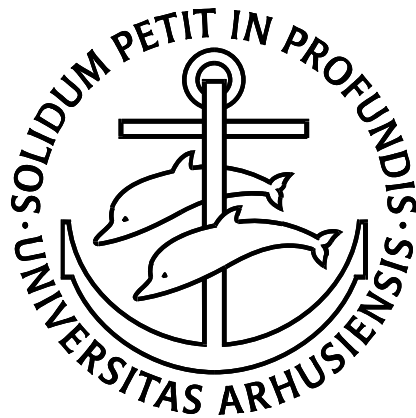# SCHOOL OF ECONOMICS AND MANAGEMENT

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Coping with Remote Control:
Scandinavian Subsidiaries in Germany and East Asia 1995-2005

Jørn Flohr Nielsen, Lars Bonderup Bjørn and Mikael Søndergaard

UNIVERSITY OF AARHUS

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Jørn Flohr Nielsen
Lars Bonderup Bjørn
Mikael Søndergaard

University of Aarhus
School of Economics and Management
Department of Management
DK-8000 Aarhus C, Denmark
e-mail: jflohr@econ.au.dk / msoendergaard@econ.au.dk

Abstract

The considerable cultural distance between Scandinavia and East Asia may be reflected in headquarters-subsidiaries relations. This paper provides a comparative analysis of this issue from a subsidiary perspective, focusing on control and coordination mechanisms of a matched sample of Danish subsidiaries in Japan and Germany including qualitative perception of problems. In order to trace general effects, this study includes other Scandinavian subsidiaries in East Asia, in total 140 subsidiaries in 1995 and 41 subsidiaries in 2005. Cultural distance is found to be associated with a configuration of control involving extensive use of informal transfers and a configuration involving formal control and supervision. These results are stable over time although there is a trend towards more use of formal and computer supported control. The subsidiary CEO is a key to understanding how uncertainties are handled in the interface, and our results indicate a perceived need to adjust control to host country conditions.

Key words: Cultural distance, East Asia, Headquarters-Subsidiary Control, Multi-country Study, Scandinavia.

1. Introduction

The relationship between headquarter and subsidiary is a classical research theme within the field of international management. It is also a challenging theme as the globalization of business environments may have altered the conditions since the classical review article by Martinez and Jarillo (1989). Simple headquarter perspectives seem insufficient.

Thus, the objective of this article is two-fold. First, factors that influence control of subsidiary of multinational companies (MNCs) will be analyzed, in particular the impact of cultural distance, and the change over time in the remote control, based on original data of matched samples of Danish subsidiaries in two equal sized economies. Second, it is analyzed how control problems are perceived by expatriate and non-expatriate CEOs of Scandinavian subsidiaries, in order to get a deeper understanding of headquarter-subsidiary relationships.

Traditionally, control and coordination mechanisms have been divided into formal/informal and personal/impersonal types of contact (Martinez and Jarillo, 1989; Harzing and Sorge, 2003). To supplement the findings made by Harzing and Sorge (2003), we argue, however, that such an analysis has to take into account that *actual* control is a combination of different mechanisms. Control strategies emphasizing monitoring and information processing and control strategies emphasizing the members' internalization of organizational goals are interrelated (Eisenhardt, 1985). Revealing combinations and configurations of foreign subsidiary control mechanisms is still an empirical issue.

Control of foreign subsidiaries is complex. It is a process used to ensure that all units of the organization strive towards common organizational goals and not just a process restricted to exercise of power. The concept of control should be connected to the linking and enabling process of coordination (Van de Ven et al., 1976; Cray, 1984). In the handling of the headquarter-subsidiary relationship, this involves outcome control, behavioral control, and cultural control (through corporate values and expatriation).

Furthermore, the globalization of business activities has led to an interest in the way the control of foreign subsidiaries functions under different types of strategy and corresponding organizational structures as suggested by Bartlett and Ghoshal (1989), i.e., multinational/multidomestic, international, global and transnational structures affecting the overall nature of the relationship to the foreign subsidiaries of the MNCs.

The network structure is argued to have an increasing importance in the transnational borderless type of organization in the global world. The role of the headquarters has changed in this organizational context (Bartlett and Ghoshal, 1989). The center of such an organization is not necessarily the headquarters. In general, large international firms have to function within a delicate balance between global integration and local responsiveness giving more attention to subsidiaries as autonomous units. The control mechanisms of subsidiaries may no longer be sufficiently understood by referring to formal control and the organizational hierarchy. Non-hierarchal as well as informal and more subtle mechanisms of control have to be

better understood. Leading researchers, including several Nordic researchers, have emphasized the importance of normative control through shared norms and outlook, internal promotion and internal transfers (Edström and Galbraith, 1977; Hedlund, 1986, 1994).

The Scandinavian cultural profile as described by Hofstede (1980, 2001) seems to support such mechanisms of control; low hierarchical inequality, low to medium high uncertainty avoidance, high individualism and high femininity seem at least not to be contradictory to the application of such mechanisms. Replications of Hofstede's IBM study indicate that the Scandinavian profile is rather robust and stable (Hoppe, 1990; Merritt, 2000; Søndergaard, 2002). In addition to cultural factors, institutional factors seem to cluster the subsidiary management from companies with the country of origin in the Nordic countries (Benito et al., 2003).

Based on these assumptions, we explore questions relating to the Danish MNCs' adjustment of control mechanisms to the country-of-location of the subsidiary; how do control mechanisms of subsidiaries in East Asia and Germany differ; and how are control problems perceived at the cultural-cultural interface of the foreign subsidiary?

