

# Localization of Human Resource Management Practices in China: A Qualitative Comparative Analysis Approach

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Wei Lu



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Localization of Human Resource Management Practices in China: A Qualitative Comparative Analysis Approach

**Publisher** Aalto University School of Business**Unit** Department of Management Studies**Series** Aalto University publication series DOCTORAL DISSERTATIONS 6/2014**Field of research** International Business, International Human Resource Management**Abstract**

The purpose of this study was to investigate under what combinatorial factors of institutions and power relations within the multinational corporation (MNC), localization of human resource management (HRM) practices occurs. I conceptualize localization as modifications of headquarters-transferred practices that foreign subsidiaries undertake to respond to the local environment. By incorporating a power perspective into institutional theory, I aim to advance institutional analysis of practice transfer in a configurational manner.

I conducted a multiple case study with thirteen subsidiaries that were operating in China and owned by Finnish MNCs. Qualitative Comparative Analysis (QCA) was applied as a research approach and crisp-set QCA as an analytical tool to the case study. The configurational nature of QCA and its ability to draw causality while keeping some degree of causal complexity are well suited to investigate the research phenomenon. A key contribution of the present study is the very configurational explanation that sheds light on why and how various constellations of institutions and headquarters-subsidiary power relationships lead to localization of HRM practices. The configurational explanation captures the specific context of practice transfer from a developed market economy to a transition economy. Moreover, this study applies QCA at the micro-level analysis which is a novel approach in International Business research.

I specified four causal conditions: labour market mobility, location, monitoring by headquarters and strategic role of subsidiary. The localization of compensation as an HRM practice resulted from the combination of these four conditions with pressure from high labour market mobility, unattractive location of the subsidiary, weak monitoring by headquarters and the strategic role of the subsidiary. No single factor alone played a decisive role. Further, four different configurations that led to localization of compensation were identified, highlighting alternative pathways to achieve the same outcome. The study demonstrates that while institutional differences between host and home country induced the need for localization, power relationships between headquarters and subsidiary also played an important role. The combined effect explains why a practice is either localized or standardized.

The study shows a high propensity to transfer of compensation and performance management practices from Finland to China among the Finnish MNCs. However, the subsidiaries were generally rather loosely monitored by their headquarters, reflecting the relatively decentralized management style employed. The study also provides up-to-date empirical evidence that high labour mobility in China is a significant driving force for localization. Similarly, an unattractive location increases the need for localizing corporate practices, which demonstrates the importance of sub-national institutions in China. Furthermore, the rapid changes of values and the growing heterogeneity of the Chinese workforce call for localization of HRM practices.

**Keywords** localization, practice transfer, human resource management (HRM) practice, Qualitative Comparative Analysis (QCA), crisp-set QCA, subsidiary, multinational corporations (MNCs), China, Finland

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Hyvinkää, Finland, December 2013

Wei Lu



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# List of Abbreviations

CMEs	coordinated market economies
csQCA	crisp-set Qualitative Comparative Analysis
fsQCA	fuzzy-set Qualitative Comparative Analysis
FDI	foreign direct investment
HR	human resource
HRM	human resource management
HQ	headquarters
IB	International Business
IM	International Management
JV	joint venture
LMEs	liberal market economies
MNC	multinational company
NBSs	national business systems
QCA	Qualitative Comparative Analysis
SOE	state-owned enterprise



# 1. Introduction

## 1.1. The Research Domain

Standardization versus localization is a distinctive line of enquiry in the field of international human resource management (HRM) (Jain, Lawler and Morishima, 1998; Morley and Collings, 2004; Pudelko and Harzing, 2007; Rosenzweig, 2006). The debate on standardization versus localization is rooted in the global integration and local responsiveness framework which was originally put forward by Doz, Bartlett and Prahalad (1981). They argue that multinational companies (MNCs) encounter two forces, which are often viewed as competing: the imperative to pursue a coherent global strategy on the one hand and responding to the diverse demands of local markets of different countries on the other hand. Bartlett and Ghoshal (1989) assert that MNCs face the challenge of having to achieve global integration and local responsiveness simultaneously. They further show that business divisions, functions and tasks within an MNC face the similar dual forces. In the HRM context, global integration can be viewed as a driving force for standardization and the host country environment generates needs for local adaptation. Thus, it is argued that HRM practices are shaped by the dual pressures for internal consistency and local adaptation (Evans, Doz and Laurent, 1989).

In mainstream international business literature, localization versus standardization has mostly been examined in terms of a subsidiary's resemblance to local HR practices versus resemblance to parent HR practices. Most studies in this stream of research do not explicitly deal with practice transfer from the parent to the subsidiary abroad. The interest of this study is in localizing the HRM practices that are transferred from HQs of MNCs to their foreign subsidiaries. The focus is on the transferred practices. The key concern

is what factors in their combinatorial forms contribute to localization of transferred practices.

A number of factors have been put forward to explain transfer of HRM practices within the MNC. Institutional explanations have received considerable attention in recent years (see, e.g., Ferner, Almond and Colling, 2005; Tempel, Edwards, Ferner, Muller-Camen and Wächter, 2006). One stream of argument is based on comparative institutionalism. Comparative institutionalism emphasizes the complex differences between national business systems in the roles of state, financial and education systems, employee-employer relations as well as market and non-market coordination (Hall and Soskice, 2001; Lane, 1995; Whitley, 1999). Scholars of comparative institutionalism maintain that institutional differences between nations have various constraints on transfer of HRM practices across national borders (e.g., Ferner, 1997; Whitley, 1999). Hence, practice transfer is influenced by the national differences between the country of the MNC parent company and that of the subsidiary's operation.

Another stream of argument draws on new institutionalism, especially the notions of institutional duality and institutional distance (Kostova, 1999; Kostova and Roth 2002). According to this view, practice transfer takes place under conditions of institutional duality: complying with the legitimacy of the parent company on the one hand and conforming to the legitimacy of host institutions on the other. These dual pressures pose challenges for MNCs when transferring practices from the parent company to the subsidiary abroad. Furthermore, the larger the institutional differences (institutional distance) between the parent country and the subsidiary's country, the more difficult is the transfer and the lower the transferability.

Given the differences of national institutions, the practices that originate in one institutional context may not work in another. The transferred practice from the MNC HQ is likely to be modified to the local context of the subsidiary and result in a hybrid form of management practice. For example, Ferner, Quintanilla and Varul (2001) show that Anglo-American business practices and some classic German approaches coexist in the UK and Spanish subsidiaries of large German MNCs operating internationally. Transferred practice may be altered in meaning or its original intention. For example, in their study of performance appraisal in Chinese-Western joint ventures,

Lindholm, Tahvanainen and Björkman (1999) show that, although the practice from the HQs was standardized, the way in which appraisal discussions were carried out at the joint ventures was different from the original intention of the transferred practice. Appraisal of the subordinate was conducted by the superior instead of mutual discussion between the superior and the subordinate.

Very recently, a growing body of literature has addressed the relevance of a power perspective in the institutional analysis of international transfer of HRM practices (Almond and Ferner, 2006; Edwards and Kuruvilla, 2005; Ferner and Edwards, 1995; Ferner et al., 2005; Ferner, Edwards and Tempel, 2012). This line of research argues that actors at various levels of the MNC possess specific power resources. Transfer of HRM practices is not only constrained by the institutions of home and host countries but also by the power relationships within the MNC and their interplay with the institutional factors. Actors within the MNC may deploy specific power resources to influence the transfer; thus, transfer is likely to be a process where the HQ and the subsidiary negotiate the terms of transfer (Ferner et al., 2005). Subsequently transfer is likely to result in various types of outcome. For example, Ferner et al. (2005) show that the ability of actors in the UK subsidiaries to mobilize specific power resources allowed them to resist full implementation of 'workforce diversity' policy of US MNCs, leading to a range of compromise accommodations. This power perspective adds to our understanding of how institutions may be enacted and utilized as resources by actors within MNCs. According to this perspective, MNCs and their subsidiaries are not simply constrained by internal and external institutions nor do they simply take advantage of them. MNCs and their subsidiaries engage with institutions through power interaction. The institutional effect is manifested through the political process of actors inside the MNC organization.

## **1.2. Research Gap**

Despite the contributions of existing literature on institutional analysis of international transfer of HRM practices a few weaknesses can be addressed. First, the empirical studies are predominated by investigation of institutional effect alone, such as the effect of host country institutions and/or effect of

country of MNC origin, or some aspects of these, such as legislation, trade unions and national culture. In a few important exceptions an integrative approach of institutional theory and power perspective has been applied in the study of the transfer of HRM practices, as in the work of Almond and Ferner (2006), Ferner et al. (2005) and Festing, Eidems and Royer (2007). As a whole, Edwards and Kuruvilla (2005) point out that the lack of an integrated way to incorporate national institutions, organizational politics and the division of labour within MNCs has constrained research progress in the international HRM field.

Second, although there is a considerable amount of studies on HRM of MNC subsidiaries and joint ventures in China (see Cooke, 2009), research on transfer of HRM practices from foreign MNCs to China remains rather limited. There are even fewer studies that have explored the process of transfer and explained why a certain type of outcome of transfer occurs. As Gamble (2003) criticized, in the studies on foreign companies in China little attempt has been made to analyse the mechanism of transfer or to compare the content of practices between the parent and the subsidiary. Much study of HRM in foreign MNCs in China has focused on the impact of China's economic systems or national culture on the HRM practices of foreign companies. By looking at this stream of study over time, it is apparent that as China has undergone a more rapid liberalization process in the recent reform period, foreign companies have become much less constrained by the formal institutional environment and are able to exercise their desired HRM practices (e.g., Child, 2000; Lindholm, 2000; Sanyal and Guvenli, 2000; Walsh and Zhu, 2007). Research also shows a convergent trend of HRM practices between foreign companies and Chinese companies (Björkman, Smale, Sumelius, Suutari and Lu, 2008).

However, some reports and studies have pointed to considerable challenges in HRM facing foreign operations in China, such as high employee turnover and fierce competition for skills. Few studies have examined how the significant changes of business systems at societal level, brought about by the ongoing transition from the central planning regime towards a market economy, affect the adoption of transferred practice. Furthermore, many studies on HR practice transfer have been conducted in Western contexts where national institutions are relatively stable and the market economy is well established.

For example, studies have been conducted on transfer from Japan to Europe and USA (e.g., Beechler and Yang, 1994; Sharpe, 2001) and transfer from USA to Europe (e.g., Almond and Ferner, 2006; Ferner et al., 2005; Tempel et al., 2006). Research of transfer from foreign MNCs to China seems rather limited. A few case studies were found to provide some in-depth insights into China's institutional and cultural impact on transfer, for example, Gamble's (2003; 2006) work on transfer from UK MNCs of retail sector to China, Taylor's (2001) study on transfer from Japanese MNCs to China, and Zou and Lansbury (2009) on transfer from Korean MNC to China. Despite these exceptions, we know less about how the transfer of HRM practices from a Western country takes place in a Chinese context. More specifically, what competing pressures subsidiaries face in terms HQs' demand and local specific conditions and how the transferred practices are implemented under such pressures remain largely unanswered. Furthermore, how specific institutional factors of China combined with power relationships between HQ and subsidiary lead to a given outcome of transfer such as localized practice or standardized practice has rarely been explored.

Third, the majority of studies on transfer of HRM practices have been conducted on MNCs of leading economies such as the USA, Japan, the UK and Germany as 'exporting' countries. Less attention has been paid to the transfer from a small, developed economy to a large, transition economy. Finland is a small and open economy and there is a strong domestic push on Finnish industries to enter international markets (Luostarinen, 1994). The internationalization of Finnish companies has been rapid with a number of large global companies in such sectors as telecommunication, forest and paper as well as industrial engineering emerging. Yet, there is rather limited research on Finnish MNCs in terms of HRM practice transfer. We know little about what, if any, HR practices Finnish MNCs carry on to their foreign operations and how the embeddedness of Finnish MNCs in their home country business systems manifests in their international operations. In the last two decades, Finnish business systems, including some subsystems and the financial system, have undergone significant change: from state level coordination to more decentralized coordination. (Lilja et al., 2011; Moen and Lilja, 2005). Given the rapid internationalization of Finnish companies and the evolution of business systems at home, it is of theoretical interest to study the extent of

transfer of HRM practices from Finnish owned MNCs to their foreign operations.

Above all, Finland as the MNC home country and China as the host country of subsidiaries provide an interesting domain to study cross-border transfer of HRM practices. Finland is typically categorized as a coordinated market economy despite the recent changes in some aspects of its business systems (Moen and Lilja, 2005) and in many ways Finland is a highly stable society. Further, Finland is typically considered to follow the Nordic model of industrial relations (Lilja, 1998). China is one of the fastest growing economies in the world. It has been undergoing a transition from a centrally planned economy towards a market economy with fundamental changes in its legal and socio-economic systems as well as norms and values in all spheres of society (Child and Tse, 2001; Leung, 2008). The contrasting institutional arrangements between China and Finland lend an interesting setting for this study to investigate institutional effect and subsequent outcome of localizing Finnish HQs' HRM practices at Chinese subsidiaries.

### **1.3. Research Question**

Against the empirical and theoretical gaps discussed above, I set out the central research question as follows:

How can localization of HRM practices be explained by a configuration of institutional factors and power relationships between subsidiary and headquarters?

Localization in this study is defined as modifying MNC HQ's HRM practices to fit the local context of subsidiary operation country. Subsequently, localization is viewed as an outcome of transfer of HRM practices from the MNC HQ to the foreign subsidiary. By answering the research question, this study addresses the research gaps discussed earlier and aims to contribute to existing literature in two ways. First, the study attempts to investigate explanations of localization of HRM practices, the outcome of HRM practice transfer in a configurational manner. While recognizing the possible impact of some other factors such as business strategy and mode of establishment on the outcome of transfer, this study focuses on institutional factors and power

relationships between subsidiary and headquarters. I examine this issue by drawing on institutional theory and the power perspective. I build on the existing literature on institutional analysis of cross-national transfer of practice (e.g., Ferner and Quintanilla, 1998; Ferner, Quintanilla and Varul, 2001; Kostova 1999, Kostova and Roth, 2002;), especially the works on HR practice transfer with an integrative approach of institutions and power of actors within MNCs (Almond and Ferner, 2006; Edwards and Kuruvilla, 2005; Ferner et al., 2005; Ferner et al., 2012; Festing et al., 2007). By contrast, the present research differs from the above studies in that it attempts to identify causal patterns with combinations of factors that lead to a given outcome of transfer. This is done through applying Qualitative Comparative Analysis (QCA) (Ragin, 1987; 2000; 2008; Rihoux and Ragin, 2009) to a multiple case study. As a set-theoretical method QCA is an appropriate approach and technique for causal analysis. Its configurational approach and formal tools provide advantage for comparing the cases systematically and extracting causal patterns from complex cases. In this way, it is hoped to advance the generalizability of case research in international transfer of HRM practices. Another difference from some of the aforementioned studies is that the focal analysis of this study is the subsidiary. Localization is looked at from the subsidiary point of view, how subsidiaries perceive the fit of HQ's practices to the local context and act upon these practices, and not from the HQ's point of view, as in the case of internalization of transferred practices (see, Kostova and Roth, 2002). This moves away from the HQ-centred approach in studying practice transfer. Subsidiaries in this study are seen as the central player that interacts with the host institutions and HQs and acts upon the elements of HQ-transferred practices in the wider context of HR practices exercised at subsidiaries.

Second, it aims to increase our understanding of localization of HRM practices transferred from a coordinated, stable market economy to a turbulent transition economy. This is done by empirically examining subsidiaries of Finnish MNCs operating in China. In line with comparative institutionalism (Hall and Soskice, 2001; Whitley, 1999), this study looks at the host country effect of Chinese institutions at societal level and their development through the economic transition of over three decades. Moreover, the impact of institutional arrangements is examined in a wider context of economic and social systems. The identification of possible causal factors to the localization

is highly contextual. This helps to select the most relevant causal factors that contribute to the localization of HRM practices at subsidiaries.

Six HRM practices are selected for the investigation. These practices are recruitment and selection, compensation, benefits, performance management, training and development as well as employee representation. It is expected that different HR areas are likely to be susceptible to different institutional and organizational pressures. For example, the transfer of compensation and performance management is expected to be influenced differently by the interplay of institutional forces from different sources (host country, MNC and home country). Subsidiary compensation practice is expected to be highly subject to host country regulations and cultural norms (Lowe, Milliman, DeCieri and Dowling, 2002; Schuler and Rogovski, 1998). The compensation practice is also expected to be influenced by MNC HQs, given the growing tendency of using budget to control cost. Furthermore, HQs' compensation practices can also be influenced by home country norms, such as emphasizing equality among employees. Performance appraisal is expected to be affected by strong internal pressures from HQs due to the increasing tendency of performance-driven strategies adopted among MNCs (Boselie, Farndale and Paauwe, 2012). Meanwhile it is expected to meet some challenges from the local institutional environment, as some studies showed clashes between the host regulation/ normative values of employee and the performance-based pay and appraisal system (e.g., Almond and Ferner, 2006; Lindholm et al., 1999). After a pre-investigation of the six HRM practices, the examination of localization is focused on compensation and performance management practices. This is because these two practices show the highest relevance in terms of competing pressures between the HQs' transfer and the local context. These two practices also exhibit high consistency in the transferred content in the cases studied.

#### **1.4. Structure of the Dissertation**

The rest of the dissertation consists of the following chapters:

Chapter 2 is literature review. First, it defines the concept of localization of HRM practice. Then, it discusses the three theoretical perspectives: new



institutionalism, comparative institutionalism and the power perspective. Review of relevant conceptual and empirical research work on HRM practice transfer of MNCs is incorporated into the review of the theories. The theoretical assumptions and their potential applicability to the present study are discussed. Finally, a theoretical framework is constructed in order to guide the empirical investigation.

Chapter 3 deals with methodology. The use of QCA as an approach as well as an analytical technique is justified through a detailed discussion of its features and potential strengths in generating causal explanations. This method is evaluated by and compared with the prevalent quantitative method and the dominant inductive case study method. The basics of technical aspects of QCA and its step-wise application are introduced. Thereafter, the process of case selection is described, followed by description of data collection and case companies. The process of identifying and selecting the causal conditions is then presented in detail. Then, the chapter describes how the conditions and the outcome are calibrated and the minimization of the truth table is conducted. Finally, the validity and reliability of the study are assessed.

Chapter 4 provides a historical review of China's institutional environment in the early reform period (1978 – early 1990s) based on documentary data and existing literature. The chapter discusses the impact on human resource management of foreign enterprises with reference to the results of early studies. The discussion highlights the central problems of localization of the HRM practices facing foreign MNCs under the strong constraints of the institutional continuity of the Chinese central planning system.

Chapter 5 describes the Chinese institutional context in the later reform period (mid-1990s to 2010) when the case companies were operating in China. The discussion follows the dual lines of macro institutional transition from a highly centralized planned economy to a market-oriented economy on the one hand and enterprise-level reform of state-owned enterprises on the other. The impacts of these reforms on the formation and development of the labour market, establishment of national labour legislation and the establishment of the social security system are discussed. Labour legislation at the national and regional levels concerning the HR practices of this study is also presented.

Chapter 6 presents the findings on localization of compensation and performance management practices. An overview of findings of the HQ-

transferred practices in the six HR areas is presented first. Then, findings on the causal conditions and the outcome of localization/ standardization of compensation and performance management practices are described. A QCA analysis on localization of compensation practice is followed. The QCA results are interpreted at the end.

Chapter 7 provides an overall discussion on the main findings, including the configurational paths to the localization, host country effect, country-of-origin effect, evolving national business systems and localization in China and finally, localization as a process. The findings of this study are contrasted with the institutional theory and power perspective as well as with previous empirical studies.

Chapter 8 concludes the dissertation with the following parts: first, it presents the contributions of this study to the institutional analysis of international transfer, to international HRM study, to the literature of localization of HRM practices in China and to methodology in International Business research. Then, it highlights the managerial implications for Finnish and non-Finnish companies. Finally, the chapter ends with discussion on the limitations of the present study and suggestions for future research.

## **2. Literature review**

This chapter reviews theories and extant research that are relevant to the research question defined in the previous chapter. The purpose is to construct a conceptual framework to guide the empirical work. First, the concept of localization is defined. Then, the new institutional theory, comparative institutionalism and a power perspective are presented. The theoretical assumptions and potential applications to the current study are elaborated. The weaknesses of these theories are discussed. Finally, a theoretical framework is constructed for examining the research question.

### **2.1. Conception of Localization of HRM Practices**

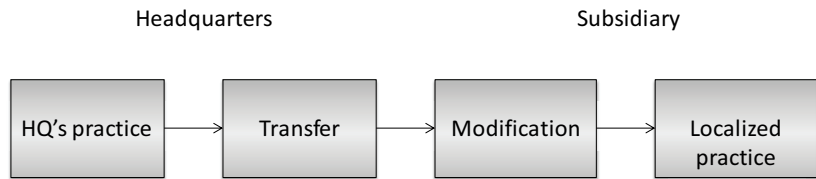
#### **2.1.1. Defining Localization of HRM Practices**

In the mainstream of international business literature localization of HRM practices has been often examined by comparing foreign subsidiary HRM practices with those of local firms or those of host country (e.g., Björkman and Lu 2001; Gunnigle, Murphy, Cleveland, Heraty and Morley, 2002; Lu and Björkman, 1997; Myloni, Harzing and Mirza, 2004; Rosenzweig and Nohria, 1994). As a result, resemblance or similarity to local practices is regarded as localization. Thus, localized practices are often equated with such terms as “local practices”, “local firm practices”, or “host country practices”. The underlying assumption is that if the subsidiary practice is similar to that of the local firm/ host country, it constitutes localization. This stream of research has made important contributions to our understanding of the external isomorphism of host institutions and the internal isomorphism of MNC organizations on HRM practices. Yet, the process of localization, the interplay of institutional

and organizational factors is little unveiled. Also, as Edwards and Kuruvilla (2005: 8-9) pointed out, much empirical study lacks a detailed account of national institutions regarding the local pressures and the country-of-origin effect, i.e., there is very little about how specific elements of the national systems such as legal regulation of employment and labour market institutions impact on foreign firms and subsequently lead to a particular practice.

In this study I conceptualize localization following the global integration and local responsiveness framework (Doz, Bartlett and Prahalad, 1981; Prahalad and Doz, 1987). According to this framework local responsiveness is to respond to differentiated local markets when the MNC operates in multiple countries. The need for local responsiveness is derived from the tension between the globally unified strategy of MNCs and the diversified local environments. It is argued that human resource management is particularly subjected to the pressures of conforming to the host conditions compared to other functions such as finance and production (Rosenzweig and Nohria, 1994; see also Rosenzweig, 2006). Extending this notion to HRM in MNCs, local responsiveness is viewed as a response to the local institutional and cultural demands, consequently adjusting the parent HRM practices to fit local conditions. In this spirit localization in this study is understood as adjusting parent practices at the subsidiary end. The basic assumption is that the parent HR practices which are generated in the institutional context of home country may not be suited to the host institutional requirements. Therefore, adaptation to the local context is expected when the HQ's practices are transferred to subsidiaries.

Thus, in this research I define localization as adaptation of HQ's standardized HR practices to local conditions. The starting point is that the HQ's HR practice is transferred to its foreign subsidiary and considered by the subsidiary unsuitable to the local context. This study is primarily interested in under what combination of conditions the foreign subsidiary modifies the transferred practice to fit the host country environment. Thus, the outcome is a localized practice, localization of the HR practice. Figure 2.1 below illustrates this concept.



**Figure 2.1** Illustration of localization

Alternatively, the subsidiary may adhere to the HQ's policy and implement the transferred practice without modification. I regard this situation as standardization. This conceptualization of standardization also differs from other studies in the literature. In many studies, the logic of conceptualizing and measuring the standardization of HRM practices is very similar to that of localization discussed earlier. If the subsidiary HR practices resemble those of the parent firm it is regarded standardization. Terms such as "MNC practices," "MNC parent company practices," "parent country practices," and "MNC home country practices" are often used as synonyms for standardized/globalized practices. Accordingly, the resemblance or similarity to MNC parent practices or MNC home country practices are often viewed as evidence of standardization of HRM practices. In fact this stream of literature informs more about convergence and non-convergence of HR practices between foreign MNCs and indigenous firms of the host country than foreign subsidiaries localizing the practices that are transferred from their parent.

Apart from localization, two other terms, translation and hybridization are often used in research on diffusion or transfer of organizational and management practices. It is necessary to distinguish between the concept of those two terms and localization in this study. The terms translation, hybridization and localization come from different traditions. The term translation used in organization studies is originally borrowed from social constructivism that uses it as a metaphor to imply the conveying of meanings in social actions (Callon and Latour, 1981; Latour, 1986). The term translation in organization studies emphasizes the shaping and reshaping of meanings in organizational change (Czarniawska and Sevón, 1996) such as change in organizational forms and practices (Sahlin-Andersson, 1996). Sahlin-Andersson (1996) further suggests that adoption of "best practices" by

organizations is a translation process where new meanings are created and ascribed to activities and experiences. In other words, organizations do not simply take on the successful practices of other organizations. They interpret and translate in different ways the experiences presented by other organizations. In this respect, institutionalists' use of the term translation captures the sense-making processes of diffusion of practices. For example, Saka (2004) shows that the cross-national diffusion of Japanese work systems to the UK adopter involved interpretative processes where the alternative systems were translated in accordance with particular situations and constraints of the institutional context.

The term 'hybridization' was introduced by a number of researchers studying Japanese transplants of production systems such as lean production abroad (see Abo, 1994). Recently, there has been a growing body of research on hybridization of practices transferred by MNCs (e.g., Boyer, Charron, Jürgens and Tolliday, 1998; Doeringer, Lorenz and Terkla, 2003; Kühlmann, 2012; Meardi and Tóth, 2006). The view represented by Boyer and his colleagues (see Boyer et al., 1998) sees hybridization as involving the insertion of a business system into a new society or context and as the processes of adaptation and learning. Boyer et al. (1998: 4) assert that "[t]he process of transfer and adaptation of a productive model from a parent context to another site will always lead to hybridization". To put it simply, hybridization is the combination of an imported and an existing model of operation.

Boyer (1998:38) further suggests three broad hybridization models: functional equivalent hybridization, partial hybridization and innovative hybridization. By functional equivalent, Boyer (1998) means that the parent model is adapted to the local context and can deliver the same performance as the industrial model in its native society; however the model itself is different from the original one. Functional equivalence is usually partial, i.e., partial hybridization. Hybridization as innovation/novelty is "the invention of system based neither on the original industrial model nor on the repertoire of local institutional forms" (Boyer, 1998: 36). Becker-Ritterspach (2009) extends Boyer's (1998) work by distinguishing between four categories of hybridization outcomes: imitation, localization, hybridization and customization/novelty. His study investigated the production systems of automobile in four subsidiaries of foreign MNCs in India. This categorization

was based on the contextual origin of the production system being either foreign/parent (imitation), local/host (localization), both foreign/parent and local/host (hybridization), or neither foreign/parent nor local/host (customization/novelty).

It can be seen from the above discussion that hybridization primarily emphasizes the outcome of diffusion although it does concern the process as well. In a hybrid model it may be possible to distinguish which elements of the model are from the parent and which are from the local subsidiary. Translation is primarily concerned with the process of diffusion. Translation emphasizes internalization of meanings and ideas through which practices are diffused. Given this it may be difficult to identify the origin of the adapted practice. Localization in this study focuses on the HQs-transferred practices in terms of their modification to the subsidiary context, not institutionalization of meanings as such. It concerns primarily the practices that originate in the parent company, usually only some elements of the practice, not an entire system (e.g., production system or model) which is often the object of study in hybridization. In this respect the concept of localization in this study is different from both translation and hybridization.

It is worth noting that I differentiate between localized practice and locally designed practice. They are different in the origin of the practice. A localized practice is initiated at the HQ and subsequently transferred to the subsidiary. During the course of implementation the practice is modified by the subsidiary to respond to the institutional context of the host country. The outcome is a localized practice. This is the focus of this study. A locally designed practice is a practice that is formulated by the subsidiary tailored to the demands of local environment and perceived as different from the practice of parent company. There is no transfer from the HQ to the subsidiary concerning this practice. Locally designed practices are also examined at some points. As the study will show later, locally designed elements, together with localized elements, often form part of the total package of a given HR practice, giving a hybrid nature of the practice.

## **2.2. New Institutional Theory and Localization of HRM Practices**

### **2.2.1. Isomorphism and Diffusion of Organizational Practices**

The institutional theory developed in the 1970s in the United States across the social sciences is called new institutional theory (Scott, 1995). It differs from the early institutional theory in that the early institutional arguments were focused on the societal level and paid little attention to organizations. Only in the 1950s and 1960s did theorists begin to recognize the existence and importance of organizations in broader social institutions and to link institutional arguments to the structures and behaviours of organizations (Scott, 1995). Later, in the 1970s and 1980s, organizational forms and organizational fields were recognized as significant levels of analysis in organization studies in relation to institutions (Scott, 2001).

The central argument of new institutional theory is that organizations are under pressures to conform to their institutional environment. Structure and behaviour of organizations are shaped by the institutional environment where organizations are embedded (DiMaggio and Powell, 1983; Meyer and Rowan, 1977). The pressures imposed upon organizations under the same institutional context lead to 'isomorphism' which is defined by DiMaggio and Powell (1983: 149) as "a constraining process that forces one unit in a population to resemble other units that face the same set of environmental conditions."

This isomorphism is a central concept in new institutional theory. DiMaggio and Powell (1983) suggest three isomorphic mechanisms: coercive isomorphism, mimetic isomorphism and normative isomorphism. Coercive isomorphism stems from coercive forces arising from powerful constituents; for example, the government imposes regulations on organizations. Mimetic isomorphism is the result of imitation of structures and practices of other organizations that are regarded as successful. Normative isomorphism is produced where norms and standards are formulated by, for example, professional organizations such as consulting firms and professional associations, and subsequently adopted by organizations.

The core idea of early new institutionalism is that isomorphic processes in organizational fields lead to increasing homogenization of organizational



structures, forms and even practices. This provides insight into the mechanism of diffusion of organizational forms and practices. That is, diffusion of organizational practices occurs due to processes of isomorphism. The shared institutional context and pressures facing organizations in the same field explain such diffusion. The notion of isomorphism is relevant for this study regarding the institutional pressures for localizing MNC parent HRM practices, as it views MNC foreign subsidiaries being embedded in the host country environment. The subsidiaries are likely to be subject to the local isomorphic pressures. For example, local labour legislation and trade unions are typically noted as sources of coercive pressures to comply with when MNCs operate abroad (e.g., Gooderham, Nordhaug and Ringdal, 1999; Rosenzweig, 2006). Organizations imitate the best HR practices of other organizations of the same field that are regarded as successful in order to minimize uncertainty (mimetic isomorphism). For example, Rosenzweig and Nohria (1994) argue that the close resemblance to local firms in training and gender participation practices adopted by US affiliates of foreign MNCs could be largely regarded as mimetic, as they were not compelled by the local regulations to do so.

However, the early new institutionalist approach paid limited attention to the circumstances where organizations may face different or even contradictory institutional forces which in turn can produce varying outcomes of diffusion rather than neat imitations of organizational forms. In effect this was recognized by the works of some early new institutionalists themselves (e.g., DiMaggio, 1988; Meyer and Rowan, 1977). Thus, they had difficulty to explain why the diffusion of the same practice may result in differentiated outcomes in degree and in kind. The next section will present the recent development of new institutionalist analysis on practice transfer.

