

## **Strategy and culture in international co-ordination mechanisms**

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## *Abstract*

Management's co-ordination mechanisms for a subsidiary located in a foreign country are influenced by headquarter's, subsidiary's and environmental characteristics. Depending on what strategy the headquarter pursuits, the role of a subsidiary can differ from purely receptive to active. A receptive subsidiary is highly integrated with the headquarters and leaves strategic design to the headquarter's management. An active one is able to influence the overall strategy of the Mother Company. The autonomy, that an active subsidiary requires, does not exist in the situation where formal and standardised control is performed. Development of multilateral relationships, joint task groups and informal contacts among the company members without the distinction between headquarter and subsidiary managers are, in our view, of vital importance for good performance. To what extent are both; formal and informal kinds of mechanisms recognised if headquarter and subsidiary are located in culturally distant countries? We categorised the answers of structured interviews of companies in Poland on two dimensions, originally proposed by Harzing(1999): formalisation and explicitness. We explored the configurations of control mechanisms between the Dutch headquarters and its Polish subsidiary. These countries represent two opposite quadrants on the Hofstede power distance/uncertainty avoidance dimension. The results of preliminary interviews are presented in this paper. These preliminary interviews did not include the assessment of the relationship between the control mechanism and performance of the subsidiary. It is necessary to include it in the next step of my research, in order to evaluate the relationships between the portfolio of co-ordination mechanisms, the role of the subsidiary and the impact of the cultural factor.

## **Introduction**

Central Eastern European markets have become promising investment areas for many western companies during the last decade. Through the integration process with the economies of the rest of Europe, institutional limitations and tax barriers have been reduced. Any company can participate in the CEEC-markets without legal and political limitations. Companies can choose an entry mode for a market between co-operation with a local partner, Greenfield investment or acquisition of an existing local enterprise. The choice is based on weighing of the risk perception, availability and a quality of the potential partners and localisation factors, like the availability of resources (1984). The criteria for the selection of a particular entry mode have received broad attention in the scientific research (Hill, Hwang et al. 1990; Agarwal and Ramaswami 1992; Bell 1996; Meyer and Estrin 1998; Pan and Tse 2000; Chen and Hu 2002). But the organisation and management of a subsidiary after the entry is still a relatively understudied area, especially the new free-economy countries in Central Eastern Europe.

Organisation, co-ordination and control play crucial roles in developing a foreign activity. Even well organised and successful multinationals are threatened by not optimally designed and implemented control activities in their subsidiaries. To mention Ahold concern, where the managers of the foreign subsidiaries miss-used a broad autonomy granted to them by headquarters. The profit expectations occurred to be largely overestimated and resulted in the collapse of the trust of the investors and in serious problems for the whole concern. Such experiences stress the importance of an efficiently designed portfolio of co-ordination mechanisms and its implementation. In this paper we will explore the configurations of control mechanisms the headquarters use for their subsidiaries, explain the relationship between control and co-ordination and will argue the importance of culture for selecting control mechanisms.

This document is structured as follows; first we will define basic concepts like control, co-ordination and the culture. Next, we will link these to Mintzberg's organisational structures and define different subsidiary roles depending on the headquarters strategy. Following, we will introduce some preliminary results from the pilot interviews conducted in July 2002 among Dutch subsidiaries in Poland. Finally, some conclusions and future steps in my research will be presented.

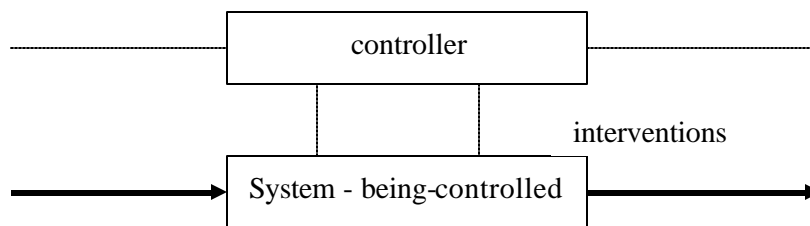
## Control and co-ordination defined

There appears some confusion in the use of the concepts of control and co-ordination among scientists in the field. In this section we will try to define control and relate control to co-ordination. Many authors defined the concept of 'control':

As to Child (1984) "Control is essentially concerned with regulating the activities within an organisation so that they are in accord with expectations established in the policies, plans and targets."

