Subsidiary Innovation in Multinational Corporation: Social Capital Perspective

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ABSTRACT

There has been a gradually increasing interest in the innovation behavior of subsidiaries. The importance of relative determinants of it in the theory and practice has been extensively discussed. Social capital can affect the productivity of the resources required for innovation behavior, and it is also a more sustainable source of competitive advantage. This study adopted “social capital theory” to explore how social capital embedded in cooperative relationships promotes the innovation behavior of subsidiaries, and to understand the impact of social capital on innovation behavior. This paper proposes how to mobilize social capital is important to explaining Chinese Subsidiaries of Taiwanese Firms’ innovation. It concludes with implications for theory, practice and research.

Keywords: Multinational Corporation, Subsidiary Innovation, Social Capital

INTRODUCTION

In the past, the causes of subsidiaries’ innovation behavior were identified as the parent company of a multinational enterprise assigning works to a subsidiary. However, the subsidiary can also through its innovation behavior enhance its own added value and assume more operational responsibilities (Birkinshaw, 1995). Birkinshaw (1997) and Birkinshaw & Hood (1998) in a series of studies emphasized the importance of the innovation behavior of subsidiaries. Birkinshaw, Hood & Jonsson (1998) believed that subsidiaries can assume the responsibility to establish exclusive advantages of multinational enterprises. Birkinshaw (1999) selected the five subsidiaries that U.S. invested in Canada as a case study to prove that the innovation behavior of subsidiaries was supported in the multinational enterprise; subsidiaries can provide valuable resources to other subsidiaries (Gupta & Govindarajan, 1994). Subsidiaries can also obtain dominance in the development and manufacture of some of the global products online (Roth & Morrison, 1992). Bartlett & Ghoshal (1986) explain that subsidiaries may become a contributor or leader in innovation projects. Therefore, we can understand that scholars are gradually attaching greater importance to subsidiary entrepreneurship. Thus, researches with subsidiaries as the objects to explore their behavior are gradually increasing.

The importance of innovative, technical, and economic determinants in the theory and practice has been extensively discussed. Over the past few years, the importance of regarding the social capital as innovative determinants has also led to a theoretical emphasis; the acquisition of enterprise knowledge no longer relies only on the market or the hierarchy, but the social capital should also be accumulated in the interactive and learning network of the area (Landry et al, 2002). Social capital can affect the productivity of the resources (for example: human resources and financial resources) required for innovation behavior, and it is also a more sustainable source of competitive advantage (Florin et al., 2003). Social capital can be obtained by promoting continued liquidity of information from different channels to facilitate acquisition of
resources (Blyler & Coff, 2003). Social capital provides the network to promote the excavation opportunity and identification, collection, and allocation of scarce resources (Birley, 1985; Greene & Brown, 1997; Uzzi, 1999 Jamali et al., 2011). Social capital can also be obtained by providing and disseminating important information and other resources to assist innovation behavior (Davidsson & Honig, 2003). Tsai and Ghoshal (1998) deemed that “social capital” can be regarded as the existing or potential resources formed by personal or community-owned network of relationships. Fukuyama (1995) deemed that “social capital” can induce cooperative behavior, so as to stimulate innovation and intimacy of the organization.

This study adopted “social capital theory” as the core theory, to explore how social capital embedded in cooperative relationships promotes the innovation behavior of subsidiaries, and the subsidiaries of Taiwan’s corporations that invested and set up factories in mainland China as the study objects, to understand the impact of social capital on innovation behavior. This study provides reference for mainland subsidiaries on how to increase their innovative ability through social capital and to enhance their position and role in multinational enterprises.

**PROPOSITION DEVELOPMENT**

**Social Capital Theory**

The multinational enterprise is an entity that constitutes of the headquarters and the several overseas subsidiaries scattered in different locations and with different objectives. Ghoshal & Bartlett (1990) believed that the entity can be conceptualized into an “inter-organizational network” embedded in the external network of the local suppliers, customers, legislators, and other organizations, and these organizations all have an interactive relationship with multinational enterprises. The social capital theory is built on the premise: “Network members access social resources embedded in the network to create value” (Bourdieu 1985; Seibert et al., 2001).