We will integrate paradigms deriving from market, culture, and organizational control in the analysis of the – less masculine? – "Viking" way of applying control mechanisms in respect to foreign subsidiaries. Drawing on data from Scandinavian subsidiaries in Germany and East Asia, we examine headquarter-subsidiary relations not on the basis of information derived from the CEOs of the subsidiary. Data from 140 subsidiaries in 1995 are supplemented with data from 41 subsidiaries in 2005.

Our purpose is also to make up for the bias that big countries' multinational corporations (MNCs) have dominated contributions to the field (Nohria and Ghoshal, 1997).

2. Research in cultural distance and control in the global era of multinational corporations

Control mechanisms of foreign subsidiaries have been associated with a number of strategic and contextual factors influencing the control strategy of multinational corporations (Gomez and Sanchez, 2003). At a specific level, it is also documented that the choice of control options depends on task programmability, information systems and uncertainty (Eisenhardt, 1985).

The issue of strategic considerations has been of particular interest to researchers who have looked into factors that make MNCs adopt specific control mechanisms, e.g. Birkinshaw and Morrison (1995), Gupta and Govindarajan (1991), Martinez and Jarillo (1989 and 1991). Within the four strategy types suggested by Bartlett and Ghoshal, (1989) the major point of the theory of the multinational corporation of the global era is that the control mechanisms of foreign subsidiaries require a different balance between local adjustment and global integration as well as worldwide learning to fit the particular overall strategy type of the multinational corporation.

The business forces of local adjustment and global integration of the subsidiary seem central to the argument of the transnational company. The argument of fit between the control mechanism mix of centralization, formalization and normative integration and organizational performance was supported by the study by Nohria and Ghoshal (1997). The specific environmental demands for the subsidiary of particular importance. Findings from a study by Ghoshal and Nohria (1993) indicate the importance of a fit between these environmental demands and choice contral mechanism applied in the headquarter subsidiary relations. Ghoshal and Nohria's results indicate that firms with such a fit outperform firms with a misfit. (1993)

Our approach on control draws on traditional agency theory, organizational theory, and information processing views (Eisenhardt, 1985; Galbraith, 1973). Basically, control of subsidiaries is seen as a solution to an agency problem. Out of the necessary delegation to a foreign subsidiary grows the potential risk that the subsidiary will pursue goals that are incongruent with the goals of the parent company. In relation to these views, cultural distance between headquarters and subsidiary reinforces the agency problems and is generally suggested to influence the choice of control mechanisms including expatriate staffing (Hamilton and Kasklak, 1999; Gong, 2003; Gomez and Sanchez, 2003).

This may be seen as a corollary of the general theory of coordination because cultural distance fosters uncertainty, and a combination of task interdependence and task uncertainty raises coordination costs (Thompson, 1967). As task uncertainty increases, studies have especially shown increases in the use of horizontal channels and both scheduled and unscheduled meetings (Van de Ven et al., 1976).

In agency theory, the concept of uncertainty is given an even more explicit emphasis as outcome of organizational activities is considered to be a function of both employees' behavior and random effects. Thus, in the distinction between output control and behavioral control, output control implies that the controlled unit bears some of the risk (Eisenhardt, 1985). Within organizations, the use of these different control modes depends on national cultures (Ouchi, 1979; Hedlund, 1986).

Inside multinational corporations, it is expected that as cultural distance increases it becomes more difficult to use both outcome control and behavioral control in headquarter-subsidiary relationships. Cultural distance increases the agency problem (Roth & O'Donnell, 1996). As consequence the multinational corporations may rely more on cultural control, for instance through the expatriation of parent country nationals who have internalized the parent firm's values (Gong, 2003). The recent study by Gong (2003) focusing on subsidiary staffing seems to support this view although the effect of expatriation seems to weaken over time. The potential weakening over time is also an important research question in our approach as learning and new information technology may change the control pattern.

The impact of cultural distance seems straightforward. Differences in language, laws and regulations, business practices and supplying attitudes are some of the manifest areas of conditions for business relationships with suppliers located internationally. This perceived difference between home country and the sourcing markets is associated with the choice of entry mode (Kogut and Singh, 1988), the degree of

control over foreign operations (Erramili and Rao, 1993), and problems in buyer-seller relationships (Hallén and Wiedersheim-Paul, 1979).

Communication problems in the hierarchical relations between superior and subordinas and problems of uncertainty should be expected. One should be careful considering the cultural distance and problems as a linear relationship. (O'Grady and Lande, 1996) Precisely because of the distance, efforts such as cultural training, language courses, and use of cultural intermediates may have been put into place to overcome the perceived distance. Furthermore, it is necessary to specify how the communication situation between two or more actors with different cultural backgrounds becomes important. In general the literature on cultural distance has been criticized for lacking rigorous conceptualization and measurement (Shenkar, 2001).

Nevertheless, Kogut and Singh (1988) took a step forward in specifying a cultural distance index based on the deviation along each of Hofstede's four dimensions (i.e. power distance, uncertainty avoidance, masculinity/femininity, and individualism). This construct giving equal weight to Hofstede's four dimensions may also have shortcomings in capturing the complexity of cross-national differences (Shenkar, 2001, Xu and Shenkar, 2002). The Kogut and Singh measure includes the sum of differences between the home country national culture and the national culture of the marked under consideration. In our perspective, the construct may be appropriate because the difference between Scandinavia and Japan especially appears in the construct's uncertainty and masculinity dimensions. These dimensions are very important in control issues and the dimensions interact in particular when related to

issues of control. This interaction is captured by the measure that integrates all four dimensions.

