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The Use of Expatriate Managers in International Joint Ventures

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This study developed a set of hypotheses concerning factors that influence the use of expatriate managers in international joint ventures' (IJVs). These hypotheses were tested on a sample drawn from U.S. firms' IJVs in Japan. Results from the empirical tests indicate that the use of expatriate managers is significantly affected by IJV age and IJV size, but not U.S. firms' size and R&D intensity.

INTRODUCTION

In a recent review article published in Journal of Management, Steve Werner (2002) identified expatriate management as an important area of research in international management. Expatriate managers serve major roles in parent firms' control over foreign subsidiaries, most notably in international joint ventures (IJVs), which represent a governance mode of international transactions located between the polar opposites of arms-length deal and those conducted within firms (Hennart, 1991). In fact, control has been a lasting popular theme of research in the IJV literature. IJV control is indispensable for a successful, cooperative IJV relationship. It is an essential component of managerial functions responsible for ensuring that parent firms' goals, interests are met, and deviations from standards are corrected for effective performance outcomes (Fenwick et al., 1999). Since IJVs operate in diversified and complicated international business environments, formal control mechanisms in the forms of standard rules, procedures, and regulations are not viable. Many

authors observed the important role played by expatriate managers as an effective informal mechanism of control (Boyacigiller, 1990; Torbiörn, 1994). By staffing IJVs' top management positions with a certain level of expatriate managers, parent firms can maintain effective control while meeting the simultaneous needs of flexibility and local responsiveness (Torbiörn, 1994; Roth, 1995).

A review of the literature, however, reveals that expatriate managers are also associated with a number of serious problems. Studies indicate that expatriate managers are very expensive (Swaak, 1995). They suffer from individual and family adjustment problems (Black, et al., 1991), difficulties in maintaining productive and satisfying social relationship with local people (Clarke and Hammer, 1995), poor job performance (Harvey, 1985), and a high rate of premature return (Shay and Tracy, 2002).

As there are compelling arguments for both using and not using expatriate managers to fill IJVs' top management positions, it is critical to study factors that relate to the use of expatriate managers in IJVs. Such studies are essential for parent firms to identify the appropriate level of expatriate managers. By identifying the appropriate level of expatriate managers, parent firms can exert sufficient control over IJVs and avoid the excessive costs that are associated with expatriate managers. However, in contrast to the expansive literature dealing with the selection, training, compensation, and cross-cultural adjustment of expatriate managers, there are surprisingly few empirical studies investigating how the use of expatriate mangers are determined (Gong, 2003). In this study, we tried to address this issue by developing a set of hypotheses regarding factors that are related to the use of expatriate managers in IJVs. These hypotheses were tested on 223 IJVs in Japan.

CONCEPTUAL FRAMEWORK

IJV Control

IJVs represent a governance mode of international transactions located between the polar opposites of arms-length market contracts and those conducted within firms (Hennart, 1991). They are jointly owned legal entities that bring together two or more legally distinct firms located in different countries through the pooling of a portion of their complementary assets. These assets are typically knowledge-based proprietary assets or intangible assets. They invariably have a tacit nature in that the creation and replication of these assets rely heavily on learning by doing (Polanyi, 1967). They reside in people who operate them and are difficult to articulate. The exchange of these assets through an arm's length deal is problematic because of contractual hazards, particularly those associated with asset specificity, resource interdependency, difficult performance measurement, and uncertainty (Williamson, 1996). Because of these contractual hazards, employing contract for IJVs is "incomplete contracting in its entirely" (Williamson, 1996, p. 9), potentially leading to extensive ex post

haggling or complete failure of the IJV relationship (Oxley, 1997). The power of courts to address these contractual hazards is also limited, given the associated difficulties in third-party verification (Oxley, 1997). It is especially difficult in the international arena since countries differ significantly in their legal systems that protect intellectual property (Mansfield, 2000). Because of difficulties in the legal enforcement over IJVs, the blueprint of contract law is rarely applied, and instead partner firms are subject to negotiation, compromises, and third-party arbitration, should conflicts arise. In situations like this, firms have to align their governance structures with transactions in order to mitigate contractual hazards (Williamson, 1996, p.3). IJV control is a crucial tool that can be used to protect parent firms' intangible assets and to ensure IJVs be managed in ways that are consistent with parent firms' interests and objectives (Oxley, 1997).