As to Aken (1978)

"Control is the use of interventions by a controller to promote preferred behaviour of a system-being-controlled." (Aken 1978)



**Figure 1 A Controlled Conversion System**

—————> Physical input and output  
————— Information

Control is a method of ensuring the proper execution of plans, consisting of three steps:

1. Establishing standards of performance,
2. Measuring current performance in relation to established standards
3. Taking corrective action necessary to fulfilment of organisational objectives.

Standard is a level of performance established to serve as a model, criterion or expectation."(Williams, DuBrin et al. 1985).

Although there are some differences in the definitions, they have two elements in common. The element of *power* in the relationship and the *ability* of managers to *direct and adjust the behaviour* of an individual in the organisation.

## Co-ordination

In contrast to control, the power element in co-ordination seems to be much more implicit. Integration, harmonisation and linking different parts of the organisation are the main aspects of co-ordination.

“Co-ordination means integrating or linking together different parts of an organisation to accomplish a collective set of tasks.” (Van de Ven, Delbecq and Koenig, 1976:322)

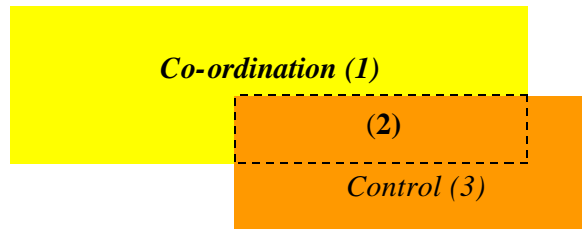
“Co-ordination is defined as the process of integrating activities that remain dispersed across subsidiaries. This process requires administrative tools - called mechanism of co-ordination.”(Martinez and Jarillo 1991)

The conceptualisation of co-ordination and control is just as fragmented as the meaning of these words. Some authors use these concepts interchangeably. Lately, scholars have pointed out the unbreakable links (interweaves) between the two. For instance, Lebas and Weigenstein (1986) argue that “management control is the process by which an organisation ensures that its sub-units act in a co-ordinated and co-operative fashion (...) in order to achieve organisation’s goals”. We will include the elements of this definition in our research.

The elements of power and authority are typical for control, whereas tuning activities and tasks characterise co-ordination (Schreuder et al, 1988 cited in Harzing, 1999:9). The final aim, however is the same, namely the direction of the processes and of people’s behaviour towards common organisational goals.

Following the definition of Cray (1984) we define management control as a set of mechanisms that *overtly limit* behavioural alternatives so that it is in *concordance with pre-set targets*. The “overt limitation of behavioural alternatives” includes the use of power. Power usage refers to the limitation of behavioural alternatives despite the resistance of the subject (Weber 1968). In this research, managerial control primarily stresses the power element in the relationship between headquarters and subsidiary. A “control”-relationship means a formal, hierarchical unbalanced relationship between headquarter and subsidiary, regulating activities according to the expectations of the headquarters.

Control can include devices to influence interpersonal behaviour: this we call co-ordination. On the other hand, not all co-ordination is control, since not all co-ordinated activities overtly limit behavioural alternatives. Otherwise stated: the power element in co-ordination seems to be more ‘implicit’ sometimes. In our view, co-ordination includes all mechanisms that influence behaviour in the direction of pre-set (explicit or implicit) goals. The relationship between the two concepts is visualised in Figure 2.



