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Control Mechanisms of MNEs: An Empirical Study

Abstract

Purpose: This paper seeks to explore variations in the extent of control mechanisms, according to country of origin and organizational characteristics, in a challenging country of domicile.

Design/methodology/approach: A survey research design involving the use of a questionnaire as the primary data source was adopted. A total of 350 subsidiaries were initially randomly selected and contacted in person, or via telephone and e-mail, of which 147 agreed to take part in the study and responded to the survey.

Findings: we find that MNEs from highly financialized Liberal Market Economies (LMEs) will be associated with a greater reliance on formalized control mechanisms; this will enable the MNE's headquarters to closely monitor subsidiary managers according to objective measures, in order to ensure that the maximum shareholder value is released.

Research limitations/implications: Our study reveals a greater reliance on control mechanisms in larger firms, reflecting a desire to maximise bureaucratic economies of scale.

Practical implications: We find that the presence of expatriates regardless of country of origin leads to greater decentralization, suggesting foreign firms do not trust local staff

Originality/value: this is one of few studies of this nature conducted for the region of Middle East – and the only one we are aware of for Saudi Arabia. Further, it sheds new light on the impact of contextual circumstances on how closely firms monitor their subsidiaries, the challenges of doing business in the Gulf region, and the consequences of the large scale usage of expatriates.

Keywords: Control mechanism, Headquarter–Subsidiary relations, Multinational Enterprises, Agency theory, Saudi Arabia, Ordinal regressions.

Introduction

How do companies change their internal control mechanisms in response to challenging external circumstances and firm level responses? This is a study of centralization and control within MNEs operating in Saudi Arabia, one of the last absolute monarchies on earth, which remains a highly challenging environment in which to do business due to insecurity over investor rights, opaque regulations, and the capture of entire arms of government by princely entrepreneurs (Ross 2011; Bradley 2011). Despite this, the country still holds an attraction for foreign investors, given its oil and gas riches and its status as the global swing producer. Traditionally, theories of strategies of control have revolved around the views of control as including output, behavioural, and normative controls; however, prior research in the area of IB indicates that the contextual factors of the MNE subsidiary, encompassing not only country of domicile, but also issues such as size, nationality of parent company, presence of

expatriate managers, and subsidiary function, all impact the relative balance of the management control systems, as well as the degree of autonomy available to the subsidiary (Birkinshaw, Hood & Jonsson 1998, Colakoglu & Caligiuri 2008, Johnston & Menguc 2007, Fang, Jiang, Makino, & Beamish 2010, Anderson & Holm 2010). This paper seeks to explore variations in the extent of control mechanisms, according to country of origin and organizational characteristics, in a challenging country of domicile. The remainder of the paper is organised as follows: the next section outlines the context and relevant prior theoretical and applied enquiry; hypotheses are developed in the subsequent section; data collection, variables, and methodology are then explained, followed by the analysis of results; finally, discussion occupies the last section.

The Saudi Context: Regulation and Volatility

Although Saudi Arabia ranks quite highly in the Word Bank 'Doing Business' index (in part, a product of perceived labour market flexibility and the near complete lack of worker rights for a large portion of the workforce), the environment for investors is a challenging one, inter alia, on account of the difficulties of litigation in Saudi courts (see Zegars 2006), and societal dynamics (Rice 2004). In practice, it has proven difficult to enact the necessary reforms to make the environment more hospitable for foreign investors (Hertog 2011). Indeed, it has been argued that Saudi Arabia represents an extreme example of the rentier state (Lawson 2011), and suffers from a particularly chronic resource curse (Auty 2001). Although in 2014 Saudi Arabia had a GDP per capita of $18,000, placing the country in the middle to upper income category, this is considerably lower than a high of some $22,000 in 1977, despite high oil prices in the 2000s (Trading Economics 2015). Moreover, as can be seen from Figure 1, below, this growth has been highly volatile, making it difficult for organizations to plan for the future with confidence, even in the oil and gas industry.

Figure 1: Changes in the Saudi GDP Per Capita
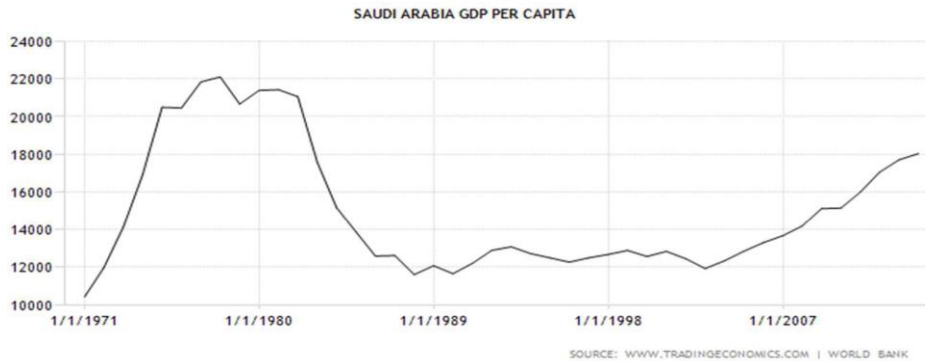
Source: Trading Economics (2015).