Choice of communication form is conceptually related to the perceived need to reduce uncertainty of the unknown future course of the subsidiary and thus is mainly associated with one of the dimensions found by Hofstede, i.e., uncertainty avoidance, defined by Hofstede (1991, p. 113) as the extent to which members of a culture feel threatened by unknown situational elements.

Uncertainty is not only the fundamental problem with which the top management of the organization must cope (Thompson, 1967). It is both an objective property of the environment and a perceptual phenomenon specific to each individual or culture (Milliken, 1987).

If people are programmed to view rules differently in different countries, difficulties are likely to occur when keeping international ventures together. Keeping such ventures together demands flexibility in the use of coordination tools as well as some degree of control. Partners programmed in weak uncertainty cultures, such as the Nordic countries, feel uncomfortable with rigid rules, especially if the rules are never followed. Partners socialized in strong uncertainty cultures feel uncomfortable without a structure of rules, even if the rules are impractical (Hofstede, 1991). Since Japan and Korea have high scores on uncertainty avoidance, one may expect a similar inclination towards rules in these countries, although specific direction may be preferred to abstract universal rules.

Research findings suggest that uncertainty avoidance is likely to affect the cross-border industrial networks as far as control and trust are concerned (Hofstede, 1991; Laurent, 1983; Schneider and de Meyer, 1991).

To further develop our understanding of the subsidiary contextual factors, we thus find it rewarding to include the distance concept at different scales of analysis into our examination of the control mechanisms of foreign subsidiaries in distant markets compared with a closer market. This leads us to formulate two major research questions:

1.   How does cultural distance affect the use of control mechanisms?
2.   How are control problems in foreign subsidiaries perceived?

The use of research questions indicates the explorative nature of the research. However, we intend to use rather structured comparative analyses and for example test the statistical significance of differences between Japanese and German subsidiaries. All in all, the analysis is guided by the model in Figure 1.

The model reflects the intention to explain the impact of cultural distance when controlling for other influential variables. Several dimensions of distance – cultural, administrative, geographic, and economic – may influence the profitability of foreign activities (Ghemawat, 2001). Thus, the operations and performance of foreign subsidiaries depend on *geographical distance*. Absence of proximity makes it difficult for headquarters to supervise directly and other means of coordination and control will be considered (O'Donnell, 2000). *Changing environment* in the economic,

political and industrial context of the foreign subsidiary is also expected to influence

operations and outcomes since it increases uncertainty (Boddewyn and Brewer,

1994; O'Donnell, 2000). Control may depend on *performance*. Performance of the

subsidiary cannot be assumed to be a simple positive result of control. Low

performance in general often makes managers react with tighter formal control, which

in turn may be dysfunctional (Simon and March, 1958). *Size* is at several levels

expected to lead to formalization, but size as well as *market strength* may also lead

to autonomy of divisions (Blau, 1968; Greiner, 1972; Van de Ven et al., 1976).

< Insert "Figure 1" >

3. Methods

The early part of our study is mainly based on data gathered in a mail questionnaire

in 1995 and is part of a rather comprehensive study of coordination problems in

Danish subsidiaries in East Asia and Europe. The study includes qualitative

interviewing, and the core survey of Danish subsidiaries in Japan and Germany are

in 1996 extended to include Danish subsidiaries in China, Hong Kong, South Korea,

as well as Swedish and Norwegian subsidiaries in Japan. The survey is replicated in

2005 with a questionnaire to subsidiaries in all the countries.

The formulation of the questionnaire is based on results from a qualitative study of 14

Danish subsidiaries in Japan. This preliminary study reveals a broad range of

coordination and control problems in the headquarter-subsidiary relationship, and a

discussion of these problems has been made available for managers in a formerly

published book. Thus, the questionnaires are sent to the CEO of each of the 66 Danish subsidiaries in Japan and to each of the 66 Danish subsidiaries in Germany with a sister company in Japan. Respondents are mainly asked to state to what degree they agreed with statements on problems on a Likert scale. Response rate: 58 and 56 %, respectively.

In the next part of the study, these results are interpreted interactively in recent interviews with 20 CEOs and other managers in the Japanese subsidiaries and in the Danish headquarters.

The questionnaire is addressed to the chief executive officer of each subsidiary, and Table 1 illustrates the response rates from the samples. The response rates seem considerably higher than in other surveys of foreign subsidiaries, which according to information provided by Gomez and Sanchez (2003) achieved a response rate of around 20%.

In the first part of the study – of the Japanese and the German subsidiaries – it was possible to analyze the response rates in more detail. In spite of the small difference between Danes and Japanese/Germans, all groups of respondents have a high response rate. Even the response rate of the follow-up study has a satisfactory response rate. This indicates that non-response bias is no major problem in itself.

< Insert Table 1 >

A major related issue in this type of questionnaire is the issue of a culture-based response bias. Assuming, for example, that the Japanese respondents tend to answer the questions more cautiously than the other nationalities, problems that are

de facto significantly more important in Japan than in Germany may not show. However, this bias is somewhat counterweighed by the fact that there are Danish respondents in both samples. It appears, surprisingly, that the Danish respondents provided more cautious answers than their Japanese and German colleagues, in particular when it comes to making statements about the German and Japanese employees and managers.

Measures: Coping with Validity and Language Problems

The research design shares features with methodological triangulation (Denzin, 1978) in the sense that concepts and hypotheses are partly grounded by unstructured qualitative methods to be followed by more structured analyses and even hypotheses testing. The interviews in the early stage were only structured to some degree. Consequently, it is possible to give the respondents' perception proper consideration in the survey. The relevance of the questions is certified by the fact that the questions have been phrased by CEOs and other leading managers in Danish subsidiaries. Furthermore, five professionals were asked to read the questionnaire thoroughly and take notice of any questions that could be interpreted in several ways. The questions should be formulated in an easy to read, unbiased language and should not be too long. This procedure involved a few changes to one of the scales and three of the questions.

