by the headquarters will increase while the degree of input control used by the headquarters will decrease. The hypotheses regarding decision-making structure are as follows:

Hypothesis 4: The type of decision-making structure (centralized or decentralized) will influence the degree of control a parent company will have over its subsidiaries.

H4a) The higher the degree of centralization, the lower the degree of input control that will be used by the parent company over its subsidiaries.

H4b) The higher the degree of centralization, the higher the degree of output control that will be used by the parent company over its subsidiaries.

H4c) The higher the degree of decentralization, the higher the degree of input control that will be used by the parent company over its subsidiaries.

H4d) The higher the degree of decentralization, the lower the degree of output control that will be used by the parent company over its subsidiaries.

### **Industry Characteristics and Control Systems**

Industry characteristics of MNC subsidiaries are likely to affect the choice and degree of control systems used by the parent companies (Beldona, 1997). Differences in the external environment would necessitate firms using different strategies for their affiliates. For example, firms in different life-cycle stages have different characteristics (Black, 1998). In general, the company begins its operation in the introduction stage by creating a vision in its founder's eye, which is called Courtship. The strategy used in the organization must incorporate commitment expressed in sacrifices commensurate with future risks and realities (Adizes, 1998). When the subsidiaries are infant and newly operating, the organization needs to promote the organizational culture desired by the parent company. The type and degree of control system used by the parent company should be in accordance with this situation. In the introductory stage with high uncertainty, a recruiting process such as assigning PCNs to work in their subsidiaries and an advanced training process for expatriates should be provided in order to reduce the risk. Hence, where subsidiaries are operating in an industry characterized by a highly volatile environment, outcome uncertainty is very high. The parent companies use a high degree of input control to diminish risk over their subsidiaries. Since the relationship between cause and effect is very difficult to measure (Beldona, 1997), the parent companies are likely to use a high degree of input control over their subsidiaries in a high dynamic situation. On the other hand, the parent companies use a high degree of output control over their subsidiaries in a low dynamic environment. In conclusion, industry characteristics will have a significant influence on outcome uncertainty, which in turn affects the degree of control used by the parent company over its subsidiaries. These arguments lead to the following hypotheses.

Hypothesis 5: The industry characteristics of the subsidiary will influence the parent company's degree of control over its subsidiaries.

H5a) When subsidiaries operate in a high dynamic environment, the degree of input control used by the parent company will likely increase.

H5b) When subsidiaries operate in a low dynamic environment, the degree of input control used by the parent company will likely decrease.

H5c) When subsidiaries operate in a high dynamic environment, the degree of output control used by the parent company will likely decrease.

H5d) When subsidiaries operate in a low dynamic environment, the degree of output control used by the parent company will likely increase.

### **RESEARCH METHODOLOGY**

This research used a survey-based methodology, cross-sectional research design, to collect data on the types of control used by American and Japanese MNCs over their subsidiaries in Thailand. Data were collected through the administration of questionnaires to top managers (Vice President and above) of both American and Japanese subsidiaries operating in Thailand. The questionnaires were mailed to the presidents of those subsidiaries in order to obtain their reports about the control practices used by their parent companies. American and Japanese subsidiaries were selected for this study because they are the two major investing nations in Thailand and their countries are considerably different when the cultural dimensions of Hofstede are measured.

It is commonly believed that the response rate of questionnaires mailed out in conducting research is very low. Therefore follow-up phone calls were made in order to increase the response rate. To minimize the impact of response bias of the research findings, the researcher took two additional steps: (1) a letter sent with each questionnaire informed respondents of 100% confidentiality; (2) the questionnaire did not seek any financial data and did not ask the name of the respondents, and did not attempt to identify the company unless the company requested a copy of the results. This request by the companies would enable them to compare themselves with others in the survey.

The procedures of this research began with the preparation of questionnaires. They were prepared in English for use by American respondents. A Japanese student of Bangkok University also translated these questionnaires into the Japanese language for use by Japanese respondents. Each item of the translated questionnaires was rechecked carefully by a Thai who used to live in Japan for six years. This was done in order to verify that the meaning of the items were as intended.

Questionnaires were sent to twenty randomly selected companies for a pilot test. Four questionnaires were returned. In order to check for an accurate understanding of the questionnaire, in-depth interviews and discussions with an American and a Japanese were held. There were several revisions made to the questionnaire based on those interview results.