Many argued, however, that IJVs are voluntary inter-firm cooperative relationships (Dyer and Singh, 1998; Adler, 2001). Cooperation has the potential to regulate partner firms' behavior through coordinated, reciprocal forbearance (Buckley and Casson, 1988). It reduces the precise contractual hazards targeted by IJV control (Dyer and Singh, 1998; Adler, 2002). It operates as a more effective and less costly self-enforcing safeguard against contractual hazard and may substitute IJV control (Adler, 2001). This raises an important question regarding whether IJV control is needed at all in a cooperative IJV relationship. We submit that IJV control is indispensable even in a cooperative IJV relationship. Although cooperation is a necessary complement that overcomes the limit of IJV control and nourishes IJVs' success, no one can rely exclusively on cooperation during IJV evolution (Luo, 2002). IJV control establishes the institutional framework and organizational setting that guide, nurture, and strengthens the course of cooperation.

Expatriate Managers and IJV Control

According to Max Weber (1946), there are two forms of organizational control. Firms can either exert formal, bureaucratic control (Perrow, 1972) or exert informal control through culture and socialization (Boyacigiller 1990; Fenwick et al., 1999). Formal, bureaucratic control relies on hierarchy and the use of explicit rules, standards and regulations. Informal control relies on implicit organization-wide worldview, customs, traditions and oral communication. Given the diversity in task and institutional environments, IJVs often face situations that are quite different from their parent firms. Under these circumstances, standard rules, procedures, and regulations may not be viable mechanisms of control and parent firms have to rely more on socialization and organizational culture to exert control over their IJVs (Boyacigiller, 1990; Torbiörn, 1994). To the extent that the IJVs' employees are "cultured" and socialized with an identical worldview, parent firms can expect IJVs to make similar decisions under similar circumstances (Boyacigiller, 1990). This allows

for local responsiveness and flexibility while maintaining effective control (Boyacigiller, 1990). However, it is very expensive and time-consuming to socialize and to transfer culture to IJVs employees (Boyacigiller, 1990). It is almost impossible to "culture" and socialize all or most of IJVs' employees. An effective alternative is to place expatriates in IJVs' top management positions (Boyacigiller, 1990; Torbiörn, 1994). Expatriate managers are more familiar with parent firms' culture and control systems. They produce more effective communication and coordination between IJVs and their parent firms (Boyacigiller, 1990; Torbiörn, 1994). They participate in IJVs' daily operations, interact and communicate routinely with other IJV employees and mangers, and have full access to both formal and informal flows of information within IJVs. Through these activities, expatriate managers facilitate superior monitoring of IJVs' activities and can effectively enforce parent firms' influences and serve their purpose of control.

HYPOTHESES

When MNCs expand into overseas markets, they usually need to operate in culturally distant locations involve a high degree of uncertainties (Boyacigiller, 1990; Gong, 2003). Given the role of expatriate managers in managing uncertainties, expatriate managers have been extensively used as an effective means to exert control (Black and Gregersen, 1999). In order to gain IJV control, one simple solution is to fill all IJVs' top management positions with expatriates. This solution, however, is not feasible because of the prohibitive costs of expatriate managers (Black, et al., 1991; Swaak, 1995; Shay and Tracy, 2002). One estimate of the direct costs is three times the domestic salary plus relocation expense (Birdseye and Hill, 1995). Others suggest that an expatriate manager can cost up to 4 times as much as recruiting a local manager in developed countries, and 8 times as much in developing regions such as Asia Pacific (Corporate Location, 1999). The indirect costs of expatriate managers can be even higher. Expatriate managers are often associated with individual and family adjustment problems (Black, et al., 1991; Clarke and Hammer 1995), difficulties in maintaining productive and satisfying social relationship with local people (Clarke and Hammer, 1995), poor job performance (Harvey, 1985), and a high rate of premature return (Varner and Palmer, 2002). It is reported that 20%-70% of expatriates return prematurely from foreign assignments (Varner and Palmer, 2002), a rate much higher than domestic turnover. These problems have the potential to incur huge indirect costs, such as damaged relations with clients, reduced productivity and efficiencies, lost sales, lost market share, weakened competitive position, unstable corporate image, and tarnished corporate reputation (Naumann, 1992). From this perspective, using expatriates to fill IJVs top management positions can be potentially counterproductive (Hailey and Lor, 1996).

