Towards a conceptual framework for the relationship between subsidiary staffing strategy and subsidiary performance

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Staffing key management positions at host country subsidiaries is a strategic challenge for most MNEs. While previous research in this domain explored the antecedents of MNE subsidiary staffing decisions, strategic outcomes of different staffing patterns (e.g., using parent, host, or home country nationals) have been mostly overlooked. Drawing from the resource-based view of the firm, we develop a theoretical model that explains the links between different strategies for staffing key management positions in host country subsidiaries and the performance of those subsidiaries in their host markets and within their MNE networks. Further, we propose contingencies that moderate the relationship between subsidiary staffing strategy and host country and MNE network performance.

Keywords: expatriate; MNE staffing; subsidiary performance

Introduction

Multinational enterprises (MNEs) purposefully staff their host country subsidiaries with managers from the headquarters’ country, the host country, or another country. This nationality-based staffing decision-making serves a multitude of strategic purposes, such as establishing and maintaining global integration and control, responding to host market conditions, and mobilizing knowledge across national borders (Edström and Galbraith 1977; Harzing 1996, 2001a; Konopaske, Werner and Neupert 2002; Scullion and Collings 2006). Given the importance of global staffing strategy for an MNE’s global competitiveness, researchers have explored the factors affecting MNEs’ staffing decisions, in particular, when MNEs utilize expatriates in their host country subsidiaries (Boyacigiller 1990; Downes 1996; Erdener and Torbiron 1999; Harzing 1996, 2001a; Delios and Bjorkman 2000). This research stream has generally demonstrated a link between host country characteristics, home country characteristics, and MNE characteristics and the level of expatriates that are deployed to host country units or the choice of a subsidiary managing director (Tung 1982; Boyacigiller 1990; Welch 1994; Richards 2001; Kessapidou and Varsakelis 2003; Thompson and Keating 2004; Tariq, Schuler and Gong 2006; Colakoglu and Caligiuri 2008).

While these findings have increased the collective understanding of the antecedents of global staffing strategies, the possible influence of different staffing strategies on subsidiary-level outcomes has not been well-investigated (see Gong 2003a for an exception). This is important given the fact that the global staffing literature clearly acknowledges the potential influence of any given subsidiary manager as a possible liability or asset to the subsidiary (Dowling, Welch and Schuler 1999; Bonache and...
Brewster 2001; Gong 2003a; Toh and DeNisi 2003). Therefore, there is a strong need to further investigate and theorize on the link between subsidiary staffing strategies and subsidiary performance.

This paper seeks to address this research gap by offering a theoretical model that explains the influence of differentially using parent country national (PCN), third country national (TCN), and host country national (HCN) managers on subsidiary performance – both host market and within MNE performance (e.g., the ability to attract scarce MNE resources to the focal subsidiary) – when the staffing strategy is aligned to fit the subsidiary’s environment (Chandler 1962; Ghoshal and Nohria 1989; Schuler, Dowling and De Cieri 1993; Nohria and Ghoshal 1994). Focusing on key management positions is important because these positions have a stronger potential to impact a host country subsidiary’s effectiveness compared to positions that are purely technical or functional.

Our theoretical model draws mainly from the resource-based view of the firm which posits that firms need to possess valuable, scarce, inimitable, and non-substitutable resources in order to create and sustain competitive advantage (Barney 1991). Different types of knowledge possessed by different national categories of subsidiary managers (e.g., host market knowledge of HCNs, firm-specific knowledge of PCNs and TCNs) is such an organizational resource that has the potential to create competitive advantage in the host market. Related, the network of relationships that expatriates have access to at MNE headquarters (e.g., their social capital) and the resources available to them through these relationships as a potential organizational resource that can aid a subsidiary achieve competitive advantage within its MNE network (Nahapiet and Ghoshal 1998; Kostova and Roth 2003).

Second, we draw from the differentiated fit framework (Ghoshal and Nohria 1989; Nohria and Ghoshal 1994) to explain why contingencies need to be considered when studying these relationships. In this framework, it is recognized that the structure of an MNE is not homogeneous throughout the organization but needs to be systematically differentiated so as to ‘fit’ the different environmental contingencies faced by different subsidiaries (Nohria and Ghoshal 1994). The contingencies explored in the model include psychic distance between home and host countries and the business strategy, mode of entry, and the role of the host country subsidiaries. The choice of these contingencies is also consistent with the most widely-accepted models of strategic international human resource management (Adler and Ghadar 1990; Milliman, Von Glinow and Nathan 1991; Schuler et al. 1993; Taylor, Beechler and Napier 1996).

This paper advances global staffing literature in three specific ways. First, it attempts to fill the research gap in this area by providing a theoretical model of the relation between staffing of managerial positions and performance in host country subsidiaries taking into account contingencies that operate at different levels. The model is based on the premise that PCN, HCN, and TCN managers possess unique knowledge bases. These knowledge bases, in turn, have a differential value under the various strategic, operational, and competitive conditions surrounding a given subsidiary and its unique need for knowledge transfer and local integration.