**Figure 3 Control and co-ordination**

- (1) Co-ordination, no control: persuasion, copying behaviour, planning etc.
- (2) Co-ordination and control: hierarchy, formalisation, flexibility etc.
- (3) Control, no co-ordination: prisoner’s situation

**Classification of the co-ordination mechanisms**

The co-ordination mechanisms can be classified on two dimensions:

- formalisation – to what extent are the rules, procedures and expected behaviour hierarchical and settled in a written form or based on instrumental artefacts
- explicitness - performed directly by the headquarters or indirectly e.g. through joint project groups or form.

For our classification we adopted the elements of the classification of (Harzing 1999), which regarded only control and elements of the typology introduced by Martinez and Jarillo(1989), that elaborated mostly on co-ordination.

	Formal	Informal
Explicit	<ul style="list-style-type: none"> <li>- Strategic autonomy</li> <li>- Standard procedures</li> <li>- Nationality of the CEO and the management team</li> </ul>	<ul style="list-style-type: none"> <li>- The extent of informal communication,</li> <li>- Direct relationship with HQ</li> </ul>
Implicit	Output control	<ul style="list-style-type: none"> <li>- multilateral relationships,</li> <li>- joint task groups</li> </ul>

**Table 1 Classification of co-ordination mechanisms adapted from Harzing (1999) and Martinez and Jarillo(1991)**

**Control and Co-ordination in the international context**

With increased international competition and deliverance of the markets the control based on hierarchy is less efficient than control based on flexibility. Pure structural and formal co-ordination mechanisms fail to respond to diverse strategic requirements of global strategy and local (national) responsiveness (Martinez and Jarillo 1989). New cross-departmental, informal and subtle mechanisms are added to – not substituted – existing structural and formal managerial devices to cope with complex environmental conditions. Successful organisations supplement traditional co-ordination mechanisms, such as international-specific departmentalisation (global matrix) centralised decision-making, highly formalised processes and systems, tight

controls and frequent reports with more subtle ones. To give an example: microstructural arrangements (lateral relations), that cross the formal lines of the macro structure - teams, task forces, committees, individual integrators and integrative departments, informal communication channels, informal relations among the managers without the distinction between HQ-managers and subsidiary managers (Martinez and Jarillo 1989).

**Co-ordination mechanisms and cultural distance**

Hofstede(1997) analysed the connotations of two dimensions: Power Distance and Uncertainty Avoidance of the Mintzberg organisations’ typology. *Power Distance*, as defined by Hofstede, is the extent to which the less powerful members of institutions and organisations within a country expect and accept that the power is distributed unequally (desirability for centralisation). *Uncertainty avoidance* is the extent to which the members of a culture feel threatened by uncertain or unknown situations. This is expressed in the need for written and unwritten rules (formalisation). Hofstede linked these two dimensions to Mintzberg’s organisation typology and suggested that people with a particular national background will prefer a particular organisational structure, other factors being equal. Lebas and Weigenstein(1986) went a step further and related two cultural dimensions to the co-ordination mechanisms.

Small power distance Weak uncertainty avoidance  Co-ordination mechanism: <b>markets</b> <i>The Netherlands</i>	Large power distance Weak uncertainty avoidance  Co-ordination mechanism: <b>culture</b> (family)
Small power distance Strong uncertainty avoidance  Co-ordination mechanism: rules (machine)	Large power distance Strong uncertainty avoidance  Co-ordination mechanism: <b>Rules</b> (pyramid) <i>Poland</i>

**Figure 4 Co-ordination mechanisms according to Henry Mintzberg projected on the Hofstede power distance-uncertainty avoidance matrix (Lebas and Weigenstein 1986; Hofstede 1997)**

The table indicates that a market model of organisation is characterised by mutual adjustment as co-ordination mechanism. It stresses ad hoc negotiation, and minimises inequality across the sub-units. In small power distance and high uncertainty avoidance countries stronger focus is put on rules, not hierarchy, in contrast to strong power distance and high uncertainty avoidance where the hierarchy is able to twist the rules. In such cultures, societies try to avoid uncertain situations and trust in absolute truth. The normative control system interfered by the hierarchy will probably be the most efficient to apply, whereas in the large power distance and weak uncertainty

avoidance cultures, family co-ordination mechanisms with direct supervision will be favoured.