Even when compared to other resource rich countries, Saudi Arabia has been remarkably unsuccessful in building a developmental state (Auty 2001; Lawson 2011; Beblawi 2007). Auty (2001) argues that this reflects Saudi Arabia's role as the key swing producer, and a deeply embedded political culture centring on authoritarian paternalism. This has led to considerable inequality, with between two and four million out of 16 million native Saudis living in poverty, with high levels of unemployment among the young (Guardian 2013). Meanwhile, a high proportion of oil and gas rents are captured by possibly as many as 15,000 princes (Economist 2014), with the Saudi monarch being one of the richest despots in the world. Hertog (2011) argues that key arms of government constitute little more than personal fiefdoms of dominant figures in the regime. Rising fears of instability – and despite a highly repressive environment and political protests – have led to the government accelerating its indigenization policy in order to create more job opportunities for local nationals. Currently, the country has some 12 million migrant workers, making the majority of those in employment foreign (Guardian 2013; Jehanzib et al. 2013). These foreign workers comprise a small minority of highly skilled expatriates, and a large grouping of unskilled and semi-skilled workers. The latter are not readily substitutable with indigenous Saudis, not only (in the case of semi-skilled and skilled occupations) because of a chronic lack of skills, but also because many Saudi firms have founded their competitiveness on a system of quasi peonage, with foreign labourers facing police brutality, confiscation of their passports, and arbitrary expulsion as instruments of labour coercion. Hence, although the Saudization policy has been in place for some two decades, it has made only limited inroads in reducing the country's reliance on foreign labour; indigenous Saudis are in a position to insist on better wages and working conditions (Niblock and Malik 2007).

Ross (2001) argues that in common with other resource rich autocracies, there are three main mechanisms that shore up the status quo. Firstly, there is the rentier effect, the ability to buy-off key interest groups, in the Saudi case, key fundamentalist religious interests. Secondly, there is the repression effect, the ability to purchase large numbers of weapons and technologies for mass surveillance (ibid.). Thirdly, there is the modernization effect, with revenue inflows reducing pressures for cultural or economic modernization. Indeed, Ross (2011) suggests: "No state with serious oil wealth has ever transformed into a democracy. Oil lets dictators buy off citizens, keep their finances secret, and spend wildly on arms".

It could be argued that the revenues have increased the range of institutional options, resulting in much variety, from relatively efficient arms of state to corrupt personal fiefdoms and "armies of bureaucratic clients" (Hertog 2011). Moreover, the Saudi state has accumulated large scale financial obligations to different interest groupings that are difficult to reverse, authoritarianism notwithstanding. On the one hand, this entrenches state dominance, yet on the other hand, makes the state less coherent (Hertog 2011). Princes serve as intermediaries between commercial interests and the state, allowing innumerable opportunities for corruption, and the blurring of personal royal wealth and state resources (Wilson 1994).

Within Saudi Arabia, there is a localization policy in place, *Saudization*, which aims to promote the employment of local people through a quota system (Sadi and Al-Buraey 2009). An initial 2003 goal was to ensure that 30% of employees in firms employing 20 or more workers were Saudi nationals, but this was watered down in 2006 (Tripp and North 2011). Nonetheless, many firms either chose to close or to nominally employ Saudis as window dressing. In 2011, the Nitaqat system was introduced, a carrot and stick approach that makes it easier for firms that meet Saudization targets in order to obtain visas for foreign workers; firms that are red-lined for a lack of progress in Saudization are no longer permitted to renew the visas of their expatriate staff.

Saudization has led to increased job opportunities for Saudi nationals, but chronic skills shortfalls have meant that firms have to employ under-skilled locals (Al Dosary and Rahman 2005). The official General Organization for Technical Education and Vocational Training (GOTEVT) is both overly bureaucratic and ineffective (see Al-Shamaari 2009), whilst the overwhelming majority of Saudis with tertiary education hold degrees in religious studies, with only 20% of graduates holding technical or job relevant qualifications (Tripp and North 2011). Again, it means that Saudis with technical qualifications are in very short supply,

leading to serious problems with staff retention, as highly skilled individuals regularly job-hop (Al-Subhi Al-Harbi 1997; c.f. Torofodar 2011). In turn, this has led to the continued employment of large numbers of expatriates.

In such a challenging environment, MNEs are pulled in different directions. On the one hand, they are under great pressure to employ and advance Saudi nationals, especially those with close links to the princely elite. The difficulties of operating in Saudi Arabia mean that managers who have experience in dealing with local circumstances are particularly valuable (see Tripp and North 2009). MNEs may have an interest in delegating as much as possible to them, given that they are better able to navigate local vicissitudes. On the other hand, local skills shortfalls and the need to ensure that staff follow the interests of the organization, and not some princely patron or other, may drive tighter control from the centre.

Forms and Practice of Control: Existing Evidence

Agency theorists have proposed that principals tend to use three primary types of control – cultural, behavioural and output – to varying degrees (Ouchi 1985). Behaviour control means that control is achieved by monitoring the behaviours of others, whilst output control involves measuring the desired quality and quantity of output. Cultural control, however, involves socialising the agent to consider his or her interests as co-identical to those of the principal; however, these are indirectly related in that the use of one method of control may affect the efficacy of another (Chang & Taylor 1999). Past research has also noted the relative popularity of output control (Egelhoff 1984) and staffing control – that is, using parent expatriates to fill management positions (Baliga & Jaegar 1984). These can be viewed as manifestations of cultural control as they are intended to create a greater sharing of values and goals between the HQ management and the subsidiary.

Given this, we investigate formal structures of control, as well as how such forces affect – either directly or indirectly – different methods adopted for control and coordination, as well as the requirement for such. With the aforementioned taken into consideration, this research provides a framework model that makes the proposition that a number of different subsidiary features, such as the size and country of origin, are able to affect the mechanisms of control and the degree to which they are applied by headquarters over their subsidiaries located in Saudi Arabia.