The sample of this study was composed of American and Japanese subsidiaries in Thailand. American subsidiaries are member companies and associations of the American Chamber of Commerce. The names of top managers and companies were selected from the "Directory of American Chamber of Commerce," Japanese subsidiaries were selected from the "Factory Directory in Thailand, Volume 4 2001/2002".

The selection of both American and Japanese subsidiaries operating in Thailand was made randomly provided that they met the following three criteria:

1. A list of the top managers had to be available.
2. The subsidiaries had to be in the manufacturing sector.
3. The subsidiaries had to be operating in Thailand for at least three years.

Data collection began in June 2002. In this study, a total of seven hundred questionnaires were mailed out to American and Japanese subsidiaries. There were 350 questionnaires for American and 350 questionnaires for Japanese companies. In order to further increase the response rate, a small note was attached on the front page of each questionnaire reminding the respondents to return the completed questionnaires by the 15<sup>th</sup> of July 2002. The reminder follow-up phone call requesting the managers to return the questionnaire back was also done two weeks after the questionnaires were mailed out.

A total of 219 usable questionnaires were received in return. 111 questionnaires were from American subsidiaries and 108 questionnaires were from Japanese subsidiaries. The response rate was 32% for the American sample and 31% for the Japanese sample. The most commonly used title for respondents from both American and Japanese subsidiaries was "Managing Director" (American firms = 37% and Japanese firms = 39.6%).

## RESULTS

### 1) Degree of Ownership and Control Systems

Hypothesis 1 investigates the effect of MNC ownership on the degree of subsidiary's control. It states that the degree of MNC ownership of its subsidiaries will influence the degree of control over its subsidiaries. The implications are discussed as follows:

H1a states that the higher the degree of ownership by the parent company of a subsidiary, the higher the degree of input control used by the parent. The hypothesis is supported as the results indicated in Table 7 show a significant positive effect of the degree of MNC ownership on the degree of input control ( $B = .155, p < .05$ ) such that as the degree of ownership increased, so did the degree of input control.

H1b posits that the higher the degree of ownership by the parent company of a subsidiary, the higher the degree of output control used by the parent. Results in Table 8 support this hypothesis ( $B =$

$.289, p < .001$ ). This shows that the degree of ownership by the parent has a significant positive effect on the degree of output control used by the parent. When the degree of ownership increased, the degree of output control also increased.

H1c holds that the higher the degree of ownership by the parent company of a subsidiary, the higher the degree of output control versus input control used by the parent. Again, the results in Table 7 and Table 8 support the hypothesis. ( $B = .155, p < .05$  for input and  $B = .289, p < .05$  for output). This indicates that the degree of output control used by the parent company is higher than input control when the degree of ownership by the parent of its subsidiaries is high.

As predicted in the above hypotheses, the effect of these two variables is positive, such that as the degree of ownership increased, so did both degrees of input and output controls.

### 2) Nationality of MNC Headquarters and Control Systems

Hypothesis 2 investigates the effect of MNC nationality of the parent company on the degree of agency control. It states that the nationality of the parent company will influence the degree of control over its subsidiaries. Each hypothesis is discussed in turn.

H2a posits that for American subsidiaries operating in Thailand, the degree of input control used by the parent company will be relatively low. The results shown in Table 9 do not support the hypothesis ( $t = 3.044, p < .01$ ). This indicates that the degree of input control used by American MNCs over their subsidiaries in Thailand is not low, but is instead significantly higher than the highest value for "low degree". The degree of input control exerted by the parent company is in the moderate level.

H2b states that for American subsidiaries operating in Thailand, the degree of output control used by the parent companies will be relatively high. This hypothesis is supported by the results shown in Table 10 ( $t = 11.221, p < .001$ ). This implies that the degree of output control exerted by the American MNCs over their subsidiaries operating in Thailand is relatively high.

H2c holds that for Japanese subsidiaries operating in Thailand, the degree of input control used by the parent company will be relatively high. The results shown in Table 11 do not support this hypothesis ( $t = -14.844, p < .001$ ). This indicates that the degree of input control used by Japanese MNCs over their subsidiaries in Thailand is relatively low.

H2d posits that for Japanese subsidiaries operating in Thailand, the degree of output control used by the parent companies will be relatively low. This hypothesis is not supported by the results shown in Table 12 ( $t = 7.785, p < .001$ ). This indicates that the degree of output control exerted in Japanese subsidiaries operating in Thailand is not low. The

degree of output control is in the moderate level. In addition, this indicates that for Japanese MNCs the degree of output control is considerably higher than the degree of input control.