Many scholars in the past interpret the social capital from different angles. The first point of view emphasizes mainly the bridging form of social capital, which focuses on the external relationships; the second point of view emphasizes the bonding form of social capital, which focuses on the internal relationships of collectivities (Kostova & Roth, 2003). The former believes that the nature of social capital belongs to the social network linking the focal members with other members. This point of view can be used to explain why the actions of individuals or groups can obtain a successful competitive strategy by means of direct or indirect bridging with the other members of the social network. The latter believes that the social capital is a collective concept (such as organization, community, or country), and there are not too many external links. It mainly emphasizes that this internal structure of individual or group linking can contribute to the overall solidarity and the pursuit of the common goal. This study used the integrated point of view to define social capital as a resource that was established by individuals, communities, networks, or social relationships and that can promote the entrepreneurship. From the internal point of view, social capital is conducive to the exchange and combination of internal resources, intellectual capital creation, and success of cross-functional teams. From an external point of view, social capital can enhance supplier relationships, regional production networks, and manufacturers’ learning.

**Subsidiaries’ Innovation Behavior**

Birkinshaw (1997), according to Kirzner’s (1973) definition of innovation and network structure point of view, divided the subsidiary innovation behavior into local market initiatives, internal market initiatives, and global market initiatives, with the addition of the global-internal hybrid initiatives. Bartlett & Ghoshal
(1986) and Vernon (1979) deemed that the overseas subsidiaries will draw on the local market opportunities and new ideas that can be used by the Company. Birkinshaw (1999) also believed that the local market environment plays an important role in the promotion of the innovation behavior of subsidiaries. Because the frequency of interaction in the daily work of the employees of overseas subsidiaries with the customers or other companies of local markets compared to that of the company managers is higher, the relationship established by the subsidiaries in the local market is an important source to engage in innovative activities. The innovation, capability upgrading, and establishment of competitive advantages are all embedded in the local industry clusters (e.g., Krugman, 1991; Porter, 1990).

This study suggests that the most important factor affecting the overseas subsidiaries’ innovation behavior is the social capital, and the acquisition of social capital can be made available from the group’s internal and external networks. In other words, the structural analysis of the multinational enterprise should proceed with the network relationships respectively between subsidiary and parent company, subsidiary and other subsidiaries, and local government as well as subsidiary and local market (Ghauri, 1992; Kumar et al., 2009).

Social Capital and Innovation Behavior

From the point of view of network theory, the external relationships formed by the organizations in the network have an important impact on the development of resources and capabilities of the subsidiary. Such interdependent relationship can provide the subsidiary the channels to exchange with the outside world and is also a source of subsidiary resources accumulation and innovation, but it also can stimulate the organizations to generate potential of industrial action (Henderson & Cockburn, 1994). Liao & Welsch (2003) also believed that social capital is usually to help entrepreneurs access venture capital, critical information, and potential consumers, which can be obtained by means of resources through the network between enterprises to greatly strengthen the viability and growth potential of a newly established company. And for an enterprise engaged in innovation activities, the accessibility of external resources depends on the breadth of the social links and positioning in the social network.

Knowledge is embedded in the network and the community; therefore, social capital becomes an important factor for understanding innovation behavior and may bring for innovation behavior benefits such as reducing the transaction costs of the subsidiaries and members of the network, building competitive advantages, reducing R&D risk, obtaining complementary resources, accelerating learning, etc (Kumar et al., 2009). This is because the frequent interaction between the organizations and establishment of the relationship will increase the confidence and trust between the interactive firms to achieve the purposes of creating profits and increasing organizational performance.

Propositions

This study mainly focused on innovation acts of subsidiaries of Taiwan companies that invested and set up factories in Mainland China. The point of view of Nahapiet & Ghoshal (1998) suggests that social capital has three dimensions: structural, relational, and cognitive. The three social capital dimensions are not entirely mutually exclusive. In fact, they are highly dependent on each other (Liao & Welsch, 2003).