Statement of Hypotheses

Home and Host Country Effect

A large body of literature suggests that it is not only country of domicile (host), but also country of origin (home), that impacts on firm level practice (Brewster et al. 2008); the latter reflects variations in shareholder rights, and the extent to which they may be diluted by the rights of other stakeholders. The literature on comparative capitalism has developed a number of country taxonomies that encompass the countries of origin encountered in this study. Firstly, there is the US and the UK, held up as quintessential or highly financialized Liberal Market Economies (LMEs), where shareholder rights are most advanced, enabling the latter to most closely direct the policies and practices of the firm (Hall and Soskice 2001). Secondly, although the literature has tended to see this category as an internally coherent one (Lane and Wood 2012), recent writers such as Konzelmann et al. (2012) have pointed to the existence of a second category of less financialized LMEs, including Canada, Australia and New Zealand. The dominance of the financial sector in the first category means that there are even stronger pressures to short term shareholder value. Thirdly, there are the continental European capitalist (coordinated markets) or "Rhineland" economies, including Germany, Sweden and the Netherlands (Amable 2013). Fourthly, there are the Scandinavian social democracies, distinguished from their peer coordinated markets by stronger social, but weaker employment, protection and less centralized financial systems (Amable 2013). Fifthly, there is Japan. While Japan is another example of a coordinated market economy (CME) and has much in common with the two preceding countries, it also has important differences in that large corporations play a particularly important role in providing stability in collaboration with the state, and state welfare and bargaining institutions are less developed (ibid.). Sixthly, there is South Korea, which, whilst sharing many features with Japan, has very distinct institutional directions given the developmental role of the state during the years of authoritarian rule, and which we treat here as a distinct category (see Whitley 1999). Seventhly, China is often depicted as having a variety of capitalism in its own right, characterized by a much higher degree of state direction than in mature market economies, but also by much internal diversity (Boyer 2012). Finally, the Middle Eastern economies have been held to have common features on account of a combination of rapid but volatile growth that has taken place largely despite, rather than on account of, institutional frameworks (Kuran 2004).

There is a body of applied work that links country of origin with control. An early pioneer of the literature on comparative capitalism, Lincoln (with colleagues) found that the difference between formal and *de facto* centralisation was very minor in American companies but rather more considerable in Japanese companies (Lincoln et al. 1986).Jain & Tucker (1995) assert that power is more centralised in Japanese companies than in American companies in general. Zaheer (1995) found that Japanese banks show higher levels of centralisation than American banks, although the difference was not statistically significant. Again, Kustin and Jones (1996) found that the influence of Japanese headquarters on their American subsidiaries was greater than the influence of American headquarters on American subsidiaries. More recent work has sought to distinguish between formal and informal systems of control (Kim, Park& Prescott 2003). It has been argued that formal control mechanisms dominate in US MNEs (O'Donnell 2004) and implicit control mechanisms in Japanese ones (Taylor 1999). A related issue is that Japanese MNEs have a relatively high presence of parent country expatriates in their subsidiaries (Kopp 1994), associated with the formation of 'mini-headquarters' in the foreign subsidiary, enhancing cultural control (Baliga & Jaegar 1984). Similarly, Ferner (1997) found Japanese MNEs were likely to make greater usage of social control, supported by a relatively high usage of expatriates, whilst US MNEs favoured formal control (see also Hulbert & Brandt 2000; Birnberg & Snodgrass 1988).

Negandhi (1987) found that that 88% of the subsidiaries of American MNEs sampled heavily relied on written policies from headquarters, a much larger amount than those from Asian and European coordinated markets: only 32% of the subsidiaries of German and 12% of the subsidiaries of Japanese firms. Similar distinctions we reencountered between US and Continental European (coordinated market) MNEs (Wolf 1994), between US and Japanese ones (Jaeger and Baliga 1985), and between US and French ones (Calori et al. 1994). Research evidence in the areas of attention seeking (Bouquet & Birkinshaw 2008) and formalisation (not investigated in this paper) are less abundant. There is similar broad consensus around *output control*. In an early study, Scholhammer (1971) found that American MNEs relied more heavily on reports than European firms. Confirming this picture, Hulbert & Brandt (2000) found that US MNEs required higher levels of reports than either Continental European or Japanese MNEs (for similar results, see Negandhi 1987;1984; 1988).

Given that Britain is also a highly financialized LME, characterized by a high degree of financialization and activist investors (Konzelmann et al. 2012), it could be argued that there would be similarly high pressures for formalization in order to ensure that a value release

agenda is adhered to. Formal controls by HQ could include, among others, the degree of standardisation the HQ may require from its subsidiary and the kind of rules and procedures that it may exert towards its subsidiary. Hence, we hypothesize that:

Hypothesis 1: Formal control in MNEs from highly financialized LMEs will be higher than that from other capitalist archetypes.

Domestic and Third Country Staff

Given gaps in local skills and capabilities, and quite rapid turnover of indigenous highly skilled staff (Al-Subhi Al-Harbi 1997; c.f. Torofodar 2011), firms that employ large numbers of domestic managers may seek to centralize decision making as much as possible. There could be two reasons for this. The first would be that, given high levels of poaching, domestic managers may soon work for competitors, and hence, may face conflict of interest dilemmas. Secondly, as a result of problems associated with "window dressing", under-skilled or under experienced locals may be employed in highly visible positions in order to meet Saudization targets and/or to win the goodwill of some royal or other, but may not be trusted with real autonomy or vested with meaningful control. This leads to hypothesis 2:

Hypothesis 2: MNEs employing high numbers of domestic staff are more likely to be centralized.