Second, the model considers two different aspects of subsidiary performance, performance in the host market and performance within the MNE network – a differentiation that has not been considered in previous global staffing literature. This is an important issue to consider given that past research has been criticized for paying inadequate attention to internal organizational politics within the MNE, despite the importance of power and politics for an MNE’s internal operations (Edwards and Kuruvilla 2005). Given that subsidiaries compete simultaneously in the host market
against host-country competitors and in the MNE network against their sister subsidiaries (Birkinshaw, Hood and Young 2005), discussing the implications of subsidiary staffing on both types of performance is the second contribution of this paper.

Finally, six testable research propositions are presented that may serve as a stimulus for future empirical research. Collectively, these contributions may further the conceptual and empirical understanding concerning the subsidiary staffing strategy-performance relationship. Subsequent sections describe the independent variable ‘subsidiary staffing strategy’ and discuss the relation between subsidiary staffing and the two types of subsidiary performance in light of the contingencies moderating this relationship. Theoretical, empirical, and practical implications are discussed at the end.

**Subsidiary staffing strategy**

MNEs configure the staffing composition of a subsidiary by utilizing different national categories of employees at different rates (Tarique et al. 2006). They have the option of choosing from PCN expatriates, TCN expatriates, or HCNs to staff the key management positions in host country units. In this categorization based on nationality, PCN expatriates are defined as employees of the MNE who are citizens of the parent country where the MNE’s headquarters is located and HCNs are defined as employees of the MNE who are working in the foreign subsidiary and are citizens of the host country where the subsidiary is located. Finally, TCN expatriates are employees of the MNE who are neither citizens of the parent country nor citizens of the host country, but are from a third and distinct country1.

This paper defines subsidiary staffing strategy based on Perlmutter’s (1969) categorization of the attitudes of top managers of MNEs towards building their worldwide operations – a categorization that is widely accepted and used in the global staffing literature to refer to different staffing strategies. According to Perlmutter (1969), such attitudes also dictate the global staffing strategy such that key positions in host country units are differentially filled with PCN, HCN, or TCN managers based on such overarching managerial attitudes.

In an ethnocentric staffing strategy, strategic decisions for the host country subsidiaries are managed at corporate headquarters, subsidiaries have limited autonomy, and key positions are filled by PCN expatriates. Such a staffing strategy helps an MNE facilitate and maintain control and coordination, and also is an assurance that the subsidiary complies with the MNE’s overall objectives and policies (Dowling et al. 1999). The second staffing strategy is the polycentric approach in which subsidiaries can act as distinct national entities with considerable decision-making autonomy. Typically, HCNs are in charge of the subsidiary operations and utilization of either PCN or TCN managers is kept at a minimum. The polycentric approach aids the MNE in dealing with cultural and language barriers in the host location and continuity of management in its host country units (Dowling et al. 1999). Finally, in a geocentric staffing strategy, PCNs, HCNs, or TCNs can all be found in key positions anywhere in an MNE’s worldwide operations. In this respect, a geocentric staffing approach would indicate a diverse staffing composition and would range from less heterogeneous to more heterogeneous based on the number and ratio of different national categories of employees present in the key management positions of a subsidiary (Gong 2003a).

Different staffing strategies result in different types of knowledge stocks to emerge in the upper echelons of host country units. This is because regardless of the different motivations for deploying expatriate managers to host country subsidiaries, (Edström and Galbraith 1977), an emergent outcome of any expatriate assignment is the transfer and flow
of tacit knowledge (i.e., best practices, core competencies, technical or managerial know-how) from the headquarters and sister subsidiaries to the focal subsidiary (Bonache and Brewster 2001; Hocking, Brown and Harzing 2004; Novecevic and Harvey 2004; Riusala and Suutari 2004; Bonache and Zarraga-Oberty 2008). Use of expatriates are related to the flow of tacit knowledge within MNE units rather than the flow of explicit or more codifiable knowledge because MNEs tend to rely on other means such as manuals and knowledge management systems to disseminate explicit knowledge and rely on expatriates to transfer tacit knowledge (Bonache and Zarraga-Oberty 2008).

For example, when expatriates are used to fill technical and functional management positions in the host location (Edström and Galbraith 1977), they can transfer product, process, technical, and functional know-how from other units in the MNE to a focal subsidiary. If the motive is to expose the expatriate manager to international experience and thus prepare him or her for future executive positions, MNE’s cultural values and managerial know-how is the type of knowledge that can be transferred along with such expatriates. When expatriates are used as part of a coordination and control strategy (Edström and Galbraith 1977), MNE-specific tacit knowledge such as core competencies and strategic values are transferred to the foreign subsidiaries. While MNE-specific knowledge (e.g., product, process, technological, and managerial know-how) would be possessed typically by PCN expatriates, TCN expatriates carry sister subsidiary-specific knowledge (e.g., process and marketing know-how of sister subsidiaries, best practices) that may bring diversity into the focal subsidiary’s knowledge stock. Finally, HCN managers possess in-depth knowledge about host country environment regarding competition, cultural norms, institutions, regulations, and the like. The implications of different knowledge flows associated with different staffing strategies in relation to subsidiary performance are discussed in the following sections.