A different way to test Hypothesis 2 is to compare the differences between Japanese subsidiaries and American firms on the level of both input control and output control. T-tests shown in Table 13 reveal that there is a significant difference between American subsidiaries and Japanese subsidiaries in the use of input controls. American firms use a higher level of input control than do Japanese firms ( $t = 3.044$ ,  $p < .01$  for American and  $t = -14.844$ ,  $p < .001$  for Japanese). T-tests shown in Table 13 also reveal that there is a significant difference between Japanese subsidiaries and American subsidiaries in the use of output controls. American subsidiaries use a higher level of output control than do Japanese firms ( $t = 11.221$ ,  $p < .001$  for American and  $t = 7.785$ ,  $p < .001$  for Japanese). It can be concluded that American firms use an overall higher level of control than do Japanese firms. This lends strong support for Hypothesis 2.

### 3) Cultural Distance and Control Systems

Hypothesis 3 investigates the cultural distance on the degree of agency control. It states that the cultural distance between the home country and the host country will influence the degree of control over its subsidiaries. The results of each hypothesis are discussed as follows:

H3a posits that the greater the cultural distance between the home country and the host country, the higher the degree of input control that will be used by the parent company. The results in Table 14 show a significant negative effect between two variables ( $B = -.360$ ,  $p < .001$ ). This implies that when the cultural distance is greater, the degree of input control used by the parent companies is less. Therefore, the hypothesis is not supported.

H3b holds that the smaller the cultural distance between the home country and the host country, the higher the degree of output control that will be used by the parent company. This hypothesis is supported by the results shown in Table 15 ( $B = -.311$ ,  $p < .001$ ). As predicted, the direction of this effect is opposite, such that when the cultural distance between the home country and the host country is close, the probability to use output control is high.

### 4) Decision Making Structure and Control Systems

Hypothesis 4 investigates the effect of the type of decision-making structure on the degree of subsidiary control used by the parent company. It indicates that the type of decision-making structure (centralization and decentralization) will influence the degree of control a parent company will have over its subsidiaries. Here are the implications of each assumption.

H4a holds that the higher the degree of centralization, the lower the degree of input control that will be used by the parent company over its subsidiaries. The results reported in Table 16 do not support the hypothesis. When the degree of centralization is high, the degree of input control used by the parent company over its subsidiaries is not relatively low ( $M = 2.7845$ ,  $p > .05$ ). Instead, this indicates a moderate degree of input control.

H4b posits that the higher the degree of centralization, the higher the degree of output control that will be used by the parent company over its subsidiaries. The results in Table 17 show that there is a significant effect between these two variables ( $M = 3.9914$ ,  $p < .001$ ). This indicates that when the degree of centralization is high, the degree of output control used by the parent companies will increase. Therefore, the results support this hypothesis.

H4c posits that the higher the degree of decentralization, the higher the degree of input control that will be used by the parent company over its subsidiaries. This hypothesis is not supported because the results reported in Table 18 show that when the degree of decentralization is high, the degree of input control used by the parent company is low ( $M = 2.5629$ ,  $p < .001$ ).

H4d states that the higher the degree of decentralization, the lower the degree of output control that will be used by the parent company over its subsidiaries. The results reported in Table 19 do not support the hypothesis ( $M = 3.6615$ ,  $p < .001$ ). When the degree of decentralization on the subsidiaries increases, the degree of output control used by the parent companies will also increase.

### 5) Industry Characteristics and Control Systems

Hypothesis 5 investigates the effect of the industry characteristics of the subsidiary on the degree of control. It states that the industry characteristics of the subsidiary will influence the degree of a parent company's control over its subsidiaries. The following implications are discussed:

H5a posits that when subsidiaries operate in a high dynamic environment, the degree of input control used by the parent company will likely increase. Further H5b posits conversely that when subsidiaries operate in a low dynamic environment, the degree of input control used by the parent company will likely decrease. Results reported in Table 20 show that there is no correlation between the industry characteristic of subsidiaries and the degree of input control ( $p > .05$ ). Therefore, the effect of these two variables is not significant. The preceding results do not support H5a and H5b.