Edstrom & Galbraith (1977) analysed the international transfer of managers in four multinational companies, one of which transferred a far greater number of managers than its direct competitor – despite their being of the same size, operating in the same industry, and having almost identical organisational charts. Further, Edstrom & Galbraith hypothesised that, in that multinational, the transfer of managers was used to socialise managers and create informal verbal international information networks. Others (Ferner, Edwards & Sisson 1995; Welch, Fenwick & DeCieri 1994) tested this hypothesis, and found that the usage of expatriates was viewed as a way for individuals to build up networks of contacts and absorb the international ethos and practices of the firm. In other words, the usage of large numbers of expatriates may be associated with a higher degree of decentralization:

Hypothesis 3: MNEs employing high numbers of third country expatriates are less likely to be centralized.

Size of the Parent and Subsidiary

According to Baliga & Jaeger (1984), as well as Snell (1992), the size of the subsidiary is linked with the design of the control mechanisms. However, two competing mechanisms could be at play here. On the one hand, the increased size of a subsidiary could mean that it can build up its own resources and become independent from the HQ; conversely, a very large subsidiary may be particularly important to the HQ as a profit centre, and may require more control than usual. And the only way to do this may be by a variety of formal, centralised, or bureaucratic controls (see section below on details of these types of controls), ultimately leading to more overall controls. We, therefore, hypothesize that:

Hypothesis 4: Size of subsidiary is positively related to the extent of controls. The larger the size of the parent and subsidiary, the greater the degree of control exercised by the parent.

Methods

Data and Measurement

A survey research design involving the use of a questionnaire as the primary data source was adopted. The survey instrument went through several iterations and was fine-tuned after a pilot study. In the main survey, data were collected from MNEs' subsidiaries in three major cities, namely Riyadh, Jeddah and Jubail. The subsidiaries studied were from the *Directory of Foreign Companies* in Saudi Arabia, published by the Saudi Arabia Investment Authority (SAGIA). Additional sources, such as business associations and government agencies, were also contacted to cross check and update the information in some instances. A total of 350 subsidiaries were initially randomly selected and contacted in person, or via telephone and e-mail, of which 147 agreed to take part in the study and responded to the survey (42% response rate). Preliminary and statistical tests (see below section on analysis) show that the data collected satisfies reliability criterion and that factor loadings, average variances extracted (AVE), and reliability tests provide sufficient confirmation of the convergent validity for the variables.

The survey instrument had five sections: section one was directed towards obtaining information on control variables, including the size of the parent and subsidiary, its age, sector, and the nationality of the manager. Subsequent sections were directed towards eliciting information on the role of expatriates, the HQ–subsidiary relationship, performance, structure

and knowledge flows. Control mechanisms were measured with the help of 11 Likert-scale questions (5 being the highest) on the four categories and formed the basis for dependent variables (see below for details). Some Replies to survey questionnaires were delayed. Follow up calls to the subsidiaries revealed that the delay occurred as a number of managers were being consulted before the questionnaire was finally filled in. Subsequent checks on the data revealed that data are consistent and reliable.

Dependent Variables

Four categories of dependent variables signifying level and variety of controls were created (see Table 1). 'Centralised' Controls (CC), which includes replies to the following areas of interest: 1. the level of autonomy in the subsidiary to decide its own strategies; 2. the degree of surveillance that headquarters' managers execute towards this subsidiary; 3. the degree to which the HQ uses expatriates to directly control the subsidiary's operations. 'Formal' Controls (FC), which includes replies to the following areas of interest: 1. the degree of standardisation that the headquarters requires from the subsidiary; 2. the kind of rules and procedures that the HQ exerts towards the subsidiary. 'Output' Controls (OC), which includes replies to the following areas of interest: 1. the degree of output control that the headquarters exerts towards the subsidiary; 2. the type of planning/goal setting/ budgeting that the headquarters uses towards the subsidiary. And finally 'informal controls' (IF), which includes replies to the following areas of interest: 1. the degree of participation by the subsidiary's executives in committees/taskforces/project groups; 2.to what extent do the executives in the subsidiary share the company's values; 3.the degree of participation of the subsidiary's executives in training programs; 4. the level of informal communication between the subsidiary and the headquarters and other subsidiaries. All variables are measured on a five-point Likert scale, ranging 1–5, with 5 signifying the highest level of control.

Independent Variables

The independent variables consist of the size, firm, and country related factors. This study employs 25 independent variables: 1 is the (log of) subsidiary employment; 2 is (log of) employees worldwide; 3 is the (log of) number of expatriates in subsidiary; 4 is the age of the subsidiary; 5–9 are industry dummies(petroleum, chemicals, electronics & electrical, motor vehicles, food & beverages); 10–17 comprise group parent nationality dummies: 10 Germany

and Switzerland, 11 Netherlands (continental European capitalist economies), 12 Australia and Canada (softer liberal market economies), 13 Denmark and Sweden (social democracies), 14 Japan (coordinated market economy), 15 Italy, 16 South Korea, 17 China, Lebanon, Kuwait, Egypt and Jordan (Middle Eastern emerging economies) – the omitted dummy (group 0) is the US and the UK (which were correlated); variables 18 and19 represent the nationality of the subsidiary (Saudi or third country); 20 and 21 represent the ownership status of the subsidiary (majority-owned or joint venture); 22–25 represent the subsidiary function – (22 marketing and sales, 23 manufacturing, 24 assembly, 25 services); 26–29 represent the four types of control exercised (26 'centralized' controls, 27 'formal' controls, 28 'Output' controls; 29 'informal' controls).