To avoid some of the interpretation problems stressed in the literature on cross-cultural comparative methods (Hui and Triandis, 1985), the questionnaires were formulated in English and Danish and then translated into each of the Asian

languages. The translators, who were all native speakers of the questionnaire language, asked questions concerning the exact meaning of words, forcing the researcher to state more precisely what was meant. Nevertheless, one Japanese respondent and one German respondent complained about the translation of a few questions. A retranslation of the questionnaire after the first survey led to the elimination of three questions.

4. Findings

Mapping Differences in Control Mechanisms

Table 2 indicates how the use of headquarter-subsidiary control seems to be adjusted to a distant host country. It shows the frequency of different forms of contact between Danish parent companies and their subsidiaries in Japan and Germany, respectively. Since the comparison is based on a matched sample in the sense that data are collected among Danish companies with subsidiaries in both Japan and Germany, this is a controlled analysis of the importance of distance. Then even significance at the 10 percent level should be noticed.

First of all, the results show that Danish multinationals to a larger extent use direct personal control mechanisms and indirect personal control/coordination devices towards Japanese subsidiaries than towards German subsidiaries. The use of international management training is significantly more extensive in the Japanese

subsidiaries at the 5 percent level. The use of detail planning is on average also more extensive, but this difference is insignificant and only based on a one-item construct.

All in all, the use of indirect (input) controls (socialization, management training) is significantly higher for subsidiaries in the culturally distant market compared to subsidiaries located in the culturally closer market. Thus, the results are in line with the expectations of Hamilton and Kasklak (1999) and Gomez and Sanchez (2003) and support our hypotheses.

The pattern holds to some extent over time, although there is a small decrease in expatriation and a significant increase in direct formal control and especially in the use of integrated computer systems in both German and Japanese subsidiaries.

< Insert Table 2 >

So far, the analysis is based on the simple four categories of control including single item (socialization and detail planning) and low reliability constructs (formalization and output evaluation). In the next step, we use explorative factor analysis of all control items in order to trace reliable dimensions in actual control and include other Scandinavian subsidiaries placed in the East Asian region. From this analysis, four interpretable dimensions emerge (see Appendix 3): (1) *Informal transfers/expatriation*: This factor covers both managerial expatriation and visits by technical staff and mixed teams. Thus it takes into account that expatriation is not restricted to the managerial level as stressed by Gong (2003); (2) *Formal control and supervision*: This factor connects control by rules with managerial visits and frequent

contacts; (3) *Cross-cultural training*: This factor connects training with control through organizational culture; (4) *Employee contacts*: This factor covers contacts below the managerial level.

In order to explore how these modes of control are affected by cultural distance, we use multiple regression analysis. Items with factor loadings above 0.50 are then used and given equal weight when computing each dependent variable. In the multiple regression analysis the main independent variable is cultural distance, but the analysis includes other contextual and organizational variables to control for these potential influential variables (Table 3).

< Insert Table 3 >

By taking the independent variables one by one, the model explains an acceptable part of the variance of the variable *informal transfers/expatriation* (Factor 1), and cultural distance is significantly related. In this sense the support for H2 can be generalized. This result is partly in line with Gong's (2003) recent study. With cultural distance, managerial visits and expatriation increase. The estimated model also indicates that geographical distance is negatively associated with this factor whereas size and competitiveness have a positive impact. *Cross-cultural training,* including development of organizational culture, is insignificantly correlated with cultural distance. In this sense, there is only weak support for Hedlund's (1986) early research on the importance of development of shared norms and cross-national understanding through training in order to control employees in subsidiaries far away.

It is also important to note that there is no support for the general hypothesis H1 since cultural distance seems to have no significant impact on other modes of control. Neither the variance of *formal control and supervision* nor the variance of *employee contacts* can be explained by our model to an acceptable extent. However, factors related to the specific firm or subsidiary, such as market competitiveness, seem to be correlated to the use of formal control and supervision.

Simple correlation analysis shows that formal coordination is only weakly negatively associated with environmental instability. Surprisingly, there is even a positive correlation between frequent use of rules (single item) and quick changes in the environment.

The explanation may relate to the complementary nature of formal and informal control. For example, it may be easy to get ad hoc permission to break the rules. Thus, we find a strong positive correlation between reports on quick changes in the environment and contact by phone between headquarters and the subsidiary management. In this way, flexibility is instituted in the headquarter-subsidiary hierarchy.

Furthermore, formalization – like bureaucracy – may be of an enabling type instead of the normally assumed coercive type. Under some circumstances, formalization provides needed guidance and clarifies responsibilities, thereby helping individuals to be and feel more effective (Adler and Borys, 1996). Especially in Japan and where asymmetric power relationships are avoided, bureaucratization may have this impact. Anyway, CEOs reporting headquarters to treat their subsidiary with special

consideration also report high scores on the use of direct supervision, formalization, and detailed plans. The increased use of formal control from 1995 to 2005 may indicate that more knowledge and better computer systems make behavioral and outcome control an easier response to control problems.