**Subsidiary performance**

The MNE subsidiary can be conceptualized as ‘a semi-autonomous entity with entrepreneurial potential, within a complex competitive arena, consisting of an internal environment of other subsidiaries, internal customers and suppliers, and an external environment consisting of customers, suppliers and competitors’ (Birkinshaw et al. 2005, p. 227). That is, host country subsidiaries of MNEs are unique organizational units in the sense that they are faced with an institutionally dual environment and need to conform and adapt simultaneously to their internal and external environments in order to be competitive in both (Kostova and Zaheer 1999; Hillman and Wan 2005).

According to this conceptualization of MNE subsidiaries, a subsidiary’s host market performance is related to its competitive position in the external environment in which it deals with host country suppliers and customers and competes against host country competitors. Such performance can typically be inferred from the financial-, customer-, and accounting-based performance results of a subsidiary such as profitability, return on investment, sales revenues, and market share (Andersson, Forsgren and Pedersen 2001).

As opposed to the external competitive environment in which the subsidiary operates, within its MNE network, the subsidiary competes against sister subsidiaries for the allocation of MNE’s scarce resources (e.g., new investment, positive attention from MNE top management team) (Birkinshaw et al. 2005; Bouquet and Birkinshaw 2008). For example, Bouquet and Birkinshaw (2008) suggest that positive attention received from MNE headquarters is one such scarce commodity that is allocated across a portfolio of countries. Positive attention can be received in the form of: (1) level of perceived
recognition and credit given to a focal subsidiary in comparison to other subsidiaries; (2) provision of discretionary resources that are in limited supply to facilitate a subsidiary’s development relative to other subsidiaries; and (3) explicit recognition (e.g., expressed in media) of a subsidiary’s existence and achievements in comparison to other subsidiaries (Bouquet and Birkinshaw 2008). Therefore, it becomes inevitable for the subsidiary to develop influencing strategies and tactics that will enhance its competitive position within the MNE and attract scarce MNE resources to the subsidiary (cf. Andersson et al. 2001). Performance, then, can be inferred from the extent to which a focal subsidiary receives such resources compared to other subsidiaries in the MNE network.

**Subsidiary staffing and performance within the MNE**

Harzing (2001b) suggests that PCN expatriates act as bumble-bees and spiders within the MNE and that they weave an informal communication network by ‘flying from plant to plant and creating cross-pollination between the various off-shoots’ (Harzing 2001b, p. 369). By possessing a network that spans boundaries, having frequent, multiple, and longer-tenured contacts with the headquarters, such expatriates build high levels of private social capital within the MNE (Kostova and Roth 2003; Björkman, Barner-Rasmussen and Li 2004) which Nahapiet and Ghoshal (1998, p. 243) define as ‘the sum of actual or potential resources embedded within, available through, and derived from the network of relationships possessed by an individual or social unit’. According to Kostova and Roth (2003) such private social capital possessed by boundary-spanners (i.e., PCN expatriates) will in turn evolve into a public good through social information processing, benefiting the subsidiary as a whole. In the case of PCN expatriates, the social capital they possess within the MNE may be valuable when it is used to influence MNE top management team in favor of decisions that benefit the subsidiary operations. In other words, social capital possessed by PCN expatriates becomes a valuable, scarce, non-substitutable, and inimitable subsidiary resource that has the potential to create competitive advantage within the MNE network.

Other than having the necessary social capital within the MNE, PCN expatriates are also subject to dual levels of organizational commitment and identification (Gregersen and Black 1992). This dual organizational commitment puts them in an ideal position to understand the dynamics of ‘institutional duality’ (Hillman and Wan 2005). They can identify both with the unique objectives of the subsidiary and also with the overall objectives of the MNE. Therefore, they can be in a better position to understand how to align the interests of both parties and thus be successful at influencing MNE top management team’s decision-making process.

Overall, PCN expatriates that are present in a subsidiary’s management team may make the subsidiary more cognizant of the political processes within the MNE (Carpenter, Sanders and Gregersen 2001). Having valuable contacts at the headquarters and an awareness of the strategic decision-making process of the MNE will provide the subsidiary with an understanding of how to influence organizational decision-makers. Neither HCNs, nor TCN expatriates would be as valuable as PCNs in influencing such performance due to their lack of social capital within the MNE. Therefore, we argue that the more PCN expatriates are present in a subsidiary’s key management team (i.e., ethnocentric staffing strategy), the better the subsidiary’s performance within its MNE network will be:

**Proposition 1:** All things equal, ethnocentric staffing strategy will lead to more favorable subsidiary performance within the MNE compared to a polycentric or a geocentric staffing strategy.
Role of the subsidiary

The role of the subsidiary within the MNE network is likely to moderate the effect of subsidiary staffing strategy on subsidiary performance within the MNE network. Although an ethnocentric staffing strategy can lead to stronger within MNE network performance in general, its real impact and the impact of other staffing strategies on this type of performance may depend on the role that was imposed on the subsidiary by the corporate headquarters such that different staffing strategies can lead to better performance under different roles.