Statistical Procedure

The statistical analysis is carried out with the help of factor analysis, mean, sd, zero-order correlations and ordinal regression analysis. The ordinal regression used to analyse part of the data may be written in the form as follows if the logit link is applied: $f[g_j(X)] = \log\{g_j(X)/[1-g_j(X)]\} = \log\{[P(Y \leq y_j \mid X)]/[P(Y > y_j \mid X)]\} = a_j + \beta X, j = 1, 2, \ldots, k-1$, and $g_j(x) = e^{(a_j + \beta X)}/[1 + e^{(a_j + \beta X)}]$, where j indexes the cut-off points for all categories (k) of the outcome variable. If multiple explanatory variables are applied to the ordinal regression model, BX is replaced by the linear combination of $\beta_1 X_1 + \beta_2 X_2 + \ldots + \beta_p X_p$. The function $f[g_j(X)]$ is referred to as the link function that connects the systematic components (i.e. $a_j + \beta X$) of the linear model. The alpha a_j represents a separate intercept or threshold for each cumulative probability. The threshold (a_j) and the regression coefficient (ß) are unknown parameters to be estimated through means of the maximum likelihood method (Chen & Hughes 2004).

Results

Reliability and Validity of Variables

Before the statistical work began the data were subjected to convergent validity (CV) which can be tested in the form of three indicators: factor loadings, average variance extracted (AVE), and reliability of the variables and their measuring items (Hair et al. 2010). The results in our case show that the factor loadings of each variable indicator are significant (in comparison to sample size), ranging from 0.55 to 0.90, demonstrating a strong association

between variables and their factors. Further, the results indicate that AVE values are higher than the required threshold value of 0.50, demonstrating adequate convergence of the variables. Finally, the results of the Cronbach's alpha test indicate that the scales satisfy the reliability criterion, with values ranging from 0.66 to 0.76. Taken together, as recorded in Table 1, the results of factor loadings, AVE, and reliability tests provide sufficient confirmation of the convergent validity for the variables listed in the table below.

Table 1: Convergent validity (standardized factor loadings, average variance extracted, and reliability results)

Items	Centralised Controls (CC)	Formal Controls (FC)	Output Controls (OC)	Informal Controls (IC)
PCC 2	0.870			
PCC 3	0.800			
PCC 1	0.748			
BFC1		0.891		
BFC2		0.881		
OC1			0.900	
OC2			0.887	
SN1				0.846
SN3				0.805
SN4				0.578
SN2				0.550
AVE	0.52	0.66	0.76	0.50
Reliability (Cronbach's α)	0.73	0.73	0.76	0.66

Descriptive Results

Table 2 reports the mean, standard deviations and zero order correlations of variables. Selected highlights of the table are as follows. Centralised controls are positively associated with the overall size of the firm, motor vehicles industry, majority subsidiary holdings, but negatively associated with subsidiaries that are performing marketing and sales functions. Formalised controls do not seem to be favourable and, notably, are negatively associated with the overall size of the firm and motor vehicles industry and with joint venture forms of business operations. Output controls are positively associated with CME parents and with majority-owned services firms where the nationality of the manager is Saudi Arabian. Finally, informal controls are positively associated with services industry, size of the firm and number of expats in the subsidiary, chemicals industry, and in firms where managers are from a third country. Informal controls are negatively associated with the joint venture form of operations.

