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## Dynamic Capabilities, Absorptive Capacity and Knowledge Sharing: A Research Agenda into Explicating the Antecedent Factors Conducive to Subsidiary Bargaining Power

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# Dynamic Capabilities, Absorptive Capacity and Knowledge Sharing: A Research Agenda into Explicating the Antecedent Factors Conducive to Subsidiary Bargaining Power

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**DYNAMIC CAPABILITIES, ABSORPTIVE CAPACITY AND  
KNOWLEDGE SHARING: A RESEARCH AGENDA INTO  
EXPLICATING THE ANTECEDENT FACTORS CONDUCTIVE TO  
SUBSIDIARY BARGAINING POWER**

**(Competitive Paper)**

This research explores the relationship between relative absorptive capacity – a firm’s proficiency at acquiring, assimilating, transforming and ultimately exploiting knowledge – and subsidiary bargaining power. In building upon the existing dynamic capabilities framework it is advanced that absorptive capacity, as a mediator, serves not only as a valid dynamic capability but also as an enabling mechanism and a vehicle by which subsidiary bargaining power can be achieved. The antecedent factors conducive to building relative absorptive capacity are critically evaluated and built upon in a subsidiary specific context. The contribution of these new factors provides insight into the enabling constructs conducive to building absorptive capacity as a dynamic capability in the subsidiary context and are proffered as; *Strategic Posture*, *Network Inclusion*, and *Environmental Specific Factors*. It is also posited that a subsidiary which is capable of exercising considerable bargaining power can leverage this position by insulating themselves to some extent from the threat of mandate loss.

**DYNAMIC CAPABILITIES, ABSORPTIVE CAPACITY AND KNOWLEDGE  
SHARING: A RESEARCH AGENDA INTO EXPLICATING THE ANTECEDENT  
FACTORS CONDUCTIVE TO SUBSIDIARY BARGAINING POWER**

**INTRODUCTION**

The extant literature on subsidiaries is founded largely on analysing autonomy and knowledge flows (Argote and Ingram 2000; Harzing and Noorderhaven 2006; Meyer, Wright and Pruthi 2004). The means by which a subsidiary is controlled and the extent of this control continues to constitute a significant area of research within the field of MNC management (Dunning 1995; Gupta and Govindarajan 1991). There appears however to be little attention paid to the potential bargaining power of subsidiaries post start-up, with some notable exceptions (Mudambi and Navarra 2004). This omission fails to recognise the relative power assumed by certain subsidiaries within the hierarchical structure. It is suggested that increased operational responsibilities for the subsidiary within the MNC network ‘have loosened the traditional hierarchical structure of MNC governance’ (Mudambi and Navarra 2004, p.386). This, it is argued, has implications not only upon the potential sustainability of the subsidiary, but also on their efforts in vying for the continued extension of mandates. There remain concerns however in establishing where this bargaining power is derived from and what are the factors conducive to its creation?

It is in response to this question that absorptive capacity is advanced as a factor which may be particularly insightful. The concept of absorptive capacity has progressed significantly since the seminal work of Cohen and Levinthal (1990). Their original concept encapsulated a firm’s ability to recognise the value of new, external information, assimilate it and then apply it to commercial means. Prompting the application of this concept as more

than a firm-level construct, Lane and Lubakin (1998, p.473) further develop the theory in terms of *relative* absorptive capacity and through acknowledging how ‘firms are increasingly relying on knowledge acquired from other firms to facilitate the development of their own capabilities’. This recognised need to continuously adapt, reconfigure and develop capabilities mirrors the integral features of the emerging dynamic capabilities framework (Teece 1997; Zollo and Winter 2002) providing a new lens through which absorptive capacity can be examined. With its roots in the resource based view (RBV) of the firm, the dynamic capability framework resolves to explain how firm’s can continuously evolve through responsive modifications made to their resource bases.

Indeed, recent scholars have touched on absorptive capacity as a dynamic capability (Zahra and George 2002) in an extension of the original concept. The established tenets of absorptive capacity creation are proffered as *knowledge acquisition, assimilation, transformation and exploitation* (Zahra and George 2002). This is upheld in recognising how the exploitation of new knowledge through absorptive capacity facilitates the flexibility needed to compete in dynamic and changing environments (Ambrosini and Bowman 2009).