1. Structural Capital

Nahapiet & Ghoshal (1998) determined that the structural dimensions of social capital are used to describe the link form of the business between network participants, meaning with whom it contacts and how to contact (Burt, 1992). Structural capital mainly refers to the ability of the network participants to
access the resources, and it is deemed that the close relationship of the network can immediately access required information and networking knowledge that will support innovation behavior. This form of social capital was widely believed by scholars to be able to encourage cooperative behavior, thus contributing to the development of innovation behavior.

The mosaic concept in network theory can clearly explain the adjustments that the subsidiary made to establish the relationship between the local organizations and the situation of interdependence (Andersson & Forsgren, 2000). This point of view holds a concept similar to the subsidiary local response proposed by Taggart (1998). Andersson & Forsgren (2000) believed that if the subsidiary is embedded in a high degree of local networks, it indicates that the subsidiary has links with important suppliers and consumers, thereby enhancing its influence in multinational enterprises. When the subsidiary has a high degree of interaction with local organizations, then the parent company has lower degree of control of subsidiary, because it is difficult for the parent company to influence the behavior of a subsidiary that has established a relationship with local organizations (Andersson & Forsgren, 1996).

Damanpour (1991) reviewed the literature on organizational innovation literature and deemed that external communication (for e.g., in this study, the links and communication between the subsidiaries in Mainland China and the host country manufacturers, and even other vendors in the global market) will increase the degree of organizational innovation and enable organizations to scan the external environment and introduce a new concept. In the case of environmental uncertainty and rigorous competition, manufacturers need to develop relationships to complement the structural holes and change the existing network structure (Burt, 1992). The network of relationships can provide organizations with the external environment resources they are more likely to come into contact with, whether it is human or financial resources or knowledge management skills (Oliver, 1990). By mutual links, organizations can expand its product and market range and have a greater market force than that of manufacturers striving alone without relationship networks. Birkinshaw (1999) proposed that in a competitive local environment, the subsidiary for the sake of survival will use the external network relationship and access external resources to form a collective power for manipulating or confronting the environment and to accumulate knowledge about the operating environment.

The high stock of the social capital of individuals or organizations indicates the advantage of individuals or organizations in the social context. This also means a good relationship of mutual assistance between each other; therefore, information can be shared among the individuals or between individual and organizations. In addition to more certainty in the acquisition of resources, the shared transaction costs are also relatively lower, and most importantly, through the friendly relations of cooperation, innovation behavior can go more smoothly.

Proposition 1: The stronger the relationship between mainland subsidiary and the local network means the higher the social capital stock of the accumulated structural dimensions; thus, the greater the extent of the mainland subsidiary’s innovation behavior will be.

2. Relational Capital

A better internal relationship indicates the position in the network occupied by the organization will have more the nature of a center. That is, the organization has more channels to access to the information and resources and has better likelihood of crossing the organization’s formal channels to access the necessary resources. So when the organization belongs to the center of excellence, the more often it can exchange and combine resources with the various units. In addition, they also believed that the higher the
ability to exchange and combine organizational resources, the higher the organizational innovation capability will be. A study by Tsai & Ghoshal (1998) proved that social capital is conducive to the exchange and combination of resources and has a positive impact on organizational innovation behavior, while Yli-Renko et al. (2001) believed that social capital can also refer to the exclusive knowledge embedded in a relationship that can be used or flow within. Tsai & Ghoshal (1998) believed that the link between subsidiaries not only affects the opportunities of subsidiary to find innovation, but will also affect the opportunities of subsidiary to use the resources to implement the innovative concepts.

Knack & Keefer (1997) deemed that the establishment of the relationship of the network to make the network members establish a sense of trust through continuous interaction, can also promote the enterprise to conduct product and process innovation, because the network with a high sense of trust can reduce the time for the enterprise to monitor the illegal activities of other partners, employees, or suppliers. Hakansson & Snehota (1995) deemed that the extent of the core of the organizational network status determines the amount of resources the organization acquired. The highest in the status of the core network relationships can more easily achieve its desired strategic resource use for innovative activities, thereby improving operational performance. In addition, the study by Tsai & Ghoshal (1998) deemed the link between the organizations as the circulation pipeline of resources and information. If located in the centrality of the structure, the possibility of the innovators to cross over formal channels of the organization to obtain the necessary resources will be greater and thus achieve the purpose of value creation.