As expected, however, cultural distance is mainly associated with the use of some of the informal control mechanisms, notably expatriate managers, but also initiatives on socialization and training. These results seem to reflect an expected reaction to the way CEOs perceive problems at a more operational level because CEOs in subsidiaries in East Asia often perceive problems such as differences in norms and misunderstandings. In other words, we need to expand the analysis by including the specific perceptions of distance (Hallén and Wiedersheim-Paul, 1979) which are held by subsidiary CEOs in order to provide a better understanding of actual adjustment to the country of location.

Perceived Problems of Control and Coordination

Thus, our analysis turns its focus from the predefined cultural distance to perceived problems generated in the interviews. The related survey responses are shown in Table 4.

< Insert Table 4 >

The perceptions reflect that management has to deal with other problems in Japan than in Germany. Subsidiary managers who are caught in the interface between Asian and Scandinavian culture may feel personally how the control problems occur. However, perceptions may also depend on the respondents' personality. The lack of

uniformity in perceptions of Danish expatriates is in itself an indication of the difficulties in achieving normative control through expatriation.

The expatriate managers are themselves part of the chosen forms of control (Gong, 2003), and expatriate respondents report another pattern of problems than other respondents. Local managers have comparable managerial responsibilities, but the expatriate (mostly Danish) managers evaluate recruitment and skill problems as more important and evaluate themselves more positively than the Japanese and German managers. Generally, these respondents perceive more problems in issues related to the foreign culture. Such conflicting views could be expected, but the pitfall may be that conflicts at the cultural interface in subsidiaries remain unproductive and hinder awareness of problems which could actually be handled.

When expatriate managers report more problems at the cultural interface it may reflect that the headquarters had found significant problems with the subsidiary and tried to gain control over the situation by locating a high-status manager from the headquarters as the managing director of the subsidiary. This is suggested in some of the interviews. Then expatriation is a reaction to antecedent problems, but the problems may still exist.

Expatriate managers often have difficulties crossing the cultural interface where the handling of uncertainty and conflicts may be crucial. To Scandinavians in East Asia this is related to language problems and they may use both informal and formal tactics to increase the intercultural communication as Peltokorpi (2007) has shown recently. As regards the expatriates' involvement in the local society, the survey

provides a somewhat surprising result. At first, it appears logical that the expatriates in Germany would be more willing to involve themselves in the local society. In other parts of the study, however, we have seen that it was easy for the Danes and the Japanese to get along while the Germans and the Danes often found it more difficult. Yet, it has been pointed out that the lack of a common language between the Danes and the Japanese makes it easy for them to get along. Without a common language, deep and thorough points of view and social patterns are not revealed. Therefore, the Danes do not get into conflicts with the Japanese, nor do they involve themselves in Japanese society. In comparison, the Danish expatriates in Germany involve themselves in the German society and consequently run the risk of a conflict.

This point implies a note of caution. The reporting of coordination problems and conflict is often an indication of coordination efforts. No reported problems indicate that the latent conflicts are handled by withdrawal, which sometimes might be dysfunctional. Thus practical interventions may involve both the promotion of conflicts as well as the reduction of conflicts in cultural interfaces (Brown, 1983). The data presented above indicate that expatriates may – but do not necessarily – play a role in getting closer to the problems instead of just stating "insufficiently skilled staff".

The number of respondents in the last survey is small for this detailed analysis, but they do not indicate notable changes in the way problems are perceived.

5. Discussion and practical implications

Although this is an exploratory study using subsidiary data, it is also based on a rather structured comparative analysis of subsidiaries in five countries. Thus it is with

some rigor that we find that adjustments of the forms of control mechanisms were made in relation to Danish subsidiaries in Japan, China and South Korea; the possible country-of-location effects were reflected in other Scandinavian subsidiaries in Japan.

We have in several respects followed Shenkar's (2001) recommendations on cautiousness in applying the distance concept. First, we control for other possible influential factors in tracing the effect of cultural distance. Second, although we use the aggregate Kogut-Singh (1988) index, our analysis is more focused on single dimensions of cultural distance. Thus, masculinity/femininity and uncertainty avoidance emerge as important dispersed components in our sample. This is easily related to general theories of control and coordination, including agency theory in which coping with uncertainty is a central task. Third, we take a closer look at the cognitive measures of cultural distance by asking managers how they perceive difficulties of adjusting control in different countries. Fourth, we generally focus on the interaction between entities and the interface between cultures rather than abstract distance. Fifth, we take time into account by a follow-up study.

Our results support the need for differentiated coordination and control systems across subsidiaries according to the environment of the subsidiary, as also advocated by other scholars, e.g. Leksell (1981), Ghoshal and Nohria (1993), Nohria and Ghoshal (1997). While Nohria and Ghoshal's (1997) argument is based on a traditional contingency approach stressing environmental factors, such as uncertainty and complexity, we take cultural factors specifically into account. One of the implications to practitioners in parent organizations may be to give a local manager latitude to use centralized and behavioral control despite the potential conflict with

norms of the home country. Thus, the survey seems to indicate that a general problem is that the Japanese employees lack the necessary education to work with the headquarters' planning systems. In the qualitative part of the study, it was demonstrated how the subsidiaries' strategies, goals, activity plans, long-term planning and budgets were unrelated to each other since the Japanese employees worked in non-systematic, non-planning patterns because of unfamiliarity with the Danish way of integrating the activities, which caused annoyance in the headquarters. In one case, the use of a Danish planning system in Japan was simply characterized as a failure. These results may also be interpreted as a need to take cultural distance into account by adapting planning and control systems to the local subsidiary.

However, our descriptive ranking of the problems perceived by the managers in the Danish subsidiaries in Japan and Germany indicates that problems related to market conditions, such as market competition and demands of customers, were ranked at a higher level of importance than cultural factors. At a lower level of importance, differences in social norms and language skills are found. The importance of the cultural distance is, however, indicated by the finding that the problems overall seem more important to the subsidiary managers in Japan than the subsidiary managers in Germany.