H5c holds that when subsidiaries operate in a high dynamic environment, the degree of output control used by the parent company will likely decrease. Further, H5d states that when subsidiaries operate in a low dynamic environment, the degree

of output control used by the parent company will likely increase. The results reported in Table 21 show positive significance on the effect between industry characteristics and the degree of output control ( $B = .149, p < .05$ ). Therefore, the results do not support these two hypotheses because the results imply that when the industry characteristic of subsidiaries is a high dynamic environment, the degree of output control will increase. Conversely, when the industry characteristic of subsidiaries is a low dynamic environment, the degree of output control will decrease.

### Effects of Control Variables

#### 1) Age of subsidiary

The number of years the subsidiary has been operating in Thailand is expected to affect the choice and degree of control exerted by the parent company. For American subsidiaries in Thailand, the results reported in Table 22 show that the age of subsidiary or the number of years since the subsidiary started its operation in Thailand has no significant effect on the degree of input control used by the parent company ( $p > .05$ ) whereas the results reported in Table 23 show a significant positive effect on the degree of output control used by the parent company ( $B = .314, p < 0.5$ ). This indicates that the higher the number of years the American subsidiaries have been operating in Thailand, the higher the degree of output control exerted by the parent company.

For Japanese subsidiaries operating in Thailand, the results reported in Tables 24 and 25 imply that the age of Japanese subsidiary has no significant effect on the degree of either input or output control used by the headquarters ( $p > .05$ ).

#### 2) Industry Stage

For American subsidiaries operating in Thailand, the industry life-cycle stage of the subsidiary is found to have a significant negative effect only on the degree of output control ( $B = -.200, p < .05$  <table 27>) while there is no significant effect on the degree of input control ( $p > .05$  <table 26>). These preceding results show that when the industry life-cycle stage of its subsidiary is in a higher stage, the degree of output control used by the headquarters will decrease. For Japanese subsidiaries operating in Thailand, Tables 28 and 29 imply that the industry life-cycle stage of a subsidiary has no significant effect on either the degree of input control or output control ( $p > .05$ ).

## DISCUSSION

Research Question 1: What factors influence the degree of management control used by parent companies on their subsidiaries in Thailand?

The study investigates the effects through five independent variables: degree of MNC ownership, nationality of MNC, cultural distance, decision-

making structure, and industry characteristics. To answer this research question, the following variables are described:

1) Degree of MNC Ownership - This study supports agency theory propositions regarding the influence of the degree of MNC ownership on the degree of input control and output control used by the parent company. The degree of MNC ownership was found to directly relate to both input control and output control. The effect of these two variables is positively correlated such that when the degree of ownership increases, the degree of either input control or output control also increases. This is in accordance with Chang's study (1993). In addition, the results show that when the degree of ownership by the parent company increases, the degree of output control would be higher than the degree of input control used by the parent company. This may be because when the degree of ownership by the parent is high, output control, which is the way to control its subsidiaries in the form of more frequent reporting to the headquarters, is probably more widely used by the parent company than input control, which requires less performance reporting from its subsidiaries (Chang, 1993). In conclusion, the degree of ownership affects the degree of agency control used by the headquarters. Increases in either the degree of input control or the degree of output control are influenced by an increase in the degree of ownership.

2) Nationality of MNC Headquarters – nationality of MNC headquarters was predicted to affect the degree of agency control exerted by the parent company, too. In comparison, American companies are found to use a high degree of both input control and output control whereas Japanese companies are found to use a lower degree of both input control and output control. Many cultural research studies have suggested that American companies are more output oriented than Japanese firms while Japanese companies are more input oriented than American firms (Chang, 1993). But with these preceding results, it can be concluded that American companies are more concerned with agency control, either input control or output control, than Japanese firms. In summary, the nationality of MNC headquarters does influence the degree of subsidiary control used by the headquarters.

3) Cultural Distance – Since cultural distance affects managerial decisions, MNCs should initially expand their businesses to overseas to the countries that are most similar in culture to its home country. It would help them more easily to implement and control their strategies. The findings show that the greater the cultural distance between the home country and the host country, the smaller the degree of input control exerted by the parent company. Conversely, the smaller the cultural distance between

the host country and the home country, the higher the degree of input control used by the parent company. When the cultural distance of both countries is close, all strategies and management practices provided by the headquarters are easier to understand and accept by their subsidiaries as they have similar cultures.

Regarding output control, the researcher predicted that the smaller the cultural distance between the home country and the host country, the higher the degree of output control that would be used by the parent company. The findings support the prediction that when the cultural distance between the host country and the home country is close, the degree of output control exerted by the parent company is high. On the other hand, when the cultural distance is distant, the degree of output control used by the parent company is low.