Location in the centrality of the network can be obtained through multi-party contacts to ensure real-time information from the external and internal and by leading the reallocation of resources at the same time (Blyler & Coff, 2003). Liao & Welsch (2003) also believed that a company can occupy the center position in the social interaction network (such as a multinational enterprise), to have more channels of communication with the rich resources available, which is conducive to the occurrence of innovation behavior. So the higher the degree of links of the mainland subsidiary with other subsidiaries, the more possible it is for subsidiaries in Mainland China to become centers of excellence and thus accumulate social capital of the relational dimension and increase the degree of innovation behavior. Therefore, we propose the following proposition.

**Proposition 2**: The better the internal relationships of mainland subsidiaries with other subsidiaries strengthen the social capital of the relational dimension of mainland subsidiaries, the higher the degree of innovation behavior will be.

### 3. Cognitive Capital

The third dimension of social capital is the cognitive dimension. They define cognitive dimensions as a system that can provide common language, the common model, and inter-group shared point of view (Nahapiet & Ghoshal, 1998). Coleman (1990) pointed out that the specification represents a degree of consensus in the social system. When the specification exists and is influential, it will constitute a powerful form of social capital. If network participants have the shared context, they can reduce the communication barriers and opportunism (Conner & Prahalad, 1996; Dyer & Singh, 1998) and increase the motive and opportunity to share knowledge resources (Adler & Kwon, 2002).

The cognitive capital within the organization reflects a shared vision or common values and encourages the development of a relationship of trust to keep the team cooperative and thus benefit the whole organization. The cognitive capital can provide a system of different groups to share the presentation, interpretation, and significance. The shared vision is embedded in the common goals and
aspirations of the organization members. When members share the same perception, it can avoid possible misunderstandings in communication and create more opportunities to exchange their ideas and resources (Tasi & Ghoshal, 1998). Furthermore, a common goal can lead them to see the potential benefits after the exchange and combination of the resources. As a result, members with a common vision will be more likely to exchange resources. Other studies have also shown that a common vision can sustain the two organizations and promote the integration of the organizations (Liao & Welsch, 2003). So the cognitive capital was originally a mosaic mechanism allowing different organizations or departments to exchange and combine resources.

In general, the implicit knowledge must be smoothly transferred through social relationships. And persons expecting the efficient transfer and sharing of highly specialized technical knowledge must have some common knowledge (Grant, 1996). The exact basis for the development of the common knowledge is the company’s internal social capital construct. Through a common language, members will be motivated to approach the information of others, and the more open the communication, the more likely it is to promote the rapid development of new technology knowledge. This is the sharing context as discussed in the cognitive dimension of social capital. Therefore, we propose the following propositions.

**Proposition 3:** The more commonality between subsidiaries in Mainland China and Taiwan parent companies strengthens social capital of cognitive dimensions of mainland subsidiaries, the higher will be the degree of innovation behavior of the mainland subsidiaries.

**CONCLUSION**

The international business field nowadays is in an era of competition that emphasizes teamwork. No organization can stand alone or be immune to contention with rival groups. So in addition to strengthening their core competitive abilities, enterprises should more quickly and efficiently create a far-reaching relationship network, good partnerships, and full exchange of knowledge with customers, strategic partners, suppliers, academic research units, and even competitors in order to survive in the rapidly changing industry environment.

This study followed the “social capital theory” point of view and integrated “the form of bridging (external source)” and “the form of bonding (internal sources)” into architecture for exploration and integrated discussion of subsidiaries’ innovation behavior. To view from a practical standpoint, this study focused on exploring the mainland subsidiaries’ innovation behavior. It is recommended that mainland subsidiaries engage in innovative activities through the acquisition of social capital and not only play a subordinate role. In addition, this study provides multi-dimensions that are conducive to giving enterprises and management that invested and set up factories in the mainland the opportunity to accumulate social capital, in order to promote innovation behavior. The sources of competitive advantage of multinational enterprises gradually shifted to let subsidiaries establish a cooperation network with the local market, in order to make full use of local resources and then feed back to the headquarters.

**REFERENCES**