Table 2 Basic statistics and correlations

	M	Sd	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28	29
1	7.21	1.04	1																												
2	10.17	1.03	.31**	1																											
3	4.33	1.33	.83**	.24**	1																										
4	.41	.49	-.34**	-023**	-.25**	1																									
5	.20	.40	.06	026**	.06	-.05	1																								
6	.56	.50	-.03	-.16	-.02	.06	-.57**	1																							
7	.37	.48	-.22**	-.23**	-.21*	-.07	-.39**	.31**	1																						
8	.37	.49	-.05	-.12	-.02	.12	.45**	-.33**	-.59**	1																					
9	.06	.24	.04	.28**	.06	-.16	-.13	.23**	-.19*	-.19*	1																				
10	.10	.30	.11	.08	.12	.13	-.11	-.06	-.26**	-.26**	-.09	1																			
11	.34	.48	.16	.32**	.15	-.05	.35**	-.14	-.28**	.36**	-.18*	.23**	1																		
12	.27	.44	-.28**	-.50**	-.25**	-.04	-.30**	.13	.50**	-.18*	-.15	-.20*	-.43**	1																	
13	.16	.37	-.22**	.04	-.19*	.04	-.22**	.09	.19*	.04	-.11	-.15	-.32**	.11	1																
14	.35	.48	.18*	.07	.11	-.27**	.16*	-.09	-.14	.38**	.11	-.24**	.32**	-.17*	-.32**	1															
15	.16	.36	.04	-.02	.08	.13	.06	-.07	-.13	-.14	.20*	.16*	-.11	-.04	-.19*	-.31**	1														
16	.06	.24	-.12	-.03	-.15	-.10	-.13	.05	.33**	-.19*	-.06	-.09	-.18*	.42**	-.11	-.18*	-.11	1													
17	.15	.36	-.14	-.14	-.10	.23**	.12	-.12	-.16	-.01	-.10	.17*	.18*	-.25**	-.18*	-.31**	-.18*	-.10	1												
18	.14	.34	-.09	.40**	-.08	.15	-.01	-.08	-.09	-.31**	-.10	.52**	.13	-.23**	.09	-.28**	.10	-.10	.11	1											
19	.13	.34	.00	-.16	.02	-.20*	-.19*	.14	.25**	-.29**	.32**	-.06	-.28**	.18*	-.17*	.27**	.11	-.09	-.10	-.15	1										
20	.08	.27	-.14	-.35**	-.12	.01	-.15	.16*	.18*	-.02	-.07	-.10	-.21**	.49**	.13	-.01	-.13	.34**	-.12	-.11	-.11	1									
21	.07	.25	-.13	-.14	-.07	.21*	-.14	.02	-.21*	.34**	-.07	-.09	-.19*	-.16*	.24**	.09	-.12	-.07	-.11	-.10	-.10	-.08	1								
22	.04	.20	.18*	.04	.18*	.24**	-.10	.04	-.09	.19*	-.05	-.07	.29**	-.12	-.09	.21*	-.08	-.05	.01	-.08	-.08	-.06	-.05	1							
23	.05	.23	.22**	.17*	.21*	-.02	-.12	.21**	-.18*	-.18*	.44**	-.08	-.17*	-.14	-.10	-.17*	.55**	-.06	-.10	-.09	-.09	-.07	-.06	-.04	1						
24	.07	.25	-.13	-.06	-.10	.04	.19*	-.09	.07	.07	-.06	-.09	-.19*	-.16*	.25**	-.20*	.25**	-.07	-.11	-.11	-.10	-.08	-.07	-.05	-.06	1					
25	.16	.36	-.26**	-.35**	-.18*	.36**	-.03	.08	.09	-.02	-.11	.10	.12	.08	-.19*	-.31**	-.18*	-.11	.60**	-.17*	-.16*	-.13	-.12	-.09	-.10	-.12	1				
26	3.22	.99	.04	.43**	.02	-.14	.30**	-.01	-.21**	.08	.16*	-.15	-.08	-.10	.05	.08	-.23**	.19*	-.08	.14	-.18*	.17*	.08	-.19*	.18*	.07	-.26**	1			
27	4.11	.74	-.06	-.17*	-.02	.11	.14	-.26**	-.14	.12	-.03	.10	-.17*	.14	.04	-.01	.14	-.21*	.15	-.05	.11	.09	.24**	.13	-.12	.14	-.09	.11	1		
28	4.19	.69	.17*	.19*	.17*	.12	.30**	-.21*	-.09	.08	-.36**	.23**	.26**	-.13	-.14	-.02	.15	.01	.09	.10	-.16*	.06	.12	.22**	-.07	.22**	-.13	.33**	.59**	1	
29	4.02	.65	.21**	.18*	.17*	.01	.35**	-.32**	-.44**	.17*	-.07	.25**	-.09	-.03	-.14	-.17*	.26**	-.12	.09	.14	-.03	-.16*	.09	-.18*	.08	.14	-.08	.33**	.45**	.49**	1

1=log subsidiary employment; 2=log employees worldwide; 3=log expatriates in subsidiary; 4=age of subsidiary; 5-9 are respective industries: petroleum, chemicals, electronics & electrical, motor vehicles, food & beverages; 10-17 are nationality of the parent: 10= Germany, Switzerland, Netherlands, 11= Australia, Canada, 12= Denmark, Sweden, 13=Japan, 14=Italy, 15=South Korea, 16=China, 17=Lebanon, Kuwait, Egypt, and Jordan; 18,19 represent the nationality of the HR director; 20-21 represent subsidiary type-majority owned or joint venture; 22-25 represent subsidiary function—22 marketing & sales, 23 manufacturing, 24 assembly, 25 services. No. 26-29 represent the type of control exercised.

Multivariate Analysis of Results

Table 3 provides the results of ordinal multivariate regression analysis on four control variables and 25 independent variables as described above. Table 3 provides the results of the hypotheses, as well as additional results discussed separately.

The first hypothesis states that formal control in MNEs from highly financialized LMEs will be higher than in those MNEs from other capitalist archetypes. Table 3 reports the results of the regression analysis on eight groups of country dummies, four of which are domiciled in Europe: Group 10 (Germany, Switzerland, Netherlands), Group 11 (Australia, Canada), Group 12 (Denmark, Sweden) and Group 13 (Italy). The US and the UK, the two highly financialized countries, were used as control group. The results for this hypothesis are revealing. The 'centralised' controls coefficient for all of these groups of countries are significant but negative. For the 'formal' method of controls, the results are negative and significant only in the case of Italian parents. For groups of countries 10, 11, and 12 the coefficient, though positive, is not significant. With regard to 'output' controls, the coefficient is significant but negative in the case of group 11 and 12 countries; it is positive but not significant in the case of group 10 countries. Finally for 'informal' means of control, the coefficient is significant but negative in the case of all the groups except Italy, in whose case the coefficient is positive but not significant. Extending the results for Asian capitalist economies, we notice that Japanese parents have a significantly negative attitude to all forms of controls except control by 'formal' mechanisms, the coefficient for which is not only positive but highly significant, contrary to what is suggested by earlier work (see Lincoln, 1986). The results for South Korean parents are similar to those of Japanese parents except that the coefficient for control by 'formal' means, though positive, is not significant. Chinese parents display a negative approach to all forms of control mechanisms. Middle Eastern market economy parent firms rely heavily on 'bureaucratic' means of controls, the coefficient for which is not only positive but highly significant. The latter might reflect an Ottoman bureaucratic tradition, which continues to exert a long term influence regarding formal regulation and organizational procedures (Findley 1980; Heper and Berkman 2009). Overall, the results support the test for the first hypothesis. Compared to the control group of the highly financialized group of countries (the US and the UK), the results for the rest of LME group of countries display a negative approach to controlling their subsidiaries by the four methods of controls analysed. For hypothesis 1, therefore, we get mixed results.