In conclusion, cultural distance influences the degree of both input control and output control used by the headquarters. This affects the degree of agency control. Conversely, the greater the cultural distance between the home and the host countries, the smaller the degree of both input control and output control that will be used by the parent company. On the other hand, the smaller the cultural distance between the home and the host countries, the higher the degree of both input control and output control that will be used by the parent company. These findings may be explained by the following: 1) when the cultural distance between the headquarters and the affiliates is close, it is easier for the headquarters to control its subsidiaries so that the degree of control used by the parent is increased; 2) when the cultural distance between the headquarters and the affiliates is distant, it is more difficult for the headquarters to control its subsidiaries so that the degree of control used by the parent decreases.

4) Decision Making Structure – The prediction indicated that the degree of decision-making structure (centralization and decentralization) used by the parent company will influence the degree of a parent company's control over its subsidiaries. This study found that there is no significant relationship between the decision-making structure (both centralization and decentralization) and the degree of input control used by the parent company. On the other hand, there is a significant effect between the decision-making structure (both centralization and decentralization) and the degree of output control used by the parent company. The study also found that when the degree of centralization increases, the degree of output control used by the parent company will also increase. On the other side, when the degree of decentralization increases, the degree of output control used by the parent company will decrease. In summary, the decision-making structure influences only the degree of output control used by the headquarters, but doesn't influence the degree of input control used by the parent company.

5) Industry Characteristics – When firms are operating in a high dynamic environment, outcome uncertainty is high. Industry characteristics can have a significant influence on outcome uncertainty, which in turn influences the type and degree of controls used in their subsidiaries (Beldona, 1997). This research study found that there is a significant effect between the industry characteristic of subsidiaries and the degree of output control used by the parent company. Conversely, there is no significant effect between the industry characteristics on the degree of input control.

Regarding the effect on output control, when the industry characteristic of subsidiaries is a high dynamic environment, the degree of output control used by the headquarters will increase. Conversely, when the industry characteristic of subsidiaries is a low dynamic environment, the degree of output control used in their affiliates will decrease. Therefore, the industry characteristic of subsidiaries will influence only the degree of output control exerted by the parent company, but not the degree of input control.

The preceding discussions lead to the conclusion that headquarters need to consider the degree of MNC ownership, nationality of MNC headquarters, cultural distance, decision-making structure, and industry characteristics when designing a control system for the subsidiaries.

Research Question 2: What differences are there between American and Japanese MNCs in the degree of management control used on their subsidiaries in Thailand?

The preceding results show that the nationality of MNC headquarters would affect the degree of agency control exerted by the parent companies. The findings show that the degree of output control is greater than the degree of input control for either Japanese or American subsidiaries operating in Thailand. The findings also show that American MNCs use a higher level of both input control and output control over their subsidiaries than do Japanese subsidiaries operating in Thailand. This is counter to many cultural studies which have suggested that Japanese companies are more input-oriented than American firms. The unexpected results that American firms use input control more than Japanese firms may be a result of the increase in output-focus by Japan. The results from this study also show that the degree of output control used in Japanese subsidiaries is greater than the degree of input control. Chang (1993) offers support for the idea that Japanese are more concerned about both performance and outcome measures than before. Moreover, the economy in Thailand has changed, with higher uncertainty, it is possible that output control rather than input control is greater attention than in the past by Japanese MNCs. Therefore, it is reasonable to find that Japanese firms may now try to exert more and more output control over their foreign subsidiaries.

Research Question 3: What factors influence the effectiveness of subsidiaries?

Among the contextual factors, the research found there is only one variable that influences the effectiveness of subsidiaries: cultural distance. According to Table 31, cultural distance has a significant negative effect on subsidiary effectiveness ( $B = -.313, p < .05$ ). This implies that the greater the cultural distance between the home and the host countries, the lower the subsidiary effectiveness. On the other hand, the smaller the cultural distance between the home country and the host country, the higher the subsidiary effectiveness. This supports the idea that, since cultural distance affects managerial decisions, an MNC should initially invest their business abroad in countries that are most similar in culture to the culture of its home country (Hamilton & Kashlak, 1999). This is done in order to more easily implement and control its strategies and to get higher subsidiary effectiveness.