#### **2.2.2. Institutional Duality and Practice Transfer**

The idea of isomorphism has recently been extended from external environment to internal pressures within the MNC organization. Westney (1993) argues that MNCs straddle organizational fields and institutional domains. The home institutional environment of the MNC creates pressure on the firm to conform to certain patterns of behaviour and structure. When the

MNC extends its operation to other institutional contexts, it inevitably encounters a situation of tension between the isomorphic pull of the home environment and that of the host environment; this fundamental tension is regarded as the heritage of the MNC itself (Westney 1993; Westney and Zaheer, 2001). This notion extends the managerial view of global integration-local responsiveness framework (Bartlett and Ghoshal, 1989; Doz et al., 1981) to the nature of the MNC as an organization operating across institutional contexts. In regard to standardization versus localization, this implies that the “MNC organization is the source of strong isomorphic pulls towards similarities across the organizational structures and processes of subsidiaries” (Westney, 1993: 67). Meanwhile, the local organizational field exerts a range of isomorphic pulls (pushes) and induces the subsidiaries to replicate routines and procedures typical of the country in which they operate.

More recently, Kostova and Roth (2002) further developed the notion of dual pressure (Rosenzweig and Singh, 1991; Westney, 1993) into an established concept, institutional duality. Westney (1993) points out that those subsidiaries which adopt the patterns institutionalized in their local organizational field would gain the legitimacy necessary to acquire the resources they need in their local environments. Kostava and Zaheer (1999) further argue that MNC subsidiaries face not only external but also internal legitimacy. According to such logic, the subsidiary is obliged to adopt structures and practices that are institutionalized within the MNC in order to gain the approval of the parent. Therefore, MNC subsidiaries operate under conditions of institutional duality (Kostova and Roth, 2002).

Scholars applying the notion of dual pressure/ institutional duality argue that MNCs, more precisely their subsidiaries face different, often regarded as conflicting pressures that pull in opposing directions (e.g., Kostova and Roth, 2002; Rosenzweig and Nohria, 1994; Tempel et al., 2006). These pressures originate from a set of host (local) contextual factors at macro institutional level and a set of organizational factors at MNC corporate and subsidiary level. Subsequently the practices transferred by the HQ can be adopted differently. The work by Kostova and Roth (2002) exemplifies this body of research. Kostova and Roth examine to what extent organizational practices mandated by MNC parent are adopted by subsidiaries. They measure this with high or low implementation and high or low internalization of practices. They show

four different patterns of adoption with different combinations of high and low of these two elements. For example, active adoption constitutes high implementation and high internalization; minimal adoption constitutes low implementation and low internalization. They argue that the success of transfer is dependent on the favorability of the host country's regulatory as well as cognitive and normative institutional profile i.e. the institutional distance between the host and home countries (Kostova, 1999).

The concept of institutional duality is relevant for studying localization of HRM practices in subsidiaries of Finnish MNCs in China. These subsidiaries can be viewed as operating under conditions of institutional duality, facing the both institutional domains of Finnish multinational organizations and that of China's local environment. These institutional terrains are likely to exert rival pressures that come to the fore when practices are transferred from the Finnish parent to Chinese operations (see Ferner et al., 2012: 164). The different institutional arrangements between the parent country Finland and host country China are expected to affect implementation of the transferred HR practices, thus giving rise to the needs for local adaptation.

While the recent contributions on new institutional analysis (Kostova, 1999; Kostova and Roth, 2002; Rosenzweig and Nohria, 1994) provide important insights into the process and outcome of practice transfer within MNCs they have a restrictive view on the role of institutions. They see the differences in home institution and host institution as primarily exerting rival isomorphic pressures when it comes to practice transfer from the parent to the host country. Jackson and Deeg (2008; also Saka-Helmhout and Geppert, 2011) note that as a theoretical approach, new institutionalism in general emphasizes the constraining effect of institutions and often attributes the MNC's success to the adaptation or fit of strategies and structures to the institutional environments of diverse host countries. Comparative institutionalism considers institutional differences not only as constraints but also as resources. Accordingly, MNCs are empowered by the institutional arrangements where they are embedded. In this respect comparative institutionalism can contribute to our understanding how the implementation of HQ's standardized HR practices might be affected by both the constraints and opportunities of the host institutions.

### **2.3. Comparative Institutionalism and Localization of HRM Practices**

According to Ferner and Tempel (2006: 11), comparative institutionalism “explores persistent differences in business organization and behaviour deriving from the national development path pursued by different countries, and by the institutions that have been generated out of interaction of social groups and classes.” Comparative institutionalism (also called comparative capitalism) is an umbrella term that covers a number of approaches. For example, Jackson and Deeg (2008, see also Amable, 2003; Aoki, 2001; Maurice and Sorge, 2000) distinguish three representative approaches under the broad label of comparative institutionalism: the varieties of capitalism approach (Hall and Soskice, 2001; Lane, 1989), the national business systems (NBSs) approach (Whitley, 1992, 1999) and the governance approach (Crouch and Streeck, 1997; Hollingworth and Boyer, 1997).

Although various approaches are labeled with different terminologies they share some basic commonalities. Jackson and Deeg (2008: 545) point out four common features of comparative institutionalism. First, it studies institutions as resources. Second, it compares institutions in configurations that stress their integrity as national ‘cases’. Third, it sees institutions as comparative advantages for different types of economic activities. Fourth, it embraces a broad notion of institutional path dependency. The view of institutions as resources for firm coordination goes beyond treating institutional diversity in terms of its ‘distance’ from the norms of a MNC home country or ideal typical liberal market economy in the new institutionalist strand (Jackson and Deeg, 2008; Saka-Helmhout and Geppert, 2011). Accordingly, different institutions are seen as having comparative advantages for different types of economic activities and being interdependent and complementary (Hall and Soskice, 2001; Whitley, 1999). Given this, the institutions between nations are compared with configurations of institutional domains of national cases.

The literature review below will focus on the NBSs as this stream conceptualizes institutions at societal levels and is more specific in the components of institution. Hence, I consider NBSs more appropriate in deriving the factors that are expected to influence the localization of HRM practices. Meanwhile, I also draw on the useful insights from the other streams of comparative institutionalism.

### **2.3.1. National Business Systems Approach**

According to Whitley (1999: 33) business systems are “distinctive patterns of economic organization that vary in their degree and mode of authoritative coordination of economic activities, and in the organization of, and interconnections between, owners, managers, experts, and other employees.” Whitley (1999) proposes two key sets of characteristics of ideal types of business systems. The first set concerns the “extent to which, and dominant ways through which, organizational routines, hierarchies and institutionalized expectations coordinate economic decisions and actors” (Whitley, 1999: 32). The second set deals with the control of economic activities and success to economic resources by “differently constituted groupings of social actors” (Whitley, 1999: 32). He regards the relationships between five broad kinds of economic actors as important in characterizing business systems: a) the providers and users of capital, b) customers and suppliers, c) competitors, d) firms in different sectors, e) employers and different kinds of employees. The organization and interconnectedness of these relationships give rise to various characteristics of business systems on the basis of which business systems in different countries can be contrasted. Whitley (1999) suggests three broad types of national business systems: a) ownership-related coordination through owner control and ownership integration, b) non-ownership coordination through alliance and collaboration, c) employment relations and work organization through employer-employee interdependence and delegation to and trust of employees. The notion of employment relations has immediate implication for the transfer and implementation of MNC HR practices in foreign subsidiaries. This will be discussed in detail in the following section on the host country effect.

The central notion of the NBSs perspective is that economic actors in different nation states are influenced by the national institutional framework in which they operate (Whitley, 1992; Whitley and Kristensen 1996). The coordination and control of economic activities are impacted by a set of elements such as the structure and policies of the state, financial institutions, systems of property rights, industrial relations and labour market institutions (Whitley, 1992). For instance, state structure and policies include the ownership

role of the state and its function in regulating markets; financial institutions determine access to capital; labour market institutions include such systems as vocational training and qualification and forms of labour representation. These elements or components of national business system interrelate in a complex whole, giving rise to the characteristic patterns of business behaviours in different countries (Ferner, 1997). The NBSs perspective questions the economic view of the firm, which assumes that market competition will select the most efficient pattern of economic organization. Instead, the NBSs perspective suggests that different kinds of managerial structures and practices in different contexts require contextual explanations (Whitley, 1992).

Ferner (1997) and Whitley (2001) argue that national institutional distinctiveness has important implications for the behaviour of MNCs. When multinational companies operate internationally they are likely to be influenced by the strategies, structures, routines, practices as well as corporate values which they have developed in response to the institutional constraints and opportunities of their home business systems. MNCs are likely to carry over their home baggage to foreign operations. This point will be further elaborated in the following section on the country-of-origin effect. By the same token, the host countries where these MNC subsidiaries operate are likely to exhibit distinctive patterns of economic organization that can be very different from those of home countries. For MNC HR practices, this implies that the interaction of these various institutional domains upon the subsidiaries is likely to alter the ways how these practices are implemented during the transfer process. As a result, the practices may be changed or deviate from the original ones.

According to Whitley (1992) a particular configuration of national business system becomes established in the institutional environment through interdependent development of business system characteristics and the dominant institutions. These institutions are often the products of the industrialization process itself and developed with the formation of the modern state. The historical roots and tight linkage between business systems characteristics and institutional arrangements render considerable persistency to and enduring influence on the national patterns of business systems. For example, Lilja, Räsänen and Tainio (1992) argued that the one-sector dominance of the forest industry in Finland should be understood as a

historically evolving whole of interrelated economic, social and political actions. The traditional engineering-focused Finnish education system can be regarded as being profoundly impacted by the historical development of the Finnish forest industry. This is because the forest industry has been one of the major employers of engineers. Forest companies have been typically led by engineers with a strong belief in technological modernism (Lilja et al., 1992).

The historical rootedness of business systems implies that the existing institutional arrangements need to be understood in connection to the historical development of the national economy, evolution of social and political system and market formation. In this regard, the current institutional context of China needs to be placed in the background of the 30 years' development since 1978 when China began its economic reform. Two chapters (Chapter 4 and 5) of this dissertation are dedicated to the context of China's institutional transition.

Based on the above discussion, I consider the comparative institutionalism providing useful tool to conceptualize national institutions. The comparative institutionalism captures the characteristics of institution at societal levels. It treats the national institution as configurations of such elements as role of the state in economic development, the financial system, the education and training system, the structure of labour organizations and labour market. This configurational approach is useful for investigating the combinatorial effects of institutional and organizational factors on practice transfer across nations. In this study the factors concern the institutional context of China and Finland and the organizational context of the Finnish MNCs. The cross-border transfer deals with the transfer of HQ's HR practices from Finland to China.

The NBSs approach has dual implications for this study. One is the country-of-origin effect and the other is the host country effect. The next section will review the literature on country-of-origin effect followed by the literature on host country effect.

### **2.3.2. Country-of-Origin Effect**

The country-of-origin effect is also known as home country effect. One of the key premises of NBSs approach is that MNC parent company is seen as being

embedded in an institutional environment located in the home country (Brewster, 1995; Ferner and Quintanilla, 1998; Hu, 1992). Whitley (2001) argues that the distinctive national institutions of the MNCs' home settings highly influence the way MNCs as firms build their managerial hierarchies, learn to exercise authority, construct markets and business network, and employ workers. When MNCs operate abroad they will carry over their practices, national templates and routines of control and coordination to international operations, and even create subsidiaries that reflect organizational forms of home country (Morgan and Kristensen 2006). A number of empirical studies have supported this argument (e.g., Lane, 1998; 2000; Morgan, Whitley, Sharpe and Kelly, 2003; also Geppert, Matten and Williams, 2002; Geppert, Williams and Matten, 2003). Empirical research shows that MNC parent companies disseminate their home country HR practices, to a varying extent, to foreign subsidiaries (e.g., Almond and Ferner, 2006; Beechler and Yang, 1994; Edwards and Ferner, 2002; Ferner and Varul, 2000; Ferner, et al. 2005; Gamble, 2003; Gill and Wong, 1998; Hurt and Hurt, 2005; Stehle and Erwee 2007; Tempel et al., 2006; Wasti, 1998). For example, US MNCs are reported to transfer non-unionization policy, which is a typical US home country based practice, to their foreign subsidiaries (Tempel et al. 2006). Ferner and Quintanilla (1998) found that human resource management retains many elements of typical German NBS in the foreign subsidiaries of German MNCs, such as a strong emphasis on training, an emphasis on 'partnership', and cooperation between companies and employees despite some evidence of the Anglo-Saxonization of international HRM in these companies. Team briefings and other similar forums implemented in Japanese manufacturing plants in China are typical of Japanese home country practices (Taylor, 1999).

It is argued that the tendency of control mechanisms deployed by MNCs is influenced by the national business system of the MNC home country (Ferner, 1997; Ferner et al., 2004), thus affects the degree of enforcement of corporate values and policies in subsidiaries abroad. Japanese MNCs are reported to rely on person control with close supervision by expatriate managers (e.g., Bartlett and Ghoshal, 1989; Harzing, 1999; Kopp, 1994; Lincoln, Kerbo and Wittenhagen, 1995). In a large-scale survey Harzing (1999) showed that Japanese MNCs rank highest in expatriate control compared with US MNCs, German MNCs and Swedish MNCs. US MNCs are regarded as



having strong bureaucratic control and the coordination process is based largely on formal systems, standards and centralized policies (Bartlett and Ghoshal, 1989; Ferner et al., 2004; Ferner et al., 2005). Harzing's (1999) study revealed that US MNCs have the highest propensity to use bureaucratic, formalized control mechanisms among Japanese, German, Swedish and US MNCs. German MNCs, however, exhibit different patterns of control: both bureaucratic control of budget and centralized personal control are prevalent, but they are willing to adapt to local conditions (Ferner and Varul, 2000; Geppert et al. 2003; Harzing, 1999; Lane, 2000).

In terms of practice transfer, research indicates that the propensity of transferring home country ways of doing things and the types of practices to foreign operations also differ among MNCs of various nationalities. The transferred practices often bear the traces of home country institutional arrangements. For example, the study by Ferner et al. (2005) shows that many US MNCs tend to promote the workforce diversity as world-wide policy. This policy has been developed as a historical legacy of social and racial heterogeneity of the US, thus placing much emphasis on diverse gender and race composition at the workplace (Kurowaki, 2002). In the UK, diversity has a different connotation. It has generally emphasized equality of opportunity against discrimination on pay and employment on grounds of gender, national origin, ethnicity, or disability. Ferner et al. (2005) show that these different regulatory contexts in the US and UK resulted in different conceptions of diversity between the UK subsidiaries and the US HQs when this policy was transferred. The subsidiaries had to negotiate with the HQ on the application of this policy in local context, resulting in a variety of outcomes. Another piece of research by Almond and Ferner (2006) and colleagues on US MNCs in Europe indicates that apart from workforce diversity, a number of other employment policies (collective representation, pay and performance and managerial career) were formulated at the US HQs and subsequently transferred to their European subsidiaries. These practices exhibited, to a large extent, distinctive American styles. However, the authors also found that variations do exist among the US MNCs, thus cautioning over-generalization of American MNCs.

For localization of HRM practices of this study, the country-of-origin effect implies that MNCs may bring their national baggage to human resource management in the host country. Furthermore, the propensity of transferring

HRM practices by MNC parent companies to host country operations and the ways of enforcing these practices may be influenced by MNC home country norms and management practices. This embeddedness of MNC in their home country context is likely to affect how standardized HR practices are transferred to and implemented at subsidiaries.

It is argued that the propensity of transfer also depends on the compatibility of the institutional arrangements between home and host country (Ferner, 1997). This means that practices that originate in a particular constellation of national business system tend to have low or no transferability to a host country with a different business system. In other words, the large institutional distance (Kostova and Roth, 2002) between home and host countries prevents subsidiaries from adopting practices transferred from MNC home country. In addition, which aspects of the home country practices the MNC transfers depend on whether they are transferable, in Taylor et al.'s (1996) words the context-generalizability<sup>1</sup>. These arguments lead to the consideration of host country effect on outcome of transfer.

### **2.3.3. Host Country Effect**

The host countries where MNC subsidiaries operate may have divergent national business systems from those of the MNC home country, as suggested by the NBSs. The institutional differences between host country and home country may prevent the MNC from transferring its home country practices to its foreign subsidiaries. According to Ferner (1997), in general there are a number of constraints in the assimilation by MNCs of their home country business culture. Labour market institutions, i.e., employment relations institutions (Whitley, 1999), are argued to have direct impact on employment and human resource practices. Employment relations institutions notably include legal framework of employment (e.g., labour laws/ regulations and trade unions) and nature of labour market.

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<sup>1</sup> I acknowledge that which aspects of the practice the MNC transfers also depends on whether the MNC sees them as beneficial to international competitiveness (see Taylor et al., 1996).

### *Legal framework for employment*

The legal framework on employee relations in the host country is regarded as having significant impact on HRM and employment practices. Labour legislation is likely to impose a coercive pressure which leaves MNCs with little choice but to conform to in the HR issues. For example, Gooderham, Nordhaug and Ringdal (1999) report in their empirical study the constraining effect of legal regulations on firms' choices of HR strategies in European multinational companies. Another example is the German co-determination system which is legitimated at company level by law, the Works Constitution Act. Works councils are powerful, employee-elected bodies that are legally entitled to consult with management, have access to important corporate information and co-determine managerial and operational issues. Consequently this restricts the degree of managerial autonomy (e.g., Page, 2011; Scholz, 1996; Wächter and Stengelhofen, 1995). In addition, sectoral based collective bargaining is a typical feature of German labour institutions legitimated by laws. Sectoral agreements classify employees primarily by their level of formal vocational education and continue to have strong influence on job classification systems in firms (see Almond, Muller-Camen, Collings and Quintanilla, 2006). Empirical studies report a number of effects of labour legislation on pay and performance practices in subsidiaries of foreign MNCs (e.g., Almond et al., 2006; Muller, 1997). Almond et al. (2006) show that individual pay for performance transferred by American MNCs met some clashes in Germany and also in UK, Ireland and Spain to some extent. In particular, the forced distribution, i.e. the links between performance and employment security caused problems in a number of subsidiaries due to incompatibilities in employment law, as well as the social norms that are structured under the distinct employment relationship of the host country systems (Almond et al., 2006). Furthermore, the US MNCs' policy could not be applied to the unionized employees because they were covered by collective bargaining agreement (Almond et al., 2006). This resulted in different pay practices between the unionized employees and non-unionized employees. This indicates the role of trade unions in determining pay related issues.

There are great variations in the scope and strength of state and its influence on employment relations across countries. For example, the US has comparatively less legislative control over (or support for) the employment

relationship than is found in Western Europe (Brewster, 1995). According to Pieper (1990: 8 in Brewster, 1995), the major difference in HRM between the US and Western Europe is the extent to which HRM is influenced and determined by state regulations. Companies have a narrower scope of choice in regard to personnel management in Western Europe than in the US. Restrictions by state regulations exist in a number of areas, e.g., recruitment and dismissal, the formalization of educational certification, pay, health and safety, working environment and hours of work. The industrial relations framework has also a number of quasi-legal characteristics including forms of employment contract, rights to trade union representation, requirements to establish consultation or co-determination arrangements at workplace. Apparently, variations are evident in the extent of labour regulation between highly regulated countries such as Germany and Scandinavian countries and less regulated countries such as UK and Ireland.

Regarding the context of this research, the differences in the scope and strengths of labour regulations can be expected between China and Finland. The labour legislation system is rather new in China. It is the product of economic reform and is still under development (see Chapter 5). The Finnish labour regulation reflects many of the central features of the Nordic model of industrial relations (Eurofound, 2009). Collective bargaining is a key feature of the regulation, and the basis of the regulation lies in the comprehensive and detailed labour legislation which is complemented by collective agreements (ILO, 2011). In this respect, Finland is regarded being among highly regulated countries in terms of employment issues. And trade unions play significant roles in collective bargaining and collective agreements at industry level (It has been at the national level.) (Fulton, 2013). Unions have strong presence at enterprise level as well involving in information sharing and consultation with employers on issues such as recruitment, training and the use of temporary/agency workers (WP, 2012). The roles and status of labour unions in China are very different from those in Finland and those in other continental European countries. In general labour unions have little involvement in management issues such as pay, dismissal and working conditions (see e.g., Ding, Goodall and Warner, 2002). But it can vary from company to company. Some cases were reported that labour unions play active role in negotiating collective contract and support to the workers whose rights were transgressed

(e.g., Ding et al., 2002; Warner and Ng, 1999). Nonetheless, these were activities at firm level, not at sector, industry or national level.

Based on the above discussion of the literature on the legal framework for employment it can be reasonably expected that Finnish subsidiaries are likely to be exposed to fewer institutional pressures from statutory requirements in their HRM practices in China. However, due to the salience of labour laws and labour unions in employment relations suggested by comparative institutionalism and the literature on international HRM, labour laws and labour unions are considered relevant and important in examining the coercive isomorphic pressure of host country regarding HQs-transferred HRM practices.

Almond et al. (2005) argue that the scope for home-country-based “innovation,” i.e. practices that are unfamiliar in the host context, is likely to be related to the degree and embeddedness of national regulation. “Innovation” in this sense may be easier in less actively regulated business and employment systems than in highly regulated business and employment systems. In this respect, the transfer and implementation of MNC parent HR practices are expected to face less constraints in less regulated business systems than in highly regulated ones. Ferner et al. (2001) report their empirical research on management of HR in Spanish subsidiaries of German MNCs. Spain was characterized by stringent regulations in redundancy and employment contract, though there has been a significant move towards de-regulation. Furthermore, Spain has a statutory model of worker representation. The workers committee at the company has significant power to consult and negotiate with management (see Quintanilla, 1998, in Ferner et al., 2001). The union-management relationships in Spain tended to be adversarial in contrast to the cooperative style of German employee relations (Ferner et al. 2001). This clearly posed limits to management decision-making.

#### *Labour market system*

Another important aspect of employment relations is the degree of employer-employee interdependence (Whitley, 1999). This refers to the extent to which a reliance of firm on external labour markets or commitment of firm to employees/ mutual investment is encouraged (Tempel and Walgenbach, 2007:

5). Comparative institutionalism argues that the interconnectedness between dominant institutions, the market structure, the financial system and the nature of corporate governance give rise to the distinctive characteristics of national business systems. For example, in Japan and Germany firms tend to have long term relationships with banks and a relative low degree reliance on the stock market as source of finance compared with the firms in Anglo-American systems such as US and UK (Ferner and Quintanilla, 1998; Pauly and Reich, 1997; Sally, 1996; Whitley, 1999).

Similarly, based on the extent of market coordination Hall and Soskice (2001) distinguish between two basic types of capitalism: liberal market economies (LMEs) and coordinated market economies (CMEs). In liberal market economies the market plays a dominant role in coordinating economic behaviour, and the state remains an arm's length enforcer of contracts. Such countries include e.g., US, UK and Canada. In contrast, in coordinated market economies firm behaviour is strategically coordinated to a large extent through non-market mechanisms that support long term industrial finance, cooperative industrial relations, high levels of vocational and firm-specific training, and cooperation in technology and standard-setting across companies (Jackson and Deeg, 2008).

The extent of market coordination reflects the labour market system in terms of inter-firm workforce mobility. In the 'long-termist' business systems or CMEs, such as Germany and Japan, companies tend to treat employees as assets and emphasize long term investment in training and skills development and create strong ties between employers and employees and a strong internal labour market. This makes poaching difficult, thus resulting in a relative low inter-firm mobility of employees in the labour market. In comparison, in 'short-termist' business systems or LMEs such as the UK and USA firms rely to a greater extent on external labour market to acquire skills; thus, there tends to be high inter-firm exchange of employees. The implication is that MNCs when operating in a country with contrasting labour market arrangement are likely to encounter challenges in transferring the practices which have been developed in the home country context. For example, Ferner, Quintanilla and Varul (2001) note that the German dual system of vocational education and training was generally not transferred to UK subsidiaries by German MNCs due to the lack of the institutional infrastructure necessary to support such a

system. Beechler and Yang's (1994) study show that the transfer of Japanese HR management to American subsidiaries clashed with the distinctive features of local labour market. New York where the subsidiaries were located was characterized by highly competitive labour market, high employee turnover rates and heterogeneous labour force. This had a negative impact on the Japanese MNCs' attempts to transfer such practices as long term employment, seniority based wage, team-working and consensus-style decision making. In addition, the Japanese implicit performance evaluation and small gaps in salary, benefits and perquisites between white-collar and blue-collar workers were in conflict with employee values of emphasis on high salary and differentiated status. The research reported by Sharpe (2001) on the transfer of lean production related management systems from a Japanese MNC to its subsidiaries in the UK indicates similar findings.

In the case of China there seems to be limited investigation of the impact of labour market system on foreign subsidiary HR practices. However, some studies point to the generally existed high labour mobility as a challenge in human resource management. For example, a study based on 54 interviews with 38 Finnish companies operating in China reported that the companies experienced a labour turnover of 10-30 % and considered it as a big challenge in business operation and people management (Kettunen, Lintunen, Lu and Kosonen, 2008). Walsh and Zhu (2007) noted that a number of their case companies (German, the UK, Japanese and US multinationals) were experiencing difficulties in employee retention in China and some case companies responded to this by raising salaries and employment benefits. The high employee turnover was observed in some other Asian countries as well (see e.g., Khatri, Fern and Budhwar, 2001). Khatri et al. (2001) reported an average turnover rate of 30 % in Singaporean manufacturing sectors. Reiche (2009) further identified some organizational factors that may translate into individual turnover decisions in foreign MNCs in Singapore. One of the key reasons for the high turnover of employees in Asia is the scarcity of skills that resulted in a constantly tight labour market. This prompted wars for talents and an augmentation of salaries. This is documented by some research on China (Goodall, Li and Warner, 2007), India (Raman, Budhwar and Balasubramanian, 2007), Vietnam (Vo, 2009), Russia (Camiah and Hollinshead, 2003) and Singapore (Barnard and Rodgers, 2000). For example, Kettunen, Korhonen,

Kosonen and Karhunen (2007) show that the high demand for Russians with foreign language skills and work experience in Western companies resulted in frequent hopping of jobs.

Based on the discussion above I consider labour market mobility a highly relevant condition to localization of HRM practices in the case of China. Labour market mobility is a distinctive and prominent feature in the Chinese labour market system. In this respect labour market mobility captures a core characteristic of employee relations in terms of employer-employee interdependence (Whitley, 1999) in the Chinese context.

#### **2.3.4. Sub-national Institutions**

The primary focus of comparative institutionalism in general has been institutions at national level because nation states have been the most important actors. Nation states are still important to determine many of the most important institutional structures, “notably systems of labour market regulation, of education and training, and of corporate governance” (Hall and Soskice, 2001: 4). There has been inadequate attention paid to institutions at sub-national level such as regions and cities. Variations of business systems within countries tend to be downplayed in comparative institutionalism. Institutions at supranational level (e.g., the European Union) has received limited attention as well although NBSs approach does recognize the influence of globalization on the embeddedness of multinational firms in their home business systems. Nation state remains as the primary level at which economic organizations are shaped (e.g., Whitley 2003; 2005; 2009).

Recently, an increasing number of studies start to address the sub-national and supranational institutions (e.g., Almond, 2011; Cox, 2000; Crouch, 2005; Edwards and Kuruvilla, 2005; Ferner and Tempel, 2006; Ortiz, 2002; Tempel and Walgenbach, 2007). Nation state as definer of institutional arrangements is being challenged by supranational regulations, such as those of EU (European Union). Within nation states there can be major variations in different regions or other levels of sub-nation, such as province or city. This can be due to historical patterns of economic development as in Italy, or due to the importance of political structures in federal structures as in the USA



(Edwards and Kuruvilla, 2005; Ferner and Tempel, 2006). Sub-national states can play a significant role in economic development. For example, regional development agencies in England have been responsible for the setting of economic strategies and worked on attracting foreign direct investment (Almond, 2011). Meyer and Nguyen (2005) show that variations of sub-national institutions impact on strategic choices of foreign direct investments. They demonstrate that foreign investors are more likely to establish their operations in the provinces of Vietnam where local governments provide land, subsidies and tax holidays to foreign companies than in the provinces where such preferential policies do not exist. Almond (2011) points out that sub-national locations vary widely in their ability to shape the skills development. The variations are mostly apparent at the level of higher education in terms of the competencies of graduates and in the capacity of creation of exploitable knowledge. Education institutions, in particular higher education institutions shape the supply of human resources available in the local labour market. Some empirical studies have documented the regional variations in employee relations, for example, in India (Bhattacharjee, 2001) and Italy (Locke, 1992). However, these studies are not concerned with human resource management in foreign subsidiaries. As Almond (2011) notes, an overwhelming majority of investigations of host effects on human resource issues in MNCs do not go beyond looking at national culture or national institutional arrangements.

Empirical studies of the impact of sub-national institutions on the transfer of MNCs' HRM practices to the host country are rather limited. A few studies indicate the regional influence of a host country on implementing MNC parent practices across foreign subsidiaries. For example, Sharpe (2001) reported her research on comparative analysis across two sites of Japanese factories in the UK. One factory was located in a greenfield site and another in a brownfield site. She found that the local context was quite different between these two locations in density of foreign direct investment (especially that of Japanese), degree of unionization, availability of the desired workforce and homogeneity/heterogeneity of skill levels of the workers. She showed that the labour market context in the greenfield largely facilitated the adoption of Japanese production management practices while the labour market context in the brownfield mostly restricted such adoption. Beechler and Yang (1994) showed similar findings in their study of transferring Japanese HR practices to the USA. They

compared two groups of subsidiaries of Japanese MNCs located in New York and Tennessee respectively. In New York the labour market was highly competitive; employee turnover rates were high; the labour pool was heterogeneous; and white-collar employees valued high pay and high status. This context negatively affected the subsidiaries' attempts to apply the Japanese HR practices. On the contrary, Tennessee offered a favourable local environment: a loose labour market, a relative homogeneous workforce, very low employee turnover, subsidies by the state government for training, and favourable taxation policies. This local environment was largely encouraging the implementing of Japanese management practices.

Saka (2002) studied the diffusion of Japanese work systems by three Japanese multinational companies of automobile industry to their affiliates that were located in different parts of the UK. She showed that location in a greenfield site associated with few pre-existing culture, together with high inward foreign investment and high education levels of workforce facilitated the internalization of Japanese practices. As a contrast, the UK affiliate located in a brownfield where workers had low levels of skills and more pre-conceptions and where foreign investment was low encountered stronger resistance to the Japanese work practices. While the study showed some similar findings as the two described above, Saka noted that organizational factors, such as the efforts made by the Japanese expatriates can play a significant role in successfully implementing the Japanese practices though the local institutional context may be unfavourable. Hence, she argues that the impact of local institutional factors on the transfer process should be considered in conjunction with organisational factors.

The question of sub-national institutions is considered particularly relevant for the present study because China is large in size and heterogeneous in many aspects. For example, China is about the same geographical size as Europe and the population is one and half times greater than that of Europe. The economic and social development of China exhibits considerable differences spanning regions and cities. Since the commencement of the economic reform in 1978 China has considerably decentralized its economic and legislative power to provincial and municipal governments. This means local governments enjoy authority to make decisions on regional development and region specific policies and regulations concerning employment. The

various economic zones and free trade areas with preferential policies in use of land, tax reduction, subsidies and labour management are examples of those<sup>2</sup>. This regional diversity implies that the pressures for localization and opportunities for taking advantages of institutional space for HRM practices are likely to vary within the country. Given this, sub-national level institutions are considered as an important, potential condition to explain the outcome of transfer of HQ's HR practices. As discussed in previous section, labour laws have been regarded as the most influential regulations at national level on human resource and employment practices. Accordingly, the local (regional) employment regulations are expected to be a relevant factor of sub-national institutions on cross-national transfer of HR practices.