The second hypothesis states that MNE subsidiaries employing large numbers of domestic managerial staff are more likely to be centralized. Results show that this seems to be the case, as out of four types of controls, the coefficients of two genres of controls – 'formal' (BFC) and 'informal' (CS&N) turn out to be positive and significant. This is a highly illuminating result as

it signifies several essential points. First a Saudi manager entrenched in   local customs and values is best placed to deal with his/her subordinate staff when it comes to interfacing formally. At the same time there will be many demands stemming from the operation of the extended informal clan and clientalist networks of support, and in order to   take account of local restrictions on working hours (e.g. during hours of prayer). An instance would be meeting certain deadlines, which might require the use of overtime or working on holidays. A manager embedded in the local culture and speaking local dialects is ideally placed to deal with such situations and get the job done. It should also be noted here that in all likelihood most non-managerial staff employed in subsidiaries will also be locally sourced, in which case junior Saudi managers are best placed to deal with them. The results thus largely support the second hypothesis.

The third hypothesis states that 'MNEs employing high numbers of third country expatriates are less likely to be centralized'. We indeed find that the presence of third country managers has a negative influence on all types of controls; in other words their presence leads to a reduction in the quantum of control exercised by the HQ over its subsidiary. Given that expatriate working and living in Saudi Arabia has a general reputation for being extremely challenging (Bradley 2015), MNEs may battle to entice suitably qualified Western nationals to take on assignments. In turn, this means that MNEs may make extensive usage of skilled managers from developing nations, who are more likely to be enticed by favourable pay rates (c.f. Mellahi and Wood 2001). However, developing country expatriates face particular challenges, which can range from petty discrimination to a greater likelihood of arbitrary expulsion (Bradley 2015; Mellahi and Wood 2011; c.f. Buhaini et al. 1996), and are likely to be particularly vulnerable to Saudization drives. Hence, whilst it may facilitate the decentralization of decision making for the reasons outlined above, it also brings with it real risks. The results thus prove the third hypothesis.

The fourth hypothesis states that the size of the subsidiary will positively relate to the extent of controls. The larger the size of the parent and subsidiary, the greater the degree of control exercised by the parent. Table 3 reports the results regarding the numbers employed in the subsidiary and its impact on four categories of controls. The results indicate that this seems to be the case as the coefficient is not only positive on account of all four control types but is also significant in the case of control by 'output' and 'informal' means. The results also show that the size of the parent has a significant positive influence too on all four categories of controls; the larger the size of the parent the greater the control exerted on its subsidiaries by all four means. The results thus support the fourth   hypothesis.

Additional Results

In addition to the results related to the testing of our hypotheses, Table 3 also reports further results in terms of 'ownership', 'age (number of years operating in Saudi)' and sector. The results show that majority-owned subsidiaries negatively influence all types of control; it seems that majority-owned subsidiaries have more delegated authority than is the case with other forms of ownership. For joint ventures none of the control mechanisms from HQ are shown to be significant. This could be owing to the simple fact that in joint operations duties and responsibilities may be equally shared. The age of the subsidiary (i.e. whether it has been established relatively recently or further in the past) does not seem to have any bearing on control mechanisms. Subsidiaries engaged in marketing and sales positively influence 'centralised' controls; the manufacturing sector views negatively 'informal' means of control. In assembly line businesses reliance seems to be more on controls by way of 'output' and 'informal' means. Assembly line businesses also negatively view control by 'centralised' methods. This makes sense as output, i.e. units assembled per worker or per shift, are easily counted, especially when the compensation is linked to output. Finally, in the service industry centralised controls predominate. This is explainable by the fact that policy and directives in the services sector are largely centrally formulated and also monitored by HQ.

Table 3: Regression results on control mechanisms

Independent variables	Centralized controls-PCC	Formal controls BFC	Output Controls-OC	Informal controls-IC
Dependent variables				
	Coefficient	Coefficient	Coefficient	Coefficient
Subsidiary Size, Expats, & Age				
1.Employees subsidiary	.488	.456	1.319**	1.314***
2.Employees worldwide	2.205***	2.009***	6.273***	4.905***
3.Expatriate numbers	-.097	-.047	-.206	-.423
4.Age	.002	.864	.389	.746
Industry				
5.Petroleum	1.586	2.082	1.636*	8.953***
6.Chemicals	-.934	-3.004*	1.597**	2.501*
7.Electronics & electrical	11.563***	-4.304**	1.538**	1.048
8.Motor vehicles	-.4.148**	13.751***	1.775**	8.934***
9.Food & beverages	-1.609	-18.169***	1.891***	-8.658***
Parent nationality				
10.Parent_GSN	-9.875***	.969	1.098	-2.919**
11.Parent_ALCA	-6.937***	1.515	-3.768*	-2.207**
12.Parent_DNSW	-6.201***	-.235	-11.067***	-2.084**
14. Parent_IT	1.963*	16.325***	-21.916***	-8.421***
13.Parent_JP	-10.689***	-11.670***	-10.787***	.928
15. Parent_SK	-19.680***	1.605	-8.146***	-5.072**
16 Parent_CH	-15.073***	-7.754***	-17.624***	-9.703***
17. Parent_MME	-2.166	9.209***	-1.484	2.198
Manager nationality				
18.Saudi nationals	-1.957**	2.073*	-2.702**	5.180***
19.Third country nationals	-7.746***	-16.240***	-12.467**	-10.589***
Subsidiary type				
20.Majority owned	-6.111***	-6.793***	-4.476***	-1.478**
21.Joint venture	-.540	-.143	-.399	-.308
Subsidiary function				
22.Marketing & Sales	4.964***	-2.407	-2.962*	-2.393
23.Manufacturing	1.867	1.691	.462	-8.725***
24.Assembly	1.832	-3.602**	12.952***	3.219**
25.Services	3.057**	-7.538**	-9.289***	-7.797***
Model Fitting Statistic				
-2 Log likelihood	429.743	227.137	205.580	380.605
χ2(21 dof)	280.310 (.000)	256.071(.000)	266.055(.000)	258.594(.000)
R^2 Cox and Snell	.85	.82	.83	.82