The other contextual variables in this study, which consist of MNC ownership, MNC nationality, decision-making structure, and industry characteristics, are found have no significant effect on subsidiary effectiveness ( $B > .05$ ). In summary, these variables have no influence on the subsidiary effectiveness. Only cultural distance plays an important role in affecting subsidiary effectiveness of American and Japanese subsidiaries in Thailand.

Research Question 4: Will the type of control used by American and Japanese MNCs affect subsidiary effectiveness?

Input control and output control are statistically independent from each other as they relate to subsidiary effectiveness. The results reported in Table 31 indicate that input control has no significant effect on subsidiary effectiveness. On the other hand, output control has a significant negative effect on subsidiary effectiveness ( $B = -.198, p < .05$ ). This means that the higher the degree of output control used by the headquarters, the lower the level of subsidiary effectiveness. However, according to the results reported in Table 31, output control would have a significant negative effect on subsidiary effectiveness when combined with other contextual variables. This implies that the degree of output control used over a firm's subsidiaries should be considered in accordance with other contextual factors in this study. For example, when the degree of ownership increases, the degree of output control also increases. Even though these variables have a significant positive relationship, they may lead to low subsidiary effectiveness. This is because if the degree of output control used over its subsidiaries is too high, the subsidiary effectiveness will be low. Therefore, the parent company may wish to reduce the degree of output control used over their subsidiaries by considering other management practices.

## CONCLUSIONS

The line of research presented in this study is critical as MNCs expand their interorganizational relationships across global markets. Control and coordination issues become increasingly more complex as the MNCs focus on identifying mechanisms to ensure effectiveness of the different types of subsidiaries within their global networks (Ellis, 2000). From a theoretical standpoint, this research studies the degree of agency control by investigating various contextual factors that affect the degree of control exerted by the headquarters of MNCs. The study gives a more comprehensive picture of MNC control than has been offered by previous studies. In the international setting, this research focuses on both input control and output control used by American and Japanese MNCs over their subsidiaries in Thailand. It investigates the significant effect between various variables and the degree of certain types of control. The results show that the degree of a particular type of control (e.g. input control, output control) used by their headquarters is affected by such variables as: (1) Degree of ownership, which plays an essential role in determining the degree of each type of control system that the parent company might choose to control its subsidiaries; (2) Nationality of MNC headquarters, which could also have influence the degree of control employed over their subsidiaries (American companies use both input control and output control more than do Japanese companies); (3) Cultural distance also plays as an important role in determining the degree of particular types of control; (4) Decision-making structure appears to influence only the degree of output control used over the subsidiaries, but does not influence the degree of input control; (5) Industry Characteristics (e.g. high/low dynamic environment) also play an important role. It will influence the degree of output control, but does not influence the degree of input control. With respect to the significance of various factors on subsidiary effectiveness, cultural distance is the only important variable that influences subsidiary effectiveness.

In addition, the degree of input control used by American and Japanese MNCs over their subsidiaries in Thailand does not play an important role in determining the effectiveness of the subsidiary. On the other hand, output control will influence the subsidiary effectiveness when considered with other contextual factors. The degree of output control will have a significant negative relationship on the subsidiary effectiveness. In summary, the subsidiary will achieve high or low effectiveness when the degree of output control used over its subsidiaries is considered or examined with other contextual variables.

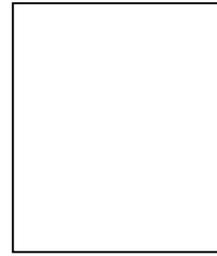
This research has identified the importance and difficulties of how to consider the various factors and the degree of particular types of control for MNCs in

a global economy. In order for a MNC to compete successfully and achieve high effectiveness, it needs a comprehensive strategy to be successfully implemented. Because an appropriate control system is the critical linkage to ensure efficiency and effectiveness in the organization, senior management needs to create the appropriate parent-subsidiary control system that fits each country individually. Choosing the appropriate type of control system and estimating the appropriate degree of a particular type of control has become more difficult as MNCs increasingly compete around the world in countries with greater cultural distance, fluctuating government restrictions, and immense economic instability. MNCs are increasingly forced to rely on both input control and output control. To help the companies create and sustain their competitive advantages in a global economy, senior management can design headquarter and subsidiary control systems that will maximize the effectiveness of the corporate strategy (Hamilton et al, 1996). This can eventually lead to the achievement of long-term viability and significantly improve performance at both the subsidiary and headquarters levels.

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