## **2.4. HQ-Subsidiary Power Relationships**

Recently, a growing body of research has contributed to study on cross-national transfer of practice by integrating power perspective into institutional analysis (see e.g., Almond and Ferner, 2006; Dörrenbächer and Geppert, 2009; Ferner and Edwards, 1995; Ferner and Tempel, 2006; Ferner, et al., 2012; Festing et al., 2007). Ferner et al. (2012; also Edwards and Kuruvilla, 2005; Ferner and Tempel, 2006) posit that institutional analysis on cross-border transfer should incorporate a power perspective.

A number of recent works have addressed the issue of MNCs as political actors (e.g., Dörrenbächer and Gammelgaard, 2011; Dörrenbächer and Geppert, 2011; Edwards and Bélanger, 2009; Ferner and Edwards, 1995; Ferner and Tempel, 2006; Levy, 2008). This stream of literature argues that

power and interests of actors shape transfer through processes that draw on institutional resources both at the 'macro' level of the host business system and the 'micro' level of the MNC. These processes in turn influence the transformations and adaptations undergone by transferred practices. (Ferner, et al., 2012: 164).

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<sup>2</sup> After China's accession to the World Trade Organization (WTO) at the end of 2002, the preferential policies for foreign investment have been gradually reduced and eventually ended.

This underlies the working of institutions on practice transfer through power relationships within the MNC. The influence of institutions on transfer is played out by the power relationships between interest groups (actors) within the MNC. The power capabilities of MNC actors addressed by Ferner et al. (2012) are particularly useful for this study. Next, I discuss the literature concerning this issue, based on which I derive the expected conditions of MNC organizational context for localization of HRM practices.

#### **2.4.1. Power Capability of Headquarters**

MNC HQs possess specific power capabilities within the MNC organization (Ferner, et al., 2012). These capabilities can be empowered by the formal authority of the organization. The authority structure in the MNC legitimates the HQ to exercise power. HQs have the authoritative power in defining rules and procedures, setting targets and delegating tasks within a centrally-determined framework, monitoring compliances, and exercising rewards and sanctions on conformity (Child, 1984; Ferner, 2000; Roth and O'Donnell, 1996). In spite of the view that MNCs move towards decentralized networks (Castells, 1996 in Almond and Ferner, 2006) research finds that hierarchical control system remains in MNCs. Almond and Ferner (2006; also, Ferner, 2000; Ferner, et al., 2004) show that there is little sign of widespread shift of formal control away from corporate headquarters in many large US MNCs in the area of employment relations and human resource policies. This is in contrast to the argument that heterarchies replace hierarchies in managerial decision making in network-based MNCs (Nohria and Ghoshal, 1997). Almond and Ferner (2006) further demonstrate that in the majority of US MNCs they investigated, HR structures were quite centralized and formalized and generally similar across a number of case subsidiaries in several European countries.

HQs' formal authority renders them power to exercise control over transfer of HRM practices. Very often, HQs define the scope and elements of global policies and standardized practices and procedures. Research indicates that financial reward and performance management are very commonly defined by MNCs as standardized policies and practices and transferred globally. For example, Lindholm et al. (1999) show that among several HR

practices (recruitment, selection, compensation and performance management), performance management exhibited highest standardization in Chinese-Western joint ventures in China. Myloni et al. (2004) show similar finding on multinational companies in Greece. Almond and Ferner (2006) found a high degree of centralization in pay and performance management in European subsidiaries of US MNCs. In addition, workforce diversity and non-unionism were found to be popular global policies/ practices among US MNCs (e.g., Ferner, et al. 2005; Tempel, et al. 2006).

HQs also determine the codification of global policies. Some may be more prescriptive and some may be of more framework type. This gives different degrees of freedom for subsidiaries to modify the practice during transfer. Policies in the form of broad framework seem to allow subsidiaries for higher autonomy for local adaptation than the strictly prescribed policies. For example, a survey on HR practices of MNCs in the UK suggests that MNCs disseminate policies commonly in broad framework in areas such as performance management, variable pay and employee involvement with the expectation for local adjustment (Edwards P, Edwards T, Ferner, Marginson and Tregaskis, 2007, in Ferner et al., 2012).

HQs are also in a position to introduce mechanisms that impose standardized HR practices on subsidiaries abroad. Studies on personnel issues in MNCs indicate pervasive bureaucratic systems to control labour costs through budgeting system; for example, budgetary control over headcount and payroll costs (see Ferner, 2000). Ferner (2000) documented that the HQ would typically intervene if the subsidiary exceeded the budget target and this was controlled by HQ approving the budget plan supplemented by regular reporting and reviews. It can be expected that HQs' control over financial budget would have direct impact on enforcing global HR policies, especially on compensation practice.

Based on the literature above, it is considered that monitoring by HQ over the transferred practices should have direct impact on the outcome of transfer as for how the practice is implemented at the subsidiary. It can be reasonable to expect that a weak monitoring system from the HQ is likely to leave more freedom for the subsidiary to modify the transferred practice and lead to localization, and a strong monitoring system from the HQ is likely to

leave less or no freedom for the subsidiary to modify the transferred practice and lead to standardization.

#### **2.4.2. Power Capability of Subsidiary**

However, subsidiaries are not totally subordinate to HQ power. It is argued that subsidiaries may influence the transfer by deploying resources they possess (Ferner et al., 2012; Ferner and Tempel, 2006; Ferner and Edwards, 1995; Zou and Lansbury, 2009). Ferner et al. (2012) maintain that if subsidiaries possess power resources they are able to resist transfer; as a result, transfer is likely to be a “negotiated process” (Ferner et al., 2005: 307). The transferred practice may be implemented in a form of modification by negotiation between the HQ and subsidiary. For example, in their study of the US multinationals, Ferner et al. (2005) show that the UK subsidiary managers deployed power resources to resist the full implementation of corporate diversity policy from the US HQs, resulting in a range of compromise outcomes. Almond and Ferner (2006) and colleagues investigate transfer of a number of employment and HR practices from the US multinationals to their European subsidiaries. They show that different actors at various levels of the organization retain some scope to pursue their own goals and may circumvent or interpret corporate guidelines liberally. The outcomes at the foreign subsidiaries of MNCs should be understood as the involving negotiation on the constraints of host country between actors involved in the transfer.

Birkinshaw (1997; also Birkinshaw and Hood, 1998) demonstrate that subsidiaries build up resources and capability over time through charter and mandate. These subsidiaries play an important role in corporate strategy. The studies on subsidiary initiatives/ entrepreneurship point out that subsidiaries are active strategizers within the wider MNC (e.g., Birkinshaw 1997; Birkinshaw and Hood, 1998; Bouquet and Birkinshaw, 2008; Dörrenbächer and Geppert, 2009; Ferner and Tempel, 2006; Kristensen and Zeitlin, 2005; Morgan and Kristensen, 2006). The competencies which subsidiaries have developed over time or a strategic position they possess may serve as crucial resources within the MNC.

Resource dependence theory (Pfeffer and Salancik, 2003) suggests that crucial resources may affect organizational behaviour. The actors who rely on crucial resources will become dependent on the actors who possess and control such scarce resources. The stronger dependence on the scarce resources the more power the focal actor (resource provider) has in terms of influencing organizational behaviour. Competence does not solely reside within the HQ. Bartlett and Ghoshal (1998) posit that in transnational corporation a subsidiary unit may operate as strategically important competence center. On the other hand, not all subsidiaries within the MNC may be at equal position in terms of their competency and strategic role. This renders some subsidiaries strategically more important than others. For example, Roth and O'Donnell (1996; also Dörrenbächer and Gammelgaard, 2011) argue that if a subsidiary is a major contributor to the MNC's profit, operates in a key market, or performs critical functions it possesses vital resources for the success of the MNC. Then, the subsidiary is mostly likely to be in an advantageous position in influencing management decisions made at the top. Festing et al. (2007) examined how the global standardized compensation strategy was implemented in various foreign subsidiaries of a large European MNC. They show that the US and Japanese subsidiaries were able to modify the HQ's rule while the other subsidiaries had to comply with the HQ's policy. The US and Japanese subsidiaries were strategically important in market size, market competitiveness and R & D function in the MNC and the other subsidiaries did not possess such a strategic role. Tempel (2001) argues that the subsidiary with research and development function is more strategically important within the MNC because the parent company is able to benefit from the subsidiary's activities. In contrast, the subsidiary that has only sales function or serves local market is likely to be less strategically important to the parent company.

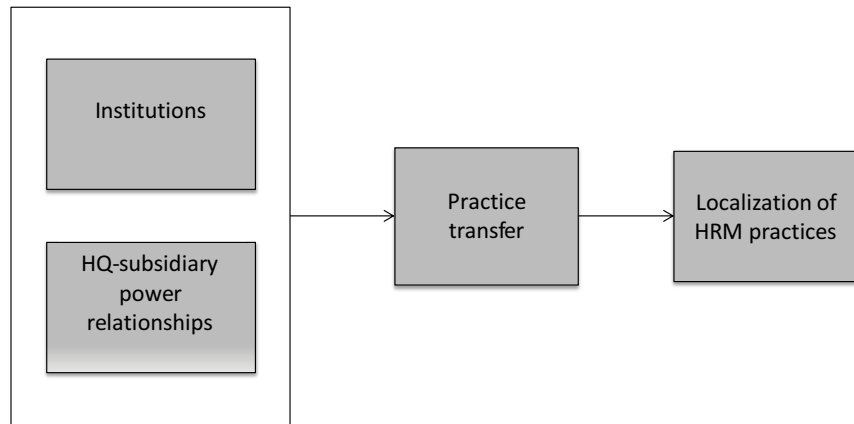
Based on the literature discussed above, I consider strategic role of subsidiary an important source of power. It is expected that the subsidiary that plays a strategic role in the MNC would have a strong position in bargaining with the HQ on the terms of transfer (see Ferner et al., 2005). Powerful subsidiaries may use internal and external institutions as resources to influence the transfer. The transferred practices are likely to be modified by the subsidiary to fit the local conditions. In this regards, strategic role of subsidiary is conceived highly relevant in the outcome of transfer.

## 2.5. Theoretical Framework

This section will summarize the literature reviewed previously and build a theoretical framework based on the discussion of the theories and extant research.

The new institutionalist notion of dual pressures acting upon MNC subsidiaries (Kostova, 1999; Kostova and Zaheer, 1999; Kostova and Roth, 2002) serves as a broad framework for examining practice transfer within MNCs. According to this notion transfer of HRM practices from the MNC parent to subsidiaries occurs under conditions of institutional duality (Kostova, 1999). Given this, the transfer under examination of this study needs to be seen as the movement of practices across institutional domains of the home country, Finland and the host country, China (see Ferner and Tempel, 2006: 29). According to comparative institutionalist view, MNCs are embedded in home country national business system (Whitley, 1992, 1999). Their strategies, structures, and management practices have been developed within the context of home national business system. The host country where MNC subsidiaries operate has its distinctive national business system. The differences of NBS in the host country context from that of MNC home country are likely to impose constraints to the implementation of parent practices. This interaction of home and host institutions is manifested through the process of transfer at subsidiary end. While MNC HQs institutionalize standards, procedures, policies and practices across the units of MNCs, subsidiaries are likely to respond to parent requirement in various ways. The outcome of transfer is likely to be influenced by the dynamics of power which the parent and the subsidiary are able to deploy. As a result, the transferred practices are likely to be modified during the transfer process. Accordingly, localization is perceived as the outcome of transfer that is affected by institutional and organizational configuration. This logic is depicted in Figure 2.2.





**Figure 2.2** The theoretical framework: Localization as an outcome of transfer affected by a configuration of institutions and power relationships between HQ and subsidiary

The central idea of this framework is that subsidiaries adjust their HRM practices in responding to host country institutional environment under multiple pressures. As Figure 2.2 shows, the combinatorial influence of institutions and MNC power relationships operate upon the transfer process, which in turn affects the localization of transferred HRM practices. Six conditions are identified based on the review of theory and existing research. The causal conditions stemming from the theoretical perspective are summarized in Table 2.1 below.

**Table 2.1** Theoretically derived causal conditions

Theoretical perspective/ literature	Relevant key contribution	Causal condition
Host institutional level		
Comparative institutionalism	Legal framework for employment as external pressures upon subsidiary	Labour law Labour unions
Comparative institutionalism	Labour market system: the degree of employer-employee interdependence	Labour market mobility
Comparative institutionalism	Sub-national institution	Local regulations
MNC organizational level		
Power capability of HQ	To control over transfer by drawing on power capability derived from hierarchy and formal authority	HQ monitoring over transfer
Power capability of subsidiary	To deploy host institutions as resources by strategic position of subsidiary within the MNC	Strategic role of subsidiary

At the host institutional level, as Table 2.1 shows, three sets of institutions are considered particularly relevant to explaining the outcome of transfer: legal framework for employment, labour market system and sub-national institutions. Labour regulations and trade unions are the most prominent aspects of labour legal framework and likely to constrain MNCs' HRM practices. This is because labour laws are statutory in nature and often regulated by nation states. Although the extent to which employment relations are regulated varies among different countries, labour regulations and trade unions are conceived as having a coercive effect. The labour market system is an integral part of business systems with the financial market system, corporate governance and market structure. Here, I consider the degree of employer-employee interdependence (Whitley, 1999) particularly relevant for this study. In the Chinese context

employer-employee interdependence is particularly reflected in the labour market mobility, as discussed in Labour market system in Section 2.3.3. In this regard the employer-employee interdependence derives the condition labour market mobility. The labour market mobility can have implications for a number of HR practices such as recruitment, compensation, training and development, and employee retention. Sub-national institutions are considered particularly relevant for China because of the country's huge size, historical development path and the regional variations. The regional variations have become increasingly apparent during the economic transition in the past three decades. As there is little empirical research on the effect of regional institutions on HR practice transfer, local regulations on employment is considered relevant. This is based on the importance of national labour regulation on subsidiary HRM practices suggested in the literature and also my personal knowledge of China's multiple level legislation system.

At the organizational level as Table 2.1 shows, practice transfer is seen as being affected by the interplay of power between the HQ and the subsidiary. The MNC HQ may use various authoritative means such as reporting, budgeting and direct supervision to monitor and enforce standardized HRM practices. The subsidiary may deploy institutional resources empowered by its strategic position within the MNC. Subsequently, the transfer is likely to be a process involving a negotiation (see Ferner et al., 2005). Therefore, HQ's control over transfer and subsidiary capability to deploy institutional resources to safeguard its own interest are considered to be highly relevant to explain the outcome of transfer. These theoretically informed conditions are further refined with the case data. The final selection of the conditions for QCA analysis is discussed in the Methodology chapter that follows.

There is no separate condition for the country-of-origin effect. As discussed in the literature review earlier (see Section 2.3.2), the country-of-origin effect is manifested in the MNCs' propensity of transferring home country norms and practices to their foreign operations, the control and coordination mechanisms used by the HQ, and the tendency of centralization/ decentralization within the MNC organization. In this study the home country effect of Finnish MNCs is examined through the aspects mentioned above.



### **3. Multiple Case Study with Qualitative Comparative Analysis Approach**

This research applies Qualitative Comparative Analysis (QCA) into a multiple case study. I begin this chapter with a brief discussion of multiple case studies in comparative case research. Then, I introduce Qualitative Comparative Analysis and discuss how its key features have potential strengths in generating multiple conjunctural explanations with a case study. Thereafter, I describe the basics of technical aspects of QCA and its step-wise application. Following this, I describe in detail how QCA is applied in this study from case selection, data collection and condition selection to calibration of the conditions and the outcome, constructing the truth table and Boolean minimization. Then, I assess the quality of the study in terms of validity and reliability. Finally, I discuss the relevance of language in cross-cultural research.

#### **3.1. The Multiple Case Study**

The case study has become an increasingly popular research strategy in management research. In their review of case study articles published in four leading IB journals, Piekkari, Welch and Paavilainen (2009) show that case study has gained an established place in IB research and become the most common qualitative research method in this field.

The multiple case study represents an ideal strategy in comparative case research. I consider the multiple case study appropriate for investigating the central question of the present research “how can localization of HRM practices be explained by a configuration of institutional factors and power relationships between subsidiary and headquarters?” This is because the research question involves looking for configurational causal explanations to the phenomenon (localization) with some specific causal factors across a number of empirical cases (subsidiaries of Finnish MNCs). Multiple case

studies allow for systematically comparing a number of cases and seek regularities across the cases. This in turn strengthens the theoretical leverage of comparison and makes generalization possible. Furthermore, multiple case studies permit the researcher to gain in-depth insights into individual cases and capturing their complexity while producing some degree of generalization (Rihoux and Ragin, 2009).

Systematic comparison is at the heart of comparative case research. Given the complexity of phenomena in the social sciences, a systematic comparison of cases while giving justice to within-case complexity, remains challenging (Rihoux and Ragin, 2009). As Rihoux and Ragin (2009) point out, in many instances the comparison of the case study material is rather “loose” or not formalized. While some methods of comparative analysis of cases do exist, such as pattern matching and explanation building (Yin, 2009), they normally do not engage in configurational logic, based on which different parts of the case are understood in relation to each other as a whole and constellations of the cases are compared. The Qualitative Comparative Analysis is meant to meet these challenges. In effect, QCA goes beyond a mere comparative method. Now I will move on to introduce QCA and its key features and justify the choice of QCA as a research approach and technique for my study.

## **3.2. Qualitative Comparative Analysis**

This section introduces QCA and its key features, justifies its choice for this study, and then describes the practical steps of general application of QCA.

### **3.2.1. What is QCA?**

QCA was developed in comparative social sciences in 1980s, particularly for exploring causality in qualitative comparative research. QCA was originally launched by Charles Ragin (1987) in his seminal work *The Comparative Method: Moving beyond Qualitative and Quantitative Strategies*. At a more general level QCA is an approach, a research strategy. The QCA approach was originally developed aiming at a “synthetic strategy” to “integrate the best

features of the case-oriented approach with the best features of the variable-oriented approach” (Ragin, 1987:84). The main shortcoming of conventional case research strategy is its inability to handle a relatively large number of cases. It tends to particularize each case and produce low generalizability. The variable-based research strategy, though does lend itself to a high degree of generalization, tends to suffer from its abstractness and its inability to address complex, conjunctural causal arguments. The QCA approach aimed to bridge the gap between case-oriented methods and variable-oriented methods. This was indeed Ragin’s (1987) ambition when the first QCA technique, crisp-set QCA was developed in late 1980s.

At a specific level QCA is a set of techniques. Since the launching of QCA, its techniques have been developed from the crisp-set QCA (csQCA) to multi-value QCA (mvQCA) and fuzzy-set QCA (fsQCA) (see e.g., Ragin, 1987, 2000, 2008a; Rihoux and Ragin, 2009; Schneider and Wagemann 2012). These three techniques share the same foundations and core features that will be presented next, but differ in the technical operations. A number of software programmes have been developed to aid the practical operations of these techniques<sup>3</sup>.

### **3.2.2. The Epistemological Foundations**

The logical foundations of QCA are primarily based on Mill’s (1967 [1843]) ‘method of agreement’ and ‘method of difference’. Mill’s method of agreement states,

If two or more instances of the phenomenon under investigation have only one circumstance in common, the circumstance in which alone all the instances agree is the cause (or effect) of the given phenomenon. (1967 [1843]: 390, in Berg-Schlosser, De Meur, Rihoux and Ragin, 2009: 2)

According to Mill, a researcher who wants to know the cause of a certain phenomenon should first identify instances of the phenomenon and then

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<sup>3</sup> A large amount of useful resources on QCA, e.g. software of QCA techniques, working papers and references can be found at the international resource site of QCA at [www.compass.org](http://www.compass.org) and Charles Ragin’s website <http://www.u.arizona.edu/~cragin/fsQCA/software.shtml>

attempt to determine which circumstance invariably precedes the appearance of that phenomenon (Ragin, 1987). Then all the other possible circumstances but the one(s) on which all the instances agree must be eliminated. Essentially this method is a search for patterns of invariance (Ragin, 1987). The circumstance(s) that constantly occurs in all instances is inferred as the cause. In case-based research, this means that if the outcome is the same for a number of cases (e.g. existence of a certain phenomenon, positive outcome), there should be similarities in the causal condition or a set of conditions across the cases.

Mill's method of difference states,

If an instance in which the phenomenon under investigation occurs, and an instance in which it does not occur, have every circumstance in common save one, that one occurring only in the former; the circumstance in which alone the two instances differ, is the effect, or the cause, or an indispensable part of the cause, of the phenomenon. (1967 [1843]: 391, in Berg-Schlosser et al., 2009: 2)

This method “establishes the absence of a common cause or effect, even if all other circumstances are identical” (Berg-Schlosser et al., 2009: 2). In case-based research this logic implies that cases that show a different outcome (e.g. non-existence of a certain phenomenon, negative outcome) should be included in the investigation of cause because it is expected that the cause which has been identified in the positive cases will be absent from these additional negative cases. Thus, the method of difference uses negative cases to reinforce conclusions drawn from the positive cases (Ragin, 1987).

Both Mill's methods are thus concerned with the systematic matching and contrasting of cases in order to establish common causal relationships by eliminating all other possibilities (Berg-Schlosser et al. 2009). QCA draws heavily on Mill's insights by eliminating irrelevant factors and approximating causal conditions in the “real” world. On the other hand, QCA goes beyond Mill in that it establishes the notion of multiple conjunctural causation. In addition, QCA adopts a configurational approach to comparative analysis to investigate causal complexity. This creates abundant room for extensive dialogues between ideas and data, i.e. between theory and evidence. Further, ontologically QCA is grounded in set-theory where set relationship and necessary and sufficient conditions play a central role in unraveling causal



relationships. The next few sections elaborate on these key features of QCA and discuss their applications to this study.

### **3.2.3. Configurational Comparative Approach**

According to Rihoux and Ragin (2009: XIX), “a configuration is a specific combination of factors [...] that produces a given outcome of interest.” The factors (or stimuli, causal variables, ingredients, determinants, etc.) are termed *conditions* in configurational comparative method. Ragin (1987:3) views cases as configurations- combinations of characteristics. Thus, comparison in qualitative traditions involves comparing configurations. This holistic approach contradicts radically the analytical approach of most quantitative research. From a critical realist view (Bhaskar, 1978), cases can be viewed as complex configurations of events, structures and objects (Ragin, 1997). In comparative social sciences this implies the notion of case analysis that the objects are similar enough and separate enough to permit treating them as comparable instances of the same general phenomenon (Ragin and Becker, 1992: 1).

In essence, techniques of configurational comparative analysis, such as QCA, are case oriented in the sense that they deal with a limited number of complex cases in a configurational way. This means that each individual case is considered as a complex combination of properties, a specific “whole” that should not be lost or obscured in the course of the analysis—this is what Rihoux and Ragin (2009) call a holistic perspective. Rihoux and Ragin (2009: XIX) continue that “the conditions will be envisaged in a combinatorial way—hence enabling one to model quite a high level of complexity even with only a few conditions.”

In QCA configurational approach means that each case is de-composed into a number of causal conditions. Each case is represented by a combination of the presence and absence of these conditions, which in turn leads to a given outcome. Cases are systematically compared based on the combinatorial conditions and causal patterns are sought. Thus, the use of QCA for systematic comparison of complex cases requires transformation of the cases into configurations. For example, Pajunen and Airo (2013) conceptualize the national context as the configuration of five institutional factors: public health

care expenditure, national income, older age, coordinated market economy and reference price system. Each country (case) is transformed into a configuration that is composed of the five causal conditions. They examine under what combinations of these factors the generic medical industry has high performance or lack of it in various European countries.

The implication of the configurational approach for this study lies in the way that effects of various factors on localization of HRM practices are examined in a combinatorial manner. Each case subsidiary is treated as a given combination of the causal conditions derived from China's institutional context and Finnish MNC context. The outcome, localization of HRM practices is assumed to result from the combinatorial effect of these conditions. The case companies are then compared with each other based on the configurations.

### **3.2.4. Multiple Conjunctural Causation**

The explanation of social phenomena by revealing the causal mechanisms that produce them is the fundamental task of social research (Danermark, Ekström, Jakobsen and Karlson, 2002). Causation is complex in the social world. According to Ragin (1987) the assessment of causal complexity is of a major importance to comparative social science. Ragin further points out,

It is the intersection of a set of conditions in time and in space that produces many of the large-scale qualitative changes, as well as many of the small-scale events, that interest social scientists, not the separate or independent effects of these conditions. (1987: 25)

These processes are called “chemical causation” by Mill (1843, in Ragin, 1987:25). That is, a phenomenon or a change emerges from the intersection of appropriate pre-conditions – the right ingredients for change. This conjunctural or combinatorial nature is a key feature of social complexity. As Ragin (1987:26) puts it, the identification and interpretation of these causal configurations (causal complexes) allows the investigator to delineate the different empirical processes and causal mechanisms relevant to a specific outcome. Social phenomena are complex because different causally relevant conditions can combine in a variety of ways to produce a given outcome.

Moreover, context forms a crucial element in causation. According to Pawson and Tilley (1997), generative mechanisms are systems of embodied complex causes. In this regard, causal mechanisms are contingent upon and operate in interaction with context.

Causation in social sciences is not only conjunctural but also multiple. Multiple means different combinations of causes may produce the same outcome (Ragin, 1987). That is, there can be multiple causal pathways to the same outcome (also known as equifinality). For example, in research on organization performance, equifinality implies the assumption that two or more organizational configurations can be equally effective in achieving high performance (Fiss, 2007). When conjunctural and multiple simultaneously exist such causality is referred to as multiple conjunctural causation. This is the central thrust of causal complexity in QCA approach (Berg-Schlosser et al. 2009; Ragin, 1987; 2000).

This view of causality as context- and conjuncture-specific in QCA approach rejects any form of permanent causality (Ragin, 1987). This stands in contrast to the quantitative statistical causal approach. In the usual statistical technique a single best causal model is sought. The means and correlation are computed as the average across all cases at the same time. QCA advocates identifying multiple causal paths that co-exist among comparable cases. It treats causal models as specific and distinctive to given cases or groups of cases. Exceptions and outliers are not discarded; instead these non-conforming cases can shed special light on the understanding of specific processes (Berg-Schlosser et al., 2009). In this respect, QCA moves away from the core assumptions of uniformity of causal effect, unit homogeneity, additivity and causal symmetry in traditional statistical approach (Berg-Schlosser et al., 2009; Ragin, 1987).

In relation to the research question of this study, multiple conjunctural causation implies that localization of HRM practices is expected to have various pathways, rather than a single model. It sees localization as processes which are formed by intersection of varying institutional and MNC organizational factors from the host and home country and the MNC. Different constellations of these factors may lead to the same outcome with regard to localization of HRM practices.

Case-oriented research and quantitative statistical approach have different logic in cause and effect. The former follows the logic of ‘causes-of-effects’ and the latter ‘effects of causes’ (Mahoney and Goertz, 2006). In quantitative tradition, the central concern is net effect of each individual variable. Accordingly, a researcher is more likely to focus on estimating the effect of individual variables. Although there are interaction statistical models, the individual effect approach continues to be the norm in the social sciences (Braumoeller, 2004; Brambor, Clark and Golder, 2006). Fiss (2007) noted that interactions that go beyond two-way effects are exceedingly difficult to interpret in regression models. Furthermore, they assume that this nonlinear relationship is relevant for all cases under investigation, thus contradicting the concept of equifinality, according to which different causal paths may lead to the same outcome (Fiss, 2007).

The qualitative tradition often focuses primarily on the impact of combination of factors and seldom on the effects of individual factors. For example, in the causal relationship expressed by the statement Y is the outcome of combination of presence of factor A, presence of factor B and absence of factor C, the qualitative researcher would not bother to estimate the net effect of factor C. This is because C sometimes has a positive effect and sometimes a negative effect, depending on the other variables with which it occurs (Mahoney and Goertz, 2006). This highlights the relatedness of causes and the setting where these causes operate. This difference from quantitative causal inference has an important implication for the current study. For example, the effects of institutional forces on the localization of subsidiary HRM practices are not assessed with the average estimation of a single factor on the entire sample of cases, but with combination(s) of factors on individual cases.

### **3.2.5. Set Relations, Necessity and Sufficiency**

QCA is a set-theoretical method (Ragin, 2000; 2008a; Fiss, 2007; Schneider and Wagemann 2012). According to Schneider and Wagemann (2012: 3), set-theoretical methods in social science research share three characteristics. First, set-theoretical methods concern membership of cases in sets. For example,

Finland is a Member State of the European Union. Thus, Finland is an element of the set of European Union. Finland's membership score in this set is 1. China is not a Member State of the European Union. China's membership score in this set is 0. This dichotomous membership is called crisp-set. Crisp-set emphasizes qualitative differences between cases. Furthermore, set membership is not limited to full inclusion/ full exclusion of a case into a set. That is, a membership is not necessarily a dichotomy as the above example shows. In fact, in social sciences the boundary of a full membership versus full non-membership is often vague. Many social science concepts vary by level or degree. For example, the concept of developed countries, while it is clear that some countries are developed and some are not, there is a broad range of in-between countries. These countries are not fully in the set of developed countries, nor are they fully excluded from this set. They form a partial membership of the set of developed countries. This is fuzzy membership. The fuzzy membership scores between 1 and 0 address the varying degree to which different cases belong to a set.

Second, set-theoretical methods perceive relations between social phenomena as set relations. As Fiss (2007:1183) states, “[a]t the center of set-theoretical approaches lies the idea that relationships among different variables are often best understood in terms of *set membership*”. Ragin (2008a: 17) further argues that set relations “involve causal or other integral connections linking phenomena”, i.e. they are not merely definitional. The set-relations are in the forms of set-subset and set-superset relationships. For example, the statement “professionals have advanced degrees” implies that professionals are a subset of people with advanced degrees (Ragin, 2000). Or expressed in set-superset relationship, this can be stated as people with advanced degrees are a superset of professionals. Professional is treated as an outcome. Holding an advanced degree is seen as a causal condition. Professionals hold an advanced degree; however, not all those with advanced degrees are professionals. This asymmetric causal relationship is a central feature of set-theoretical thinking.

Third, set relationships unravel causal complexity which is interpreted in terms of necessity and sufficiency (Ragin, 1987; 2000; 2008a; Rihoux and Ragin, 2009; Schneider and Wagemann 2012). Necessity and sufficiency are much in line with the notion of multiple conjunctural causation discussed earlier. A condition is considered necessary if, whenever the outcome is

present, the condition is also present. In other words, the outcome cannot occur without the condition. A condition is considered sufficient if, whenever it is present, the outcome is also present. That is, a cause is defined as sufficient if by itself it can produce a given outcome. In other words, there should not be a single case that shows the condition but does not have the outcome (Schneider and Wagemann 2012). It is worth noting that necessity and sufficiency are meaningful only in the context of theoretical assumptions. As Ragin (1987: 99) points out, “[n]o cause is necessary, for example, independent of a theory that specifies it as a relevant cause. Neither necessity nor sufficiency exists independent of theories that propose causes.” A condition is both necessary and sufficient if it is the only condition that produces the outcome and it is singular. A condition is sufficient but not necessary if it can generate the outcome but is not the only cause with this capability. The outcome can also result from other conditions. A cause is necessary but not sufficient if it is capable of producing an outcome in combination with other conditions and appears in all such combinations (Ragin, 1987:99).

The following examples illustrate the notions of necessity and sufficiency: suppose there are three conditions A, B and C and outcome Y and there are two paths to the outcome. They are expressed as follows:

$$A * C + B * C \rightarrow Y \text{ (1)}$$

(Uppercase letter denotes the presence of a condition; lowercase letter denotes absence of a condition. \* denotes the logical AND. + denotes the logical OR.)

C is a necessary condition for the outcome to occur because when the outcome Y is present C is also present. However, it is not a sufficient condition because C alone does not produce the outcome. It needs to combine with either A or B for the outcome to occur. Neither A nor B is a necessary condition or a sufficient condition.