***p<.0.01; **p<0.05; *p<0.10

1=log subsidiary employment; 2=log employees worldwide; 3=log expatriates in subsidiary; 4=age of subsidiary; 5-9 are respective industries: petroleum, chemicals, electronics & electrical, motor vehicles, food & beverages; 10-17 are nationality of the parent: 10=Germany, Switzerland, Netherlands, 11= Australia, Canada, 12= Denmark, Sweden, 13=Japan, 14=Italy, 15=South Korea, 16=China, 17=Lebanon, Kuwait, Egypt, and Jordan; 18,19 represent the nationality of the HR director; 20-21 represent subsidiary type-majority owned or joint venture; 22-25 represent subsidiary function—22 marketing & sales, 23 manufacturing, 24 assembly, 25 services. No. 26-29 represent the type of control exercised.

Discussion

This study explores the relationship between country of origin, indigenization and control mechanisms exerted by of MNEs over their subsidiaries. Whilst some of the findings confirm   a wide base of existing knowledge, inter alia, encompassing the reliance on more formal methods of control in larger firms, we also find evidence of a proclivity of MNEs from highly financialized LMEs for greater control, possibly in order to more directly appease the demands of activist shareholders. In contrast, the existing literature suggests that the latter is   the case for

US MNEs, the study confirms that this is also so for British ones, highlighting the common ground between the two highly financialized LMEs. This is very different behaviour to those of MNEs from other LMEs, which have more in common with their CME peers. And, whilst there are strong government pressures to employ and advance Saudi nationals, existing research highlights the slow progress this may have made (Sadi and Al-Buraey 2009). What this study adds is that when firms do employ significant numbers of Saudi nationals, they appear not to be trusted: in such instances, the head office exerts tighter and more formal control. With regard to size, it seems that larger the organization, the higher the degree of control, probably because more is at stake. More specifically, output controls become progressively important as firms increase in size. At the same time, the level of autonomy and informal communication between the HQ and fellow subsidiaries decreases; this reflects the extent to which larger firms rely on more formalized and bureaucratic mechanisms of control, which, at the same time, allow for economies of scale (Brewster et al. 2007).

Firms can also exercise controls by means of non-measurable cultural bindings, commonly referred to as control by informal and social means (Ferner 1997). This may be attained by locating a sizeable number of managers from home within the subsidiary. However, we find that it is the usage of expatriates per se, rather than simply parent country nationals, that leads to greater autonomy. In other words, this difference cannot be explained by the usage of social or informal control mechanisms, as the expatriate managers did not originate from the same nation or cultural background. What appears to be the case is that firms simply trust host country nationals less. There are two possible explanations for this. The first is that, subsidiaries may primarily hire locals to meet Saudization requirements. Chronic shortfalls in technical training and a bias of tertiary education towards fundamentalist religious subjects, means that there is a shortage of suitably qualified locals, with firms responding through resorting to "window dressing", whilst making sure that important decisions are left to head office. A reliance on formal control mechanisms makes it easier to manage the aspirations of Saudi managers, creates an impression of equity between domestic and expatriate managers (as all are subject to the same rules and procedures), and reduces the chance of accusations of favouritism or discrimination. It may also reflect deeply embedded cultural stereotypes – and prejudices – widely held by outsiders in dealing with the Middle East, a reflection of specific colonial legacies and strategies developed towards the exploitation of the region's natural resources (see Said 2003); this may make for a mutually reinforcing cycle of mistrust, necessitating, but also worsened by, low levels of local autonomy.

Taggart and Hood (1999) suggest that higher autonomy in MNE subsidiaries makes for greater innovative capabilities. However, our study reveals that in the manufacturing and high technology sectors, direct control is greater. The former might simply reflect the present state

of Saudi manufacturing, geared towards standardized goods, manufactured through the usage of Taylorist methods. However, the latter might, again, indicate, a lack of trust, and the desire to protect proprietary knowledge (Buckley and Casson 1976; Richards 2000). We also find that controls are significantly less in majority-owned subsidiaries. MNEs which have been operating longer in the country are less likely to make usage of direct controls, probably indicative of a greater experience in navigating local waters, the operation of informal networks, and a more nuanced awareness of the signifiers of trustworthiness in local partners and staff.

Research Contributions, Limitations, and Extensions

The relationship between HQ and subsidiaries, and the degree of autonomy accorded to the latter is a very mature area of research. However, this is one of few studies of this nature conducted for the region of Middle East – and the only one we are aware of for Saudi Arabia
– and sheds new light on the impact of contextual circumstances on how closely firms monitor their subsidiaries. Our empirical work not only replicates earlier studies, retesting propositions encountered in the existing literature, but also sheds new light on the challenges of doing business in the Gulf region, and the consequences of the large scale usage of expatriates. .

The methodology adopted can be extended to other host countries. A useful extension would be to link different control mechanisms with the perceived and actual financial performance of subsidiaries. They can also be linked with the objectives and strategies of subsidiaries vis- à-vis HQ. In a multi-country study of this nature, it can be researched if inter-country differences exist between the control mechanisms of subsidiaries of the same parent operating in different host countries. Such a study would also account for the limitations of one-country studies, and shed further light on what really defines individual national settings.

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