Hofstede (1997) posited that it is easier for the headquarters, to organise and manage subsidiary situated in the same or neighbouring quadrant of the countries (see Figure 4). The differences in power distance seem to be more manageable than differences in uncertainty avoidance. Local managers can adopt more authoritative management practices when the subsidiary is established in a country with larger power distance than the headquarters, regardless of the participative attitude of their international bosses. The situation is more complicated if two companies are located in opposite quadrants. That is the case in the situation, in which the headquarters is Dutch and the subsidiary is Polish (see Table 4).

	Power distance	Uncertainty Avoidance
The Netherlands	38	53
Poland	68	93

Table 2 Score of the Netherlands and Poland on national cultures profiles. (Source Hofstede 2001)

Therefore our research question is - *To what extent are both kinds of mechanisms mentioned above recognised when headquarter and subsidiary are located in culturally distant countries?*

If the Dutch way (market) of co-ordinating is applied then there will be a high interaction between subsidiary and headquarters and a high level of informal communication (explicit and implicit). The subsidiary is autonomous and is authorised to make strategic decisions.

### **Research Design**

In order to answer the research question a large survey among polish subsidiaries is scheduled at the end of this year. However, we performed a pilot study in August 2002 that provided us with some preliminary insights. We interviewed CEO's (Chief Executive Officer or management team member) of 35 Dutch subsidiaries from different industries in three large cities in Poland: Warsaw, Poznan and Wroclaw.

Most of the subsidiaries were rather small, up to 20 employees and were founded in the 90 ties after the beginning of the transformation process. Almost half of them operate in the food sector and sell their products to retailers and wholesalers.

### *Variables*

We operationalized set of variables that tried to capture the use of the co-ordination mechanisms analysed above:



Formal - explicit: Personal supervision on: turnover reports, sales volume, an expansion to new markets.

- Implicit: Output control: the frequency of contacts with headquarter on production capacity and sales volume

Informal – explicit: - informal communication, relationship with managers of headquarters (R&D, production, sales and marketing)

- implicit: - participation in project and task groups

### *Analysis and Results*

The companies in the sample were not selected randomly. The selection was dictated by financial and time limit considerations. That's why we limited our analysis to descriptive statistics.

### **Co-ordination mechanisms**

Investigating the co-ordination mechanism in the sample, we found mixed results.

#### *Formal explicit and implicit control*

In 62% of the cases [N=35], the nationality of the CEO (Chief Executive Officer) was Polish, also the nationality of management team members was in majority Polish irrespective of the nationality of the CEO. Low use of expatriates suggests large freedom granted to subsidiary. On the other hand, we found that the majority of subsidiaries in the sample operated according to standardised rules and procedures imposed upon them by the headquarters, for number of the subsidiaries there was a possibility of an adjustment. The first result is typical for small power distance and weak uncertainty avoidance countries, in our case the Netherlands. Whereas the second is typical for strong uncertainty avoidance and large power distance countries, in our case Poland. It seems that in this group of companies, headquarters is willing to co-operate with local managers but according to its own rules and policies. The output of the subsidiary is being strongly co-ordinated by the headquarters. Almost 90% of the subsidiaries stated that they are fully or to a large extent controlled by the headquarters concerning turnover reporting. In the sample we found high levels of supervision in issues concerning the sales volume, the entrance to new markets, production capacity and product development, mostly on daily or weekly contacts. However, the headquarters granted a large freedom to the subsidiaries in the employment of new staff - 72% of managers stated that their company is little or not at all, controlled by the headquarters.