Our findings may be claimed to reveal mechanisms that are important to East Asian subsidiaries of most Western companies, though all the companies in our sample have a Danish headquarter. This argument would require that the sample of the Danish multinationals represents an exemplary case of Western country of origin.

However, there are significant differences even between European countries (Harzing and Sorge, 2003). Unfortunately, the Harzing-Sorge study does not trace specific explanatory factors in the national societies.

These reflections seem to indicate that multinational studies of heterogeneous samples are needed to enable us to balance effects of country of origin and country of location on the control mechanism in more rigorous analyses of explanatory factors. Ideal approaches may combine data from subsidiary and headquarters. This may further our understanding of interactive control and coordination as well as related problems.

Our analysis only takes a few steps towards solving the problems connected to the concept of cultural distance and its static views (Shenkar, 2001). Notably future research should take into account that the effect of time and cultural distance is interrelated, for instance in the sense that productivity gains in using expatriates in remote subsidiaries diminish as years of operation increase (Gong, 2003). Furthermore, our study only indicates subsidiary perceptions of control problems. The results in this part stress the dependence on the respondents' nationality, and problems of reliability remain to be established. Finally, qualitative and quantitative approaches should open up for analyzing the complex dependencies between perceptions of distance, control and performance. Especially the role of new information technology should be given more attention since our analysis shows an increasing importance of this factor. This seems to make traditional typologies of control less useful.

6. Conclusion

Cultural distance matters, still. As part of a research stream that has addressed formal and informal relations between headquarters and subsidiary, this study indicates how Scandinavian multinationals may adjust to an East Asian context.

Analyzing the control mechanisms of Scandinavian MNCs operating in Asia should provide special insight into the interface between the Asian cultures and the very different Scandinavian cultures, characterized by relatively low scores on masculinity and uncertainty avoidance. On this assumption, we examined matched samples of headquarter-subsidiary relations of Danish multinationals in Japan and in Germany. In addition, we examined Norwegian and Swedish multinationals in Japan as well as Danish multinationals in South Korea, Hong Kong and China.

The findings indicate that Japanese subsidiaries are more controlled and coordinated by informal mechanisms such as direct supervision, socialization and international management training than the German subsidiaries. When analyzing the entire sample, a factor of informal transfers appears to be significantly related to cultural distance in a multiple regression model controlling for other influential variables. Thus, our model explains a configuration of control including extensive visits by technical staff and mixed teams as well as managerial expatriation. This seems exactly what cultural distance in the Kogut-Singh (1988) sense explains of control. To some extent this result seems stable over time as indicated by our 2005-replication. However, the replication also indicates small changes at a specific level. As time

goes by there is a decrease in expatriation as well as a significant increase in direct formal control and especially in the use of integrated computer systems.

The concept of cultural distance was also measured by perceptions of subsidiary CEOs in respect to problems with the headquarters. Problems relating to cultural distance were indicated although problems relating to market environment seemed to be of higher importance. Thus, the perspective of subsidiaries as interfaces of different cultures proved useful in more specific analyses. Further improvements in the research of headquarter-subsidiary relations require a closer look at both sides and at the dynamics of the interface.

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Figure 1:

Framework – Model of Cultural Distance and Subsidiary Control
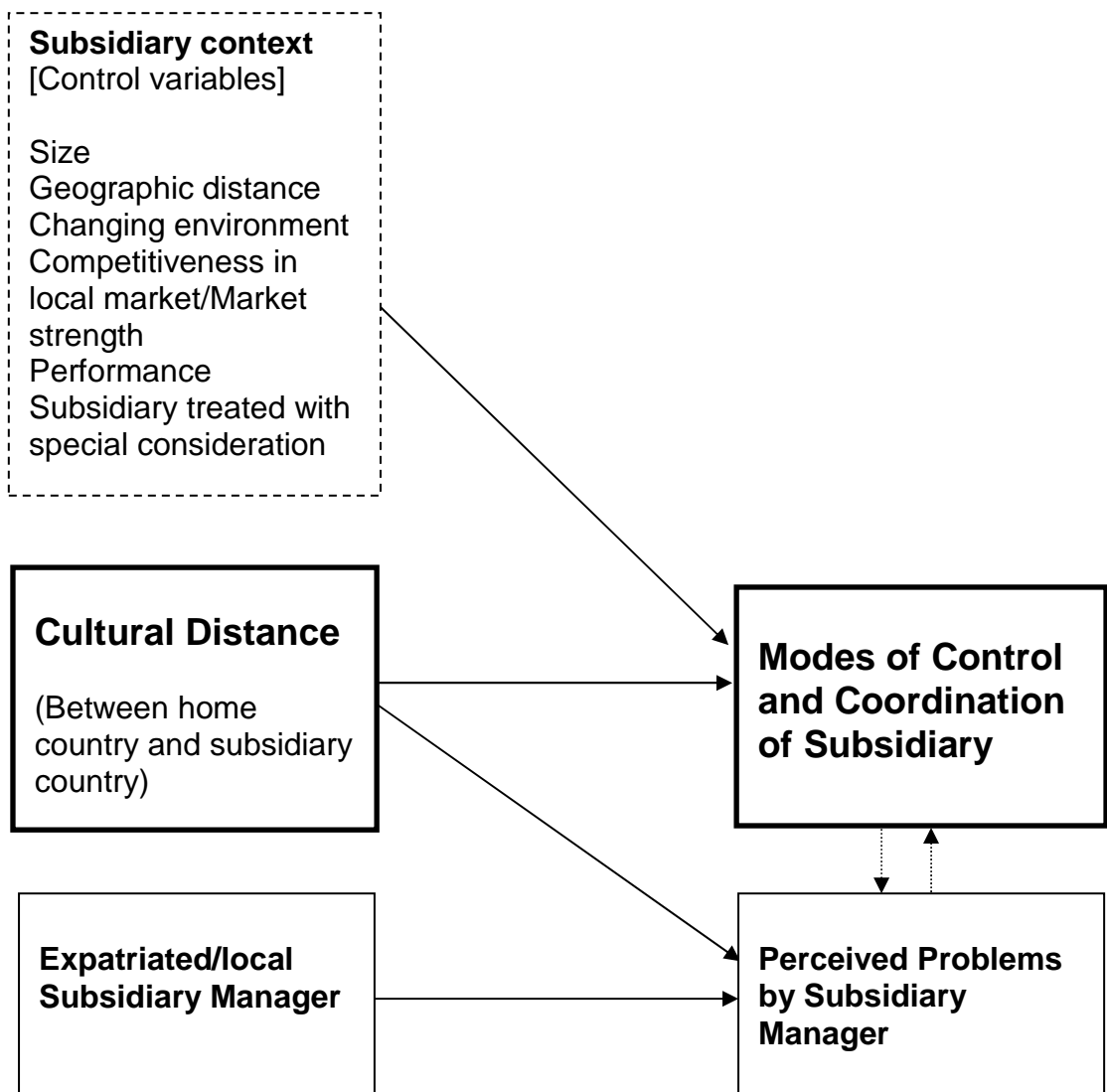
Table 1: Sample size and response rates