In this paper, these factors, as explanatory variables, will act as a platform by which absorptive capacity can be examined. In contributing to existing knowledge, three additional categories are also included in capturing the characteristic features conducive to dynamic capability creation in a subsidiary specific context. These categories comprise of *Strategic Posture, Network Inclusion and Environmental Specific Factors*. It is contended, absorptive capacity, as a dynamic capability and as a mediating construct, will shed light not only on the potential bargaining power, or *voice* (Bouquet and Birkinshaw 2008) of a subsidiary but also into the potential for strategic learning within the firm (Anderson, Covin and Slevin, 2009).

This paper takes the format of a research agenda. The absorptive capacity (ACAP) literature is re-visited through the lens of its application as a valid dynamic capability (DC).

The antecedent factors conducive to ACAP creation are discussed and critically evaluated in a subsidiary context. The literature germane to the DC framework is then addressed, in clarifying the framework; presenting it not only as a tangible concept but also one which is constructive in subsidiary development. Finally the emerging bargaining power concept is examined as a potential outcome of absorptive capacity with suggestions for future research in this area.

### **ABSORPTIVE CAPACITY AS A DYNAMIC CAPABILITY**

Cohen and Levinthal's (1990) seminal work encapsulated a firm's ability to recognise the value of new, external knowledge information, assimilate it and then apply it to commercial means. With an emphasis on cognitive abilities; 'the premise of the notion of absorptive capacity is that the organization needs prior related knowledge to assimilate and use new knowledge' (Cohen and Levinthal 1990, p.129). The absorptive capacity of a firm is not merely the sum of its employees absorptive capacities but also reliant upon; 'transfers of knowledge across and within subunits' (Cohen and Levinthal 1990, p.129). In response to this a notable advance in theory is Lane and Lubakin's (1998) discussion of *relative* absorptive capacity. This adaptation of absorptive capacity, through establishing a *relative* differential; provides a useful lens by which subsidiary specific factors can be analysed. The *relative* aspect of their study incorporates the idiosyncratic characteristics of both the receiving and diffusing units, and in particular the relationship between their knowledge processing systems.

In acknowledging subsidiary specific factors the shared and uniform characteristics of the MNC will likely dictate how knowledge is assimilated thus bearing influence on its utility. Further to this the distinction between potential and realised ACAP, with explicit

implications for the leveraging of capabilities, is one which is addressed in the literature (Minbaeva et al. 2003; Zahra and George 2002). In contending that the structural drivers for the rationalisation of a MNC are based upon synergistic returns, leveraging of economies of scale and differences in competitive advantage (Birkinshaw, Morrison and Hulland 1995) and the leveraging of shared firm specific resources (Rugman and Verbeke 2001) the concept of absorptive capacity is of pivotal concern. It is thus argued that for the MNC to affectively utilise its capability base it must facilitate the articulation and codification of learning mechanisms within the firm (Zollo and Winter 2002). This it is argued, in conjunction with developing the capacity for units to diffuse these processes within the collective MNC, demonstrates the dynamic tenets of absorptive capacity.

Before proceeding however, it is necessary to clarify the DC framework. In addressing and easing current concerns within academia regarding structural inadequacies, tautologies and unclear definitions the theoretical framework of DC's will be presented not only as tangible, but also as a constructive and responsive means by which the subsidiary can protect, enhance and leverage their position within the collective MNC network.

### **Dynamic Capabilities, What Are They?**

Strategic management theorists and practitioners have long acknowledged the role of scarce and difficult to replicate assets in creating competitive advantage (Ansoff 1979; Barney 1991; 1995; Hofer and Schendel 1978). Indeed it has been largely accepted that the potential for sustainable competitive advantage lies in a firm's heterogeneous resource configuration (Barney 1991). It is claimed however that this static view fails to explain how future valuable resources can be created or refreshed and thus cannot explain why some firms can consistently earn above normal profits in equilibrium (Ambrosini and Bowman 2009). In conceding how 'both superiority and viability will prove transient for an organization that has

no dynamic capabilities' (Zollo and Winter 2002, p.341) it is arguably the DC perspective which attempts to resolve these issues.