Because of the huge costs and other negative aspects that are associated with expatriate managers, parent firms are motivated to restrict the excessive use of expatriate managers (Hailey and Lor, 1996). A viable approach is to strike a balance between fulfilling the need to control and avoiding the huge costs. Parent firms need to use expatriates to fill IJVs' top management positions, but only up to a level that is sufficient to fulfill their need of control. This implies that the use of managerial expatriates in IJVs will vary with parent firms' need to control. If parent firms need more control, more expatriate managers will be used in IJVs. Whereas fewer expatriate managers will be used if parent firms' need to control is low. The IJV literature suggests that parent firms' need to control, and hence their use of expatriate managers, will be influenced by the following factors:

IJV Age

Age is an important variable in organizational studies. New IJVs are associated with the "liability of newness" due to the lack of shared values among new employees, the weak communication paths, the fragile trust between partner firms, and the uncertainties in the new environments. In dealing with the "liability of newness", parent firms tend to exert tight control and have heavy reliance on expatriate managers during the initial stages of IJVs' evolution (Hosler, 1990). Expatriate managers play major roles in communicating with parent firms. They facilitate the development of cooperation between partner firms, serve as the agents to transfer parent firms' norms and values to IJVs, and help monitor fluctuations in the new environment. Over time, as systems and practices are imparted and IJVs start to follow the planned trajectory, expatriate managers' role will decline (Downes and Thomas, 2000). As IJV ages, the MNCs will gradually become more proficient in dealing with a different culture through a learning-by-doing process (Gong, 2003). Further, an IJV's longer presence in a host country will also contribute to the formation of trust relationships with local partners through repeated transactions (Luo, 2002). These factors, coupled with the prohibitive cost and high failure rate of expatriate managers, will open doors for hiring more local managers (Shay and Tracy, 2002). Therefore, IJV age should be negatively related to the use of expatriate managers in IJVs. Thus:

H1: There is a negative relationship between IJV age and the use of expatriate managers.

R&D Intensity

Previous studies of IJV control often use parent firms' R&D intensity as a significant independent variable to explain variations in parent firms' level of control (e.g. Anderson and Gatignon, 1986; Hennart, 1991). The logic is that the higher the R&D intensity, the more proprietary assets will be at stake, and

the more control parent firms need to acquire in order to protect their proprietary assets (Hennart, 1991). Following this line of thinking, we expect the use of expatriate managers to be positively related to parent firms R&D intensity. Hence:

Hypothesis 2: There is a positive relationship between parent firms' R&D intensity and the use of expatriate managers.

IJV Size

According to transaction cost economics (TCE) (Williamson, 1996), the shared investment in IJVs operates as an effective hostage for partner firms. IJVs' value depends on the continued operation of IJVs and partner firms' respective contribution is at best partially redeemable should IJVs cease to operate (Oxley, 1997). Compared to small IJVs, large IJVs imply that more resources will be at stake. This constitutes a strong mutual hostage position for partner firms. The strong mutual hostage position promotes mutual trust, reduces potential conflicts, stabilizes the cooperative relationship, and limits opportunistic behavior (Williamson, 1996, p. 120). Therefore, parent firms of large IJVs tend to have low need of control. They are expected to use fewer expatriates to fill IJVs' top management positions.

Hypothesis 3: There is a negative relationship between IJV size and the' use of expatriate managers.

METHODOLOGY

Toyo Keizei's data on foreign affiliated firms in Japan (Toyo Keizei, 1991) was used in this study. The data is compiled from publicly available information and from surveys of senior manager in each foreign-affiliated firm in Japan (Toyo Keizei, 1991). In this study, we selected manufacturing IJVs formed between U.S. firms and their local Japanese partners. To make things simpler, IJVs that have more than two parents were excluded from the sample. This resulted in a sample of 233 observations. A further step removed IJVs whose age is less than two years and this reduced the sample size to 223 observations. Data on U.S. parent firms' size and R&D intensity were collected from COMPUSTAT, which is a database compiled by Standard and Poor's Inc.

Measurement

The Use of Expatriate Managers: The use of expatriate managers is measured by the proportion of expatriate managers in IJVs' top management teams, which is calculated by dividing the number of U.S. expatriate managers by the total number of managers in the IJV's top management team.

IJV Age: IJV age is measured by the calendar years from the time the IJV starts operation to the time the data were collected.

Parent firm's R&D Intensity: R&D intensity is measured by the U.S. firm's R&D expenditure as a percentage of total sales.

IJV Size: IJV size is measured by the IJV's total number of employees.

Control Variables

Control variables included parent firms' size and dummy variables for IJVs' industry. The dummy variable for chemical and allied products industry is coded one if the IJV operates in chemical and allied industry, and zero otherwise; The dummy variable for computer and electronics industry is coded one if the IJV operates in the computer and electronics industry, and zero otherwise; The dummy variable for machinery industry is coded one if the IJV operates in the machinery industry, and zero otherwise; The dummy variable for other manufacturing industry is coded one if the IJV operates in paper, food, glass, ceramics, forestry industries, and etc., and zero otherwise.