Birkinshaw and Morrison (1996) developed a useful typology that differentiates between three types of roles that are imposed on MNE subsidiaries. Accordingly, a subsidiary that is a ‘local implementer’ has limited geographic scope, as well as limited product or value-added scope within the MNE. Such a subsidiary’s role is to adapt global products to the needs of the local market. A ‘specialized contributor’ has considerable expertise in certain functions or activities, but its activities are tightly coordinated with the activities of other subsidiaries. Thus, it is characterized by a narrow set of value activities and high levels of interdependence with the rest of the MNC. ‘The world mandate’ works with the headquarters to develop and implement strategy. Such a subsidiary has worldwide or regional responsibility for a product line or entire business and typically has unconstrained product scope and broad value-added scope.

As noted by Birkinshaw and Morrison (1996), role suggests a deterministic process whereby the subsidiary is required to fulfill the function ‘imposed’ by the headquarters. Therefore, successfully fulfilling the imposed role can have implications for the subsidiary’s performance within the MNE network. A subsidiary which fulfills its role successfully and meets the expectations of the corporate headquarters will in turn be in a better position to negotiate with the headquarters for its own interests and influence them.

Because the role of the local implementer is to adapt the global products to local needs, the amount of local knowledge that resides in the subsidiary is more important in terms of getting favorable performance outcomes against headquarters’ expectations. HCN managers are the kind of employees who have the critical tacit knowledge to tailor products and services according to local customer needs. The ability to modify global products and services into localized ones that match the needs and wants of local customers will also meet the expectations of the headquarters. Subsidiaries will in turn have better negotiating power with the corporate headquarters and influence decision-makers.

In the case of a specialized contributor, the interdependence between other subsidiaries requires the subsidiary to effectively coordinate its activities with the rest of the organization. One of the purposes for utilizing expatriates is to achieve this coordination role by building effective informal networks throughout the MNE (Edström and Galbraith 1977; Harzing 2001b). In addition, this subsidiary role requires the presence of human capital that is aligned with the special expertise that is needed in such centers of excellence. Therefore, a subsidiary staffing strategy that utilizes expatriates either in an ethnocentric or a geocentric form is aligned with the specialized contributor subsidiary role as long as the expatriates present in the subsidiary are the ones who have a social network spread around the globe (not confined to social capital in the headquarters) and have the specific type of know-how required by the subsidiary role. By managing the coordination of activities with the rest of the MNE network through the use of expatriates, it is possible for the subsidiary to successfully fulfill its role imposed by the headquarters and influence the MNE political processes for its own interests in return.
Finally, the world mandate can be considered as a mini-replica of the MNE, a diverse range of capabilities and competencies are needed within the subsidiary so that subsidiary learning that is needed to realize the high value-added role can be achieved. Therefore a geocentric subsidiary staffing is in line with this subsidiary role. PCNs, TCNs, and HCNs all bring diverse perspectives and competencies into the subsidiary and can bring about the innovative energy into the subsidiary. In line with the argument for the two previous roles, successfully fulfilling the role imposed by the MNE will have a positive impact on the performance of the subsidiary within the MNE.

Proposition 2: The role of the subsidiary will moderate the relation between subsidiary staffing and performance within the MNE such that polycentric staffing will lead to more favorable performance in local implementers; geocentric staffing will lead to more favorable performance in world mandates; and either ethnocentric or geocentric staffing will lead to more favorable performance in specialized contributors.

Subsidiary staffing and performance in the host market

According to the resource-based view of the firm, having valuable, scarce, inimitable, and non-substitutable firm resources is the most important source for creating and sustaining competitive advantage (Barney 1991). Among the many resources an MNE may have, firm-specific knowledge that is valuable, rare, inimitable, and non-substitutable has the greatest potential to provide global competitive advantage (Hymer 1976; Caves 1982; Kogut and Zander 1993; Grant 1996; Buckley and Carter 2004). Therefore, we argue that the impact of subsidiary staffing strategy on host market performance largely results from the different types of knowledge that resides in HCN, PCN, and TCN managers and the creation of unique knowledge stocks that emerge from different strategies for staffing subsidiary management positions. Yet, the stock of knowledge that would be conductive to a host country subsidiary’s competitive advantage could be different under different circumstances. Therefore, we argue that the relationship between subsidiary staffing strategy and their associated knowledge flows and subsidiary host market performance is not linear but depends on the environmental contingencies surrounding the subsidiary.

In certain circumstances, MNE-specific knowledge that typically resides in PCN managers can be particularly critical since MNEs exist to transfer and exploit MNE-specific knowledge and advantages across borders (Kogut and Zander 1993). MNE-specific knowledge stock can be valuable since different types of know-how, mostly tacit (i.e., hard to codify, record), that made the MNE successful in its home market and abroad is embedded in it. This type of knowledge is also inimitable since its transfer is a causally ambiguous and socially complex process making the knowledge-based advantage hard to imitate by competitors in the host country (cf. Reed and DeFillippi 1990; Barney 1991; Kogut and Zander 1993). Moreover, this type of knowledge is scarce and non-substitutable because it is MNE-specific and not possessed by host country counterparts. In other circumstances, a diverse knowledge base that is associated with a geocentric staffing strategy can be a source of competitive advantage for host country units against host country competitors. A diverse knowledge base that results from combining and integrating knowledge that resides in PCN, HCN, and TCN managers can also be valuable, rare, inimitable, and non-substitutable leading to favorable performance results.