In the extant literature the benefits of building DC's has thus far overshadowed an empirical need to establish what factors influence their very creation and assessing the tangibility of this process. In addition, it also needs to be addressed what exactly constitutes a dynamic capability; and how this modification of the resource base differs from mere ad-hoc problem solving. It is partially in resolving these issues that this paper is presented. The purpose is thus one of inquiry, extension and evolution of the DC framework. The capacity of the subsidiary to absorb, assimilate and transfer knowledge is advanced as a foremost area of analysis and as a valid dynamic capability. The importance of outlining the antecedents of dynamic capabilities constitutes an imperative gap if the emerging DC framework is to be constructive in any practitioner capacity. In adopting the subsidiary as the unit of analysis a theoretical framework is proposed in ascertaining how the unit can build DC's and in explicating the antecedent factors in this development process.

It is emerging that to meet the exacerbating challenges of fast moving, globally competitive markets, MNC's need unique and difficult to replicate DC's. The need to move to higher value added services is imperative for subsidiaries operating in open and exposed environments. This charge is further exacerbated amid concerns over increased economic turbulence globally. It is argued that in this turbulent context DC's can be harnessed to 'continuously create, extend, upgrade, protect and keep relevant the enterprise's unique asset base' (Teece 2007, p.1319). Essentially comprising of the technological, organisational and managerial processes that firms leverage to achieve sustainable competitive advantage, DC's continuously integrate knowledge in developing new organisational capabilities (Jacobides and Winter 2005).



A distinction must be made however between operational, organisational and higher level capabilities (Winter 2003) and defining what exactly constitutes a DC. This particular aspect of DC theory has seen considerable debate within the literature (Helfat and Peteraf 2003; Winter 2003; Newey and Zahra 2009; Pandza and Thorpe 2009). In illustrating the distinction between operational and dynamic capabilities Helfat and Peteraf (2003) contend that operational capabilities are high level routines used in a repetitive fashion in the production or performing of an activity. These capabilities essentially incorporate the distinguishing operational functioning of the unit allowing it to earn rents. It is held that operational capabilities as a patterned behaviour differ from mere ad-hoc problem solving, which merely equates to a once off idiosyncratic change to the resource base (Helfat et al. 2007). Similarly Winter (2003) discusses organisational capabilities as a collection of routines, highly patterned and repetitious or at least quasi-repetitious. It is in the sense that a capability must be repeatable and patterned which can cause some ambiguity. Newey and Zahra (2009) somewhat clarify this haziness in contending that whilst exogenous shocks can turn patterned routinisation into a rigidity and a source of inertia, it is the ability of the firm to reconfigure its operating capabilities that constitutes a DC. It is this distinction between routines and capabilities that forms a focal part of the DC framework. In recognising the dangers of core competencies turning into core rigidities (Leonard-Barton 1992) it is arguably the DC framework that can mitigate such concerns through the firm's ability to adapt and reconfigure its capabilities. This is facilitated through developing the 'capacity with which to identify the need or opportunity or change, formulating a response to such a need or opportunity, and implement a course of action' (Helfat et al. 2007, p.2).

With the scope of producing potentially value creating strategies, it is argued the DC framework must utilise current resources whilst simultaneously adapting, integrating and developing new areas of competencies. This is outlined as combining the 'antecedent

organisational and strategic routines by which managers alter their resource base- acquire and shed resources, integrate them together, and recombine them' (Eisenhardt and Martin 2000, p.1107). The integration and reconfiguration of resources is thus an imperative response to recognising the need for change brought about through exogenous threats or opportunities in the external environment and for adaptive learning within the firm. Zollo and Winter (2002) discuss the development of DC's in similar terms contending they are created through learning processes in the operational functioning of the firm, which they refer to as operating routines; whilst the adaption of such routines constitutes the dynamic capability.

An emerging consensus therefore is that DC's are significantly distinct from ordinary or operational capabilities. In summary it can be held that ordinary capabilities allow the firm to earn rents, whereas DC's continually operate to modify, extend or further capabilities (Winter 2003). It is conceded that in turbulent environments above normal rents are transitory and subject to exogenous change and competitor efforts. In allowing the subsidiary to actively respond and engage with change; the potential for competitive advantage, albeit transitory, is arguably more attainable as is the ability to earn Ricardian rents. The renewing nature of DC's as a relative differentiating factor among subsidiaries is thus a significant factor in illustrating the value of the concept.

### **What Constitutes a Dynamic Capability?**

The extant literature provides varying examples of capabilities which can be termed as *dynamic*. These include managerial cognition with its emphasis on directing learning efforts and the heterogeneous nature of managerial decision making (Adner and Helfat 2003; Pandza and Thorpe 2009; Tripas and Gavetti 2000). Such capabilities are perhaps most relevant in combating inflexibility. This is facilitated through deviations from current project trajectories

where exogenous changes are perceived as relevant and force adaptation by the firm (Pandza and Thorpe 2009).