### *Informal control explicit*

According to the level of informal communication, the sample can be divided in two approximately equal groups: one with many daily informal contacts concerning many operational issues and the second with hardly any informal communication. The interviewed managers recognised the interrelationships between subsidiaries and headquarters and shared the same approach to planning (60% of the sample). We asked about the quality of contacts between departments of headquarters and a subsidiary. A significantly large percentage of subsidiary managers (18%) stated that they do not have to maintain any contacts with the HQ departments R&D, production and marketing. Generally the inter-departmental relationships were evaluated as satisfactorily (34% cases). A third of the subsidiaries (30%) developed and sustained very good contacts with HQ-departments. When we compared the answers on the quality of relationships between these three departments, we noticed that relationships with marketing departments scored higher than the other two. Especially the group of subsidiaries that did not develop an own marketing plan highly valued the relationships with HQ-marketing department.

### *Informal control implicit*

As to informal implicit co-ordination, we mentioned the importance of the organisation and participation in project and task groups at the super cross-organisational level, in which managers from different subsidiaries and headquarters participate. The majority (54%) of subsidiary executives makes part of permanent and temporary project groups and task forces, cross-departmental committees. The other 31 % stated they would appreciate such co-operation but there was no initiative from the headquarters.

The overview of the results is presented in the table:

Type of co-ordination mechanism	Level
Formal - explicit	
1. Strategic autonomy	Low
2. Standard procedures	High
3. Nationality of the CEO	Low
4. Nationality of the management team	Low
5. Personal supervision: – turnover	High
- product development	High
- new markets expansion	High
- sales volume	High
- labour employment	Low
Formal –Implicit	
Output control – production capacity	High
- sales volume	High

Informal Explicit	
1. Level of informal communication	High
2. The quality of relationship with HQ-departments:	
- R&D	Satisfactory
- Production	Satisfactory
- Marketing	Very good
Informal Implicit	
1. Participation of subsidiary managers in project groups and task forces organised together or by HQ	High
2. Recognition for HQ-subsidiary interrelationships	High

Table 3 the overview of the results

### Conclusion and discussion

We used the pilot study to draw some preliminary conclusions, concerning this sample. The first one is that we found that subsidiaries perform different roles, this is visible in the configuration of their value-added chain activities. The subsidiaries that perform more activities of the value-added chain operate more independently from the headquarters. We did not find significant differences in the portfolio of co-ordination mechanisms between subsidiaries performing different roles. We suppose that this was due to the small and non-representative sample. In the second part of our study we investigated to what extent four kinds of control mechanisms (Table 1) are used when the headquarters and subsidiary are located in the culturally distant countries. We found that the Dutch headquarter applied combined elements of market and pyramid co-ordination mechanisms (Table 4).

In our sample, the Dutch headquarters granted a large autonomy to the subsidiaries with respect to human resource issues: the Polish nationality of CEO, the composition of the management team and independence in employment policy. Simultaneously, the headquarters imposes own standardised rules and procedures on the subsidiary and makes – elements of co-ordination mechanism characteristic for large power distance and strong uncertainty avoidance countries - Poland. Many informal contacts between headquarter and a subsidiary, take place on daily operational basis. The employees of subsidiaries in our sample participate in projects groups, task forces and joint meetings with employees from headquarters and other subsidiaries. This feature is typical for weak uncertainty avoidance and small power distance countries.

Unfortunately we are not able to make a statement about the whole population of subsidiaries in Poland. We can notice however, that our conclusion is in line with the suggestion of Hofstede (1997) who underlined that following one principle in the management of international organisations (single co-ordination mechanism) in intercultural encounters will threaten the success of an enterprise.

This study will be further developed and performed in future with the use of a representative sample of subsidiaries in Poland. We will also include performance measures in our model in order to investigate the relationship between co-ordination mechanism, national culture, and performance of the subsidiary.

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