Both ethnocentric and geocentric staffing strategies require the transfer, sharing, integration, and combination of individuals’ tacit knowledge within the host country unit.
to have an impact on subsidiary performance. However research on knowledge suggests that although it is relatively easier to transfer explicit (i.e., codified) knowledge, tacit knowledge is more difficult to convey, and its transfer requires greater effort, time, resources, and stronger ties between the parties in which knowledge transfer and integration takes place (Polanyi 1966; Hansen 1999; Reagans and McEvily 2003). Such transfer and integration is even harder to realize when the degree of homophily – the degree to which individuals are similar in certain attributes such as beliefs and values – is low. Because the presence of different national categories of managers lowers the degree of homophily within the subsidiary management team, it also lowers the ability of PCN, TCN, and HCN managers to share common meanings, a mutual sub-cultural language, and relationship specific heuristics that ease the knowledge transfer and integration process (Hansen 1999).

Thus, knowledge transfer and integration at the subsidiary level is a costly and risky endeavor due to motivational (e.g., expatriates ‘dragging their feet’ or HCNs engaging in ‘not-invented-here’ syndrome), knowledge related (e.g., lack of absorptive capacity in HCN managers such as their lack of ability and motivation to learn from expatriates), and/or coordination related problems (e.g., lack of understanding of PCN, HCN, and TCN managers of complementary knowledge bases) (Cohen and Levinthal 1990; Szulanski 1996; Buckley and Carter 2004; Bonache and Zarraga-Oberty 2008). For example, a geocentric staffing strategy may enhance the learning, innovation potential, and performance of a subsidiary by facilitating the knowledge integration process if these issues are adequately dealt with (Gong 2003a). However, if the motivational, knowledge-related, and coordination problems are not effectively managed, it may also lead to nationality-based social categorization and identification that may work against knowledge integration by creating conflict (Kopp 1994; Gong 2003a; Toh and DeNisi 2003). The differentiated fit perspective (Ghoshal and Nohria 1989, 1994) supports the argument that the cost-benefit ratio of using different staffing strategies needs to be taken into account.

**Differentiated fit perspective**

Ghoshal and Nohria (1989, p. 1994) argue that managing host country subsidiaries requires an understanding of the different contingencies that each host country context presents. Accordingly, an MNE is not a collection of homogeneous units – but rather – it needs to be systematically differentiated so as to fit the environmental contingencies faced by different host country units (Ghoshal and Bartlett 1990). In this respect, the differentiated fit perspective adopts an economizing approach to managing subsidiary operations in its specification of structural elements by which each subsidiary should be managed (Ghoshal and Nohria 1989; Nohria and Ghoshal 1994). Conditions of fit are said to be obtained when optimal trade-offs exist between the cost of each structural element and its efficacy in the context of the subsidiary under consideration (Ghoshal and Nohria 1989; Nohria and Ghoshal 1994).

Applying this perspective to the subsidiary staffing decision, the alignment between staffing strategy and the subsidiary context has an impact on subsidiary performance not only because of a synergistic potential (Chandler 1962), but also because it optimizes the costs and benefits of adopting different subsidiary staffing approaches (Ghoshal and Nohria 1989; Nohria and Ghoshal 1994). That is, due to the costs related to transferring and combining knowledge and associated motivational and coordination problems, MNE managers are faced with an optimization problem (Szulanski 1996; Buckley and Carter 2004). They need to analyze the costs of transferring and integrating the knowledge
of different national categories of managers and the benefits of doing so under different subsidiary circumstances. As a result, we suggest that the subsidiary staffing strategy needs to fit the contingencies that are operating at different levels in order to optimize the costs of knowledge transfer and integration and benefits of doing so (Bonache and Brewster 2001; Novecevic and Harvey 2004; Riusala and Suutari 2004). In the following sections, we highlight those contingencies.

**Psychic distance between home and host countries**

Psychic distance refers to the distance between two countries due to the differences in culture, language, level of education, industrial development, and legal and political systems (Johanson and Vahlne 1977). As such, it encompasses both the cultural distance between two countries (Hofstede 1980; Kogut and Singh 1988) and the institutional distance that is based on the regulative, normative, and cognitive aspects of the host country environment (Kostova 1999; Kostova and Zaheer 1999). The crux of the argument in the distance concept is that, as the psychic distance between home and host countries increases, the uncertainty and risk related to the host environment also increases leading to a higher perceived need to control those subsidiaries (Balgia and Jaeger 1984). Therefore, MNEs have an urge to deploy more PCN expatriates to overcome the uncertainty that they are facing in the host locations (Boyacigiller 1990; Harzing 1996). However, when studied from the differentiated fit perspective, such an ethnocentric staffing strategy creates an inherent paradox for MNEs. Although psychic distance increases the probability of implementing an ethnocentric staffing strategy (see Boyacigiller 1990; Gong 2003b; Harzing 1996 for empirical evidence), it will also amplify the performance inhibiting outcomes of using PCN expatriates leading to a decrease in host market performance.