Another emerging field of research is based upon dynamic marketing capabilities (Bruni and Verona 2009; Cavusgil, Seggie and Talay 2007; Danneels 2002; Malik and Kotabe 2009). The bridging of the cognitive abilities of management with marketing acumen can be seen in considering how; 'capabilities, unlike resources, are based on developing, carrying, and exchanging information through the firm's human capital' (Cavusgil, Seggie and Talay 2007, p.160). In utilising this human capital it is held that market knowledge in its creation and diffusion may benefit the business unit through fostering new product development processes (Bruni and Verona 2009). In drawing upon Eisenhardt and Martin (2000) who contend that dynamic capabilities can shape environmental change as opposed to merely responding to it; the scope for dynamic marketing capabilities is particularly evident. This is observed in Danneel's assertion that the adaptive firm should not merely focus on its current customer base but also invest in exploring new market segments which offer potential allowing; 'firms to mitigate path dependencies in their development, escaping from the trap laid by their current competencies' (2002, p.1097).

A third and final emerging area of research concerns acquisition based dynamic capabilities (ABDC), alliances and divestment capabilities. In acknowledging how DC's are path dependent (Teece 1997; Zollo and Winter 2002; Kor and Mahoney 2005 and Newey and Zahra 2009) the ability to acquire relevant resource bases which complement existing trajectories may be easier and less costly than building these capabilities internally. In their research on acquisitions Zollo and Singh (2004) illustrate how pre-acquisition routines can be patterned, ensuring greater integration, fit and ultimately leading to increased performance. This builds upon Zollo and Winter's (2002) paper which emphasises how the ability to effectively execute post-acquisition integration processes constitutes a dynamic capability.

For an extensive discussion on resource acquisition, alliances and acute divestment capabilities see Helfat et al. (2007).

The three preceding kinds of capabilities, although not exhaustive, are reflective of the current direction of work on contrasting types of dynamic capabilities. This typology will now be built upon with the addition of ACAP as an area of analysis and as a valid DC.

## **ANTECEDENTS OF ABSORPTIVE CAPACITY AS A DYNAMIC CAPABILITY**

It is proposed that in following an emerging consensus on the recognition of ACAP as a DC the significant antecedents of this capability creation process can be verified and refuted. As informed by the literature, ACAP is built upon the foundations of *knowledge acquisition, assimilation, transformation* and *exploitation* (Zahra and George 2002). Individually each of these factors will now be addressed before illustrating the contributions of this paper to existing knowledge.

*Knowledge acquisition*, the ability to acquire new and relevant knowledge is arguably contingent upon knowledge flows within the MNC. It also incorporates externally sourced knowledge which is critical to subsidiary operations (Zahra and George 2002). Knowledge relevance theory provides insight into the acquisition process where *relevance*; ‘is a term used to describe how pertinent, connected, or applicable some information is to a given matter’ (Yang, Mudambi and Keyer 2008, p.884). This applicability is of particular importance in ensuring a good fit given the resources expended in the acquisition and ultimate absorption of knowledge.

*Knowledge assimilation* encompasses the capacity to interpret and grasp information, to understand its application and the processes from which it is derived. The comprehension

of this knowledge is essential if it is to be internalised, and is thus likely a function of the firms pre-existing stock of knowledge (Dierickx and Cool 1989). Further to this, *internal stickiness* (Szulanski 1996), the extent to which the knowledge is embedded in its source will also dictate the ease or difficulty at which the knowledge can be assimilated. The factors of *knowledge acquisition* and *assimilation* form the basis of *potential* absorptive capacity, yet as delineated by Zahra and George (2002, p.191), whilst ‘firms can acquire and assimilate knowledge but might not have the capability to transform and exploit the knowledge for profit generation’. This now paves the way for us to consider the factors conducive to *realised* absorptive capacity.