If the paths would be

$$A + B * c \rightarrow Y \text{ (2)}$$

Then, A would be a sufficient condition because it is capable of producing the outcome alone. However, A is not a necessary condition because it is not the only cause that can lead to the outcome. The other path, B\*c is capable to produce the outcome as well.

In equation (1) although neither A nor B is sufficient condition, each when combined with the other condition C, becomes a necessary part of a conjunction,  $A \cdot C$ , or  $B \cdot C$ , which in turn is sufficient for producing the outcome Y. This kind of condition is called INUS condition (Goertz, 2003; Mahoney, 2008; Schneider and Wagemann, 2012).

Necessity and sufficiency are at the heart of QCA because they unravel causal complexity: equifinality, conjunctural causation and causal asymmetry. For example, equation (1) illustrates the notion of equifinality, i.e. the same phenomenon can have different, mutually non-exclusive explanations. It also tells conjunctural causation where the effect of single conditions A, B and C unfold only in combination with other condition. In effect, social phenomena rarely result from single causes. It is typical that relevant causes combine to produce a given outcome and very often the same outcome results from several different combinations of causes (Ragin, 2000).

### **3.2.6. Application of QCA in Management and Business Studies**

Initially, in the late 1980s and early 1990s, QCA was developed for comparative research in political science (comparative politics) and historical sociology (e.g. welfare states studies). The specific subjects in the empirical research have been at the macro level of entire societies, economies, states, or other complex social and cultural formations (Berg-Schlosser et al., 2009). Against this background, QCA has been naturally conceived as a macro-comparative approach in social scientific disciplines. As Rihoux (2003) points out, the applications of QCA have been mostly limited to macro-sociological or meso-sociological phenomena. Hence, the number of cases included in the empirical studies has been low. Thus, QCA is widely seen a small-N strategy. The small-N is regarded as between two and ten – fifteen cases (Berg-Schlosser et al., 2009). A three-case study (Häge, 2005) was found to be the smallest-N in QCA application<sup>4</sup>. More recently applications of QCA have begun to extend to other fields, such as organizational sociology, management and education, and to large-N case studies as well (see e.g. Berg-Schlosser et al., 2009; Rihoux and Ragin, 2009; Yamasaki and Rihoux, 2009). The two

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<sup>4</sup> However, some scholars are critical of applying QCA to a very small number of cases (e.g., Marx, 2010; Schneider and Wagemann, 2012).

latest studies conducted by Marx, Rihoux and Ragin (2013) and Rihoux, Álamos-Concha, Bol, Marx and Rezsöházy (2013) provide the most updated overview of QCA applications over the past 25 years since it was launched.

The fields of management and business have shown growing interest in applying QCA as a methodological approach and technique in recent years. Empirical applications were found in a number of subjects<sup>5</sup>. In International Business research, for example, Crilly (2011) examines whether MNC foreign subsidiaries adopt a stakeholder-centric orientation or a shareholder-centric orientation. He uses interview and documentary data to derive conditions that shape subsidiaries' stakeholder/ shareholder orientation. Marx (2008) assesses the conditions under which multinational firms join a multi-stakeholder certification initiative based on 17 international companies in sport footwear industry. Pajunen (2008) investigates the institutional factors of 47 countries and concludes several institutional configurations that may lead to attractiveness/ unattractiveness of these countries as FDI recipients. In addition, QCA applications were conducted in studies on e.g., export performance (Allen and Aldred, 2011; Schneider, Schulze-Bentrop and Paunescu, 2010) and performance of generic medicines industry in Europe (Pajunen and Airo, 2013). In marketing research Vassinen (2012) applies fuzzy-set QCA to build a practical process, the "configurational explanation of marketing outcome" model to assess marketing performance. He specifies how and under what circumstances fuzzy-set QCA can provide knowledge on complex configurational causality as a marketing management support system. In organization research Fiss (2011) investigates with fuzzy-set QCA configurations of performance of high-technology firms and contributes to building better theories in causal analysis of configurational core, periphery and asymmetry. Fiss (2007) also introduced QCA as a set-theoretical approach for studies of organizational phenomena. Fiss (2009) suggests that set-theoretical methods such as QCA provide a viable alternative much better suited to the configurational nature of the case study approach in studying organizational configurations than some other methods such as cluster analysis, interaction effect and hierarchical linear modeling.

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<sup>5</sup> For an exhaustive bibliography of QCA applications and QCA related articles, see COMPASS, the international resource site of QCA at [www.compass.org](http://www.compass.org); for a summary of applications of fuzzy-set QCA in business research, see Vassinen (2012).



Rihoux et al. (2013) show that QCA applications in management studies have experienced a sharp rise in most recent years. This is not surprising, as Marx, Cambré and Rihoux (2013) suggest that QCA appears particular well suited for many core management topics. As justified through the earlier sections, QCA is an appropriate approach and tool for the interest of this research to uncover the conditions under which localization occurs.

### **3.2.7. Practical Steps for Application of QCA**

This section briefly outlines the practical steps in performing QCA techniques. The detailed description of applying QCA to the present research will be presented in the sections followed. Crisp-set QCA (csQCA) is the most widely used QCA technique (Rihoux, et al. 2013). The description below focuses on this technique which the current study adopts.

The first step is to define the subject of interest. QCA can be regarded as an outcome driven method. An outcome is the research problem which a researcher wants to explain, for example; attractiveness or unattractiveness of a country for foreign direct investment (see, Pajunen, 2008). A clear outcome of interest should be specified at very early stage of the QCA because it is indispensable for case selection (Berg-Schlosser and De Meur, 2009). It is worth noting that defining the outcome of interest is likely to be iterative (Rihoux and Lobe, 2009). The outcome may be sharpened or refined during the research process when cases are unfolded.

The second step is to select cases. QCA is a comparative case research method. This means that cases should be comparable (Rihoux, 2003; Rihoux and Ragin, 2009; Rihoux and Lobe, 2009). The cases should share enough background characteristics to permit comparison. It is worth noting that case selection in QCA is not “sampling”. Each case matters. Further, cases should not be taken as given. Instead, selection of cases is a process where theory and data encounter each other. As a result cases may be added or removed during the course of research project (Berg-Schlosser and De Meur, 2009; Rihoux and Lobe, 2009). Therefore, case selection is likely to be tentative at the early stage of research. In effect, case selection is tightly linked to the next step, the

selection of conditions, because the researcher needs some level of case knowledge.

The third step is to identify the possible causal conditions which are expected to produce the phenomenon under examination. As mentioned earlier, the central philosophy of QCA is the notion of causal complexity in the social sciences. A social phenomenon is viewed as an outcome of a set of interrelated pre-conditions. A general principle for selecting causal conditions is theoretical criteria (Berg-Schlosser and De Meur, 2009), i.e. selection of conditions should be guided by theories and literature. However, this may not be a straightforward process as this study will show. Thus, this principle should not be applied rigidly. The researcher should take into account any significant factor that emerges from the data. Thus, selection of conditions can be empirically driven as well (Rihoux and Lobe, 2009; Yamasaki and Rihoux, 2009). Often, the researcher needs to go back and forth between theory and data before deciding on the final conditions for the analysis.

The fourth step is to calibrate conditions and outcome. Calibration is a process of assigning set membership to cases with scores (Ragin, 2000; 2008a; Rihoux and Ragin, 2009; Rihoux and Lobe, 2009; Schneider and Wagemann 2012). For crisp-set QCA a binary value (1 or 0) is used to assign each explanatory condition and outcome. If the condition is present or favorable to the outcome the value 1 is given. If the condition is absent or unfavorable the value 0 is given. The outcome is assigned with value 1 when it is present and with value 0 when it is absent. For fuzzy-set QCA an interval score between 0 and 1 (including 0 and 1) is used to assign the data. A membership score of 1 indicates full membership in a set; a score of 0 indicates full non membership in a set. Scores between 0 and 1 indicate partial membership. The closer to 1 the higher the membership a case belongs to a set; the closer to 0 the lower the membership a case belongs to a set. fsQCA allows more fine-grained categorization of membership of cases. In fact csQCA is a special type of fsQCA. Again, similar to selection of cases and conditions, calibration of set membership is an iterative process between theory and data.

The fifth step is to create a data table. The conditions and the outcome that have been assigned with membership scores are organized to a table matrix. In this way, all the cases are transformed into configurations. A configuration is a given combination of conditions associated with a given outcome (Rihoux

and De Meur, 2009). Each case corresponds to a configuration of a specific combination of some conditions and an outcome (Rihoux, 2003). An explanatory model is thus preliminarily established.

The sixth step is to construct a truth table (Ragin, 1987; Rihoux and Ragin, 2009; Schneider and Wagemann 2012). The truth table is constructed based on the causal conditions and the outcome identified previously. The truth table includes all logically possible combinations of conditions including those that do have empirical instances (cases). Contradictory configurations may occur in csQCA due to the dichotomous nature of Boolean algebra technique. A contradictory configuration is a combination of conditions that leads to [1] outcome for some observed cases and [0] outcome for other observed cases. Contradictory configurations should be resolved before proceeding to further analysis (Rihoux and De Meur, 2009; Yamasaki and Rihoux, 2009). Marx (2010) even suggests that resolving the contradictions be a necessary step to build a robust explanatory model.

The seventh step is Boolean minimization (Ragin, 1987; 2008a; Rihoux and De Meur, 2009; Rihoux and Ragin, 2009; Schneider and Wagemann 2012). The long Boolean expression in the truth table, the configuration of a set of conditions and an outcome, can be reduced to the shortest possible expression that unveils the causal regularities in the data. The expression can be simplified by eliminating redundancies and commonalities. The basic rule is if two Boolean expressions differ in only one causal condition in its presence and absence, yet produce the same outcome, then this causal condition can be considered irrelevant and can be removed to create a simpler, combined expression. This technique is Boolean minimization algorithms. The following example is a Boolean expression with three conditions (A, B and C) and one outcome (Y), expressed as:

$$A * B * C + A * B * c \rightarrow Y$$

The sign \* denotes the logical AND. The sign + denotes the logical OR. The uppercase letter represents the [1] value for a binary variable and lowercase letter represents [0] value for a binary variable. The arrow symbol  $\rightarrow$  is used to express the causal link between a set of conditions and the outcome.

In the above Boolean expression the condition C can be removed because no matter which value the C condition takes, value 1 or value 0, the outcome

value is the same. Thus, a reduced expression, a minimal formula, is obtained as follows:

$$A * B \rightarrow Y$$

The minimization of all configurations may produce one or several paths (minimal formula). That is, a solution may contain more than one solution term. When minimization is conducted on the configurations of empirical cases the resultant solution is called “complex solution” (Ragin and Davey, 2009: 51-53) or “conservative solution” (Schneider and Wagemann, 2012: 162). The researcher does not make assumption about any logical remainder and is entirely guided by the empirical information at hand (Schneider and Wagemann, 2012). A logical remainder is a configuration that is logically possible but does not have a corresponding empirical case.

A parsimonious solution is produced by including any logical remainder that may help generate a logically simpler solution, regardless of whether it constitutes an “easy” or a “difficult” counterfactual case (Ragin, 2008b: 81). A casual combination that lacks empirical instances is imagined as a counterfactual case (Ragin, 2008a:150). An intermediate solution takes into account only the “easy” counterfactual cases. That is, the researcher is able to make assumptions about whether the presence, absence, or presence or absence of the condition(s) would lead to the outcome. These simplifying assumptions should be made according to the researcher’s substantial knowledge on theory and/ or cases. Simply said, in a complex solution remainder combinations are not taken into account. Only the configurations that show the empirical cases are minimized. In parsimonious solution and intermediate solution the logical remainders are also minimized and the resultant configurations are usually simpler (containing fewer conditions) than the configurations in the complex solution.

The final step is interpretation of the minimal formulas obtained with QCA technique. This requires returning to the cases (Rihoux and De Meur, 2009; Rihoux and Lobe, 2009; Schneider and Wagemann 2012). QCA is a case-oriented technique. The formulas allow the researcher to focus on the elements producing or not producing a given outcome of interest in a holistic way. The interpretations of the elements and the causal mechanism require within case narratives and cross-case analysis (Rihoux and De Meur, 2009; Rihoux and Lobe, 2009; Schneider and Wagemann 2012).

In effect, QCA as an analytical approach can be used in a variety of ways (Rihoux, 2003; Rihoux and Ragin, 2009). For example, it can be used to summarize data, check coherence of data, check hypotheses or existing theories, test conjectures and develop new theoretical arguments (Berg-Schlosser et al., 2009). These uses of QCA (except the last one - developing new theoretical arguments) do not need to involve Boolean minimization. It is not necessary to reduce the Boolean expressions to a minimal equation. However, for seeking multiple conjunctural causality a complete QCA should be performed. Thus, in the present study I chose to go through the Boolean minimization and obtain the minimum equations (formulas).

### **3.3. Selection of the Cases**

The case selection in this study is guided by the preliminary assumptions and the empirical evidence (see, Berg-Schlosser and De Meur, 2009; Ragin, 1987; Rihoux and Lobe, 2009; Rihoux and Ragin, 2009). Thus, selecting the cases is a highly iterative process involving moving back and forth between theory and evidence. The term “casing” by Ragin (1992) best conceptualizes this process.

A domain of investigation must be defined in order to establish the boundary for selecting the cases (see, Berg-Schlosser and De Meur, 2009; Rihoux and Ragin, 2009). The subject of interest of this study is defined in the chapter of introduction and further elaborated in the chapter of literature review. The aim of this study is to seek explanations to localization of HRM practices with a configuration of institutional factors and HQs-subsidiary power relations. The context where the phenomenon is situated is transfer of HRM practices from a small coordinated market economy, Finland to a large transition economy, China. Thus, subsidiaries that were operating in China and owned by Finnish MNCs are the population from which a sample of cases was selected. This specifies the common property of the cases (subsidiaries) that belonged to the MNCs of the same country of origin.

As a comparative method, an essential feature of QCA is to have as comparable cases as possible at the outset. This means that cases should be sufficiently similar to allow comparison. This is the strategy of MSDO (“most similar, different outcomes”) (Przeworski and Teune, 1970 cited in Berg-

Schlosser and De Meur, 2009). That is, cases are matched as similar as possible. By “controlling” most of “variables” different outcomes may be attributed to the remaining factors that differentiate these cases (Berg-Schlosser and De Meur, 2009: 22). To permit comparing among cases, the case companies in the present should have similar HRM practices that are transferred from the parent. A minimum number of 40 employees was set as a criterion for selecting the subsidiaries. It is considered that smaller companies are unlikely to have full HR functions and the HQs are less likely to transfer standardized HR practices to their foreign subsidiaries.

It is argued that in case-oriented research, inclusion of the cases and the number of cases should not be viewed as a prior (see e.g., Rihoux and Lobe, 2009). Case selection may be deferred until a later stage of research; hence cases may be added or removed from the original sample (Berg-Schlosser and De Meur, 2009; Ragin, 1992). This is indeed the case in this study. The case selection underwent two phases. In the first phase thirteen subsidiaries of Finnish MNCs were initially selected based on the list provided by Finnish Business Council in China and my own knowledge. The second phase involved matching the cases with similar practices that were transferred from the HQs of the case subsidiaries. Using the interview data I investigated the transfer of six HR practices across the thirteen cases. Although some of the cases involved the transfer of recruitment and selection and training and development practices they are not very interesting theoretically because there was little evidence of conflicting pressures between the subsidiaries and the HQs. No HQs’ practice in benefits and employee representation was found being transferred to any of the thirteen case firms. The practices of compensation and performance management were transferred in a majority of the cases. Ten cases (from Case No. 1 to Case No. 10 in Table 3.1) had HQs-transferred compensation policy. Nine cases (from Case No. 1 to Case No. 9 in Table 3.1) had HQs-transferred performance management practice. These two practices also exhibit the most consistent content in terms of transfer and show competing pressures at varying extent between the HQs and the local context across these cases. Based on these preliminary findings, the final cases were chosen.

The selection of cases in this study indicates that the case selection is not a single decision, instead a multilevel approach as suggested by Fletcher and Plakoyiannaki (2011). This approach involves a process that spans different

levels and the researcher makes informed decisions about the various levels such as country, industry, organization and within organization where the case selection takes place. The levels in this study include country (Finland and China), organization (Finnish MNCs) and within organization (subsidiary and HRM practice). Case selection involved justification of the each level and balance between these levels. As described throughout this section the selection decisions at different levels of the case study process were made at various stages of the research project, rather than a one-time decision taken before data collection (see, Fletcher and Plakoyiannaki, 2011). This highlights the challenges in indentifying the unit of analysis and boundaries of cases in international business research (see, Pekkari et al., 2009).

### **3.4. Description of the Cases**

The thirteen subsidiaries belonged to different Finnish parent companies. For reasons of anonymity, the case companies are coded with pseudonyms. To protect the identification of the companies, their specific sector or industry could not be fully revealed, for most companies were the only one that had a China operation in the sector concerned. Instead, sectoral or industrial information on the companies is broadly indicated. The attributes of the cases are summarized in Table 3.1.

**Table 3.1** Summary of the case subsidiaries of Finnish MNCs in China

Case No.	Case subsidiary	Age (year)	No. of employees	Founding mode /Ownership	Sector/ Industry	Location
1	IndCo1	5	60	WO/ WO	Industrial product	Shanghai
2	EquCo1	4	100	WO/ WO	Equipment	Shanghai
3	IndCo2	9	150	JV/ WO	Industrial product	Jiangsu
4	EngCo1	10	600	WO/ WO	Engineering	Jiangsu
5	EquCo2	7	400	WO/ WO	Equipment	Shanghai
6	EngCo2	6	450	WO/ WO	Engineering	Shanghai
7	MecCo	9	80	WO/ WO	Machinery	Beijing
8	ServCo	4	100	WO/ WO	Service	Beijing
9	ConCo	10	1650	JV/ WO	Consumer product (electronics)	Beijing
10	IndCo3	7	80	WO/ WO	Industrial product	Shanghai
11	EquCo3	4	40	WO/ WO	Equipment	Shanghai
12	IndCo4	9	80	WO/ WO	Machinery	Shanghai
13	EquCo4	14	70	JV/ JV	Equipment	Shanghai

Note:

WO: wholly owned by Finnish parent.

JV: joint venture between Chinese partner and Finnish parent.

Founding mode: refers to mode of establishment.

Ownership: refers to the status at the time of the interview. For example, WO/WO means the subsidiary was founded as a wholly owned Finnish company and it remained so at the time of the interview.

As Table 3.1 shows, twelve case subsidiaries were manufacturing companies. Most of them were engaged in engineering, machinery, equipment or industrial products. Only one company, ConCo was a manufacturer of consumer goods in electronics/ telecommunication products. Two case companies, IndCo2 and ConCo employed more manual worker employees than professional employees and may be labeled as labour intensive companies. The rest eleven case



companies were capital and/or technology intensive in nature. Of the thirteen cases one was a service company (ServCo). Due to the rare presence of Finnish service MNCs in China only one service company could be selected. The number of employees ranged from 40 to 1650. The subsidiary age ranged from fourteen years to four years. Among the total thirteen case subsidiaries nine were founded as wholly Finnish-owned. EquCo4, IndCo2 and ConCo were established to be joint ventures between the Finnish parent and the Chinese partner. IndCo2 and ConCo later became wholly Finnish-owned subsidiaries while EquCo4 remained a joint venture. Eight companies were located in Shanghai, two in Jiangsu province and three in Beijing/Tianjin area. The Greater Shanghai area (Shanghai and its nearby cities in Jiangsu province) had the highest concentration of Finnish direct investment and Beijing ranked second (FBCS, 2008; Finpro, 2008). The locations of the case subsidiaries reflect the general geographical distribution of Finnish operations in China.

The subsidiary is defined as a case. Defining a subsidiary – determining where the boundary lies – turned out to be somewhat complicated. The conventional way of using a legal entity to define the subsidiary is somewhat problematic in this study. For example, some subsidiaries with legal entity status had two or more units in different locations in China. Some units had their own HR department. This would mean that within the same subsidiary, if defined by legal entity, there could be more than one HR department or HR administration. The other situation was that although some Finnish MNCs had more than one legal entity in China, these subsidiaries had one common HR department, which was physically located in one of the subsidiaries. A decision was made that a unit that had its own HR department or HR administration was treated as a subsidiary. All the thirteen cases included in this study come under this definition. The number would be different if the subsidiary were defined differently.

### **3.5. Data Collection**

This study uses multiple sources of data: interviews and documents. This data collection approach is supported by the literature on the importance of using a variety of data sources in case studies. Yin (2003) notes that case studies often

involve collecting data over a period of time and allow for use of varying methods such as interviews, documentary analysis and archival analysis, surveys, and participation observations. Some scholars even specify multiple data sources as a criterion for defining a case study; for example, Yin's "multiple sources of evidence" (2003:14). In research practice, however, mixing data sources seems to be applied much less. Piekkari et al. (2009) found that interviews are the dominant source of data in case studies in the IB research; other sources of data are underutilized or barely acknowledged. They advocate greater use of a variety of data sources including documents, observation and quantitative data in addition to interviews. This research thus paid attention to diverse sources of data. Apart from interviews, I employ various forms of documentary data.

### **3.5.1. In-depth Personal Interviews**

A total of 43 interviews were used in this study. The interviews were conducted with the thirteen case companies between 2006 and 2010 in two projects, thus labeled as two sets.

#### *The first set of interviews*

This set includes nine interviews conducted between 2006 and 2007. These interviews were part of the total interviews for the research project on the operations of Finnish companies in China<sup>6</sup> where I was working as a researcher in collecting the data and writing the report (Kettunen et al., 2008). A colleague and I conducted these nine interviews with the following case subsidiaries: EquCo3, IndCo2, EngCo1, EquCo2, EngCo2 and ConCo. Part of the interview protocol concerned Chinese business environment and employee relations of Finnish companies in China. The interviews provided me with a general understanding of the Chinese institutional environment, especially the labour market context- the high labour mobility and fierce competition for skills. The interviews also supplemented the information collected in the second set and

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<sup>6</sup> This dissertation was a sub-project of "Managing Business in Turbulent Markets" funded by the Finnish Funding Agency for Technology and Innovation and carried out at the Center for Markets in Transition (CEMAT), Helsinki School of Economics in 2005-2008.

helped understand the overall picture of the respective case companies. In addition, the interviews served as checking reference to clarify or confirm/disconfirm some ambiguous points that appeared in the second set of interviews.

### *The second set of interviews*

This set consists of 34 in-depth personal interviews with the thirteen case subsidiaries. These interviews were designed solely for this research and carried out by myself. My doctoral dissertation was part of the research project entitled “Globalization and International Management: Successful Governance of Intercultural Communication in Finnish-Chinese Business Operations”, funded by the Academy of Finland for the period of 2008 - 2010. This project facilitated good access to the case companies as I was working as a researcher during the three year period of project.

I conducted the 34 interviews at the companies’ sites in China (except two in Finland) during three trips: August-September 2008, January-February 2009, and February-March 2010. Three interviewees were interviewed twice. The interviews lasted from forty minutes to three hours. All the interviews were recorded with a digital recorder and transcribed verbatim later. A summary of the total interviews in both sets can be found in Appendix 1.

An interview guide was designed and tested with one subsidiary. It proved appropriate, and therefore only a few minor modifications were made. The test interview was included in the study. The interview guide includes three major areas for investigation: the impact of the Chinese institutional environment on HRM practices, the transfer of HQs’ HRM practices and subsidiary perception of and implementation of these practices (see Appendix 2). The company information (such as establishment, operational history and functions), presence of expatriates over time and interviewee profile were also collected during the interviews. The specific questions and how they were asked depended on the context of the interviews. Retrospective questions were asked to investigate the developmental aspect of the HRM practices, for example, evolvement of HQ-transferred practices over time, changes in HR practices, especially before and after the enactment of the Labour Contract Law of China in 2008.

The interviews were semi-structured with open-ended questions (Silverman, 2000). This allowed the interviewees to talk about what they felt to be important on the subjects chosen for the interviews. In fact, a few themes that are less addressed in the literature emerged from the interviews, such as the important influence of the labour market competition, the diverging values of Chinese employees and impact of socio-economic conditions on HR practices.

#### *The interviewees*

The interviewees included senior business managers, functional managers and HR managers. The positions of the interviewees in each case company are summarized in Table 3.2 below.

**Table 3.2** The interviewees' positions, nationality and their code

Case company	Interviewee position	Nationality	Interviewee code
IndCo1	General manager	Finnish	IndCo1 1
	HR deputy manager	Chinese	IndCo1 2
	HR manager	Chinese	IndCo1 3
EquCo1	Vice general manager	Chinese	EquCo1 1
	Business director	Finnish	EquCo1 2
	HR manager	Chinese	EquCo1 3
IndCo2	Asia-pacific president	Finnish	IndCo2 1
	Admin. manager	Chinese	IndCo2 2
	HR manager for China and Asia-pacific	Chinese	IndCo2 3
EngCo1	General manager	Chinese	EngCo1 1
	Finance director	Third country	EngCo1 2
	R & D director	Finnish	EngCo1 3
	HR director for China and Asia-pacific	Chinese	EngCo1 4
	HR manager	Chinese	EngCo1 5
	Business Director	Finnish	EngCo1 6
EquCo2	East Asia president	Finnish	EquCo2 1
	General manager	Third country	EquCo2 2
	HR manager	Chinese	EquCo2 3
	Sales manager	Finnish	EquCo2 4
EngCo2	China vice president	Chinese	EngCo2 1
	General manager	Finnish	EngCo2 2
	HR manager for China	Chinese	EngCo2 3
MecCo	General manager	Finnish	MecCo 1
	HR manager	Chinese	MecCo 2
ServCo	China President	Finnish	ServCo 1
	HR manager for China	Chinese	ServCo 2
ConCo	Asia-pacific president	Finnish	ConCo 1
	General manager	Chinese	ConCo 2
	HR manager	Chinese	ConCo 3
IndCo3	Business director	Finnish	IndCo3 1
	HR director for China	Chinese	IndCo3 2
EquCo3	General manager	Finnish	EquCo3 1
IndCo4	General manager 1	Finnish	IndCo4 1
	General manager 2	Finnish	IndCo4 2
	HR manager	Chinese	IndCo4 3
EquCo4	General manager	Finnish	EquCo4 1
	HR manager	Chinese	EquCo4 2

As Table 3.2 shows, in all the case companies except EquCo3, there was minimum one HR manager interviewee. IndCo1 and EngCo1 had two HR managers. The HR managers worked at various levels, e.g., subsidiary level, China level or Asia-Pacific level. When the Finnish MNC had several subsidiaries in China there tended to be a China HR manager at country level. In IndCo2 and EngCo1 the China HR manager also held a concurrent position as Asia-Pacific HR director. It was obviously because of the important position of China in Asia-Pacific area in the corporate strategies. In EquCo1 and ServCo the China HR manager also acted as HR manager for one of the subsidiaries. This was probably because the China units were few and small. In the small case subsidiaries, such as EquCo3, EquCo4 and IndCo1, the HR manager also acted as administration manager/ sales manager. These companies combined HR and administration into one department.

In all the case companies there was at least one top manager (general manager or equivalent) as an interviewee. The general managers were responsible for the operation of one local unit, such as a factory or a plant. There were also several regional (China or Asia) directors/ presidents. The inclusion of one subsidiary top manager and one HR manager in each case (except EquCo3) was to ensure that balanced information on the Chinese context, HQs policies, subsidiary HR decisions, and practice execution was obtained. It also made cross-checking possible in the case of ambiguity.

For reason of transparency all the interviewees are coded with the subsidiary's pseudonym followed by a number (see Table 3.2). For example, IndCo1 3 denotes that the interviewee is the third interviewee in the case company IndCo1. The interviewees' codes are used when their direct quotations are presented.

All the 14 HR managers were Chinese nationals. They were mostly Chinese females (11 females out of total 14 HR managers). Out of the 23 senior managers and functional managers, 16 were Finnish nationals, five were Chinese, and two were third country nationals. The profile of the total 37 interviewees is summarized in Table 3.3 below.

**Table 3.3** The profile of the total 37 interviewees by position, gender and nationality

Position	By gender		By nationality		
	Male	Female	Finnish	Chinese	Other national
Senior business manager (general manager, director, China/Asia president)	20	1	15	4	2
Functional manager (admin. and sales)	2	0	1	1	0
HR manager (at subsidiary level and at China or Asia- pacific level)	3	11	0	14	0
Sub-total	25	12	16	19	2
Total	37		37		

As Table 3.3 shows, the senior business managers were dominated by expatriates, especially Finnish male expatriates. It was apparent that the emphasis on expatriates, especially home country expatriates was fairly common among the case companies. Apart from top management positions, there were expatriates in technical and functional positions as well. The number of expatriates in a few large case subsidiaries (EngCo1, EquCo2 and EngCo2) had been relatively high; for example, there were some 40 expatriates in EngCo2. There was, to some extent, localization of subsidiary management in some case companies. For example, the general manager of EngCo1 and ConCo was originally a Finn at the establishment and early operation and was replaced by a Chinese later. The number of expatriates was also reduced in some large case subsidiaries such as EngCo1, EquCo2, EngCo2 and ConCo.

### 3.5.2. Documentary Data

It is worth noting that documentary data form an important part of the total data set of the present study. The documents include relevant laws and regulations of China in the period from 1980 to 2010. The laws in the early period of reform, namely from the 1980s to early 1990s, were often in the form of

decrees or decisions made at the national level by the Chinese government because the legal system had not been well established. Most of these laws in this period had been abolished and became historical documents. Important laws and regulations were selected at both the national level and the provincial/municipal level. For example, Labour Law of People's Republic of China (promulgated in July 1994 and enacted on January 1, 1995) and the Labour Contract Law of People's Republic of China (promulgated in June 2007 and enacted on January 1, 2008) were the most important pieces of labour legislation. I collected the national labour laws from published books and Internet. The provincial and municipal regulations were collected partly from some of the interviewees and partly from the Internet.

The Chinese Communist Party has pursued economic reform and guided China's transition from a centrally planned economy towards a market economy. Party Congress documents were important references for understanding the progress and direction of the reform. The published documents of the Chinese Communist Party were publically available in collections and on the Internet as well. I collected these materials from those sources. Other sources of documents are news, reports and surveys. They were collected from newspapers, magazines and Internet. These materials concern e.g. China's official report on the important events of the economic reform, China country reports and business surveys conducted by various organizations such as OECD and the World Bank, publications and Internet materials on Finnish industrial relations, and reports and surveys on Finnish labour market and Finnish employees. A list of the published documentary data used in this study can be found in Appendix 3.

In addition, company documents were collected in forms of paper materials and Internet materials such as annual reports, newsletters and brochures. I obtained part of these from the interviews and part from the companies' websites. Other company documents include company presentations, operational guidelines, organization charts, HQ's policies and practices, and employee handbooks. These documents were collected together with interviews from some of the case subsidiaries with permission. Because most of these documents were confidential not all the subsidiaries were willing to release them.



### 3.5.3. Use of Multiple Data Sources

The multiple sources of information complemented each other and supported the overall study in answering the research questions. Table 3.4 summarizes the sources and use of the data for the study.