Population	Japan	Germany	Hong Kong	China	South Korea	Norway	Sweden
Total number of subsidiaries according to the MFA	66	660	66	56	18	----	----
Corrected sample (*)	50	50	62	55	17	----	----
Number of respondents	29	28	20	18	8	14	23
Response rate	58%	56%	32%	33%	47%	----	----
Follow-up 2005	14	9	8	7	3	----	----
(Response rate for corrected 2005 sample in brackets)	(37%)	(21%)	(25%)	(17%)	(21%)	---	---

(*) The sample was reduced because some of the companies listed in the official list were not subsidiaries or did not report directly to the headquarters. In one case, the headquarters requested us not to send questionnaires to the subsidiaries.

Table 2: Control of Danish Subsidiaries in Japan and in Germany

Mean Scores		Japan		Germany	
		1995 (N=29)	2005 (N=14)	1995 (N=28)	2005 (N=9)
Direct, personal					
Direct supervision (visits, meetings, written and phone contact)*		3.69	3.77	3.39	3.59
Expatriate control (degree of expatriate presence)		2.03	1.77	2.12	2.03
Direct, impersonal					
Formalization		3.93	4.14	3.77	4.50
Indirect, personal					
Socialization	*	2.92	3.38	2.27	2.78
Informal communication		3.76	4.10	3.79	4.00
International management training	**	2.74	2.71	2.13	2.17
Indirect, impersonal					
Output evaluation		2.87	2.58	2.67	2.56
Detail planning		3.73	3.75	3.15	3.75
Computer systems ("Integrated EDP ...")		3.22	4.08	3.00	4.67

Measures are defined in the appendix.

Scale: The scale ranges from (1) "Never", through (2) "Seldom", (3) "From time to time", (4) "Often", to (5) "Fixed part of the relationship".

*)   Difference between the 1995 samples significant at a 10% level (t-test of distributions).
**) Difference between the 1995 samples significant at a 5% level (t-test of distributions).

Table 3. Multiple Regression Results

(Based on Subsidiary Manager Responses, 119 used observations)

	Dependent variables (cf. Appendix)			
Variables	Informal transfers/ expatriation	Formal control and supervision	Cross-cultural training	Employee contacts
Cultural distance	0.525 ***)	0.347 *)	0.221	-0.013
Geographical distance	- 2.819 ***)	-1.622	0.279	-0.251
Number of employees in subsidiary	0.004 **)	0.001	0.003 **)	-0.000
Competitiveness in local market	0.525 **)	0.272	-0.285	-0.275
Performance (Sales per employee)	- 0.014	0.003	0.000	-0.007 *)
Subsidiary treated with special consideration	0.729 ***)	0.737 **)	0.013	0.144
"Ten-years-after"-dummy: 1995 (0); 2005 (1)	0.754	0.915	0.516	0.280
Model R^2	0.27	0.09	0.14	0.09
Adjusted R^2	0.25	0.04	0.08	0.03

Values are unstandardized parameter estimates
*) $p < 0.10$
**) $p < 0.05$
***) $p < 0.01$

Measures of independent variables defined in Appendix.

Table 4: Perceived problems in Danish Subsidiaries in Japan:

Share of respondents stating the suggested problem as large or one of the largest problems experienced.
Differences attributed to the nationality of the respondent.