*Transformation* involves the conversion and refinement of knowledge to suit the unit’s own idiosyncratic needs. The internalisation of this knowledge is achieved whilst also making the relevant modifications in accordance with their own distinct needs. Partially a learning process, Lane and Lubatkin (1998, p.464) provide insight into how knowledge can be absorbed and transformed using a dyadic student-teacher typology where; ‘student firms have the greatest potential to learn from teachers with similar basic knowledge but different specialized knowledge’. This is grounded in the existing capabilities and path dependencies of the student firm. In building upon their prior experience and proven capabilities the student firm is in a better position to readily internalise this knowledge and adapt it in accordance with their own requirements. The tenor of pre-existing knowledge stocks (Dierickx and Cool 1989) is again acknowledged where; ‘the ability of firms to recognize two apparently incongruous sets of information and then combine them to arrive at a new schema represents a transformation capability’ (Zahra and George 2002, p.190).

*Exploitation* of knowledge, the final component and one which encompasses the realisation of ACAP, concerns the processes by which newly absorbed capabilities can be leveraged. Minbaeva et al. (2003) contend that organisational practices, and in particular

employee ability and motivation are key aspects in the exploitation process. The existing literature on managerial cognition acknowledges how non-technological assets, such as managerial aptitudes can influence the direction of technology trajectories and the exploitation of capabilities (Dosi 1982). It can also be claimed that where lacking; managerial cognition can equally be contributed to organisational inertia (Tripas and Gavetti 2000). The importance therefore of actually realising the exploitation of knowledge is of pivotal concern. This is likely facilitated through intensive scanning of the environment, recognising potential opportunities and ultimately in leveraging the resources necessary to exploit them (Barringer and Bluedorn 1999).

In contributing to existing knowledge, three additional categories are also included in capturing the characteristic features conducive to dynamic capability creation in a subsidiary specific context. These categories comprise of *Strategic Posture*, *Network Inclusion* and *Environmental Specific Factors*.

*Strategic Posture*; essentially examines the position of the subsidiary in assessing their assumed role within the collective MNC. Typologies range from the dichotomy of exploitation versus exploration (March 1991) to differentiating between the subsidiary motives of market-seeking, resource-seeking, efficiency seeking and strategic asset seeking as the basis for subsidiary deployment and development (Dunning 1993). Perhaps, more succinctly Gupta and Govindarajan (1991) differentiate between subsidiaries on the basis of whether they are net users or providers of knowledge; thus encapsulating a firms ability to continuously add value to the firm. This conceptualisation of the firm as a knowledge creating entity continues to gain recognition within academia (Nonaka, Toyama and Nagata 2000; Nonaka and Toyama 2005) building upon Ghoshal and Bartlett's (1988) linear model of knowledge creation, adoption and diffusion within the firm.

It is argued that a subsidiary which continues to provide new and relevant knowledge, codify this knowledge and ultimately diffuse it throughout the collective MNC is positioned in a more favourable hierarchical space than the subsidiary which is merely exploiting a local market under standardised mandates imposed by headquarters. In accordance, the distinction between a subsidiary engaging in adding value through *receptive strategies* (Jarillo and Martinez 1990) facilitated through a high degree of integration and those who add value through lower cost manufacturing contributions to the value chain are reflective of the contrasting subsidiary roles.

These contrasting roles, in dictating if a subsidiary is a net user or provider of knowledge will likely have an impact on their ability to absorb new knowledge. It is thus concluded that on the basis of their existing knowledge reservoirs (Argote and Ingram 2000; Miller and Chen 1996) and strategic orientation, subsidiaries likely sway towards one of following two typologies. Those that are capable of exhibiting the dexterity needed to absorb knowledge and utilise it to its full potential through their entrepreneurial orientation (Anderson, Covin and Slevin 2009) or those that lack such a capacity.

*Network Inclusion*; the potential for intra-organisational relationships to foster learning within the MNC is upheld in the literature (Edstrom and Galbraith 1977; Harzing 2001). In conceptualising the MNC as a differentiated network of dispersed operations with subsidiary specific advantages (Rugman and Verbeke 2001) the potential for learning is further exacerbated where differentiated capabilities can be assimilated. The leveraging of knowledge from dispersed subsidiaries is credited with paving the way for competitive advantage (Gupta and Govindarajan 1991; Mudambi 2002; Yang et al. 2008) yet the ability to tap into these knowledge reservoirs (Argote and Ingram 2000; Miller and Chen 1996) is arguably conditional upon network inclusion and subject to inclusive knowledge flows. It is

thus proposed that a measure of network inclusion be considered in incorporating headquarter-subsidary and intra-subsidary relationships, and establishing if this equates to increased or reduced access to collective firm resources. The inclusion of socialisation aspects such as frequency of intra-organisational communication should also be analysed, as should the extent of codified knowledge (Zollo and Winter 2002) available and potential access to this codified knowledge.