**Table 3.4** Summary of the whole data set and their use

Source of data	Language	Content of data	Where the data were used
Interviews (personal interviews with managers of the case companies)	English Chinese	Information on the case subsidiaries and their HQs	Chapter 3: Description of the cases Chapter 5: Chinese institutional context in later reform period Chapter 6: Overall findings including transfer of Finnish MNC HQs' practices, localization of HQs-transferred practices, subsidiary locally designed practices.
Documents (published books, Internet, newspaper, company brochure and annual report, website, presentation and internal documents)	Chinese	Policy and decisions of Chinese Communist Party on economic reform	Chapter 4 Historical context
	Chinese	China's laws and decrees on enterprise reform, China's laws on foreign investment, China's Labour laws and employment regulations at national and local level	Chapter 4: Historical context Chapter 5: Chinese institutional context in later reform period
	English Chinese Finnish	Public surveys and reports on China and Finland	Chapter 5 Chinese institutional context in later reform period; comparison between China and Finland Chapter 7: Discussion on differences between Finnish and Chinese institution
	English Chinese	Information on the case subsidiaries (including their HQs and MNC organization)	Chapter 6: findings on HQs' HR policies and practices, subsidiary strategic role, subsidiary HR practices

It is worth noting that documentary data form an important part of the total data set of the present study. The documents include relevant laws and regulations

of China in the period from 1980 to 2010. The laws in the early period of reform, namely from the 1980s to early 1990s, were often in the form of decrees or decisions made at the national level by the Chinese government because the legal system had not been well established. Most of these laws in this period had been abolished and became historical documents. Important laws and regulations were selected at both the national level and the provincial/municipal level. For example, Labour Law of People's Republic of China (promulgated in July 1994 and enacted on January 1, 1995) and the Labour Contract Law of People's Republic of China (promulgated in June 2007 and enacted on January 1, 2008) were the most important pieces of labour legislation. I collected the national labour laws from published books and Internet. The provincial and municipal regulations were collected partly from some of the interviewees and partly from the Internet.

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most of these documents were confidential not all the subsidiaries were willing to release them.

### **3.6. Data Processing and Analysis**

#### **3.6.1. Selection of the Causal Conditions**

The selection of causal conditions is made based on three major considerations: theoretical relevance, empirical data, and the proportion of the number of conditions to the number of cases. The result is the overall balance between these three.

Rihoux and Ragin (2009; also Rihoux, 2003) argue that identifying and selecting the causal conditions are the most demanding part of the QCA. The choice of causal conditions should be theoretically informed (Berg-Schlusser and De Meur, 2009). Institutional theory and MNC HQs-subsidiary power relationships are the core theoretical perspectives of this research. I identified six conditions according to the theoretical perspectives and existing research as discussed in Chapter 3 (see Section 2.5 for a summary of the preselected conditions).

Empirical case knowledge plays an important role in selection of conditions as well (Rihoux and Lobe, 2009; Yamasaki and Rihoux, 2009). Theoretically identified conditions may be refined with case knowledge during the research process. During the data processing, two conditions, labour laws and labour unions, were found no impact on the localization of both compensation and performance practices. Thus these two conditions are not included in the QCA analysis, but the findings on them are presented briefly in Chapter 6. The data revealed that it was not only the local regulations and policies but also other factors (industrial development, potential job opportunities, living standards, etc.) that mattered in how subsidiaries perceived HQs compensation policies and practices fit to the local context. Therefore, the condition local regulation was refined to a more comprehensive concept – location – to reflect the overall attractiveness of the location where the respective case subsidiaries were located.

The number of conditions is limited by the technique used in crisp-set QCA, Boolean algebra. As discussed earlier, the causal conditions should be converted into binary values. The number of logically possible combinations of causal conditions increases geometrically as the number of conditions increases. For example, six causal conditions can result in 64 ( $2^6$ ) possible combinations (observable from the empirical cases and logically possible but unobservable from empirically cases). This will generate a considerable amount of logical remainders when there are only a small number of empirical cases. This is the problem of “limited diversity” in social sciences (Ragin, 1987, 2000, 2008a). One consequence of this is that the Boolean minimization on the intermediate solution and parsimonious solution will be made heavily relying on simplifying assumptions about the logical remainders, which might lack empirical support. The other consequence is that it tends to produce individualized causal paths for each case, thus difficult to seek synthetic explanation of outcome across the cases (Marx, 2010; Rihoux and Ragin, 2009).

This “few cases, many conditions” problem is a common challenge in QCA applications (Rihoux and Ragin, 2009). The question is more about the balance between the number of conditions and the number of cases (Berg-Schlosser and De Meur, 2009), though the limit to the maximum number of conditions is important as well (Marx, 2010). The general recommendation is that the number of conditions should be kept moderate (Rihoux and Ragin, 2009; Wagemann and Schneider, 2010). Marx (2010) even suggests that the number of conditions should be significantly lower than the number of cases. Berg-Schlosser and De Meur (2009: 28) inform that for the number of cases from ten to 40, a common practice would be to select from four to six or seven conditions. Marx (2010) suggests a more fine-grained benchmark to the number of conditions in relation to the number of cases. According to these suggestions four causal conditions would be appropriate for ten cases as used in this study.

There are many possible factors that would affect whether a subsidiary adopts a localized or standardized practice. For example, at the Chinese institutional side, apart from labour market mobility and location, the data revealed that work related values of employee are highly relevant to the localization of HRM practices. At the MNC organization side, apart from HQ monitoring by means of formal authority, means of informal or social control

such as communication, expatriate, and networking could be relevant (see, e.g., Blazejewski, 2006; Gamble, 2003; Harzing, 2001; Marschan, Welch and Welch, 1996). The key principle followed by this study in selecting the very limited number of causal conditions is to focus on the core causal conditions rather than all possible factors<sup>7</sup> (Ragin, 1987; Rihoux and Ragin, 2009). The interest of this research is to examine localization of HRM practices under competing pressures of host and home country institutions and HQs-subsidary power relationships. The core conditions should reflect this theoretical assumption. Meanwhile empirical relevance was an important consideration as well. For example, the data indicate that networking of HR managers was less apparent than HQs monitoring in terms of the outcome of transferred practice. Table 3.5 below summarizes the four conditions that were finally included in QCA analysis on the localization of compensation practice.

**Table 3.5** The causal conditions for QCA

Condition	Definition
Labour market mobility	Labour market mobility refers to voluntary employee turnover.
Location	A combination of specific conditions of the locality (labour regulations, wage level, quality of living, skills supply) where the subsidiary operates.
HQs monitoring	HRs monitoring refers to the monitoring by the HQs on the implementation of HQs transferred practices.
Strategic role of subsidiary	Strategic position of subsidiary within the MNC corporation.

The four conditions shown in Table 3.5 correspond to the two key theoretical perspectives used as the theoretical guidance of this study. The first two conditions, labour market mobility and location, capture the host country institutions in comparison with those of home country and the last two conditions, HQ monitoring and strategic role of subsidiary, capture the MNC HQs-subsidary power relationships. Further, these four conditions were verified by the case data being relevant. The ratio of four conditions to ten

<sup>7</sup> See Berg-Schlosser and De Meur (2009) and Yamasaki and Rihoux (2009) for detailed discussion on several strategies to reduce the number of conditions.

cases complies with the suggestion of Berg-Schlosser and De Meur (2009) and Marx (2010). Unavoidably, the reduction of the conditions causes some loss of the data. This will be discussed later in the limitations of the study.

### **3.6.2. Calibration of the Conditions and the Outcome**

As discussed earlier, QCA is a configurational comparative method. This requires comparing cases in the form of combinations of attributes of cases. Cases are transformed into configurations with a number of causal conditions and an outcome which have been identified theoretically (and empirically). Each causal condition and the outcome are regarded as a domain or set where a case may be a member. A case may have a membership in multiple sets. The purpose of calibration is to assess the membership of each case to these different sets. Cases are coded with set membership scores. This process of translating the raw data into set membership scores is calibration.

In csQCA, a case's set membership is evaluated on the two mutually exclusive states of membership or non membership. A threshold must be defined in order to specify whether a case is a member of the set or a non member of the set, i.e., fully in (presence) or fully out (absence). The causal conditions and the outcome are dichotomized into presence and absence and subsequently assigned the value 1 or 0 respectively. In this study each of the four causal factors – labour market mobility, location, HQs monitoring and strategic role of subsidiary and the outcome localization – are dichotomized with the state of presence or absence. Ragin (2000:150) posits that calibration of set-membership should be based on the combination of theoretical assumptions and empirical evidence. Threshold-setting is best guided by both theory and data knowledge, and is often iterative between theory and data (Ragin, 2000, 2008a; Rihoux and De Meur, 2009; Rihoux and Ragin, 2009). Essentially, the calibration should enable to categorize the cases into qualitatively different sets. As Ragin puts it, “crisp sets establish distinctions that are wholly qualitative”. (Ragin, 2000: 153) As for the types of data, generally, information obtained from various data sources, such as questionnaire, interview, focus group, and participatory observation, can be used for set calibration (Schneider and Wagemann, 2012). This study uses

qualitative data, interview and documentation to calibrate the conditions and outcome, similar to the study of Crilly (2011). Below, I elaborate on the dichotomization of the conditions and the outcome respectively.

#### *Calibration of the conditions*

The measurements for labour market mobility, location and HQs monitoring are defined according to the theory discussed in the literature review combined with the knowledge of the cases at hand. For crisp set QCA technique, it is suggested that the coding of presence and absence with the value 1 and 0 indicates a direction of association between the condition and the outcome. That is, the presence of a condition coded with the value 1 is theoretically expected to be associated with a positive outcome ([1] outcome), and the absence of a condition coded with the value 0 is theoretically expected to be associated with a negative outcome ([0] outcome) (Rihoux and De Meur, 2009). That is, explicit or implicit hypothesis may be made based on the theoretical assumptions or existing research. Table 3.6 presents the measure and coding of the four conditions.

**Table 3.6** Calibrating and coding of the conditions for localization of compensation practice

Condition	Calibration	Coding of binary values
High labour market mobility	Pressure of high labour market mobility	Value 1 (presence of the condition): Subsidiary perceives/ experiences a pressure of high labour market mobility.  Value 0 (absence of the condition): Subsidiary perceives/ experiences no pressure of high labour mobility.
Unattractive location	Unattractiveness versus attractiveness of the location	Value 1 (presence of the condition): The location is unattractive.  Value 0 (absence of the condition): The location is attractive.
HQs monitoring	Weak versus strong monitoring by the HQ over implementation of transferred practice	Value 1 (presence of the condition): Weak monitoring by the HQ.  Value 0 (absence of the condition): Strong monitoring by the HQ.
Strategic role of subsidiary	The size of the market and R & D function of the subsidiary	Value 1 (presence of the condition): If a subsidiary operates in a big market or a key growth market or has an R & D function.  Value 0 (absence of the condition): If a subsidiary operates in a small or a non key growth market or has no R & D function.

As discussed earlier (see Section 2.3.3) the condition labour market mobility is derived from the notion of employer-employee interdependence. As Table 3.6 shows, the condition labour market mobility is re-worded to high labour market mobility to indicate a direction of the condition. The measurement of this condition is defined according to the assumption that the subsidiaries that face pressure of high labour market mobility will have big need for adapting the HQ-transferred practices to the local environment in the case of misfit between the HQ's practices and perception of subsidiary. Conversely the subsidiaries that face no pressure of high labour market mobility will have no/ little need



for adapting the HQs' practices to the local environment. Hence, in the former situation the value 1 is given and in the latter situation the value 0 is given.

The condition location is derived from the sub-national institutions (see Section 2.3.3). In a similar logic to labour market mobility, the condition location is reworded to unattractive location as shown in Table 3.6. It is assumed that an unattractive location would prevent the subsidiary to fully implement the HQ-transferred practices and have a higher need for localization in the case of misfit of HQ's practices to the local context. Hence, an unattractive location would induce the subsidiary to modify the HQ-transferred practices, resulting in localization. Conversely, an attractive location would facilitate the subsidiary implementing the HQ-transferred practices and have lower need for modifying the HQ's practices. Thus the outcome of transfer is likely to be standardization. Accordingly, in the former situation the value 1 is coded and in the latter situation the value 0 is coded.

I use interview and documentary data to calibrate the causal conditions (see Crilly, 2011 for a similar approach). The calibration of the three conditions – high labour market mobility, unattractive location and HQ monitoring – was entirely based on interview data. For examples, for the condition of high labour market mobility, value 1 is assigned when a subsidiary reported its experiences or perception of pressure from high labour mobility on its compensation practice. The subsidiary felt that the HQ's standardized policy could not meet the demands of the local labour market in terms of retaining desired employees. In the case of unattractive location, employees needed additional incentive beyond those provided by standardized MNC policy of remuneration in order to encourage them to come to the location in the first place. The subsidiaries that located in an unattractive location perceived a greater need to modify the transferred compensation practice than those that located in an attractive location where recruitment and retention were relatively easy and the need to modify the HQ's policy was less or little. As for the condition strategic role of subsidiary, market size and R & D responsibility of subsidiary are used for calibration. As discussed in Section 2.4.2, when a subsidiary operates in a large market/ a key growth market it tends to be an important profit contributor to the MNC organization. If a subsidiary has an R & D function it tends to be a knowledge competence centre. Festing et al.'s (2007) study especially confirms this. If the case subsidiary possessed one of these two elements it is considered

strategically important. Then it is calibrated to the full membership. The value 1 is assigned. Conversely if a subsidiary operated in a small or non-key growth market or had no R & D function it is calibrated to full non membership. The value 0 is assigned. This factual information is primarily based on the annual reports and other documents published on the companies' websites and news published in newspapers and Internet. The interviews also provide some useful information concerning some case subsidiaries.

### *Calibration of the outcome*

The outcome which this study investigates is localization of HRM practices. As defined in Section 2.1.1, localization is conceptualized as modifying MNC HQ-transferred HRM practices to the local context. This theoretically justified concept itself entails a measure to the outcome. Similar to the study conducted by Crilly (2011) I calibrate on the outcome with substantive case knowledge. I coded interview transcriptions on the modification of HQs HRM practices for each subsidiary. By comparing across the cases, I identify that five subsidiaries adjusted the HQs practice to make it appropriate to the local context. These cases are calibrated into presence of the outcome, localization and assigned the value 1. Three subsidiaries implemented the transferred practice with a minor modification and two subsidiaries implemented the transferred practice without modification. These five cases are calibrated into the set of absence of outcome, standardization and assigned the value 0. Although there is a difference in the extent of modification across the cases this calibration differentiates the cases into two different kinds: those that adjusted the HQs practice to the local context and those that primarily adopted the HQs practice as it was. This indicates a qualitative difference between the two sets (see, Ragin, 2000; 2008a) in the outcome of transfer. In the localization set the modified practice was substantially different from the HQ-transferred one. In the standardization set the minor-modified or unmodified practice was basically the same as the HQ-transferred one.

### 3.6.3. Construction of the Truth Table and Boolean Minimization

According to Ragin,

[t]he goal of truth table construction is to identify explicit connections between combinations of causal conditions and outcomes. Using the truth table, it is possible to assess the sufficiency of all logically possible combinations of presence/absence conditions. (2008a: 125)

Each combination of conditions represents a sufficient path to a given outcome in the truth table. Each configuration may correspond to one or more cases.

In order to construct the truth table I first made a data matrix. I inserted the information on the findings of causal conditions and outcome to a table matrix. Each case exhibits a configuration of four causal conditions (high labour market mobility, unattractive location, HQ monitoring, and strategic role of subsidiary) with a membership value 1 or 0 and an outcome (localization) with a membership value 1 or 0.

Before proceeding to the analysis of sufficient conditions, I tested the necessity. This step should be performed separately and before minimization (Schneider and Wagemann, 2012) because a necessary condition may be dropped out from the solution due to minimization. Next, I carried out the minimizations following “standardized analysis” procedure recommended by Ragin (2008b) and obtained the “complex solution” (Ragin and Davey, 2009). As explained in Section 3.2.7., the complex solution informs the causal path(s) from the observed cases, i.e., the empirical cases. It is also referred to as “conservative solution”, i.e., the researcher does not make assumption about any logical remainder and is entirely guided by the empirical information at hand (Schneider and Wagemann, 2012). Then, I proceeded to minimizing the configurations with logical remainders, i.e., including some of the configurations where no empirical case exists. This resulted in two simpler solutions termed as “parsimonious solution” and “intermediate solution” (Ragin, 2008b; Ragin and Davey, 2009). Upon comparison of the three solutions I opted for the complex solution because it matches better the purpose of this study to explain the localization with interplay of the competing

pressures between the host- and home-country institutions and the MNC organization.

### **3.7. Evaluating the Quality of the Study**

I evaluate the quality of this study with two sets of criteria. One concerns the conventional criteria on the quality of empirical social research, in particular, case studies (Yin, 2009). The other concerns the criteria on the QCA method (Rihoux and Ragin, 2009; Wagemann and Schneider, 2010). These two sets of criteria are applied in an integrated manner to assess the validity and reliability of the study. In addition, the role of language in cross-cultural research setting (Marschan-Piekkari and Reis 2004) is discussed in relation to the validity and reliability.

#### **3.7.1. Validity**

##### *Construct validity*

Construct validity refers to establishing correct operational measures for the concepts being studied (Yin, 2009). To increase the construct validity, Yin (2009) suggests three tactics: using multiple sources of evidence, establishing a chain of evidence, and having key informants review the case report. All these three tactics were followed. The multiple data sources I used in this study combined interviews, the most common method, with documents.

The advantage of applying multiple data sources in this research is that the strengths of one data type compensated for the weaknesses of another data type (see, Patton, 1990). While interviews can generate rich content they are sensitive to the context. The richness of the information obtained depends to some extent on the relationship between the interviewer and interviewee and a number of other factors (Patton, 1990:245). Documents can provide additional information to interviews and along a period of time for longitudinal study. This complementary role of different sources of evidence is clearly shown in this study. For example, the historical context of Chinese early economic reform and the labour legislations at national and local levels in China relied

primarily on documentary data. The company internal documents allowed me to compare in detail the performance appraisal forms of the subsidiaries, which were not all described by the interviewees. The comparison with Finnish home country institutional environment and cultural values relied heavily on documents (reports, surveys, newspapers and Internet) as well.

Use of multiple informants in each case also helped make the data more credible and reliable (Yin, 2003). There were multiple interviewees per case in all the subsidiaries except EquCo3. EquCo3 was a small company of 40 employees. The general manager was closely involved in HR issues, thus was considered being able to provide sufficient information on the HR practices of the company. The multiple informants increased data validity by obtaining a more holistic picture of the phenomenon. For example, in IndCo2 the top manager reported that they had HQ-transferred performance management. The HR manager explained that the performance appraisal was not carried out in practice though the evaluation template was in place. This became an important finding; it showed that practice transfer does not necessarily mean implementation. The top manager might have limited knowledge of specific practices. It was crucial to include HR managers as informants. On the other hand, the HR manager, depending on the position level and the MNC in question, might lack awareness of HQs policies, such as budget arrangements between the subsidiary and HQ, and the subsequent effect on pay levels and compensation practices. For example, negotiations on the pay rise often happened between the subsidiary top manager and the HQ. Hence, it was important to include top managers in the interviews as well.

Other measures were also taken to increase the validity of the data. I conducted a pilot interview in Finland with the general manager of one case subsidiary. After the interviews, I did some follow-up telephone calls and emails to make up the missing information and check the ambiguous points. An interview report was sent to the interviewees for review. In writing up the research the data sources were cited and talks by the interviewees were quoted to provide a chain of evidence for the reader to follow. I also assigned a code to each interviewee in a systematic way (see Table 3.2) to increase the transparency of the data source.

One major weakness of the data is the lack of interviews with HQs' representatives. This implies that the findings on localization of the practices

were generated from the interviews with the subsidiaries. That is, the HQs' monitoring and the subsidiaries' modification of the practices were the views of subsidiaries. There is no cross-check with the HQs. The possible consequence on the results of the study will be further discussed in the section on the limitations (see Chapter 8). Additionally, EquCo3 had only one interviewee, the general manager. There was no verification of the interview data with the HR manager of the company. Some HR specific information might be missing. This is considered as a minor weakness as EquCo3 was not included in the examination of localization of the compensation and performance management practices, which is the core of the study.

### *Internal validity*

Internal validity defined by Yin (2009:40) refers to establishing a causal relationship, whereby certain conditions are shown to lead to other conditions, as distinguished from a spurious relationship. The QCA method applied in this study offers high potential in generating causal relationship in case studies. Exploring causal complexity is the central purpose of the QCA approach. The key strengths of QCA, multiple conjunctural causation, configurational approach and a set-theoretical method, represent a logical, rigorous methodological approach to uncover causal complexity. These are discussed at length in Section 3.2. The technique of crisp-set QCA uses Boolean algebra as a formal tool and combines both qualitative and quantitative features. This allows for drawing parsimonious causality from complex cases and meanwhile keeping the richness of narratives on individual cases. These features of QCA warrant the use of this method appropriate for the research question of this study- investigating explanations to localization with configurational conditions. In terms of the five types of use of QCA (Berg-Schlosser et al. 2009, see also Rihoux, 2003), this study can be regarded being the fifth type- developing theoretical arguments. The four solution formulas of localization of compensation practice are interpreted through a dialog with the cases. The combinatorial effects of the causal conditions are analyzed. The causal mechanisms are explored through "process observation" within the individual cases (Collier, Brady and Seawright, 2004: 252).

Selection of the cases for QCA analysis on compensation practice followed the MSDO (most similar cases, different outcomes) strategy (Berg-Schlosser and De Meur, 2009). The cases are matched with commonalities in, such as the transferred practice, the country of origin of the MNCs, Finland, and the host country, China. This increased the comparability of the cases and thus, the internal validity of the observed relationships was enhanced (see, Berg-Schlosser and De Meur, 2009).

Ideally, selection of cases should include both positive cases and negative cases (Berg-Schlosser and De Meur, 2009). In this study positive cases can be regarded as the cases of localization. Negative cases can be regarded as the cases of standardization. In effect this suggestion may be seen as rooted in the background of QCA. QCA was originally developed for comparative study in social and political sciences where nation-states, political groups and ethical groups are often the subjects of interests. As mentioned earlier, the majority of QCA applications are at the macro- or meso-level studies and the knowledge about cases mostly derives from secondary sources such as documents, newspapers articles and monograph accounts, or reports (Rihoux and Lobe, 2009). The practice level information which this research concerns, i.e. which companies localized HQs-transferred HR practices and which did not, was not available prior to selecting the case subsidiaries. The outcome could not be used as a criterion in the selection of cases at the first place. Nonetheless, both localization and standardization of compensation practice were observed from the cases.

QCA is not only a case-sensitive method but also a condition-sensitive method. The inclusion of conditions affects the causal patterns produced. While the general recommendation for a moderate number of cases was followed this also limited the choice of the conditions, which in turn affected the model. That is, the model is built on the four conditions: labour market mobility, location, HQs monitoring and strategic role of subsidiary. Although work related values of employees emerged as being highly relevant to localization of compensation practice it could not be included as a separate factor. This inevitably caused some loss of the data. Another relevant factor, emphasis on expatriates indicated by the literature to be relevant in cross-border transfer of HR practices, could not be included as a condition either. As already discussed in Section 3.5.1, the restriction of the number of cases is a

common challenge in QCA application. In fact this limitation applies to any empirical analysis that involves a relatively large number of variables, such as statistical analysis (De Meur, Rihoux and Yamasaki, 2009). De Meur et al. (2009) argue that the difficulty in selecting conditions can be an advantage because it forces the researcher to be rigorous and transparent with the choices of factors and theories. In this study the choice of HQs monitoring over expatriates was based on the higher relevance of HQs monitoring than expatriates revealed in the empirical data. In addition, two preselected conditions, labour law and labour unions proved to be irrelevant and thus removed from the preliminary conditions. These can be seen as steps increasing the internal validity of the model.

The calibration of set membership in this study used qualitative information. The three conditions labour market mobility, location and HQs monitoring were dichotomized with interview data. This qualitative threshold setting required in-depth knowledge of each case and was an iterative comparison between the cases. Efforts were made to systematically code the interviews of each case concerning the conditions. An Excel form was used in coding. Based on this the cases were calibrated. Quotations or summary of relevant interview talks were provided to show the evidence. As Yamasaki and Rihoux (2009: 132) assert, although this type of strategy does not ensure replicability, it offers strong empirical justification, given its anchor in case knowledge.

Crisp-set QCA has been criticized of its dichotomous treatment of data. This is indeed a limitation of this technique. It does not capture the fine-grained differences between cases<sup>8</sup>. In this study there was a minor change of HQs-transferred compensation practice in two case companies that are calibrated to the set of standardization. It should be noted, however, the study addresses two types of outcome of cross-border transfer of HR practice. The dichotomy distinguishes essentially the two different types of outcome: the HQ's practice is implemented differently from the original one (localization) and the HQ's practice is implemented largely the same as the original one (standardization). In this way, the choice of crisp set QCA is considered to be grounded in theory and empirical data.

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<sup>8</sup> For detailed discussion on the critiques and the responses to them, see De Meur et al. (2009).



It is recommended that QCA should be used in combination with other method(s) (e.g. Schneider and Wagemann, 2010). This study combines QCA with qualitative in-depth case study. All the cases are traceable in the QCA solution terms. The in-depth case knowledge allowed me to go back to individual cases in interpretation of the QCA results (the solution terms). The within-case analysis revealed the causal mechanisms how different paths lead to the same type of outcome of localization.

### *External validity*

The QCA approach adopted by this study has their philosophical foundation closely associated with critical realism. This necessitates a re-consideration of the conventional criteria for external validity of case study research. Yin (2009) suggests that external validity concerns establishing the domain to which findings gained from the case study can be generalized. According to Yin (2009: 54; 43-44), a comparative case study is like experimental research design where replication logic can be applied. Thus, if a number of carefully selected cases exhibits similar results (literal replication), or produces contrasting results (theoretical replication) but for anticipatable reasons, then an analytical generalization is achieved. Tsoukas (1989) posits that this view of case studies limits our understanding of the role of comparative case studies in generalization of social empirical research.

Critical realism acknowledges that the existence of reality is independent of our perception of it, but our comprehension of reality is theory-laden and subjective (Bhaskar, 1978, 1998; Sayer, 1992, 2000). This critical realism stresses the need to retain both objective and subjective side of knowledge and views the world as consisting of three domains: real domain, actual domain and empirical domain. According to Sayer (2000) the real domain is a realm of objects, their structures and powers. They are unobservable and objective. “‘Structure’ suggests a set of internally related elements whose causal powers, when combined, are emergent from those of their constituents (Sayer, 2000: 14)”. The actual domain refers to partially observable events that are objective as well (Morais, 2011). The empirical domain consists of observable experience which is subjective. Sayer argues that

[w]hat causes something to happen has nothing to do with the number of times we have observed it happening. Explanation depends instead on identifying causal mechanisms and how they work, and discovering if they have been activated and under what conditions. (2000: 14)

This differentiates the realist view of causation from the positivist one that views causation as regular successions of events.

The critical realist paradigm may be seen as an alternative thinking of generalization from case studies to the positivist tradition (see, Easton, 2010; Morais, 2011; Piekkari and Welch, 2011; Tsoukas, 1989; Welch, Piekkari, Plakoyiannaki and Paavilainen-Mantymaki, 2011). Tsoukas (1989: 556) argues that within the realist paradigm, explanatory idiographic studies (case study being one of the most representative forms of such studies) are epistemologically valid because they are concerned with the clarification of structures and their associated generative mechanisms, which have been contingently capable of producing the observed phenomena. Generative mechanisms refer to causal powers (causal mechanisms) of objects, structures and entities. Thus, causal explanation is transcendental, irrespective of their individual manifestation in the domain of experience (empirical domain). That is to say causal powers are externally valid; however, their activation is, and thus their effects are, contingently determined.

The present study is primarily concerned with finding out the pertinent configurational patterns of localization of HRM practices in selected MNC subsidiaries in China and trying to produce explanations for the outcome of localization. Four different paths (configurations) of localization are identified with the combination of labour market mobility, location, HQs monitoring and strategic role of subsidiary (see Section 6.3.2). These four causal conditions are derived from institutional theory and power perspective. They are verified by the empirical case data. The causal mechanisms leading to the outcome are identified with a process through within case analysis (see, Brady and Collier, 2010; George and Bennett, 2005; Gerring, 2010; Mahoney, 2004). This involves returning back to the cases, a backwards link to the causal conditions, which differ from replication logic (Yin, 2009). From critical realist view, this implies that the results of this study would transcend the boundaries of the cases investigated (the empirical domain). In other words, the causal paths of

the localization are considered to be externally valid, i.e. generalizable to other foreign subsidiaries of the MNCs from matured, coordinated market economies such as the Nordic countries and some Western European countries. The results of this study are considered being extendable also to other host countries that share similar institutional environment with China, such as Vietnam, Russia, Eastern and Central Europe.

### **3.7.2. Reliability**

The reliability of this study is evaluated with transparency and good practices of QCA.

#### *Transparency*

The central thrust of reliability lies in transparency. Firstly, the research process should be transparent. Moisander and Valtonen (2006: 27) suggest that the data production process, analytical procedure and principles, how interpretation were developed, and conclusions drawn should be described explicitly. In this way, readers themselves can judge the results of study. In this study the various phases of the case selection are described carefully from the initial thirteen companies to the ten cases for examination of compensation practice and the nine cases for performance management practice. The selection of the conditions is documented in detail in their theoretical backgrounds and empirical relevance and in how the four finally selected conditions were derived from the initially chosen conditions. The selection of the HR practices, how the initial six practices were narrowed down to two practices, and eventually one for QCA analysis is described step by step. For each case, the process from calibrating the set membership on the conditions and the outcome to interpreting the results is described in a visible way. The reader can follow the whole chain of each case. Evidence from the data, such as interviews, company documents, public surveys is presented with their sources whenever possible.

Secondly, how the researcher's own background and stance might affect understanding and interpreting of the phenomenon under investigation should

be stated. Michailova (2004) argues that it is important to be aware – and make the reader aware – of the researcher's own conditioning and background, since they serve as the starting point of the research process. I would argue one step further that this can be especially relevant when the research is conducted in a across cultural context and the researcher is the cultural spanner, as in my case. I was born in China and educated in a Chinese university as an economist in international trade, and became a university lecturer in Beijing. For the past 15 years I have worked and lived in Finland as a lecturer, researcher, and manager for executive training programmes. All my work in teaching, research, and management training in Finland has been related to China, with frequent visits to China. My background bridges across the two cultures, Chinese and Finnish, and has greatly facilitated the research process in many ways.

Understanding the Chinese context was not based purely on the hard data which I collected during the research project. My personal experience as a Chinese who has lived through most of China's economic reform and transition thus far provided a rich and important source of knowledge for the study. For example, the role of Danwei (work unit) as a mini-welfare state and a kind of social institution remains in my memory from childhood. This system gradually diminished during the 1980s and eventually vanished in the early 1990s. However, some traits of its legacies remain. Many benefit practices identified from the case subsidiaries, e.g. the housing fund, extension of medical insurance to employees' family members, and provision of free lunch at the workplace reflected this. With my background I was able to see the development of the Chinese institutional environment on the one hand, and path dependency on the other hand. My background also influenced me to look at the impact of the Chinese environment on HRM practices from the broad contexts of China's transition and resultant social and economic changes. My experience of working and living in both Finland and China allowed me to better comprehend the differences in management culture, and business and social systems between these two countries. This in turn helped me in comparing the practices of the case subsidiaries with those of the Finnish home country.

### *Good practices of QCA*

Rihoux and Ragin (2009) and Schneider and Wagemann (2010; 2012) recommend a number of good practices for conducting a solid QCA application. Some important good practices were discussed in previous sections. The good practices of case selection followed by this study (see Section 3.3 for detail) include: The cases share sufficient background characteristics; the sample of cases was not taken as given, instead case selection was decided at a later stage of the research; the researcher has intimate knowledge of all the cases. The good practices on condition selection (see Section 3.6) include: The number of conditions is kept low; a good balance is achieved between the number of conditions and the number of cases. The outcome of interest to be explained (localization of HRM practice) is clearly defined.