RESULTS

Linear regression (OLS) model was used to test the hypotheses. The model can be specified in the following equation:

Proportion of expatriate managers = f (IJV age, U.S. firm's R&D intensity, IJV size, U.S. firm's size, dummy for chemical industry, dummy for computer and electronics industry; dummy for machinery industry)

The dummy variable for the other industry was not entered in this model since this permits us to treat the other industry as a base case and the effects of the remaining industries can be measured relative to it. We tested this model on 223 IJVs formed between U.S. companies and their Japanese partners. We performed regression analysis with SPSS and Table 1 presents results from the regression analysis. This model generated a reasonable R square of 0.154. The adjusted R square is 0.126. This model's F statistic is 5.593 with a p value below the .000 level, which implies that this model significantly predicts the uses of expatriate managers. The threat of multicollinearity did not exist as evident by the low VIF values (1.32 – 1.57) and the low condition indexes (1.00 – 7.48).

As illustrated in Table 1, IJV age is found to be negatively related to the proportion of expatriate managers, which implies that expatriate managers' role declines as IJV matures and they will gradually be replaced by local managers. IJV size is found to have a negative effect on the proportion of expatriate managers. This is consistent with our hypothesis that big IJV size constitutes a strong mutual hostage position for partner firms, which leads to the use of

fewer expatriates in IJVs' top management teams. Our regression analysis also generated a significant and negative regression coefficient for the dummy variable for chemical and allied products industry. This suggests that, compared to IJVs operating in the other manufacturing industry, fewer expatriate managers will be used in IJVs operating in chemical and allied products industry. However, the regression coefficients for the dummy variables of machinery industry and computer and electronics industry are not statistically significant. This implies that the use of expatriates does not very much among IJVs operating in machinery industry, computer and electronics industry, and the other manufacturing industry.

The results also indicate that U.S. firms' R&D intensity and U.S. firms' size, do not significantly linked up with the proportion of expatriate managers, which suggests that there is no significant direct relationship between U.S. firms' specific characteristics and the use of expatriate managers.

In sum, this study provides strong support for Hypotheses 1 and 3, but not Hypotheses 2 and 4.

TABLE 1
Results of Regression Analysis

N=223

	Standardized Coefficients	**t-value**	**p-value**
Independent variables			
IJV age	-.174	-2.414	.017
U.S. firm's R&D intensity	-.069	-1.068	.287
IJV size	-.190	-2.509	.013
Control variable			
U.S. firm's size	-.088	-1.260	.209
Dummy for chemical industry	-.180	-2.124	.035
Dummy for com. and electronic industry	-.032	-.384	.701
Dummy for machinery industry	-.072	-.915	.361
R-square	.154		
Adj. R-square	.126		
Model F statistic	5.593		
p-value	<.000		

As illustrated in Table 1, IJV age is found to be negatively related to the proportion of expatriate managers, which implies that expatriate managers' role declines as IJV matures and they will gradually be replaced by local managers. IJV size is found to have a negative effect on the proportion of expatriate managers. This is consistent with our hypothesis that big IJV size constitutes a strong mutual hostage position for partner firms, which leads to the use of fewer expatriates in IJVs' top management teams. The results, however, indi-

cate that U.S. parent firms' R&D intensity, does not significantly linked up with the proportion of expatriate managers, which suggests that there is no significant direct relationship between U.S. firms' specific characteristics and the use of expatriate managers.

Our regression analysis generated a significant and negative regression coefficient for the dummy variable for chemical and allied products industry. This suggests that, compared to IJVs operating in the other manufacturing industry, fewer expatriate managers will be used in IJVs operating in chemical and allied products industry. However, the regression coefficients for the dummy variables of machinery industry and computer and electronics industry are not statistically significant. This implies that the use of expatriates does not very much among IJVs operating in machinery industry, computer and electronics industry, and the other manufacturing industry.

In sum, this study provides strong support for Hypotheses 1 and 3, but not for Hypotheses 2.