A second feature of *Network Inclusion* is based upon *Proven Capabilities*. It has been addressed how dynamic capabilities are path dependent, a view which is widely supported in the literature (Teece 1997; Zollo and Winter 2002; Kor and Mahoney 2005 and Newey and Zahra 2009). Indeed, on addressing the future potential for a firm, Teece et al. (2004, p.17) hold that 'where it can go will, however, be a function of where it has been'. The concept of *proven capabilities* is advanced as a factor which encompasses a subsidiaries historic progress, its credibility and recognition within the collective MNC. Yang, Mudambi and Keyer (2008) address how reverse knowledge flows, as distinct from the conventional headquarter-subsidary flows can result in increased recognition for the subsidiary. Birkenshaw, Hood and Jonsson (1998) discuss subsidiary specific advantages, whilst Frost, Birkinshaw and Ensign (2002) refer to centres of excellence within the MNC. All of these factors, although disparate in their phrasing have strikingly similar outcomes; they position the subsidiary in a favourable light within the MNC on the basis of their proven capacity to create value. With this increased recognition comes greater access to collective firm resources. Mudambi and Navarra (2004) maintain that the subsidiary which is closely linked to international networks is in a better position to leverage these collective resources which ultimately culminates in increased knowledge accessibility. The ability to build upon *proven capabilities* and basic collective firm knowledge combined with specialised knowledge sourced internally within the organisation epitomises the very criteria of relative absorptive



capacity (Lane and Lubakin 1998). In building upon their prior experience and *proven capabilities* the subsidiary is in a better position to readily internalise this knowledge, adapt it in accordance with their own requirements and ultimately diffuse within the organisation. In demonstrating the benefits of *proven capabilities*, Birkenshaw (1996) has shown, empirically, that *proven capabilities* as a relative differential, act as a significant factor in dictating if subsidiary mandates are maintained or further developed. It can thus be held that *proven capabilities*, acting as a significant antecedent to absorptive capacity can prompt the further development of firm specific competencies in accordance with the very criteria of dynamic capabilities as delineated by Teece and Pisano (1994).

*Environmental Specific Factors*; as a final construct, must also come into consideration when assessing not just the market in which the subsidiary competes but their potential to build ACAP. The need to distinguish between moderately dynamic markets and high velocity markets is one which is expressed in the literature (Eisenhardt and Martin 2000). It is held that in high velocity markets there is an imperative need to develop higher order capabilities, capable of continual value creation. These higher order capabilities are characterised by experimental processes in which the subsidiary must unify their own prior knowledge with new assimilated knowledge in direct response to the demands of the environment in which they operate. An example of the latter is illustrated in the high technology sector where *Yahoo!* sought to continually revive their transient competitive advantage through regenerative capabilities, or *continuous morphing* on the internet, (Rindova and Kotha 2001). The need for change in such a sector is arguably more prevalent, as evidenced by rapid changes in technology. This is in contrast to moderately dynamic environments where it is argued that a firm too adaptive and responsive to the market may fail to offset the costs of developing DC's if their costs exceed the benefits gained, (Eisenhardt and Martin 2000). It is

thus held that environmental factors will have a bearing on both the extent of new knowledge absorption necessary and in ensuring that the process is economically viable. Environmental factors are thus advanced as an essential control variable in examining how subsidiaries can build ACAP.

The proceeding sections have addressed the concept of ACAP, clarified the DC framework and presented a well grounded synthesis of both these frameworks in the advancement of absorptive capacity as a valid dynamic capability. This fulfils the first function of this paper. The section that follows assesses the impact ACAP in its implementation, as a relative differential, may have on the subsidiary's operations. Through assessing casual relationships, it is claimed that ACAP may be the enabling mechanism by which subsidiary bargaining power can be achieved. The literature germane to bargaining power is advanced, as is an analysis of control systems which stem from the corporate governance literature (Williamson 1981). In claiming how a cross-fertilization approach is favorable to studying what happens at MNC levels of management, and acknowledging how; 'many, if not all, scholars of MNC management have underexploited the theories available to them' (Doz and Prahalad 1991, p.161) a multifaceted research approach is proposed. By incorporating both existing subsidiary theory and the DC framework it is suggested that a valuable contribution to theory on subsidiary level intra-unit bargaining, differentials and the effective leveraging of collective resources may be achieved.