Type of problem experienced:	Japanese sample		German sample	
	Danish (N=15)	Japanese (N=12)	Danish (N=8)	German (N=20)
Strong competition	60%	67%	63%	75%
Different quality standards are required by the Japanese/German customers	53%	42%	13%	40%
Recruiting of qualified staff	53%	33%	13%	20%
Higher, but identical quality standards are required by the Japanese/German customers	33%	42%	13%	20%
Bureaucracy in the headquarters	27%	17%	25%	30%
Differences between Danish and Japanese/German social norms	33%	42%	0%	10%
Lacking information from headquarters	13%	33%	13%	20%
Technical trade barriers	7%	25%	0%	10%
Managers and staff are not sufficiently skilled (either technically, managerially or language-wise)	27%	8%	0%	15%
Information is misinterpreted even though good will is present	20%	17%	0%	15%
The employees feel uncomfortable about unknown and unpredictable situations	27%	0%	13%	10%
Frequent or significant changes in the environment	7%	17%	13%	10%
Bureaucracy in the subsidiary	7%	0%	0%	15%
Lack of loyalty or commitment or 'cheating' characterize the behavior of employees and managers	7%	0%	0%	10%

Appendices

Appendix 1
Measures of control/coordination (predefined)

Direct, Personal Control

Direct supervision – Mean score of 4 items ($\alpha = 0.74$):
1. Short management visits from the headquarters to the subsidiary
2. Short management visits from the subsidiary to the headquarters
3. Short visits from technical staff at the headquarters to the subsidiary
4. Short visits from technical staff at the subsidiary to the headquarters

Expatriate control – Mean score of 4 items ($\alpha = 0.63$):
1. Expatriate managers from the headquarters to the subsidiary
2. Expatriate managers from the subsidiary to the headquarters
3. Expatriate technical staff from the headquarters to the subsidiary
4. Expatriate technical staff from the subsidiary to the headquarters

Direct, Impersonal Control

Formalization – Mean score of 2 items ($\alpha = 0.39$):
1. Contact in writing between the headquarters and the subsidiary management
2. Rules concerning how the subsidiary should solve its tasks1 2 3 4 5

Indirect, Personal Control

Socialization – 1 item:
1. Plans concerning the development of the organization's culture

Informal communication – Mean score of 3 items ($\alpha = 0.66$):
1. Contact by phone between employees below the management level
2. Contact in writing between employees below the management level
3. Teams consisting of members from both the headquarters and the subsidiary

International management training – Mean score of 3 items ($\alpha = 0.64$):
1. Education of Danish personnel in working with the Japanese
2. Education of Danish personnel in the Japanese language
3. Education of the Japanese personnel in Danish or English

Indirect, Impersonal Control

Output evaluation – Mean score of 2 items ($\alpha = 0.45$):
1. Plans without details, but with key numbers
2. Plans without any specification of numbers

Detail planning – 1 item:
1. Detail plans

The scale is a 5-point scale ranging from 'Never' (1), through 'Seldom' (2), 'From time to time' (3), 'Often' (4) to 'Fixed part of the relationship' (5).

Appendix 2
Measures of Independent Variables

Cultural distance

Cultural distance is calculated as a version of Kogut and Singh's (1988) cultural distance index in which the difference between home and host country cultures is measured by the use of Hofstede's (1980, 2001) country scores giving equal weight to all four dimensions but without correcting for differences in the variances of the dimensions.

Geographical distance

Geograhical distance is a dummy variable coded '0' for German subsidary and '1' for East Asian subsidiary.

Change in environment

'Frequent or significant changes in the environment'

Ranking Scale: 'No problem' (1), 'An insignificant problem' (2),
'A problem however not large' (3), 'A large problem' (4),
'One of the largest problems your company has' (5).

Size of subsidiary

Turnover in 1994 (approx.)

Market strength

'Please describe the position of the subsidiary in the Japanese market'
a) among the leading companies in the business (4)
b) solid position, without being a leading company (3)
c) a good position within a limited range of products, though generally a small company (2)
d) an overall insignificant position (1)

Appendix 3
Factor analysis of items indicating the content of the relationships between headquarter and subsidiary in 1995 (N = 119)

"Here, you are asked to indicate to what extent you use the stated tools in the relationship between the headquarters and the subsidiary. Please circle the (most) correct answer. "

1 = Never
2 = Seldom
3 = From time to time
4 = Often
5 = Fixed part of the relationship

Item	Loadings
Factor 1: Informal technical transfers and expatriation	
(face-to face interaction) staff relationships	
Short visits from technical staff at the subsidiary to the headquarters	.76
Expatriate technical staff from the subsidiary to the headquarters	.61
Short visits from technical staff at the headquarters to the subsidiary	.61
Teams consisting of members from both the headquarters and the subsidiary	.55
Expatriate managers from the headquarters to the subsidiary	.52
Expatriate technical staff from the headquarters to the subsidiary1	*.46*
Education of the Japanese personnel in Danish or English2	*.45*
Short visits from technical staff at the headquarters to the subsidiary	*.41*
Factor 2: Formal control and supervision (input from management)	
(vertical relationship)	
Management meetings between the headquarters and the subsidiary held in the subsidiary	.67
Contact in writing between the headquarters and the subsidiary management	.64
Short management visits from the subsidiary to the headquarters	.62
Rules concerning how the subsidiary should solve its tasks	.55
Contact by phone between the headquarters and the subsidiary management	.55
Detail plans	*.48*
Plans without details but with key numbers	*.45*
Factor 3: Socialization: training practices & language, information	
Education of Danish personnel in working with the Japanese	.70
Education of Danish personnel in the Japanese language	.70
Plans concerning the development of the organization's culture	.61
Education of the Japanese personnel in Danish or English3	*.48*
Plans without any specification of numbers	*.45*
Integrated on-line EDP systems	*.45*
Factor 4: Non specific contacts	
Contact in writing between employees below the management level	*.78*
Contact by phone between employees below the management level	*.75*
Contact in writing between the headquarters and the subsidiary management4	*.43*

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1 Items loading less the .5 but beyond .4 are listed for observation only. Items
2 Second loading
3 First loading
4 Second loading

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