As the psychic distance increases, the ability of PCN expatriates to transfer knowledge, cope with the demands of the host country, interact with HCN colleagues and subordinates, and manage relations with customers, suppliers, and government officials will decrease. Therefore, the costs incurred to transfer MNE-specific knowledge of PCN expatriates and/or attempts to combine the knowledge bases of PCNs and HCNs will be too great to reap any benefits. Therefore, we argue that polycentric staffing strategy will lead to better host market performance when the psychic distance between the home and host countries is large². In support of this argument, Colakoglu and Caligiuri (2008) found that MNEs rely on a greater number of PCN expatriates as cultural distance increases but that a higher ratio of PCN expatriates is related to lower subsidiary performance in cases when cultural distance is high. Consistent with these arguments and past research findings, we propose the following:

**Proposition 3:** Psychic distance will moderate the relation between subsidiary staffing strategy and host market performance such that polycentric staffing strategy will lead to more favorable performance for those subsidiaries that are located in psychically distant locations.

**Subsidiary business strategy**

Because host country units are semi-autonomous entities with entrepreneurial potential, they sometimes tend to pursue their own business interests and strategies in the host market independent of the MNE (Birkinshaw et al. 2005). Accordingly, a subsidiary that makes a strategic decision to compete by differentiating its products or services in the host
market needs to be high on innovation and find new ways or segments to market its products and services (cf. Porter 1980). In this case, the value created out of knowledge diversity can help these subsidiaries implement their strategies more effectively. Even though the costs of combining knowledge among PCN, HCN, and TCN managers will be large in a geocentric staffing strategy, the benefits of knowledge integration will exceed the costs for those subsidiaries due to the innovative products and processes that result from the emergence of a diverse subsidiary knowledge stock.

On the other hand, successfully competing based on costs requires organizational practices and policies that are aimed at maintaining a low cost structure (Porter 1980). On average, expatriates cost employers two to five times as much as home-country counterparts and frequently 10 or more times as much as local nationals in the country to which they are assigned (Reynolds 1997). Therefore, using TCN or PCN expatriates will diminish the ability of those subsidiaries to compete on low cost. This means that the payroll costs will increase at least 10 times the number of expatriates present in the subsidiary and the value their knowledge will add to a low cost strategy is questionable. Therefore, polycentric staffing strategy will lead to better performance for this type of business strategy.

**Proposition 4a**: Business strategy of the subsidiary will moderate the relation between subsidiary staffing strategy and host market performance such that polycentric staffing will be related to more favorable performance for those subsidiaries competing on low cost and geocentric staffing will lead to more favorable performance for those subsidiaries competing on innovation/differentiation.

However, the impact of a geocentric staffing strategy in subsidiaries with a differentiation/innovation strategy will take time to materialize. Based on social identification theory (Tajfel and Turner 1986), Gong (2003a) suggests that a heterogeneous staffing composition (e.g., geocentric staffing strategy) will lead to lower cohesion and higher emotional conflict in MNE subsidiaries. Such outcomes, in turn, may block the innovative potential of different nationalities of managers working for the same subsidiary. The innovative potential of a geocentric staffing strategy will be unleashed once the managers develop positive attitudes towards each other through continued contacts over time. As the managers learn to draw from each other’s diverse sources of knowledge, innovation and subsequent subsidiary performance will follow. Based on this argument, we propose a three-way interaction between geocentric staffing strategy, differentiation/innovation strategy, and host market performance.

**Proposition 4a**: The proposition that geocentric staffing will be more strongly related to subsidiary performance that competes on innovation/differentiation (per proposition 4a) will be stronger for subsidiaries with more experience in the host market.

**Mode of entry**

MNEs can choose from a number of different options when entering into a new market. They can either choose to enter with a wholly owned entry mode (e.g., greenfield investments) or opt for equity based entry modes (e.g., international joint ventures and mergers and acquisitions). In wholly owned entry modes, the MNE maximizes the amount of control it can exert on the subsidiary while limiting the local resources it can gain access
to (Konopaske et al. 2002; Woodcock, Beamish and Makino 1994). In equity based entry modes, the MNE has less control on the subsidiary operations but have rapid access to new markets and can operate effectively by partnering with local companies (Schuler, Jackson and Luo 2004). Equity based entry modes facilitate organizational learning and enable MNEs to capitalize on the existing competence and resources of their alliance partners (Makino and Delios 1996).

When the MNE chooses to enter a new market with a wholly owned entry mode, it relies mostly on the MNE-specific knowledge residing in its own employees to compete effectively in the local market. Therefore, it is important that PCN managers be deployed to the subsidiary to engage in an extensive knowledge transfer process and control the uncertainty surrounding the subsidiary based on lack of local competence. Firm specific know-how, then, will be a differentiator for the subsidiary in the host country and a source of competitive advantage against local competitors and in turn, enhance performance. For example, Konopaske, Werner and Neupert (2002) documented that wholly owned subsidiaries of Japanese MNEs performed better when they utilized an ethnocentric staffing strategy.