## **A SYNTHESIS OF SUBSIDIARY BARGAINING POWER AND ABSORPTIVE CAPACITY**

Recent literature identifies how the internationalization of R&D has resulted in considerable tension among subsidiary units of many MNCs. It is argued that intra-unit competition can

impede knowledge flow processes with aspects of opportunism becoming apparent. This has been attributed to rent-seeking subsidiary managers acting in their own myopic interests (Mudambi and Navarra, 2004). In such a scenario managers act in the interest of the domestic unit, with the collective MNE incurring a subjacent focus, as ‘opportunism makes provision for self-interest with guile’ (Williamson 1981, p.554). It is thus held that self interest can mitigate the potential for knowledge transfer and diffusion of firm specific capabilities within the collective MNC network.

The recent work of Mudambi and Navarra (2004) identifies this dilemma and suggests that subsidiary units can distinguish themselves from their sister units through strengthening their bargaining power. Interestingly, it is suggested that the bargaining power of subsidiaries is not merely attributed to financial metrics but in terms of the potential for leveraging of intangible knowledge stocks and flows. (Mudambi and Navarra 2004; Asakawa 2001) This echoes the work of Dierickx and Cool (1989) who emphasize the role of unique asset stock bases, capable of differentiating the subsidiary; ultimately enabling them to leverage their position within the collective MNC.

Further to this the role of corporate governance structures (Williamson 1981) and agency theory as a ‘testable perspective on problems of cooperative effort’ Eisenhardt (1989, p.72) are gaining prevalence as a means of understanding how organisational decision making is shaped at the subsidiary level. In a similar manner to opportunism, agency theory attempts to provide insight into issues of autonomy using a dyadic principal-agent approach. Such a perspective essentially presents the subsidiary as a mere implementer of headquarter driven mandates; which potentially limits their scope for opportunity development due to *risk aversion* (Eisenhardt 1989; Grossman and Hart 1986). However, as observed by O’Donnell (2000, p.541) ‘the simplicity of the dichotomous choice between monitoring and incentives posited by agency theory prevents it from addressing more complex combinations of control

types'. The importance of control types is upheld in this paper as a fundamental feature in any analysis of a subsidiary's strategic mobility. In accordance, control as an integral feature of bargaining power is discussed.

### **Control Types**

Control types are frequently cited as a major determinant of subsidiary flexibility in operations and autonomy (Dunning 1995; Gupta and Govindarajan 1991). It is arguably through addressing complex control types and through acknowledging the move towards a more profound involvement by the subsidiary unit; that a more interdependent, rather than dependent position of the subsidiary can be examined (Pearce 1999). This is illustrated in the typologies of subsidiaries presented by Dunning (1995) where differences in external orientation and R&D capabilities are recognized as focal subsidiary differentials and thus reflective of more complex control mechanisms imposed by the parent.

Gupta and Govindarajan's perspective supports analysing subsidiaries through control types, recognising that 'differences are likely to be reflected in the mix of formal and informal administrative mechanisms that corporate headquarters might utilize to shape the decisions and actions of various subsidiaries' (1991, p.769). It is thus proposed that an analysis of both subsidiary *bargaining power* (Mudambi and Navarra 2004) and *voice* (Bouquet and Birkinshaw 2008) is inextricably linked to examining how control mechanisms are shaped, and ultimately in ascertaining their determinants.

In considering the importance of control systems and the consequent flexibility of operations achievable it has been illustrated how it is crucial for the subsidiary to assume the role of a net provider of knowledge as opposed to a net receiver. Gupta and Govindarajan (1991) analyse this along the dimensions of the extent to which a subsidiary is a user of knowledge, and the extent to which they are capable of imparting knowledge to the rest of the corporation. This is likely an emergent process where the subsidiary gains recognition over

time as a valued contributor to the collective MNC. In drawing upon Mintzberg and Waters (1985) and considering control in the subsidiary context ‘the ability to leverage resources and competencies allows a firm to take advantage of strategic decision making in order to develop distinct competencies’ (Sinkovics and Roath 2004, p.45). This observation provides support for examining how regenerative DC’s can be developed. In acknowledging how subsidiaries can influence strategic decisions, the leveraging of current capabilities as a bargaining mechanism in this process may provide insight into the cyclical nature of the development of further capabilities. The contention that the ‘voice of a subsidiary becomes increasingly important as a means of capturing attention when the subsidiary is at risk of strategic isolation’ (Bouquet and Birkinshaw 2008, p.578) further presents a potential avenue of inquiry in examining the impact that DC’s in their implementation have on this *voice*.