The good practices on technical operations concern the issues such as the sequence of QCA analysis, presentation of data and results, use of software, and proper use of QCA terminology. Necessity analysis on both the presence and absence of the outcome was performed before the sufficiency analysis so that important condition(s) was not eliminated during the subsequent analysis on sufficient conditions. QCA analysis was carried out on both the presence of the outcome and absence of the outcome, but in a separate procedure (see, Rihoux and De Meur, 2009). The raw data matrix, truth table, results of QCA solutions and consistency and coverage are reported either in Section 6.3 and 6.4, or in the Appendixes. The software fsQCA (Ragin and Davey, 2009) was used in the entire operation of QCA analysis from constructing the truth table to producing the solution. Following these technical requirements helped minimize errors (see, Schneider and Wagemann, 2010), thus increased the reliability of the results.

QCA has developed its own terminology. QCA is based on the principles of formal logics and the techniques of Boolean or fuzzy algebra. Correct QCA terminology is followed; for example, the term “condition” is used, instead of “independent variable” as in linear algebra. Similarly, the phenomenon to be explained is termed “outcome” instead of “dependent variable”. Use of appropriate QCA language helped to express QCA notions correctly and avoided confusion with some other techniques, such as regression analysis that is based on a different epistemology and mathematical procedure from QCA (Schneider and Wagemann, 2010).

### **3.8. Sensitivity to Language in Cross-Cultural Research Setting**

Language can affect the quality of research in cross-cultural studies. The impact of language on the validity and reliability of this study is discussed here together. In qualitative IB research language use is not a mere technical issue; it has broad implications for the accuracy and authenticity of data (Welch and Piekkari, 2006). This is because the data are collected in the cross-cultural context involving different languages (Marschan-Piekkari and Reis, 2004). The same word may carry different connotations depending on the cultural bias (Patton, 2002). For example, Marschan (1996) showed that in Germany the question of relationship building had a connotation of unofficial activity and in Italy the term “personal relationship” even had more private meaning. This elucidates the idea that when assessing the validity of the data the possible effect of language has to be taken into account.

The language choice for data collection of this study was made based on the consideration of maximizing data accuracy. I interviewed Chinese interviewees in Chinese language (except one who preferred to speak English), taking advantage of being a native Chinese speaker. The Chinese language, my mother tongue, was obviously an advantage in collecting data in China. Talking in their own language enabled the Chinese managers to provide richer information than in a foreign language. Not all of them could communicate in English on the interview subjects. In addition, speaking the same language helped establish a relationship with the Chinese interviewees quickly. This is important in China, where personal relationships, Guanxi, play a bigger role than in Finland. In fact, some interviewees were eager to verify their impression of Finnish management culture with me when they learned of my long-term work experience in Finland. This created an interactive atmosphere during the interview.

The interviews with the Finnish managers and managers of other nationals were conducted in English. It was considered that the Finnish expatriate managers should have sufficient English proficiency to manage in day-to-day business in China. There was no noticeable language problem in my interviews with Finnish managers. They were all experienced international

managers who had worked abroad for a number of years. I used Finnish in small talk with some Finnish interviewees. It turned out to be positive in rapport-building (see, Welch and Piekkari, 2006).

The language effect is also extended to translation phase. Some researchers have pointed out the challenges in translating data between different languages in international business research (e.g. Marschan-Piekkari and Reis, 2004; Xian, 2008). My experience in translating Chinese interview transcriptions/quotes into English shows that translation is a highly contextualized process. The Chinese language is highly context-sensitive (Probably this is true for any language.). One reason is the linguistic differences between Chinese and English. For example, in Chinese language verbs are not conjugated. The temporal dimension is indicated by adverbs such as the words “today” and “tomorrow”. In spoken language these modifiers are often omitted. One has to understand the time frame in the context of the speech and use the appropriate tense in the translation.

One dilemma I faced in translation is whether I should translate according to the meaning or from the original words. Marschan-Piekkari and Reis (2004) used the meaning-based approach in translating interview data to English, i.e. the original meaning of the interviewee is revealed through paraphrasing and interpretation of the local context. The question is how far this approach can be used if the richness of the original language is to be retained. Sometimes there is simply no equivalent English for the Chinese word simply because of the social/ cultural differences. For example, the word 单位 (Danwei), the connotation of which is far from the word “organization” or “workplace” in the Western world, and its meaning has evolved continuously, along with China’s transition from a central planning economy towards a market-based economy.

Even when there is an equivalent word the meaning can be very different. For example the word 户口 (Hukou) can be translated as “residence registry” or “residential registration”. The Chinese residential registration system differs considerably from that of Finland. The Chinese Hukou system has severely restricted the spatial mobility of labour and divides the population into rural and urban societies with different rights to social welfare. The word Hukou is the special product of the central planning regime. Language is highly

embedded in the social and cultural context where it is generated. The words 跳槽 (job hopping), 70 后 (post-70 generation), 80 后 (post-80 generation) and 90 后 (post-90 generation) are the language products of the particular conditions of China's economic and social transformation since the late 1970s. The English translations do not lend themselves to the embedded connotations of these words. Indeed, it is a challenge to maintain the richness of the original data while conveying an understandable meaning to readers who are from another culture (e.g. Macdonald and Hellgren, 2004; Xian, 2008).



## **4. A Historical Review: China's Institutional Context and Its Impact on Early HRM Practices (1978 – Early 1990s)**

This chapter describes the macro institutional transition of China during the earlier reform period from 1978 to early 1990s. In line with the NBS approach, the current institutional arrangements of China need to be understood in the historical context.

Before describing the institutional environment during the period of 1978 – 1994 it is necessary to understand China's economic system before the reform. The pre-reform period 1949 – 1977 was characterized by centrally controlled economic activities in production, distribution of products and allocation of resources (Granick, 1975; Richman, 1969 in Peng, 2000). Decision on pricing, investment, technology and foreign trade were undertaken by the central planning bureaucracy (Beissinger, 1988; Child, 1994).

Consistent with this economic system the labour system was highly centralized and administered. The spatial mobility of labour was severely controlled and restricted by means of a residential registration system, i.e. Hukou system (户口制度) (Knight and Song 2005). This was especially true for the migration from small towns to large cities and from rural areas to urban areas. The labour resource was centrally planned and allocated top down. Workers were assigned to the enterprises by labour bureaus and cadres were appointed by the Communist Party (Tung, 1982; Walder, 1989). They enjoyed lifetime employment, the so-called “iron rice bowl” (铁饭碗). The cadres once appointed, were seldom dismissed. They could hold the position as long as they adhered to the Party line. This is the so-called “iron chair” (铁交椅). The total wage fund and the wage grades were determined in a uniformed manner by the administrative authorities, emphasizing seniority and equalitarian ideology (Takahara, 1992). This is the third “iron”, the “iron wage” (铁工资). The

lifetime employment even extended to children. They were entitled to work in the same work unit once their parent had retired (replacement system, 顶替) or to have the priority to be recruited compared to those assigned from outside (internal recruitment, 内部招工).

Under the central planning system, the enterprises acted as mini welfare states. They were called Danwei (work unit or workplace) (单位). A Danwei referred to an urban, publicly (state or collectively) owned organizational unit. It could be, for example, a factory, a school, a hospital, an administrative or a party organ. Knight and Song provide an incisive idea of Danwei:

Danwei have played a pervasive role in China's urban society, binding their employees to them in a culture of dependence. With their many functions, they are not just a workplace but a social institution. They satisfy the basic needs of their employees and their dependants, represent their interests, define their social status, accord them various rights, and control and influence their behaviour. (2005: 27)

From this description, one can see that the Danwei is a very different concept from that of the employer in the Western sense. This term Danwei is still used to refer to a workplace, however, to a lesser extent, and retains less of the original meaning. The terms such as company, employer and employee are relatively new concepts. They emerged after the economic reform when the market economy was introduced. In the central planning economy, the enterprises were not companies. They were the units to produce social wealth for the entire nation. The relationship between the work unit and the people was not that of employer-employee. Instead everyone was a member of the work unit. The central planning system began to undergo fundamental changes when the economic reform commenced in 1978.

## **4.1. Macro Institutional Transition in China**

### **4.1.1. Decentralization of Economic Activities and Reform of State-Owned Enterprises**

The Three Plenary Session of the Eleventh Congress of Communist Party of China in 1978 marked the starting point of China's economic reform and open door policy. Unlike the East and Central Europe and the former Soviet Union which launched a rapid, massive privatization programme of state enterprises in the first place, the economic reform in China started from the agricultural sector. "Household contractual responsibility system" (家庭联产承包责任制) in rural areas was initiated from the countryside in 1978 and soon spread over the rural areas in the country (Chai, 1998). By the end of 1984, 93 per cent of China's cultivated land had been contracted to households, and 100 per cent rural villages had chosen to fix production quotas on a household basis (Chen 1995: 23). The People's Communes (人民公社) became vanished. This new system greatly motivated the peasants to produce more crops and other agricultural produces.

From 1984 the reform shifted to the urban sector and industrial reform began (Chai 1998). Two important policies were made in that year: 1) in May the State Council promulgated the provisional decree on further expanding the autonomy of the state industrial enterprises in ten operational areas- production planning, product sales, product pricing, material purchasing and labour issues (e.g., defining wage level) among others; 2) The Third Plenary Session of the Twelfth Communist Party Congress passed the decision on economic reform which stated that socialist economy is planned, commodity economy based on public ownership. This is the first official documentation that recognized a commodity economy. The Communist Party decided to gradually dismantle the central planning system. The early industrial reform was focused on expanding SOEs' autonomy and restoration of enterprise financial incentives. Expanding SOEs' autonomy means decentralizing economic activities. The degree of planning was decreased. Profits retention was allowed. Procurement of materials- the number of materials under planning allocation was reduced. Enterprises began to purchase part of raw materials from market channels. Investment decisions began to decentralize to local governments and further

down to the enterprises. Sources of financing were also enlarged to borrowing from banks, taking investment from domestic and foreign enterprises (Chai, 1998).

Borrowed from the successful model of household responsibility system in the agricultural reform, “enterprise contractual responsibility system” (企业承包经营责任制) was introduced to SOEs in 1987 (OECD, 2005). This was one key form of early reform of SOEs. The other was leasing out the small and medium sized SOEs. The objective of the reform of SOEs was to “separate the ownership right and operation right to an appropriate degree”, i.e. the enterprises were still owned by the state, however, were allowed to be operated by managers. The other important reform was to separate state administration from enterprise operation. With these measures, enterprises started to bear responsibilities for the profits and losses. In 1986 the provisional law on bankruptcy was passed for SOEs. In 1988 the enterprise law for state-owned enterprises was promulgated by the State Council. This was the first enterprise law concerning the SOEs since 1949. SOEs were officially recognized as an economic entity that takes responsibility for its own operation, profits and loss, and economic result. This period also experienced the emergence and rapid growth of private sector. During 1984 - 1991 the growth rate of industrial output of SOEs was only 8% while that of collectives was 19%, self proprietorship (个体户) and private enterprises (私营企业) was 45% and foreign invested enterprise 47% (China net, 3 April 2003). A number of laws on self proprietorship and private enterprises were introduced as well. The reform of this period is labeled as “planned socialist economy with assistance of market force”.

#### **4.1.2. Foreign Direct Investment**

Along with the economic reform China opened its door to outside. Economic reform and open door policy went side by side. This period saw a dramatic change from a country totally closed to foreign investors to welcoming foreign investment to encouraging foreign investment. Similar to its economic reform, the liberalization of foreign direct investment (FDI) also underwent a gradual process. The policies on FDI also evolved over time. During 1978 – 1986 FDI

was high regulated. There were many restrictions in the investment sector, investment mode, geographical areas of the investment and ways of operations. For instance, joint venture was preferred and wholly owned foreign enterprise was discouraged. The domestic sale of the products was severely restricted. RMB earnings could not be converted to foreign currency; therefore, foreign enterprises had to balance their foreign exchange expenditures with their foreign exchange earnings (see Chai 1998).

From 1986 the government introduced new policies on FDI and significantly reduced government intervention in FDI. The approval of FDI projects was further decentralized to local governments and procedures were simplified. Informal restrictions on foreign ownership were abandoned and wholly owned foreign enterprises were encouraged (Chai, 1998). Foreign companies were given more autonomy in domestic sale and purchase of domestic raw materials. Export-oriented and technology advanced foreign investors were allowed to raise loans from Chinese banks. Requirement for foreign exchange balance was relaxed as well. Swap centers were set up for foreign enterprises to convert their Chinese currency (RMB) earnings to foreign currency within certain limits. In addition, foreign enterprises were given preferential treatment. The investment incentives were mainly factor based- tax holidays, investment allowance, reduction of or exemption from sales tax and customs duties, priority and reduced fees for use of land and labour and other public utilities.

In 1992 FDI policy was further liberalized following Deng Xiaoping's south China tour and his call for further opening of the Chinese economy. 28 more cities and eight prefectures along Yangtze River and 13 border cities in northeastern, southeastern and northwestern regions were open to foreign investment. As part of the efforts to gain the entrance to GATT (General Agreement on Tariffs and Trade, now known as World Trade Organization, WTO) China opened service sector such as banking, retailing, telecommunication and major infrastructural facilities which had been closed to foreign investors. However, there were still restrictions on full foreign ownership and scope of business.

## **4.2. Dual Track of Labour Regulations and Predominant Central Employment System**

### **4.2.1. Domestic Enterprises**

The government had different regulations for enterprises of different ownerships. For SOEs the early policies and regulations were primarily lifting the bans inbuilt in the central planning regime and granting autonomy to the SOEs. Compared with foreign enterprises and private domestic enterprises, Chinese state-owned enterprises were much more affected by the old centrally controlled system. Before the reform a labour quota was assigned from the upper level bureaucracy in the form of a mandatory target. Firing was impossible. The entire work-force, the total number of workers, the composition of the work force, the wage was set by the authorities. From 1985 the labour quota was no longer a fixed one but a floating one (Chai, 1998). Enterprises were given limited rights to recruit workers and dismiss unsuitable workers and redundant workers (Provisional regulations on labour contract, 1986; Provisional regulations on recruiting workers, 1986; Provisional regulations on dismissing employees, 1986). In reality it was not until early 1990s with the development of labour contract system that state-owned enterprises could exercise their rights to fire excessive workers. Law on State-Owned Enterprises was promulgated in 1988.

The first law on domestic private enterprises was promulgated in 1988, Provisional regulations of People's Republic of China on Private Enterprises. This law granted right to private Chinese enterprises to manage the labour issues according to the labour contract signed between the enterprise and employee. It permitted the enterprises to make own decision on recruitment and dismissal of employees. The private enterprises seemed to be least affected by the central planning system and legacies because they emerged as a new type of ownership after the economic reform. They did not have the history of state-owned enterprises that used to operate under the state control of labour and other resources. On the other hand they received no support from the state either.

#### **4.2.2. Foreign Invested Enterprises**

While Chinese SOEs were still operating under the regime of state allocation of labour resources, lifetime employment and centrally controlled wage system, laws with certain market economy features were introduced to foreign enterprises from 1980 already. The Provisions on Labour Management in Chinese-Foreign Equity Joint Ventures that was promulgated in 1980 by the State Council was an important state regulation on labour management for foreign enterprises. The Provisions permitted joint ventures/ foreign enterprises to manage their employees in recruiting, dismissal, remuneration, labour protection, and labour insurance through labour contract. However, the Provisions also put a number of restrictions in hiring, firing and setting wages. For example, the labour contract in the JVs had to be approved by the provincial governments; JVs were to recruit employees recommended by the Chinese partner's administration organization, a government bureau; recruiting from other channels had to approved by the labour authority; the JV's wage should be set at 120 to 150 per cent of the SOEs in the same sector of the region/ area; dismissal due to breaking company rule and causing economic consequence had to be approved by the industrial bureau and labour authority. Furthermore, the chairman of the board of directors, the highest decision-making authority in a joint venture, had to be a Chinese from the Chinese partner of the joint venture.

Along with the relaxation policy on foreign investment, the regulations on labour issues for foreign companies became relaxed as well in late 1980s. Many restrictions mentioned above were removed. One important decree is the Circular of the general office of the State Council in 1988 on the approval and transmission of the proposals submitted by the Ministry of Labour and Ministry of Personnel concerning further implementation of the policy of granting decision-making power to enterprises with foreign investment. The regulations allowed foreign enterprises to recruit directly without having to hire from the government channels, and also from other regions than the company location, conclude a labour contract without approval by the government bureau, and dismiss employees based on the terms of the labour contract. The limits on wages were abolished in 1986 (Horsley, 1988). However the

relaxation was not linear. Some restrictions were restored later, e.g., the wage limits (Greene 1991; Zhu and Dowling, 2000).

### **4.3. Highly Restricted Labour Practices in Foreign Invested Enterprises**

#### **4.3.1. Staffing (Hiring and Firing)**

With the early restrictions mentioned, the main source of employees in JVs came from the Chinese partner, normally as part of the agreement. There were many restrictions by the Chinese government on setting up a wholly owned foreign company. Joint venture was the dominant mode of foreign direct investment in the early period of the reform. The Chinese partner became a natural source of labour as well. Many SOEs had excess labour. Normally the workers were transferred to the joint venture when the Chinese company allied with a foreign partner. So, this inherited problem of over staffing was partially brought to the joint ventures (Verburg, 1996). Because the major source of labour was the Chinese partners via internal transfer, there was little open recruitment. Furthermore, the regulations restricted external recruitment within the local area, normally city wise. The foreign invested companies could visit the job centre and “labour market” (劳务市场) events that were established and organized by the local labour authority. These were the sources for operational workers. The local managers were recommended by the Chinese partners or their upper administrative organization, often the Communist Party organization. The personnel manager in joint ventures had to be a Chinese (Verburg, 1996).

Firing of unsatisfactory workers was reported a problem by Child (1994) in 29 JVs out of 30 JVs investigated in 1989 due to Chinese managers’ protection of their employees. This might reflect the deep rooted thinking of life time employment. The social system was still that of a central planning regime, meaning that enterprises were responsible for employee welfare, and there was no social security, such as unemployment pension. Being unemployed meant losing the basic income for one’s livelihood. Therefore, it was not only the mental barrier but also the systemic barrier that prevented



firing and laying-off. It was reported that one way to get rid of excess workers transferred from the Chinese partner of the joint venture was early retirement (Verburg 1996).

However, companies maintained strict rules in controlling the employees. Verburg (1996) noted that in the joint ventures he investigated, especially in the large plants, an extensive system of sanctions existed for keeping the workforce in line. One example was the punishment for being late for work. A worker was fined a considerable sum of money for being late at work. The second time the salary was cut immediately, and the third time the employee was fired (Verburg, 1996).

#### **4.3.2. Reward (Salary and Bonus)**

Research shows that there were both internal resistance in JVs and external pressures against introducing performance-based incentives that reflected job responsibility levels (e.g., Child, 1994; Greene, 1991). Although the regulations on wage limit of joint venture employee were abolished external influence from labour authorities still existed up to 1990. Greene (1991) reported that a majority of the FIEs interviewed by the US-China Business Council in the summer of 1990 indicated that they were being pressured to control the level of wages. Even though bonuses were applied they tended to be distributed equally to all workers and managers and often became part of basic wage (e.g., Laaksonen, 1988; Nelson and Reeder, 1985; Tu and Jones, 1991; Zhu and Dowling, 2000). This reflected the strong influence of the equalitarian philosophy of the central planning regime. In the investigation of 10 foreign-Chinese joint ventures Verburg (1996) found that most of them used standard bonuses, such as national holiday bonus, profit-sharing and overtime, and performance-related pay was applied only marginally in these joint ventures. Furthermore, production targets were often set and measured at group or company level. Chinese managers were assessed by the Party and labour unions on their political conduct (Child, 1994). Chinese managers and staff were sometimes rewarded by being offered training in the country of foreign partners (Verburg, 1996).

#### **4.3.3. Changing towards Freer Labour Practices**

At the end of 1980s foreign companies were not officially restricted to hire people outside their location city. Publicly hiring employees also gained wider acceptance (Greene, 1991). Foreign companies experienced more freedom in hiring, setting wages and incentive schemes (Greene, 1991). Firing became less difficult as well. Some foreign invested companies could pay off so called unproductive workers (Greene, 1991). On the other hand, in practice externally recruiting a person who was fully employed by a SOE was difficult (Child, 1994). One obstacle was the Hukou system (residential registration system). The other was the personnel file (人事档案) system. Under the central planning regime, a person's personnel file was kept by his/ her Danwei (work unit). Access to one own personnel file was forbidden. In the situation of changing the work unit, the personnel file had to be transferred from the leaving work unit to the recipient work unit via inter-work unit transfer. Without the personnel file the recipient work unit was not allowed to take in the person. In this way it prevented mobility of workforce. This system still prevailed in the early reform period. Today, the role of personnel file is much less important. Foreign and private Chinese companies usually do not require a personnel file. But state-owned enterprises and government organizations still require the personnel file in recruitment.

Detaining the personnel file was a common mean in SOEs to prevent employees changing job to another company. Even a foreign company could find a suitable candidate it might not be able to recruit the person due to the personnel file problem. This problem was reported with varying degree for the foreign companies. Some had significant problems in getting a recruit transferred from a SOE while others had few problems. Seemingly it was not easy to recruit a person from a large SOE or state organization. It meant the SOEs would lose their best people to foreign enterprises. Often the foreign companies had to resort to the labour bureau for help to get the potential candidate released from his/her Chinese work unit, and pay compensation to arrange this (Greene, 1991).

#### 4.4. Summary

During the early economic reform the Chinese economic system had dual tracks: the centrally planned and controlled economic system and some form of market economy system. Accordingly the legislation had dual systems as well: the rules for state-owned enterprises and the rules for foreign invested enterprises respectively. The overall formal institutions were on dual track. This period was characterized by the co-existence of dual systems. A market economy system was introduced. Central planning was decreased. The state role in direct administration of enterprise operation was gradually reduced. SOEs were granted some autonomy to manage their operations. In the later phase of this period SOEs were allowed to recruit and dismiss workers. However, it was difficult for them to do so in practice, because most workers still relied on their enterprise for free housing, medical care, education and other social services (Chai, 1998). Labour mobility was rather low. The central planning system still worked to a large extent and played a more important role than market mechanisms. The overall economic system was still dominated by the central planning bureaucracy and it was the same for the labour system. Therefore, the typical features of central labour practices such as life employment, equalitarian reward, and enterprise responsibility in social programmes were still part of the formal system.

Although foreign companies were granted by laws with more freedom in people management than Chinese SOEs, they were essentially surrounded by a centrally planned, dominant institutional environment; therefore, their HRM practices were highly restricted compared with the practices of market economy in the Western sense. Under this institutional environment the central issue of localization was to cope with the constraints of Chinese formal systems and the strong legacies of such system. For example workers were primarily hired from the Chinese partner of the joint venture and external recruitment relied on local labour authority. The bonus practice was implemented as part of the normal salary as the result of equalitarian thinking prevalent among Chinese employees and managers. Strong institutional constraints on firm strategies and behaviour in early transition were observed in other transition economies as well. For example, Kosonen's (2002) study on

enterprises adaptation to post socialist Vyborg, Russia, shows that firms had to combine institutional legacies and novelties in coordination of social relations. Karhunen (2007) studied the strategic response of hotel enterprises to post-socialism in St. Petersburg, Russia. She shows that in the early transition foreign owned hotels could not effectively utilize their management advantages in the environment where a market-based institutional framework was lacking. The difference in the pace of transition is that many Central and Eastern European countries adopted a radical approach to reform, a 'shock therapy' (Peng, 2000). The command economy collapsed quickly and the market economy was established. Institutional legacies became the main influence on firm behaviour. China adopted a gradualism approach. As described earlier the central planning system and market oriented system co-existed for a considerable time in China, compared with e.g., Russia. Thus, the old formal system and its agencies had a strong influence on foreign enterprises in China.

It has to be noted that during this phase the general trend in formal institutions was moving towards more freedom for foreign companies in personnel issues. The official restrictions became much less at the beginning of 1990s. The economic reform began proceeding to a deeper phase. The macro institutional transition and its impact on the socio-economic and legislation systems in the later reform period will be described in the following chapter.

## **5. China's Institutional Context (Mid-1990s to 2010)**

This chapter describes the Chinese institutional context. It follows the dual lines of institutional transition: on the macro level the transition from a highly centralized planned economy to a market-oriented economy, and at enterprise-level the reform of state-owned enterprises. The impacts of these reforms on the formation and development of the labour market, establishment of national labour legislation, and establishment of a social security system are discussed. The labour legislation at the national and regional levels concerning the HR practices of this study is presented. The materials used in this chapter include documentary data, interview data, and literature.

### **5.1. Institutional Transition at the Macro and Enterprise Levels**

China began to pursue deeper reform in 1992. Two important events indicate this shift. One was Deng Xiaoping's South China tour at the beginning of the year where he announced a further opening up to the outside world. The other was the Fourteenth Communist Party Congress in 1992, which decided that the goal of economic reform was to establish a "socialist market economy" (社会主义市场经济) and that all enterprises should enter into and compete in the market. The concept of market economy was officially recognized for the first time. The Third Plenary Session of the Fourteenth Communist Party Congress in 1993 set transformation of the operational system and establishment of a modern enterprise system as the targets of the SOE reform. In 1994 the first company law was introduced. This law came to govern all types of enterprises, which indicated a shift to market coordination of economic activities in all sectors. The Fifteenth Communist Party Congress in 1997 called for acceleration of the marketization (市场化) of the national economy as an important target. Market mechanisms were increasingly applied in many

economic activities, e.g. the commodity market and the capital market. At enterprise level, this marked the beginning of a massive restructuring of SOEs. Marketization of state-owned enterprises meant restructuring enterprise ownership, transforming SOEs into stock companies, establishing a market-operation mechanism within the enterprises, and inducing SOEs to compete in the market. The goal was to retain the large SOEs and let go of the small and medium-sized. Most of the SOEs lost their support, subsidies, or free loans from the government and began to strive for profitability in order to survive in the market. As a result, a huge number of small and medium-sized SOEs were merged, restructured, acquired, or allowed to go bankrupt (see Yusuf, Nabeshima and Perkins, 2006).

The later reform of Chinese SOEs focused on the transformation of SOEs to stock companies, which took place from the early 1990s throughout the 2000s (People net, 2009). In fact, the experiment in 100 big SOEs began in the mid-1990s (China net, 2003). The state ownership in SOEs was transformed into tradable stock. Governments at the central, provincial, and municipal levels became owners of stock in SOEs. Some stock companies were listed on Chinese stock exchanges in Shenzhen and Shanghai (China net, 2003).

The private sector began to emerge in the mid-1980s and expanded rapidly after the beginning of the 1990s. The average annual growth of industrial output in the individual and private sector during the period from 1984 to 1991 was 45% while in the state sector it was only 8% (OECD, 2005). Private ownership in enterprises was officially accepted as one part of national economy in 1997 at the party congress mentioned earlier. The Third Plenary Session of the Fifteenth Communist Party Congress in 1998 further defined China's economic system to be based mainly on public ownership with the coexistence of multi-ownerships. The Constitution was revised in 1999 and explicitly recognized private ownership for the first time after 1949. The 2004 Constitution was amended to further guarantee the right to own private property. This series of official recognitions of private ownership and private property were important steps and landmarks in development towards a market economy. By 2008 Chinese private enterprises had grown to 70 per cent of the total number of domestic enterprises from about 30 per cent in 1998 (China Statistical Yearbook 2009; OECD, 2005).

The deeper reform expanded from enterprise restructuring to other spheres of the social-economic systems. The obligations of state-owned enterprises to run social programs (e.g., providing housing, medical services, schools, etc.) were decreased, and eventually terminated at the end of the 1990s and the beginning of the 2000s. Establishment of a social security system began with the aim of seeing to the welfare of workers. A labour market emerged and developed along with the establishment of labour legislation. This overall socio-economic development has had an ever greater impact on values of Chinese people as well.

## **5.2. Labour System: from Labour Immobility to a Highly Fluid Labour Market**

The formation of China's labour market took shape during the 1980s and 1990s (Knight and Song, 2005). It was the deep reform of the SOEs during this period that eventually triggered the emergence of a labour market. As briefly introduced in Chapter 4, the pre-reform labour system was characterized by the three irons - iron bowl, iron wage, and iron chair. Labour was assigned according to quotas set by the administration authority of the enterprise. In other words, an enterprise had to obtain a labour quota (招工指标) if it wanted to hire people. Furthermore, there was strict control over the mobility of the population, especially from the rural areas to urban areas. This control was administrated by the Hukou system (residential registry system) that tied residents to their place of birth. This centralized labour system was part of the central planning regime.

When the economic reform went deeper, economic activities were conducted more and more on the market. These changes required a market-supportive labour system. In the mid-1980s, enterprises were granted more freedom in hiring and firing thanks to a central government policy in 1984 called the Provisional Regulations on Further Expanding State-Owned Production Enterprise Autonomy. Since 1985, the labour quotas for most large and medium-sized state enterprises were no longer fixed but allowed to fluctuate according to the production output volume (Chai, 1998). For small enterprises under a contractual or leasing system, labour quotas were completely abolished (Chai, 1998). Enterprises started experiencing a degree of

freedom in hiring and firing. Nevertheless, this right remained largely theoretical in the 1980s, especially because it was difficult to enforce in the state enterprises (Chai, 1998). This considerably constrained the free movement of the labour, which was the pre-requisite of a labour market.

One key factor behind this was that SOEs continued to play the role of Danwei (work unit), a mini welfare state. Workers still relied on their work unit to provide housing, medical care, schooling, and other social services. The second reason was that the state still controlled part of the labour supply. Even in 1992, one-third of the new employment in SOEs was still assigned by the government, and two-thirds was recruited by the enterprises themselves (Chen, 1995). The third reason was the Hukou system (residence registry system), which prevented people from moving between cities and regions, especially from rural to urban areas and from small towns to large cities.

It was not until the early and mid-1990s when restructuring of the SOEs began that hiring and firing became part of enterprise behaviour in the sense of a market economy, rather than the responsibility of the state. Under the pressures of survival in the market, SOEs began to seek efficiency. They had to let redundant workers go. Restructuring the SOEs also meant closing down unprofitable state enterprises. Chai's (1998) research revealed that China's coal industry laid off 187,000 workers in the first half of 1993 (South China Morning Post Internationally Weekly, 9-10 Oct. 1993), and total 1.13 million workers in SOEs were laid off during the first nine months of 1997 (South China Morning Post Internationally Weekly, 10 Jan. 1998). The planning quota for recruitment of state enterprises was eventually abolished in the mid-1990s; thereafter SOEs were completely free to choose their own workers (Knight and Song 2005).

The Labour Law promulgated in 1994 and enacted in 1995 officially defined the right of enterprises to hire and fire in the form of a national law. Enterprise autonomy in hiring and laying-off employees greatly facilitated the free mobility of the workforce and contributed to the development of a labour market. Since then, the employment market underwent a rapid liberalization process. This was the period of time when the case subsidiaries of this study were established and operating.

With the requirement of the Labour Law the use of the labour contract became the means to establishment employment relationship between the



worker and the company. The life employment system, the ‘iron bowl’, was officially abolished. The change from life employment to use of labour contracts of limited period of time has greatly facilitated labour movement. The short term labour contract has become the prevailing form of employment relationship, especially in private and foreign sectors. Labour mobility across cities and regions, especially from rural areas to urban areas, has been rapidly growing since the 2000s when the restrictive role of Hukou (residence registry system) decreased. It is evident from the data of this study that Hukou did not prevent labour mobility as such, but it still served as the divide between rural migrant workers and urban employees, which in turn has resulted in unequal opportunity and unequal treatment to rural migrants in social services and benefits. This is evident in the case subsidiaries reported by interviewees.