In the case of equity based entry modes, the level of control the MNE can exert on the subsidiary is limited and is shared by its partners. Because learning is a stated goal of such an entry strategy, an ethnocentric staffing strategy can create a sense of hostility or a perceived attempt to dominate the subsidiary operations on the part of the host country partners which can increase knowledge costs. In such entry modes, the staffing approach chosen needs to reflect the level of control and equity each partner has on the subsidiary so that the costs of knowledge transfer and combination is minimized by reducing conflict and tension. If the partner is a local one, a staffing strategy oriented towards polycentrism is more appropriate and can lead to more favorable host market performance. Such an orientation can facilitate and ease communication and coordination among existing PCNs and HCNs and lead to a less costly knowledge integration process. If the partner is from a third country, the use of a geocentric staffing strategy will lead to more favorable performance outcomes since such a staffing approach represents the interests of all the parties involved in the venture and does not create conflict that can inhibit knowledge integration and performance.

**Proposition 5:** Entry mode will moderate the relation between subsidiary staffing and host market performance such that ethnocentric staffing will lead to more favorable performance for wholly owned entry modes; polycentric staffing will lead to more favorable performance in equity based entry modes with a local partner, and geocentric staffing will lead to more favorable performance in equity based entry modes with a third country partner.

**Discussion**

**Research implications**

This paper provided a model of subsidiary staffing strategy and subsidiary performance based on the differentiated fit framework that identifies variables moderating this relationship (Chandler 1962; Nohria and Ghoshal 1994). These moderating variables represent conditions that determine under what conditions different approaches to subsidiary staffing can aid or hinder performance by balancing the benefits and costs of knowledge transfer and integration. The underlying concept of the model is that different
national categories of subsidiary managers (PCNs, HCNs, and TCNs) have unique knowledge bases that provide differential value under different conditions. Under certain conditions, the subsidiaries are highly reliant on the local tacit knowledge residing in HCN managers. In other situations, the MNE-specific knowledge and the social capital of PCNs provide a competitive advantage for the subsidiary against both local competitors and other subsidiaries in the MNE network. Still in other cases, the knowledge integration process among different national categories of managers is worth investing in since innovation that is created out of diversity can be critical for the subsidiary’s performance.

The moderators included in this model are evident in much of the subsidiary staffing and strategic international human resource management literature (Milliman et al. 1991; Schuler et al. 1993; Taylor et al. 1996). By building upon this stream of literature, this paper extended the global staffing literature by discussing how these variables can lead to increased host market performance if they have the right fit with the staffing approach. This paper also responds to the strong need in the international human resource management (IHRM) literature to link international HRM policies with behavioral and financial outcomes/firm’s performance in individual business units and the overall firm (Schuler, Budhwar and Florkowski 2002). In the model provided in this paper, it was acknowledged that subsidiaries compete within the MNE with other subsidiaries to influence strategic decisions such as investment allocations. It was proposed that presence of PCN expatriates in the subsidiary will make the subsidiary more cognizant of the political processes within the MNE and aid performance in this respect. By doing so, this paper introduced the political and power issues within the MNE to the staffing literature which were not considered in previous studies and frameworks (Edwards and Kuruvilla 2005).

The challenges of carrying-out international research are widely acknowledged. This is in part why most of the understanding about subsidiary staffing is based on the subsidiaries of Japanese MNEs. Researchers utilizing the Toyo Keizai database have started to establish an understanding of how the presence of expatriates impacts the performance of foreign subsidiaries of Japanese MNEs (Delios and Bjorkman 2000; Konopaske et al. 2002; Gong 2003b, Dutta and Beamish 2005; Gaur, Delios and Singh 2005). However, when considering the empirical examination of the relationships proposed in this paper, researchers need to rely on a survey methodology since it would not be possible to collect data about all the variables using secondary or archival data. For this purpose, researchers can take one of several approaches in terms of sampling. The ideal approach would be to conduct a large-scale international study that includes MNEs from multiple home countries operating in multiple host locations. An alternative approach can be to focus on a single country and test part of the model on the subsidiaries of foreign multinationals in that country. A third approach can be to focus on a single MNE and test part of the model on the subsidiaries of that MNE. Also, a longitudinal design would be desired since the impact of subsidiary staffing strategy on performance may materialize over time.