DISCUSSION AND CONCLUSIONS

This study identified several key variables that influence parent firms' use of expatriates in IJVs' top management teams. Except for R&D intensity, all factors that were hypothesized to impact on the use of expatriate managers were statistically significant in the expected direction. This study found that IJV age has a negative effect on the use of expatriate managers. As IJV matures, expatriate managers' role in fulfilling parent firms' purpose of control will decline and more local managers will be hired to fill the IJV's top management positions. IJV size is found to be negatively related to the use of expatriate managers in that large IJVs constitute a strong mutual hostage position for partner firms and parent firms of large IJVs tend to use fewer expatriates in IJVs' top management teams. Our analysis generated an insignificant regression coefficient for U.S. parent firms' R&D intensity.

Among the four industry groups, our analysis found that the use of expatriate managers vary significantly between other manufacturing industry and chemical and allied products industry, but not among machinery industry, computer and electronics industry, and other manufacturing industry.

The U.S. parent firm's size was included in this model as a control variable. Previous research suggests that firms' size is a good indicator of firms' slack resources. One concern we have is that large U.S. parent firms with more slack resources may use a disproportionately large number of expatriate managers in their IJVs that may go beyond the need to exert sufficient control. Results of this empirical test indicate that this concern is groundless. No significant relationship is reported between U.S. parent firms' size and the use of expatriate managers in IJVs. This might suggest that U.S. parent firms have

acted in a rational manner. They are not wasting shareholders' money and using expatriate manager excessively in their IJVs. They use expatriates to fill IJVs' top management positions, but only up to a level which is sufficient to exert control.

These results also reveal perhaps the most important finding of the current study: that it is characteristics of the IJV (such as IJV age and IJV size) and not parent firm characteristics (e.g. parent firms' R&D intensity and parent firms' size) that determine the use of expatriate managers. This is consistent with TCE's argument that the transaction should be the basic unit of analysis (Williamson, 1996, p.6). Results from this empirical study confirms that it is the attributes of the transactions (i.e. the IJVs), and not those of the participating firm as a whole, that determine the mode of governance in IJVs.

The limitation of this study is that it did not address the influence of country factors. Country factors such as political risk, cultural distance, government policy, legal system, and intensity of competition, are exogenous factors that firms have to consider when penetrating foreign markets. Although restricting our study to U.S. - Japanese IJVs helps control for variations among different countries, these country factors may have significant impact on firms' expatriate policies. This is clearly a useful undertaking for future research.

Finally, since there are only a few empirical studies exist that examine factors leading to the use of expatriate managers, it is difficult to evaluate and generalize results from this study in light of findings from previous studies. Both consistencies and inconsistencies, however, are noticeable. For instance, this study found that IJV age has a negative effect. This result is consistent with findings from empirical studies by Boyacigiller (1990) and Harzing (2001), but contradicts the findings by Gong (2003). IJV size is found to be negatively related to the use of expatriate managers, which confirms findings from Boyacigiller (1990) study, but contradict those of Harzing (2001) and Gong (2003). A careful examination of these studies reveals that there are significant differences among these studies in terms of both sample, the operationalization of the concept, and statistical method. The current study used a sample drawn from manufacturing IJVs' operated in Japan, which were formed between American firms and their Japanese partners. An ordinary least square regression model is employed and the use of expatriate managers was operationalized as the proportion of expatriate managers in the IJVs' top management teams. Boyacigiller (1990) studied the use of expatriate managers in the overseas branches of a single international bank. She operationalized the use of expatriate managers as the proportion of expatriate managers. Harzing (2001) studied 2,689 observations that represent subsidiaries located in 48 different countries and operate in 23 different industries, which are formed by more than 200 MNCs. She used a discrete dependent variable (1 or 0) to depict the choice for either a expatriate manager or home country nationals at the subsidiaries' top management levels (managing directors), and correspondingly a logistic

regression has been employed to analyze the data. Gong (2003) studied the use of expatriate managers in Japanese firms' overseas subsidiaries. Similar to Harzing's (2001)'s approach, he used a discrete dependent variable (1 or 0) to depict the choice for either a Japanese manager or local country nationals at the subsidiaries' top management levels (CEO and subsidiaries' top management teams). Gong (2003) also used a logistic regression model to analyze the factors that leading to the use of expatriate managers. Further, although Gong claimed that a dummy variable will be used to control the industry factor, it seem that such dummy variable has not been entered in the logistic regression models.

Since significant variations exist in terms of sample, operationalization of key concept, and statistical method, meaningful generalization and comparison are impossible to conduct among these studies. The inconsistent findings might be results of different samples, different operationalizations, and different statistical methods being employed in these studies, instead of the inherent relationship underlying these factors that leading to the use of expatriate managers. To what extend have our findings been affected by different methodologies are another interesting avenue for further studies.

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