Alongside these institutional changes, China has been experiencing fast economic growth for over two decades since the 1990s with an annual GNP growth rate of around 10% (IMF, 2008). The 2000s reflected a period of new economic boom up to the 2008 world financial crisis. This continuous fast economic growth resulted in a shortage of experienced professionals and qualified specialists, competent managers, and skilled workers<sup>9</sup>. Most case companies in this study reported difficulties in finding suitable employees. As one interviewee stated,

It is very difficult to recruit people. In recent years there has been overheating in this sector. Qualified professionals were very few. (EquCo3 1)

The comment of this interviewee represented a common situation of many sectors in China. Another interviewee reported the difficulty to recruit experienced engineers,

Technical people are too few. In our technology department there are three whom we call old guys. They are engineers around 60 years old, of that old generation. We want to find good, qualified younger mechanical engineers, e.g. around 40 years old, very, very difficult. (EquCo4 2)

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<sup>9</sup> Now even manual workers are in shortage of supply (see, Businessweek, 16 September 2013).

The increasing lack of skills intensified fierce competition for talents (MGI, 2005). The tight labour market further accelerated the inter-firm mobility of those people who were in high demand, because they had many opportunities to choose their job and were often poached by other companies directly or by headhunters. The employee turnover rate was generally between 10 to 30 per cent in China according to a report based on the interviews with over 50 Finnish companies operating in China (Kettunen et al., 2008). The average turnover in private sector of China was reported around 20 per cent in 2010 (EU SME Centre). In Finland the labour market mobility was generally around 10 per cent (Norden, 2010), considerably lower than in China. The high mobility of employees in China posed considerable challenges in recruitment and retention of employees for Finnish companies (Kettunen et al., 2008) and for foreign companies in general (EUCCC, 2012; EU SME Centre).

Apart from shortage of supply of skills, the high employee mobility is partly due to the changing values of Chinese employees. The changes of values and attitudes of Chinese workforce have been significant since the economic reform in 1978, especially after 1990s. Extrinsic rewards (money, promotion, etc.) have become much more important for people to choose a job. According to the interview data of this study pay level was usually one key factor in considering the choice of employer. Long term employment thinking has become less important; at least it was no longer regarded as the most important thing as it was in the past. As one interviewee noted,

Nowadays employees' thinking is very active, not like the old generation who worked all their life in one company. (EngCo2 1)

Salary was often considered as an important element in career success. High salary target and fast career expectation were often the key motives for choosing and staying with a company. According to an international survey of 15 000 urban city employees, 62 per cent of respondents in Beijing consider salary as the most important in career success while only 28 per cent of respondents think so in Finland (Metro, 21.9.2011). According to the same survey Mumbai and Seoul have a similar percentage to Beijing. These figures indicate a higher perceived importance of salary in job success in Asia than in Finland.

In China young people were especially more mobile than elder people and tended to have a higher turnover rate than elder employees (interview data). Young people refer to those who were born in the 1980s and 1990s after China's economic reform and open-door policy. They are labeled “80 后” (post-80 generation) and “90 后” (post-90 generation). They are a distinct group of people and are very different from those who were born in the 1970s who are called “70 后” (post-70 generation) and earlier. The post-80s and post-90s generations are eager to seek positions with higher pay and have a higher tendency to move between companies. One interviewee described their characteristics:

The most mobile people here are those between 30 and 36. These people are trying hard to solve... ‘I have no house. I need to buy one. I want to treat my wife well. I need to raise the child’, etc. They have very high economic (salary) targets. This makes them flow to the talent market, looking for higher position. (EquCo1 1)

The young generations had a very different starting point in their career from the elder generations. A Chinese manager noted,

What they [post-80 and post-90 generations] have seen is the fast development. Having worked for a couple of years, if not able to buy an apartment or a car they feel bad. They are too eager seeking immediate benefits. (EngCo1 1)

On the other hand, they also possess some merits which the elder generations are lacking. They are more individualistic, more straightforward in communication and less concerned with bureaucracy. The same manager made the following comments:

The 80's and 90's generations have a lot of good merits. They are less influenced by the traditions. They have stronger personality. They are more individualistic and talk what they think. They have less misgiving than the generation of 1960s like me. The older generation has even more misgivings. They [the 80's and 90's generations] don't have burdens in career, emotion and personal life. There are excellent young business people among them. When they have a target they go for it straightway. (EngCo1 1)

There are apparent differences between China and Finland in the mainstream of work related values. In Finland employees and young graduates consider factors relating to quality of work more important than pay when choosing an employer (Helsingin yliopisto, 2007; T-Media, 2011; [www.employerbrandingtoday.com/fi/](http://www.employerbrandingtoday.com/fi/), 16.8.2011). According to a survey conducted with over 10 000 university students in Finland, 80 per cent consider work environment very important in selecting an employer and only a couple of per cent consider it not important (Helsingin yliopisto, 2007). The other important criteria to choose an employer include matching of personal values with organizational values, interesting tasks at work and career development (Helsingin yliopisto, 2007). A survey of 25 000 employees and university students in Finland shows that stable work relationship, work environment and interesting job are the top three criteria for choosing a work place (T-Media, 2011). The Nordic countries seem to share similar values in selection criteria for workplace. According to the Universum Student Survey 2011, professional training and development, creative and dynamic work environment, good prospects for future career and supportive leaders are placed before good prospects for future earnings and competitive base salary ([www.employerbrandingtoday.com/fi/](http://www.employerbrandingtoday.com/fi/), 16.8.2011). The survey covers over 34,000 students at top academic institutions in Sweden, Denmark, Norway and Finland.

The interview data show that work related values in China have become divergent as well. While younger employees tend to be highly mobile and place much emphasis on financial reward at work, older employees are stable and prefer a long term work relationship to high pay. Differences were noted between male employees and female employees as well. Female employees were appreciated for their loyalty and steady progression of career while male employees were regarded as being more mobile and driven by the desire for rapid career achievement. Rural migrant workers were primarily income-based wage earners. They were sensitive to wage level and highly mobile in nature. Their social status (see later sections of this chapter) also contributed to their loose bond to workplace. The divergent and heterogeneous workforce in China contrasted with the relative homogeneous workforce in Finland. The differences in the workforce between China and Finland described above are

likely to induce subsidiaries of Finnish MNCs to adapt HRM practices to the Chinese context.

### **5.3. Establishment of National Labour Legislation and Its Development**

The Labour Law of the People's Republic of China (Labour Law), the first national labour law governing employment practices in the market-oriented economy, was adopted in 1994 and enacted in 1995. The law combined most key, scattered labour regulations and rules into one document (Josephs 1995 in Warner 2001).

The Labour Law officially marked the transition of the centrally controlled labour system towards a free market labour system. It was aimed at serving two purposes: 1) safeguarding the market labour system which is characterized by free mobility of the labour force and management autonomy in personnel decisions; 2) protecting the interests of the workers and employers by stipulating the basic rights and obligations for both sides (Cao and Zhao 2007). Overall, this law attempted to build a foundation for a wide range of issues in employment relations (Zhu, 2002) and is regarded as comprehensive and significant in covering labour issues (Warner 1995).

Since enactment of this labour law the Chinese employment system underwent rapid liberalization. The liberalized system on the one hand greatly facilitated the development of a free labour market and on the other hand largely failed to protect workers' interests and rights (Gallagher, 2004; Wu, 2006). The latter is regarded as primarily due to a lack of enforcement of employer obligations to employees, especially extremely weak surveillance by local governments, who were faced with the need to attract and retain investment and grow the local economy (Gallagher 2005). Economic development has been the priority for both the central government and local governments since the reform in 1978. The promotion criteria of local officials have been measured by the economic growth of the region. They lacked the incentive to vigorously oversee the compliance of enterprises to the obligations required in the labour regulations. Furthermore, corruption on the part of local authorities also contributed to the lack of enforcement. According to a survey of the China's National People's Congress in 2005, less than 20 per cent of the

small and medium-sized enterprises used labour contracts (Wu, 2006) though the use of labour contracts had already become a legal requirement under the Labour Law of 1995. An interviewee recalled his early observation of the poor implementation of the Labour Law:

The Labour Law has been in place for some 15 years. The first version stipulated 5 working days per week and overtime should not exceed 36 hours [per month]. I was in Guangdong at that time. In the first years nobody followed [it]. (EngCo1 1)

The number of labour disputes was reported to be 10 times more in 2005 than it had been in 1995 and 94% of the cases were filed by employees (Wu, 2006). The media frequently reported that employers had failed to make wage payments, paid wages below minimum standards, evaded social insurance contributions, neglected safety at work, failed to make adequate compensation for overtime work, or treated workers badly. Many disputes erupted into public demonstration, even riots. Against this background, the Labour Contract Law of the People's Republic of China was promulgated in 2007 and took effect on January 1, 2008.

The core of the new law is to enhance employee protection by stricter rules for employer obligations and tighter surveillance. In effect the changes in the content between this new law and the Labour Law of 1995 are not significant (A detailed comparison of these two laws can be found in Appendix 4). More salient effects of this new law came from the enhanced enforcing actions taken by the government and authorities on the existing laws than the Labour Contract Law itself. The major impacts were identified in employment contracts, dismissals and employee representation (Lu, 2009). The relevant influence of this new law on the case subsidiaries within the scope of this study was mostly in employee representation practice.

#### **5.4. National Labour Laws**

Chinese legislation operates at multiple levels. At the national level there are state laws. At the provincial and municipal levels there are local regulations.

The most important national labour laws are the Labour Law of 1995 and the Labour Contract Law of 2008. The Labour Law includes all the important issues in terms of employment relations: employee rights, employment principles, labour unions, employee participation, labour contracts, working hours, rest and leave, wages, work safety and sanitation, special protection for female workers and juvenile workers, vocational training, social insurance and welfare, labour disputes, authority supervision and inspection, and legal responsibilities for non-compliance (Labour Law, 1995). Other important labour laws include the Trade Union Law, Law of Mediation and Arbitration of Labour Disputes, Regulation on Paid Annual Leave of Employees and the Marriage Law (documentary data). The rules on minimum wages and social insurance and benefits are of importance for this study.

#### *Minimum wage*

The Labour Law requires enterprises to follow the minimum wage. The minimum wage standard is set by the provincial/ municipal governments. This rule had more impact on companies where manual workers were the main workforce than on companies where skilled workers or white-collar workers were the main workforce. Most of the case companies were in the latter category. The salary level of these companies was naturally higher than the minimum wage.

#### *Benefits*

Benefits include paid annual leave, marriage leave, and maternity leave. Paid annual leave is regulated in the Regulation on Paid Annual Leave of Employees of January 1, 2008. This is the first national law on paid annual leave in China. Prior to this law, the regulation on annual leave was left up to the provincial or municipal governments. Under this new law, employees are entitled to 5 to 15 days of paid leave per year depending on the cumulative length of employment. An employee with employment of between one and nine years is entitled to 5 days paid annual leave; between 10 and 19 years, 10 days; and 20 years or longer, 15 days. The marriage leave is three days and the maternity leave 90 days.

### *Social insurance*

The Labour Law only stipulates the basic types of social insurance to which companies should contribute. Basic social security included retirement pensions, medical insurance, unemployment insurance, work accident insurance, and birth insurance. They are called the “five insurances” (五險) in China. Some interviewees called them the “three insurances” (三險), because only the first three are social security, and both employees and employers are obliged to contribute. The latter two were contributed to only by employers. The standards of social insurance are regulated by the provincial/ municipal governments. According to the Labour Law, employer obligations to contribute to social insurance are to be included in the labour contract. Therefore, the labour contract was an important means for binding employers to contribute to social insurance.

## **5.5. Social Insurance System**

The social welfare of the workers, housing, medical care, education, pension, and other benefits used to be the responsibilities of the SOEs under the central planning system. Furthermore, there was no unemployment benefit because there had been full employment provided by the state. As enterprises became independent economic entities operating in a market-oriented system, it was imperative to establish a social security system to provide employees with medical care, pensions, and unemployment benefits. A social insurance experiment began in 1986 in a very small number of SOEs (Burell, 2001). From 1995, medical insurance, pension insurance, unemployment insurance and work-injury and maternity insurance became legal requirements for all enterprises in the Labour Law of 1995. However, in practice, establishment and implementation of the social security system across the country has been a long process (see Burell 2001 on the early development of China’s social insurance system).

First, social security is characterized by the urban-rural divide (Chen, 1995), an “invisible Great Wall” (Knight and Song, 2005). The social security system started in the urban area and had spread over the urban part of the country. The reform in rural areas began only in the late 2000s. Basically, rural



areas are not yet covered by the social insurance scheme. Second, the social security system is characterized by regional diversity. There are great variations in the coverage of the social insurance system between the provinces and cities (see Burell, 2001). Third, the system is locally based. While the state has national regulations and central government policies, the provincial and municipal governments have been allowed to make decisions as to what extent they adapt them to local conditions in the form of local regulations and policies. This partly explains the reason for the regional variations in the second point. This third point and the subsequent impact on HRM practices will be further elaborated in the following sections of this chapter. The fourth is the migrant-urban worker divide caused by Hukou. Because rural areas were not covered by the system, those rural migrant workers who held rural Hukou (rural residence status), though working in cities, were not entitled to the social insurance (medical insurance, pension insurance, unemployment insurance) that was enjoyed by urban Hukou workers (Chen 1995). They did not enjoy some other social benefits as well, e.g. the housing fund which urban employees have been granted. This situation has its historical root in the central planning regime where a rural-urban divide was drawn and institutionalized for over four decades. Gradual integration of migrant workers into the social security system began only recently. Rural migrant workers began to receive some social benefits. The first national law on social insurance, the Social Insurance Law was promulgated in 2010 and enacted in 2011. This law officially includes rural migrant workers into China's social security system. Yet, the nationwide execution of the law seems to have a long way to go.

The development of China's social security system has been remarkable given the vast disparity of social-economic development, significant differences in regional capability to generate wealth and the uneven starting point of the system across the country. Nonetheless, there are considerable differences in the level and extent of converge of social security between Finland and China. Finland is typically regarded as a welfare state, together with Denmark, Iceland, Norway, and Sweden sharing a so-called Nordic welfare model ([www.norden.org](http://www.norden.org)). The most salient features of Finnish social security system can be described as high level of social security, extensive coverage of benefits and equal entitlement for everyone (see, Kela; Kela, 2013; Niemelä and Salminen, 2006).

## **5.6. Local Government Role in Labour Regulations**

Provincial governments (including municipalities directly under the central government) are responsible for making the implementing rules based on national laws and also have certain authority to define local regulations and policies.

### **5.6.1. Local Regulations as Detailed Guidance on Firm-Level HR Practices**

The local regulations formed an important part of the overall labour legislation. The state laws are often made sketchy because there are considerable variations across the regions, provinces, and cities; hence, the provincial governments are often entrusted to make implementing rules based on the principles of the state laws. In this respect, the local regulations complement state laws and provide detailed rules that are suitable for the respective provincial conditions. For companies it is not enough to look at only the national laws. The local regulations act as operational guidance on company-level HR policies and have to be treated seriously. For example, two HR manager commented,

Beijing municipal laws and regulations are many, like salary/ wage and leaves, etc. (ConCo 3).

Shanghai regulations are the detailed rules on e.g. work attendance, accident, overtime pay and wage calculation. The regulations on these things are different in different regions. (IndCo4 3)

In principle, provincial rules should not be contradictory to the state laws. As one interviewee noted,

Shanghai has its own labour implementing rules. But the state can promulgate a national law to invalidate Shanghai regulations, i.e. Shanghai regulations cannot contradict the national laws; however, there can be certain flexibilities in the local rules. (EquCo1 3)

Because of this complicated legislation system the Chinese HR managers were better aware of the labour laws and regulation, especially the local rules, than the Finnish managers. A Finnish manager openly admitted,

I am not a Chinese. I have difficulty to understand the Labour Contract Law.  
(EngCo1 3)

The other Finnish manager commented,

I don't go into details of these things. It is not only because of the language, but the complexity of the Chinese system. (IndCo1 1)

Normally the issues concerning the local rules were fully delegated to the HR manager. As described in Section 3.4.1, all the HR managers, including China country HR managers, in the case subsidiaries were Chinese nationals. Because of the local nature of the labour legislation it was of the utmost importance to have a local Chinese person as HR manager. The typical local rules on pay and benefits included minimum wage, social insurance payments and the housing fund. These will be described below.

### **5.6.2. Minimum Wage Standards**

The minimum wage standard was decided by the municipal or provincial governments. Each city has its own standard of minimum wage; or sometimes a region (formed by a few/ several neighbouring cities) shares one standard. The minimum wage is universal within the same city or wage zone regardless of the sector. For example, the minimum wages in 2008 in Shanghai, Beijing, Tianjin, and Chengdu (the capital city of Sichuan Province) were 960 Yuan<sup>10</sup>, 800 Yuan, 820 Yuan and 650 Yuan respectively<sup>11</sup>. Local governments were also responsible for adjusting the minimum wage rate. In addition, the

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<sup>10</sup> Yuan is the Chinese currency. The average exchange rate between Euro and Yuan in 2008 was 1 Euro = 9 Yuan (European Central Bank and Reuters (SDR rate), Bank of Finland, available at [http://www.suomenpankki.fi/en/tilastot/valuuttakurssit/pages/tilastot\\_valuuttakurssit\\_valuuttakurssit\\_short\\_en.aspx](http://www.suomenpankki.fi/en/tilastot/valuuttakurssit/pages/tilastot_valuuttakurssit_valuuttakurssit_short_en.aspx))

<sup>11</sup> The minimum wage standards in China have risen considerably in recent year. For example, the minimum wage of Shanghai in 2013 was 1620 Yuan (see, china.org.cn, 1 July 2013; chinanews, 1 September 2013) contrasting with 960 Yuan in 2008.

municipal and provincial governments were in charge of a publishing consumer price index (CPI). This index served as reference for organizations to increase the salaries of employees though there was no mandated rule on it. The Chinese minimum wage system was different from the Finnish system according to which minimum wage rates, among other terms of employment, were determined by collective agreements between trade unions and employer associations in various sectors. Therefore, the minimum wage rate could vary from sector to sector. Almost all employees in Finland were covered by the collective agreement in its applicable sector.

### **5.6.3. Social Benefit Standards**

The social security standards were defined by the provincial or the municipal governments. The employers' contribution to pension insurance was around 20 % and medical insurance around 10% in 2008 in Shanghai, Beijing, and Tianjin with slight variations among them. The differences in standards between large cities and medium and small-sized cities or between the east coastal area and the central area were much bigger. For example, the enterprise contribution to medical insurance was 7.5% in Chengdu, the capital city of Sichuan Province in central China; this was 37.5% lower than the Shanghai standard. The housing fund had the most variations between different cities, even among large cities. It varied from 5% to 20% (see Table 5.1). Further, due to the gap in salaries among cities there could be considerable difference in the real amount of social insurance payment by enterprises. This also meant that the social benefits standards of employees could vary according to the location of the unit, even though they worked for the same company in China.

One important feature of Chinese standards of social benefits is that the government requires minimum standards and allows enterprises to decide on higher standards. It was common to set the standards as a range between a minimum and maximum rate. For example, the ranges of housing fund standards of five large cities in China are shown in Table 5.1 below.

**Table 5.1** Standards of housing fund in five large cities in China in 2008

City	Employee contribution	Employer contribution
Shanghai	7% / 22%*	7% / 22%*
Beijing	8% - 12%	8% - 12%
Tianjin	10% / 15%	10% / 15%
Guangzhou	5% - 20%	5% - 20%
Chengdu	6% - 15%	6% - 15%

\*The 22% was formed by a minimum rate of 7 % plus a complementary fund of 15%.

Data source: Respective municipal regulations

As Table 5.1 shows the range between minimum rate and maximum rate is considerable. Companies could choose the percentage from within a range since it was not fixed, or choose the minimum or maximum as in the case of Shanghai and Tianjin. This enabled companies to pay according to their preference. The housing fund is completely regulated by local governments. Normally large and medium-sized cities have such regulations and smaller cities do not require housing fund. The housing fund together with the social insurances mentioned earlier were often referred by the Chinese HR managers as “five insurances and one fund” (五险一金) or “three insurances and one fund” (三险一金).

The local nature of the social insurance system and housing fund system implies that the contributions from company side and the social benefits received by employees could vary considerably from city to city. According to the regulations, migrant rural workers were not entitled to social insurances and housing fund mentioned above. Employees in the same company had different statuses and enjoyed different standards of social benefits.

To summarize, during the later reform period China’s economic system was transformed from a central planned economy towards a market-oriented economy. The ownership of enterprises changed from state-owned dominance to diverse modes of ownership - state-owned, domestic privately owned, collectively owned, a mixture of state, collective or private ownership, and foreign ownership. This marketisation had important consequences for labour market formation, establishment of the legislation system, and building the social welfare system in China. Along with the macro transition in the

economic system and enterprise reform, the Chinese employment environment underwent a rapid liberalization process. Labour laws and regulations became unified for foreign enterprises and Chinese domestic enterprises. This macro institutional context, the evolution of the institutional transition, and consequent changes in legal and socio-economic systems in China since 1978 serve as the basis for examining the impacts of Chinese context on the subsidiaries of Finnish MNCs in China. This will be described in the following chapter on localization of subsidiary HRM practices.

## **6. Explaining Localization of Human Resource Management Practices**

In this chapter I report the findings in four steps. Firstly, I describe what HR policies and practices were transferred from the HQs to the subsidiaries concerning the six HR areas that are defined as the scope of initial investigation in Introduction. Secondly, I report on the localization of compensation practice. Thirdly, the QCA analysis of the localization of compensation practice is described. Finally, I present the findings on the localization of performance management practice.

### **6.1. HQs-Transferred Practices in Six HRM Practice Areas**

This section reports the overview of findings of the HQs-transferred practices in benefits, employee representation, recruitment and selection, training and development, compensation and performance management. These findings serve as the basis for choosing the last two practices as the focus of analysis on localization.

#### **6.1.1. Benefits and Employee Representation**

No standardized HQs policy in benefits issues was found to be transferred among the case subsidiaries. Instead, the companies reported that benefits issues are much regulated by the Chinese laws and that the regulations at national and local levels, especially the latter, are the primary guidelines for making benefits practices. The major benefits stipulated by the Chinese laws which employers should contribute included unemployment insurance, pension insurance, medical insurance, birth insurance and housing fund. These are described in detail in Chapter 5. It is worth noting the Chinese characteristics of social security system: a) the standards of the social benefits varied

considerably across the regions and cities; b) the mandatory nature of various social benefits depended on local regulations and varied across the country; 3) the legal requirements for the standards are often set at the minimum level and the higher standards are left for enterprises to decide. This flexible nature of regulations offered a lot of opportunities for the subsidiaries to design their benefits practices and to use them as a means of people management. The case companies tried, to a varying extent, to provide higher standards or voluntary benefits (not required by law but permitted) to employees as means of increasing employee commitment to the company and creating a good employer image. For example, extra number of paid days for annual leave, annual health check, commercial medical insurance, free lunch at workplace, and free transportation between home and work were mentioned by a number of case subsidiaries. Some benefits were even extended to family members. The benefits practices were often made in conjunction with the salary and bonus practices as a total compensation package. The HR managers in the interviews often referred compensation and benefits to a bundle of C & B (compensation and benefits).

Similar to the benefits practice there was no mention of the transfer of employee representation practice from the HQs in the interviews. When being asked about global policies the interviewees did no report on the HQs policy in employee representation issue. However, some parent organizations (EquCo1 and EngCo2) did have an explicit statement in their annual report that the corporation recognizes collective bargaining and employee organizations in respective host countries where subsidiaries operate. A common comment by the interviewees was that the subsidiary acts according to the Chinese laws.

The situation of employee representation among the case companies was that five subsidiaries (EquCo3, EquCo4, IndCo2, EngCo1 and ConCo) had a labour union in house. The founding ownership seemed to have an impact on unionism. EquCo4 and ConCo were founded as a joint venture with a Chinese state-owned enterprise. The labour union in EquCo4 was directly inherited from the Chinese partner and had been with the company since the founding of the subsidiary. The labour union in ConCo was set up soon after the subsidiary had begun the operation. The union in EquCo3 and EngCo1 was established recently after the Labour Contract Law was promulgated in 2007. EquCo2 and IndCo1 had an employee representative(s), in the company instead of a labour



union. The six other cases (IndCo4, EquCo1, EngCo2, MecCo, ServCo and IndCo3) had neither a labour union nor a worker representative.

#### **6.1.2. Recruitment and Selection**

Only a minority of the case companies (EngCo1, EquCo2, EngCo2 and ServCo) reported that some aspects of the recruitment and selection practices were transferred from the HQs, such as Internal Labour Market, recruitment procedure, assessment test and interview grading method.

The internal labour market (ILM) meant that job vacancies had to be posted on the corporate Intranet. The purpose was obviously to facilitate internal mobility among the units across their global firms. While the subsidiaries complied with this requirement it seemed to have little relevance to recruiting local Chinese employees. One interviewee (EngCo1 4) reported that to avoid the unwanted applications from units of other countries, they specified that the applicant must be fluent in both speaking and writing Chinese. The standardized interview grading method in EngCo2 was regarded as useful in evaluating candidates.

The assessment tests were generally applied for recruiting managerial employees but also used for key personnel who were not managers. This personality test was Internet-based. While assessment tests were common in the parent companies in Finland, they were much less used in the subsidiaries in China. The tests tended to play a less important role the selection as well. The HR manager of EquCo2 and EngCo1 reported that these tests were not important and only served as a reference. The downplaying of personality and psychological tests may be explained by the lack of applicability in China as these tests have been developed in a Western context. The other reason could be related to the particular context of China. Psychological and personality assessment is a relative new phenomenon in China – the country does not have such a tradition. Under the central planning system, employee assessments were politically oriented; loyalty to the Communist Party was the most important element. During the Cultural Revolution psychology as a science was criticized as bourgeois and harmful to the interests of the proletariat, and there was no room for this discipline.

The data show that the primary challenge facing most of the subsidiaries in recruitment and selection was finding, or more precisely, attracting suitable job candidates and retaining employees. Great efforts were put in various kinds of recruiting activities, such as Internet, job fair, direct intake from universities and colleges, headhunter, and even poaching. The Internet appeared to be the most important recruitment channel. In China the particular role of Internet is its borderless coverage of job seekers related to the vast size of the country and its fragmented regions. The Internet has the capacity to disseminate information throughout the country, whereas any newspaper would be regarded as local in this respect. The Internet was used to maximize the number of job applicants to cope with lacking suitable candidates resulted from skills shortage. As one interviewee noted,

Our purpose is to get the maximum number of applicants through Internet.  
(EngCo1 3)

In addition, a number of innovative recruiting methods, suited to the local context were used by some case subsidiaries, for example, sponsoring study programmes of local universities and direct intake of graduates from local universities and colleges/ vocational schools based on cooperation agreements.

In all, the data seem to indicate that the recruitment and selection area had few standardized practices transferred from the parent companies. The subsidiaries seemed to have high autonomy in designing what they believed locally suitable practices. In terms of the theoretical focus of this study, there seems to be little evidence of counter pressures from the local context of subsidiary to transferred practices.

### **6.1.3. Training and Development**

Over half of the subsidiaries (IndCo2, EngCo1, EquCo2, EngCo2, ServCo, ConCo and IndCo3) reported some standardized policies from the HQs in management training and development. The policies included global standardized management training programmes for subsidiary managers at varying levels, training frameworks, training materials, and talent management.

The content and scope of these policies varied somewhat among the subsidiaries.

The global training programmes for high level managers were organized by the HQs HR department. The programmes were options for the subsidiaries. There was no mandatory requirement from the HQs. However, these training programmes were perceived very positively by the subsidiaries and actively participated in by local managers. The training programmes for low level managers were designed and run by the subsidiary or by the China country HR following the framework or guidelines from the HQs. The HR manager of EngCo2 described it as follows;

We have a junior manager programme. The framework came from the HQs, but we design the content and run the programme ourselves. We made some adjustment. We invite external consultants to conduct the courses. The training in e.g. finance and strategy is similar. (EngCo2 3)

Another company, EngCo1 developed local programmes with the concepts provided by the HQs, e.g. leadership and competence. Overall, the HQ training policies were in the form of general guidelines and broad framework. The subsidiaries had freedom to take initiatives of their own and contributed considerable input into developing the training in response to local needs and local conditions. Little evidence was revealed from the data in terms of conflicts of interests between subsidiary and HQs or competing pressures between the Chinese institutional environment and the HQs requirement.

#### **6.1.4. Compensation and Performance Management**

In contrast to recruitment and selection, compensation and performance management practices were transferred to a majority of the subsidiaries from their parent organizations. Ten out of thirteen subsidiaries had the HQ-transferred compensation practice in place. The common elements in the compensation practice among these cases included job position grading system, salary standards and pay rise, and bonus system. Although variations existed in the level of employees to whom the practice applied and the mandatory nature of the practice, the substance of the practice elements had much in common.

Similar to recruitment and training, compensation practice was also a mix of the local elements and transferred elements. For example, the bonus scheme for managers was global and the bonus structure for workers was often designed by the subsidiaries. Nine out of the thirteen cases had HQ practice on performance management. This practice also showed high similarity across the cases in the content of the appraisal evaluation, the way to conduct the appraisal discussion, and the linkage of performance to pay. A detailed description of these two practices will follow in the next section.

To summarize, no transfer in benefits and employee representation was found across the cases. The practices in these two HR areas were locally defined, i.e., formulated and decided by the subsidiaries. In recruitment and selection and training and development there were some elements of HQs-transferred practices in some case companies. Compensation and performance management exhibit the highest propensity of practice transfer across the companies. In addition, the case companies experienced varying conflicts between the China's institutional and cultural context and the requirements of the Finnish HQs. These two practices capture the theoretical interest of the study and are chosen for examination of localization, which I will present next.

## **6.2. Localization of the Compensation Practice**

In this section I will present the findings on the transfer of the compensation practice from the HQs of case subsidiaries. Then, I will describe the findings on the influences of institutions and power relations in the MNC organization (the conditions) followed by the findings on the localization of compensation practice (the outcome).

### **6.2.1. Transfer of the Practice from the HQs**

As reported above, the data revealed three common elements in the HQs-transferred compensation practice across the ten case companies: position grading system, salary standard and pay rise, and bonus scheme. Although there are some differences in the scope of the employees covered by the HQs' practice and in the prescriptive nature of the practice the substance of the

practice can be considered rather similar across the cases. Table 6.1 below summarizes the key findings on the content of the transferred practice in the case companies.

**Table 6.1** Summary of the HQs-transferred compensation practice

<b>Case</b>	<b>Content of transferred practice</b>	<b>Employee groups covered by the practice</b>
IndCo1	Bonus scheme	Top management team
EquCo1	Bonus scheme	High-level managers (general manger and equivalent)
IndCo2	Salary standard and adjustment Position grading system bonus scheme	All employees Managers and professionals Up to middle managers
EngCo1	Salary standard and adjustment Position grading system Bonus scheme covering	Managers and professionals Managers and professionals From lower managers upwards
EquCo2	Salary standard and adjustment Position grading Bonus scheme	Managers and professionals Managers and professionals Managers
EngCo2	Salary standard and adjustment Position grading system Bonus scheme	Managers and professionals Managers and professionals Managers
MecCo	Salary standard and adjustment Position grading system bonus scheme	Managers and professionals Managers Managers
ServCo	Salary standard and adjustment Position grading Bonus scheme and overall bonus policy	All employees All employees Managers (non-managerial employees were covered by the general policy but not the bonus practice)
ConCo	Salary standard and adjustment Position grading system Bonus scheme and overall bonus policy	All employees All employees Managers and professionals (workers followed the general policy but not the bonus practice)
IndCo3	Salary standard and adjustment Bonus scheme	Managers and professionals High level managers

The position grading system was to define what grading system ought to be used in ranking job positions. This would build a base for deciding the salary level for each position rank. It was fairly common for the HQs to require the case subsidiaries using the grading standards designed by a certain international consulting firm. For example, the position grading system

required by all the parent companies except ConCo was that of Mercer's (a global HR service consulting firm) International Position Evaluation (IPE) system. The HQ of ConCo used the position grading method of Hay (a global management consulting firm).