Existing or newly created measures can be used for the independent and dependent variables as well as the moderators. Subsidiary staffing strategy can be measured as the number of managers from different national categories and the extent to which they are represented in the subsidiary management team. Previous subsidiary staffing research has predominantly inferred subsidiary staffing from whether the managing director of the subsidiary was from the parent or the host country (Harzing 1996; 2001a) or by calculating the ratio of PCN expatriates at the top management team or subsidiary workforce levels (e.g. Boyacigiller 1990; Konopaske et al. 2002; Gong 2003b). In this respect, the focus has been on the continuum or dichotomy between an ethnocentric and a polycentric staffing
strategy. Measures that can be borrowed from the diversity literature can be used to measure a geocentric staffing strategy. For example, Gong (2003a) suggests using Blau’s (1977) index to measure the national heterogeneity of subsidiary staffing. He suggests that when there is an equal number of PCNs, TCNs, and HCNs, this index reaches its largest value of .67. Alternatively, subjective measures of the three staffing approaches can be created by asking respondents to reflect on the extent to which PCNs, HCNs, or TCNs are influential in the management and daily operations of the subsidiaries. In terms of our dependent variable, subjective indices of performance can be created to measure subsidiary performance both in the local market and within the MNE network since it is notoriously difficult to get objective performance data for the subsidiaries (cf. Taggart 1999; Andersson et al. 2001).

The country level variable psychic distance is maybe the trickiest construct that needs to be dealt with among the proposed variables. Psychic distance had usually been reduced to cultural distance and measured by Kogut and Singh’s (1988) cultural distance index based on Hofstede’s (1980) country scores on the dimensions of power distance, uncertainty avoidance, individualism, and masculinity. This measure has been criticized by many scholars (Shenkar 2001; Harzing 2003; Kirkman, Lowe and Gibson 2006). Such indices assume both corporate and spatial homogeneity which decreases the validity of these measures (Shenkar 2001). An alternative, but a less convenient way to measure psychic distance can be to supplement these indices by cognitive and perceptual measures such as asking the PCN expatriates the extent to which they think the cultural and institutional frameworks of the host country is similar to the home country and aggregating the responses. In addition, geographic distance, religious and language similarities can be assessed to fully capture the psychic distance between home and host countries. This way, a better and a more valid understanding of the actual distance can be obtained.

Subsidiary-level moderators can also be measured using objective or subjective measures. Entry mode can be measured using archival data or getting information from respondents. The role of the subsidiary can be determined by the extent of interdependence between the subsidiary and the headquarters as well as between the subsidiary and other subsidiaries in the MNE in the flow of resources (Rosenzweig and Nohria 1994). The generic strategy typologies have been around for some time and can be measured using existing measures (e.g., Jackson, Schuler and Riviero 1989; Huselid 1995).

Despite the contributions our paper makes to the global staffing literature, it is not without its limitations. Specifically, our model is limited by the current status of global staffing theory and literature. For example, while the dominant framework for categorizing MNE staffing approaches is to make a distinction between ethnocentric, polycentric, and geocentric staffing patterns, MNEs use a multitude of employees within each national category. For example, Briscoe and Schuler (2004) differentiate between permanent transfers, second-generation expatriates, immigrants, and just-in-time assignees among others. Tarique et al. (2006) differentiate between those HCNs and TCNs that have been socialized at parent country headquarters, host country subsidiary, or regional headquarters. Future studies can make a finer distinction between different types of MNE employees and thus improve the model we developed in this paper.

**Practical implications**

This paper has several implications for the subsidiary staffing practices of MNEs. When staffing foreign subsidiaries, MNEs need to examine carefully the configuration of the internal and external contingencies for each of their subsidiaries and take a differentiated
staffing approach that is going to optimize the constraints imposed on the subsidiaries by
the unique strategic, competitive, cultural, and institutional environments they are facing.
This way, MNEs can utilize the different knowledge bases of PCNs, TCNs and HCNs
strategically and create a competitive advantage in the host market. Given that many
MNEs prefer to adopt ethnocentric staffing approaches irrespective of these contingencies
(Mayrhofer and Brewster 1996), our model provides a guideline for the type of staffing
approach that is appropriate under different conditions.

Second, our paper has implications for the management of expatriation which includes
practices such as selection, preparation for the expatriate assignment, managing their
performance during the assignment, and managing the repatriation process after the
assignment (Stroh and Caligiuri 1998; Caligiuri and Colakoglu 2007). However, MNEs
differ on the extent to which these practices are used (Tung 1982; Kopp 1994; Peterson,
Sargent, Napier and Shim 1996) and how effectively they are designed (Brewster and
Scullion 1997; Mendenhall, Dunbar and Oddou 1987) which may inhibit or facilitate the
knowledge integration process among different national categories of employees. Carefully
designed expatriate management practices can aid knowledge transfer and integration
between PCNs, TCNs, and HCNs. Especially in the case of ethnocentric and geocentric
staffing approaches where the presence of PCN and TCN expatriates are significant, high
investment expatriate management practices will pay off in terms of improving communi-
cation, trust, and interaction between different categories of employees, and by catalyzing the
knowledge integration process.

Notes
1. Although there are many variations of international employees within this general categorization
based on nationality (Briscoe and Schuler 2004; Tarique et al. 2006), focusing on each and every
type of international employee such as permanent transfers, second-generation expatriates,
immigrants, or just-in-time assignees is beyond the scope of this paper.
2. For this contingency, use of polycentric vs. ethnocentric staffing approach is only considered
since the distance concept is related to the existence of two distinct nationalities. Therefore,
consideration of a geocentric staffing approach is not applicable.

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