In considering if subsidiary *bargaining power* and *voice* are contingent upon autonomy, it can be hypothesised that a lack of autonomy or imposed control as a decision of the parent, may be mitigated through the possession of intangible capabilities. Thus the focus is not merely on the creation of DC’s but in the leveraging and reconfiguration of existing capabilities as bargaining chips. The rationale for the development and adaption of current capabilities as opposed to the creation of new ones is grounded in interpreting the work of Ghoshal and Bartlett (1988) as supportive to this approach. In acknowledging how the diffusion of capabilities and processes can be plagued by the *Not Invented Here* (NIH) syndrome in addition to intra-unit tensions it is perhaps more astute for the subsidiary to develop current capabilities along existing trajectories as a differentiating factor for the firm rather than try to integrate, upgrade or replicate processes from sister subsidiaries. This is essentially where the role of path dependencies plays a pivotal role. In pertaining to the path dependency school of thought and in emphasising how firm evolution is non-stochastic, Helfat et al. (2007, p.100) are quite unyielding in claiming; ‘as in evolutionary economics,

which underpins much of the logic of dynamic capabilities, firm evolution and change is non-random and depends on prior history’.

### **Path Dependencies**

In taking the stance that DC’s are path dependent (Teece and Pisano 1994; Teece, Pisano and Shuen 1997; Teece 2007; Helfat and Peteraf 2003; Zollo and Winter 2002) it is suggestive that the possession of such capabilities which cannot be easily imitated may present a viable platform for the subsidiary to protect and enhance their position within the collective MNC. This is also likely to ease headquarter concerns over the distribution of financial resources as the foundations of capability creation are already in place. In illustrating how this leveraging of project trajectories can be achieved, the seminal work of Coase (1937) can be interpreted as supportive of the role and extent of the potential bargaining power of subsidiaries in contending; ‘that which distinguishes an agent from its servant is not the absence or presence of a fixed wage or the payment only of commission on business done, but rather the freedom with which an agent may carry out his employment’ (Blatt, Cited in Coase 1937, p.404).

Bouquet and Birkinshaw (2008) contend that the attention a subsidiary receives, or their *voice*, in conjunction with their bargaining power is more subjective and thus less stable than a subsidiary’s strategic role. In response to this and in acknowledging how firms must continuously reaffirm their commitment to the MNC headquarters, the potential for adopting a DC approach is further accentuated. This reaffirmation of capabilities may take the form of dynamic processes that contentiously morph and adapt (Rindova and Kotha 2001) in accordance with the need for change and exogenous forces. The role of up-stream competencies (Mudambi and Navarra 2004) and the corresponding attention and recognition gained from their implementation arguably positions the subsidiary in a more favorable space within the MNC hierarchal structure. Further to this, the potential for strategic learning, as a

casual result from experimental and innovative processes undertaken is arguably another consequence. This is resultant from a 'firm's proficiency at deriving knowledge from past strategic actions and subsequently leveraging that knowledge to adjust firm strategy' (Anderson, Covin and Slevin 2009, p.219).

## **CONCLUSION AND SUGGESTIONS FOR FURTHER RESEARCH**

In concluding, it has been delineated how a subsidiary which is capable of exercising considerable bargaining power can leverage this position by insulating themselves to some extent from the threat of mandate loss. This favored position, it is posited, is dependent on their ability to build absorptive capacity as a mediating factor. Through the enabling factors of *knowledge acquisition, assimilation, transformation* and *exploitation* in conjunction with subsidiary specific constructs of *Strategic Posture, Network Inclusion* and *Environmental Specific Factors* the potential to exercise considerable bargaining power is arguably more attainable.

Theoretical in nature, the constructs developed in this paper require empirical testing in verifying or refuting these causal effects. Further avenues of inquiry could incorporate the HQ perspective; in examining if subsidiary bargaining power created through delivering DC's creates an effective barrier to knowledge sharing within the MNC? If such a scenario is likely to impede knowledge flows within the MNC, what internal processes can be utilised in mitigating this safeguarding of power?

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