The salary standard, another common area of compensation practice, was about defining the salary level for each job position or a group of employees. This was closely related to the position grading. The common policy of the HQs of the case subsidiaries was to use the median salary level of the local labour market as the reference, with an allowance of plus or minus certain percentage. The reported fluctuating rate was between 10 and 20 per cent. However, the use of a plus rate had to be justified by the subsidiary. Normally the HQ policy was to use the same consulting firm, such as Mercer mentioned above, in both the position grading methods and local salary information, to keep consistency. IndCo2 and ConCo were different from the other eight companies in that they also had HQ's policy concerning manual workers. The policy was to follow the local wage level. In labour intensive sector where these two companies were operating this meant the minimum wage of the locality.

The corporate bonus practice was fairly similar across these cases in the composition of bonuses, the corresponding percentage for each component, the total percentage of the bonus, and the level of subsidiary employees to which the practice was applied. For example, the bonus scheme was applied to managers in all the companies, and in some case companies also to key personnel. In addition, in two companies (ServCo and ConCo) there was a general bonus policy applied to all employees. For managers the bonus was linked to the financial result of the subsidiary or the financial results of both the subsidiary and the corporation. In addition, the maximum bonus percentage normally went upwards along the organizational hierarchy: the higher the position, the higher the percentage of the bonus. The maximum bonus set by the HQs was reported to range from 10 to 30% of the yearly salary.

Across the cases, the bonus policy and bonus scheme were all mandatorily required by the HQs. Salary standards and pay rise, as well as position grading were also mandated by the HQs in all except IndCo1, EquCo1 and IndCo4. Overall, the data show evidence of a high tendency of mandatory nature in the transfer of the compensation practice.

### **6.2.2. Influences of Institutions and Power in the MNC**

The causal conditions under investigation include labour regulation, labour union, labour market mobility, location, HQs monitoring, and strategic role of subsidiary. The two conditions – labour regulation and labour union – appeared to have no effect on the practice. The findings on these two conditions are briefly described here.

For the condition labour regulation, the interviews revealed that the regulations on minimum, overtime pay and wage payment are the most important legal rules which the case companies had to follow in their compensation practices. No conflict was observed between the HQ-transferred practices and the requirements of the Chinese laws on wage issues. As I will show later the key issue in localization was not the question of complying with the minimum wage standards but tackling the problem of retention with locally adapted practice.

As for the condition labour union, although five subsidiaries (IndCo2, Sun G, ConCo and IndCo3) had a union in the company none of these unions was involved in salary and bonus issues. There was an incident in IndCo2 where the union supported the workers in a strike caused by a dispute on overtime pay between the management and workers. However, the union did not play a real role in the decision-making on defining the wages standard. Labour unions where existed appeared no influence on implementing the HQ-transferred compensation practices.

In the following part I will present the findings on the causal conditions of labour market mobility, location, HQs monitoring, and strategic role of subsidiary.

#### *Labour market mobility*

The Chinese labour market presented a special challenge for the case subsidiaries. As discussed in Chapter 5, since mid-1990s China has experienced a rapid liberalization in the labour system. The old “three irons” system, the ‘iron bowl’, ‘iron chair’ and ‘iron wage’, was eventually abolished. The labour market developed rapidly towards free mobility of workforce. The

continuous economic growth at a high speed resulted in a shortage of experienced professionals and qualified specialists, competent managers, and skilled workers. This tight labour market further accelerated the inter-firm mobility of the people who were in high demand.

Operating in this institutional environment, namely high labour mobility coupled with a lack of skills was very different from the Finnish home country of stable labour market and low labour mobility. The subsidiaries faced considerable challenges in recruiting and retaining suitable employees. However, whether they regarded this as an acute pressure on their compensation practice varied across the cases. Table 6.2 below summarizes the findings on the pressure of high labour mobility. Based on the findings, the condition high labour mobility is dichotomized for the QCA analysis that follows in the next section. The subsidiaries that perceived or experienced pressure of high labour mobility are calibrated to the presence of the condition. The subsidiaries that perceived or experienced no pressure of high labour mobility are calibrated to the absence of the condition.

**Table 6.2** Pressure of high labour market mobility

Case	Pressure of high labour market mobility	Dichotomization on the condition for QCA
IndCo1	Yes	Present
EquCo1	No	Absent
IndCo2	No	Absent
EngCo1	Yes	Present
EquCo2	Yes	Present
EngCo2	Yes	Present
MecCo	No	Absent
ServCo	No	Absent
ConCo	Yes	Present
IndCo3	No	Absent

As Table 6.2 shows, five case companies – IndCo1, EngCo1, EquCo2, EngCo2, and ConCo – regarded high labour market mobility a pressure on their



compensation practice. EngCo1 and EngCo2 are typical examples of this. The director of EngCo1 commented like this,

Our problem has been how to keep good people...They go to other companies. We do not have enough of them. We want to have the best people working for us. (EngCo1 3)

The company regarded retention as one of the priorities in the overall HR functions and the compensation policies had to tackle this problem. EngCo2 experienced a loss of highly competent employees to their competitors. The interviewee of EngCo2 reported,

From a market point of view, it is the situation of heavily competing for talents... We have been facing many small Chinese companies who tried to poach people from us, a large multinational company. They offered very high salary... We have had such cases that our people moved to them. (EngCo2 3)

This reveals the concern on the less competitive salary of the company that directly affected its employee turnover. The pressure of high labour mobility often reflects some kind of misfit between the HQ compensation practice and the local labour market conditions.

For IndCo1 and EquCo2, the employee stability was worsened with the niche market they were operating in and the fast expansion of their business in China. These two companies were in a small sector where much fewer experienced professionals and graduates were available for the jobs the companies needed. The general manager of IndCo1 stated,

It is quite difficult to recruit qualified workers. We normally cannot find people who have worked in this sector... We have to start from scratch” (IndCo1 1).

According to the general manager, it took a few years to train a new worker to become a competent performer to fully cope with the demand of the job. This meant a high priority to retain skills inside the company. EquCo2 expressed a similar view:

We are a small sector. It is very difficult to find people who can work on the job immediately, especially when we expand fast. (EquCo2 3)

The challenge of retention was apparent for EquCo2 as well, as the following quotation shows:

People always talk about a few things- how you retain people, how you treat people, and how you train people that they don't run away. (EquCo2 2)

It was apparent that labour intensive sectors had higher employee turnover than technology intensive and capital intensive sectors. ConCo reported a turnover rate of 30 – 40 per cent. In fact this was fairly common in labour intensive manufacturing sectors according to the interviewee (ConCo 2). High labour turnover was not necessarily an acute pressure in terms of unskilled workers because they were easily available in the labour market. Young rural migrants were the main source of this type of workforce<sup>12</sup>. Further, a very short training – normally a couple of weeks – was sufficient for the workers to be able to work on the production lines. Thus, for IndCo2 the high labour turnover was not considered as a pressing problem. However, it was a different case for ConCo. ConCo employed nearly 2000 employees and more than half were manual workers. The high flow of workers created a constant challenge for mass recruitment. One of the performance targets of the HR manager was to reduce the turnover rate down to below 20 per cent. In addition, the company had a small group of core workers who had worked for the company for a long time and possessed expertise in the production lines. The company was concerned for their stability. As the HR manager commented,

Our workers, especially those well trained workers are highly desirable for the companies in this economic zone. They easily get a job there if leaving us. (ConCo 2)

ServCo regarded employee turnover as a rather normal phenomenon. The HR manager commented,

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<sup>12</sup> Now the situation is different. Unskilled workers are in short supply as well.

Nowadays employees move between companies. I think this kind of career move is a natural thing. Between two and three years is an ideal interval. We should respect every individual's choice. If an employee stays in the company less than two or three years, he/she may have too much pressure at work, or may not be happy with pay, career development, promotion, or training. In this situation we need to think if there is a problem in the work arrangement, the reward package, or our retention policy. (ServCo 2)

The company did not regard employee mobility as a challenge particularly to compensation practice, rather a benchmark to measure the congruence of employee expectation with various HR policies or work organization of the company.

Similarly, EquCo1, IndCo3 and MecCo did not perceive the generally existed high mobility of employees as a pressing factor on their compensation practice. The director of EquCo1 commented,

Our principle of HR is that we treat people well because they work very hard. But this is not necessarily done by offering a high salary and such things. We give employees opportunities and put them to the job there they can best utilize their skills, ability and personality. (EquCo1 1)

The HR director of IndCo3 stated,

Many employees have been working in the company for a long time. We take care of our people by providing an equal opportunity to everyone. (IndCo3 2)

These quotations indicate that these subsidiaries believed that other factors such as well designed work arrangement and a fair and equal work environment can facilitate workforce stability.

### *Location*

Three subsidiaries (MecCo, ServCo, and ConCo) were located in Beijing, two subsidiaries (IndCo2, EngCo1) in Jiangsu Province, the neighbour of Shanghai, and the rest of five subsidiaries (IndCo1, EquCo1, EquCo2, EngCo2, IndCo3) in Shanghai. The locations of the case subsidiaries are in much more developed

region of China contrasting to other regions such as the middle and western regions. Nonetheless, marked variations were observed in economic and social development, minimum wage standard, living standard, quality of life, level of social security and overall business environment. The subsidiaries reported differences in the attractiveness of these three regions in terms of acquiring and retaining employees. In the same manner as in the causal condition high labour mobility, the condition location is dichotomized for the purpose of the QCA analysis. The subsidiaries that reported their location unattractive are calibrated to the presence of the condition. The subsidiaries that reported their location attractive are calibrated to the absence of the condition. Table 6.3 below summarizes the key findings and the calibration of this factor.

**Table 6.3** Unattractiveness/ attractiveness of the location

Case	Unattractiveness / attractiveness of the location	Dichotomization of the condition for QCA
IndCo1	Attractive	Absent
EquCo1	Attractive	Absent
IndCo2	Unattractive	Present
EngCo1	Unattractive	Present
EquCo2	Attractive	Absent
EngCo2	Attractive	Absent
MecCo	Unattractive	Present
ServCo	Attractive	Absent
ConCo	Unattractive	Present
IndCo3	Attractive	Absent

The data show that the Yangtze River Delta area where Jiangsu province and Shanghai are situated seemed to be more attractive than Beijing area. Also, large cities seemed to be more attractive than smaller cities and newly developed industrial area just at the outskirts of large city. The disadvantage of the location of ConCo (located in Beijing) was largely due to the difference in wage level between the Beijing area and the Shanghai area. The HR manager

commented in light of the minimum wage in Beijing (800 Yuan) and Shanghai (960 Yuan)<sup>13</sup>,

If the wage is higher in the Shanghai area they [the workers] go there. It is true that in the Yangtze River Delta the wage is higher than here [Beijing]. (ConCo 2)

The main site of EngCo1 was located in a relative small city (in Chinese scale) near Shanghai and another site of EngCo1 was located in Shanghai. It turned out that it was much more difficult to recruit competent managers and qualified professionals to the small city. The interviewee of EngCo1 noted the following:

If you need a manager, an expert, or a specialist, the location [of the company] is a challenge, difficult. (EngCo1 3)

There was a big contrast between these two cities in terms of living standard, infrastructure, and urban life and social activities. Shanghai in all respects was more advanced than the smaller city. IndCo2, situated in another smaller city in Jiangsu province faced a similar challenge as EngCo1. It was much difficult to recruit managers to the factory, the main site of the subsidiary than to its Shanghai office. MecCo was situated in an economic zone which used to be a farming area at the far outskirts of Beijing. According to the interviewees (MecCo 1 and 2) the company faced a similar problem as EngCo1 in attracting professionals and specialists. Further, the location was not very attractive to workers either because they tended to move to the region of higher wage, e.g. to Shanghai or Yangtze River Delta area, similar to that reported by ConCo. Another subsidiary, ServCo, however, perceived the location as quite positive though it was also located in Beijing, but in the city centre. Also, a majority of employees in ServCo was specialists and professionals.

Those subsidiaries that were located in Shanghai perceived Shanghai as an attractive location in terms of obtaining highly skilled professionals and specialists, and competent managers. Overall, Shanghai seemed to be the most attractive location. Shanghai not only enjoyed the highest wage level among

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<sup>13</sup> The minimum wage standards in Beijing and Shanghai were the figures of year 2008 published by the respective municipal government.

these locations but also was somewhat more advanced in social security system than Beijing. Shanghai was one of the first few cities in the country that began to integrate the rural migrant workers into the social insurance system and granted them some social security benefits which have been enjoyed only by urban employees. Further, Shanghai had a high concentration of foreign multinational companies. The attractiveness of Shanghai as both an employment location and investment location found in this research is further illustrated by the fact that among the three clusters of Finnish direct investment in China, Greater Shanghai area accounted for over two third of Finnish companies while the Beijing area and the Guangzhou area together had only less than one quarter of Finnish companies (FBCS, 2008).

#### *HQs monitoring*

Reporting and budgeting systems were common among the case companies. There was a monthly or weekly reporting on such issues as sales, orders and headcount. The budgeting system was exercised in all the ten case companies as well. Salary budget was part of the total operation budget which went through an annual planning and review with the HQs. Normally the subsidiary made a proposal for the yearly budget and reported it to the HQ. Then, the HQ approved or disapproved the budget plan. Very often it was a negotiated process between the subsidiary and the HQ to reach an agreement on the budget. The control of headcount (number of personnel) was reported by a number of subsidiaries (EquCo1, EngCo1, EquCo2, EngCo2, ServCo) in the interviews conducted in autumn 2009 and spring 2009. This was largely associated with the financial crisis during which the HQs had tightened the budget control.

However, there were some variations in how strictly the HQs of the case subsidiaries monitored the transfer of particular HR practices. Table 6.4 shows the summary of findings of HQs monitoring of the subsidiaries' implementation of standardized compensation practice.

**Table 6.4** HQs monitoring on implementation of transferred compensation practice

Case	HQs monitoring on the transferred practice	Dichotomization of the condition for QCA
IndCo1	Strong	Absent
EquCo1	Weak	Present
IndCo2	strong	Absent
EngCo1	Weak	Present
EquCo2	Weak	Present
EngCo2	Strong	Absent
MecCo	Strong	Absent
ServCo	Weak	Present
ConCo	Strong	Absent
IndCo3	Strong	Absent

As Table 6.4 shows, IndCo1, IndCo2, MecCo, EngCo2, ConCo, and IndCo3 had strong monitoring by HQs of the implementation of transferred compensation practice. IndCo2 and ConCo are typical cases in this respect. In IndCo2, there was an approval system for the salary and bonus policies made at the subsidiary concerning the part of pay standardized by HQ. The HR manager described the HQ monitoring of the position evaluation as follows:

The evaluation of the position rankings is very scientific. The evaluation results [of position grading] must be approved by the HQ. We have a framework from the HQ. There are definitions. As a HR person you do the evaluation according to these lines. After we have made the rankings the global HQ needs to approve them. For example, if I give 57 to a local sales manager they [the HQ] may say it is too high. Then, this has to be re-evaluated. Generally there should not be a big difference in the evaluation done by different persons. There may be a difference of a couple of rankings, such as 56 and 57. (IndCo2 3)

The standardized bonus schemes were well supervised under HQ's rules. The top manager of IndCo2 commented,

The bonus matrix, levels of bonus for people at different levels of organization are decided in the global policy by the [corporate] group. Then, the global

policy is implemented locally quite strictly. So, we don't have flexibility to modify. (IndCo2 1)

Similar to IndCo2, ConCo also experienced a strict enforcement of HQ's compensation policies. The HR manager of ConCo commented,

The incentives policies in particular, such as salary increase and bonus are strictly administered by the HQ. The global HR makes the final decision on the yearly salary adjustment and bonus plan. Bonus calculation and position evaluation all follow HQ's templates. The positions gradings have to follow the HQ's policy and be made down to operators. At factory level we are executing these policies. We cannot make our own incentive policies. It doesn't work if we try to invent something new. (ConCo 2)

EngCo2 reported HQ's control of salary policy as follows:

We have quite a few HR policies made at local level. Salary is a different matter. It is a sensitive issue. The global HQ has some control over it. We have the approval system policy on the salary budget... These issues are coordinated at the corporate HQ and also at regional HQ. (EngCo2 3)

Compared with the HQs' strong monitoring described above, the HQs' supervision in EquCo1, EngCo1, EquCo2, and ServCo seemed to be rather moderate. In EquCo1 the HQ's policy on bonus concerned only country level managers and key personnel. The policy on salary standards was a brief guideline and the subsidiary could decide how to implement. The situation was similar to EquCo2. In the case of EngCo1 the MNC has been rather decentralized. In recent years there have been more standardized processes, tools and procedures. As the HR director commented,

X (name of the MNC corporation) used to be very decentralized, meaning that subsidiaries of local companies enjoyed high freedom in making decisions and choosing business models and types of customers. Now there are a lot of corporate initiatives trying to standardize processes. It is a good thing but how to address the local needs is an issue. Also some global processes are very slow.



It becomes slower and slower when standardizing more and more things.  
(EngCo1 4)

As for HR, there seemed to be relatively fewer standardized policies. Concerning the area of compensation, although there were a number of standardized elements such as position grading, salary structure and standards and bonus guidelines, and some were even rather detailed, the overall supervision and oversight seemed to be moderate. This was commented on by the general manager of EngCo1:

We have these global policies. They are guidelines. I feel that the HQ does not demand. If you are active you do it. If you don't do it, it does not matter.  
(EngCo1 1)

#### *Strategic role of subsidiary*

This causal condition is examined in terms of whether the subsidiary operated in a large/ key market and had an R & D function. If the subsidiary possessed one of these two elements it is considered strategically important. A large market is judged on whether the subsidiary operated in a large market which contributed to a substantial portion of the MNC profit. A key market refers to a growth market that the MNC perceived as strategically important. Table 6.5 presents the findings on the strategic role of subsidiaries. Similar to the other conditions the dichotomization on the condition for QCA is also presented in the table.

**Table 6.5** Strategic role of the case subsidiaries

Case	Strategic role of subsidiary	Dichotomization on the condition for QCA
IndCo1	Yes	Present
EquCo1	No	Absent
IndCo2	No	Absent
EngCo1	Yes	Present
EquCo2	No	Absent
EngCo2	Yes	Present
MecCo	Yes	Present
ServCo	No	Absent
ConCo	Yes	Present
IndCo3	Yes	Present

Table 6.5 shows that IndCo1, EngCo1, EngCo2, MecCo, ConCo and IndCo3 possessed a strategic role in their respective MNC organization. IndCo1 was the production site for one of the four product lines of the MNC. It served the whole Asian market which was a key growth market for the whole corporation. IndCo1's products had been mainly exported to other countries in Asia. Recently, the subsidiary began to explore China market and this would further strengthen its position. EngCo1 had a very strong position in terms of both market size and R & D in the whole corporation. China was not only the largest single market and the fastest growing market, but also accounted for a substantial portion of the overall global market of the MNC. In addition, the market share of EngCo1 in China has increased among the competitors. An R & D center was established a few years after the founding of the subsidiary. In this respect EngCo1 built up a strong knowledge competence and became a technology innovation center of the corporation. The business director of EngCo1 commented on this when talking about the history of the company,

Most important of all, this factory was built to manufacture the products with latest technology, so we did not use any old technology which the mother company has had. With the technology developed here (in China) we have been able to gain certain market share. (EngCo1 1)

For EngCo2 China was the most important market for the core business line of the corporation. The sector has experienced extremely fast growth globally for several years. The company has benefited from the huge market demand for its products. The HQ has reduced the manufacturing in the home country Finland and increased the production capacity in China. This further enhanced EngCo2's strategic position in the corporate business. Apart from the core business, other business units were also present in China. This made China an important market for the overall business of the corporation. For MecCo, Europe has been the traditional market for the corporation. The importance of Asia has risen in recent years. China has become the most significant market in Asia because of the continuous expansion of the sectors where MecCo's products were used. China was the only manufacturing site in Asia that supplied the products not only to China but also to the whole of Asia. The overall importance of China has grown further in the slowdown of demand in Europe after the financial crisis of 2008.

In the case of ConCo, the subsidiary was the largest manufacturing plant of the MNC and China was the key market for the corporation. ConCo had a fast start up in China and experienced a rapid growth for several years after the establishment. However, the sector was heavily hit by the financial crisis of 2008. Further, the corporation had suffered continuous losses. There had been a major restructuring and cost reduction programme going on. Within two years two plants were shut down and another two plants were merged together. This resulted in a dramatic decrease of the number of employees in the corporation.

The other four subsidiaries EquCo1, IndCo2, EquCo2 and ServCo were not operating in a large market/ key growth market, nor did they have an R & D function. EquCo1 and IndCo2 were not operating in the corporation's core business area. Both served only the Chinese market. The key market of these two corporations was Europe. Further, the sales of these two subsidiaries have grown moderately and accounted for a very small portion of the corporation's total sales. In the case of EquCo2, Europe and North America have been the main markets for the corporation. Although in recent year China has become increasingly important for the corporation the relative share of sales of Asia-pacific was still small. In the case of ServCo, the key market of the corporation was Europe. The sales in Asia accounted for a very small proportion of the total sales. The China operation was rather new compared with the European

market where the corporation has had a much longer history. The subsidiary was founded very recently and had full operation for only a couple of years. The financial crisis of 2008 occurred just at the time when the subsidiary business was taking off. This had serious negative impact on the expansion of ServCo in the China market.

### **6.2.3. The Outcome: Localization of Compensation Practice**

The localization of compensation practice at the subsidiaries is looked at in the context of appropriateness of HQs-transferred policies to the local conditions and subsidiary interest. There were some misfits between the HQs-transferred practice and the local context in majority of the case subsidiaries (see the summary in Table 6.6 and Table 6.7). The pressure from the high labour mobility and/or unattractiveness of the location which was described earlier often revealed underlying difficulty in implementing the HQs-transferred practice. In a majority of the companies the global practice was perceived somewhat as an obstacle to responding to high labour market mobility and a mismatch with employees' values in reward. The subsidiaries are examined, in the situation of misfit between the transferred practice and local context, whether they primarily modified the transferred practice and made it more acceptable to the local conditions (localization) or they primarily adopted the HQs-transferred practice without modification (standardization). Localization is the focal issue which this study aims to explain. The findings on localization are presented first. The findings on standardization are described as well thereafter. Following the same manner as in the findings of the conditions described earlier, the outcome is dichotomized to present (localization) and absent (standardization).

#### *Localization of the compensation practice*

The key findings on the outcome of localization of HQ-transferred compensation practice are summarized in Table 6.6 below.

**Table 6.6** Outcome of transferring compensation practice: localization

Case	Appropriateness of HQ-transferred practice	Outcome of transfer	Dichotomization for QCA
IndCo1	Misfit: bonus policy fell below managers' expectation.	Localization: Bonus plan was adjusted.	Present
EngCo1	Misfit: HQ's salary standard and bonus did not meet the highly competitive labour market for talents.	Localization: Salary standard and bonus percentages were adjusted to a higher level than the global standardized. China-specific saving plan for key personnel and highly potentials was added.	Present
EquCo2	Misfit: pay rise was lower than the labour market competition and would cause high employee turnover.	Localization: General pay rise was adjusted to a higher level than the HQ required. Salary increase for selected employees (key personnel) was much higher than the global policy.	Present
EngCo2	Misfit: low pay rise fell under employee expectation and would worsen employee turnover.	Localization: General pay rise was adjusted and exceeded the HQ's standardized percentage.	Present
MecCo	Misfit: low pay rise fell under employee expectation and would worsen employee turnover.	Localization: General pay rise exceeded the HQ's standardized rate, and for key personnel the increase was much higher than the HQ's requirement.	Present

As Table 6.6 shows, IndCo1, EngCo1, EquCo2, EngCo2 and MecCo adjusted the unsuitable elements of the HQs-transferred practice and made them more acceptable to the local condition. These five cases are thus categorized as localization.

For EngCo1 the primary pressure was the high mobility of the workforce coupled with high competition and scarce skills in the labour market. In addition the location site was a disadvantage in attracting managers and high skills. The subsidiary's salary and bonus policies emphasized attracting talent, retaining workforce stability, motivating employees, and responding proactively to labour market competition. Maintaining a competitive pay level was crucial for retaining talent and workforce in a highly competitive labour market. This became particularly important in China where employees valued financial rewards much higher than in Finland. The HQ's global salary standard was to follow the median salary of the local market allowing a fluctuation of 20 per cent plus or minus by justification of the subsidiary. For the general salary standard the pay level of EngCo1 was adjusted to 20 per cent higher than the median salary in the same tier area. Mercer's salary survey was used as references for the market salary level. This meant that the benchmark was made with reference to foreign companies rather than the local Chinese enterprises. Usually the salary levels were higher in foreign sector than the domestic sector. In general Chinese employees expected higher salary from foreign companies. For the highly desirable candidates whom the company particularly wanted to recruit and key personnel, the salary level of Shanghai was applied instead of that of the smaller city to which EngCo1 ought to benchmark according to the HQ's policy. The salary level was higher in Shanghai than that in the smaller city where the main site of EngCo1 was located. Additionally the company offered a special incentive package, such as a saving plan, a special bonus plan, or a special allowance to key personnel. The saving plan was a retention bonus for the employee who had stayed with the company for an agreed number of years. The business director of EngCo1 stated the following:

Our problem has been how to keep good people. Now there is this kind of employee saving plan implemented just for the first time here in China which is different from what it is in the corporation. This is China-specific, tailored to China. (EngCo1 6)

EngCo1 also adjusted HQ's standardized bonus scheme to a certain extent and fit the local situation. For example, the bonus percentage for managerial and

specialist employees in China was higher than the standardized bonus. This was another “China-specific” adjustment. Bonus practices were also targeted to motivating employees at work; monthly bonuses for workers and annual bonuses for managers and staff were directly linked to the evaluation of the work and performance appraisal scores.

In EquCo2 and MecCo a major modification was made to the HQ’s practice on pay rises. The percentage of yearly salary increase defined by HQ was perceived by the subsidiaries as too low to meet the local labour market conditions. In MecCo the HQ’s policy was to follow the inflation rate of the country. In China the official index was the consumer price index (CPI). Local governments were responsible for publishing this index. Enterprises were expected to follow it as a reference to increase employees’ salary though there was no explicit regulation on it. The HR manager noted,

The head office has put the limit that the salary rise could not exceed the CPI in China. So, the rise has been some 3-4 per cent yearly. Employees have complained about the small increase of salary. (MecCo 2)

In effect the salary growth in China was much higher than the CPI. The general manager of MecCo commented the following:

Global policies are made too much Finland-based. For example, the salary rise, there [in Finland] they are talking about 2-3 per cent. Here [in China] the salary growth is much higher, and is getting even higher. The salary increase can be 20 per cent yearly. (MecCo 1)

The interviewee of EquCo2 commented,

Our salaries were seemingly lower than those of our competitors. We had relatively low annual increase in our salaries. We faced problem losing people. (EquCo2 3)

These two subsidiaries negotiated with the HQ and succeeded to go over the standardized rule and reached a higher rate in raising the salary. The interviewee of EquCo2 noted:

In the past HQ set the rate of salary rise. For a couple of years we have been giving a proposal and asking them to approve. If HQ comes back with some concern we will provide more justification and show that production would run into trouble with this high [employee] turnover rate. (EquCo2 2)

Apart from the higher percentage of the general pay rise, for certain employees (key people) the salary rise was even higher. For example, EquCo2 reported cases of doubling the salary for some employees. The general manager of EquCo2 further explained,

Of course we have to give reasons why this person should be given this rise in salary. (EquCo2 2)

In addition to the adjustment to HQ's salary policy, EquCo2 considered HQ's position evaluation system not quite suitable for its current situation. The company has experienced fast expansion and new job positions continuously appeared along with the increase of the functions. Further, there were several units of various sizes. The HR manager stated the following:

When I came to this company five years ago we had less than 100 people. It was a small factory. Gradually there came production, services, sales and design. Now we have over 800 people in China. (EquCo2 3)

Further, the unified HQ's position grading method could not reflect the differentiated structure and size of the units. Eventually the position grading system could not be established. The same HR manager of EquCo2 commented the difficulty to apply a standardized position grading system,

The business units are complicated. It is difficult to unify. A small BU [business unit] general manager may be equivalent to a middle manager or even lower manager of a large BU, but the small BU requires a general manager. It is difficult to coordinate. There has been such as a plan to set up the position evaluation. But the company is expanding so quickly that it is difficult to establish this system. The business grows faster than the set-up of the system. (EquCo2 3)



IndCo1 only had a bonus policy from HQ for the top management term. The bonus plan was negotiated between the subsidiary and HQ. The subsidiary could exert substantial influence on the bonus structure and the share of bonus in the total profit. The bonus policy for the rest of employees was made by the subsidiary itself. Also, the other elements of compensation practice, such as salary standard, pay rise, and job grading were defined by the subsidiary. The major adjustment of EngCo2 was a higher pay rise than the HQ standardized requirement.

*Standardization of the compensation practice*

IndCo2, ServCo and ConCo by and large adopted the global practice in spite of the misfit. EquCo1 and IndCo3 reported no misfit, and the HQs' practice was implemented without modification. These five cases are calibrated to standardization. Table 6.7 below summarizes the key findings.

**Table 6.7** Outcome of transferring compensation practice: standardization

Case	Appropriateness of HQ-transferred practice	Outcome of transfer	Dichotomization for QCA
EquCo1	Fit: bonus policy for high level managers was suitable.	Standardization: Transferred practice was implemented without modification.	Absent
IndCo2	Misfit: workers were dissatisfied with low wage. Salary standard was not attractive enough for recruiting managers.	Standardization: No modification to the low wage policy. A minor adjustment was made in using high end salary standard for recruiting high potentials.	Absent
ServCo	Misfit: performance-based bonus mismatches employee expectation for bonus.	Standardization: No modification to the global policy.	Absent
ConCo	Misfit: minimum wage for workers caused them leaving the company. “No profits, no bonus” policy demotivated workers. Flat salary structure did not reflect employee responsibilities and experiences.	Standardization: HQ’s bonus practice and minimum wage standard for workers were implemented despite of the disjunction. The flat wage structure was implemented with exception for line leaders.	Absent
IndCo3	Fit: bonus policy for managers was suitable. No misfit in the salary grading practice.	Standardization: Transferred practice was implemented without modification.	Absent

There were a number of misfits between the HQs-transferred practice and the local context in ConCo, and in IndCo2 as well, but to a lesser extent. These two subsidiaries basically did not (were not able to) modify the unsuitable elements of the HQs’ practice and had to implement them to a large extent. ConCo is a typical case and deserves more space. Firstly, The HQ’s minimum wage policy for manual workers met the challenge of the wage gap between regions. As the HR manager of ConCo noted, workers were leaving the company for the regions of higher minimum wage, such as Shanghai and the Yangtze River Delta region. A majority of the manual workers were rural migrants. Migrant

workers were especially sensitive to pay levels. This was largely due to their economic background. For many of them the motive for work was mainly income-based – looking for a job in cities in order to improve their financial status and support the family at home in the countryside. They were mostly unskilled workers and paid at lowest level. With a basic wage of 800 Yuan per month in Beijing, a difference of 100 Yuan could be decisive in persuading them to change jobs. Thus, with the minimum wage policy ConCo faced a considerable challenge in retaining workers. Basically it failed to respond to the market price of salaries and employee expectations regarding pay level. According to the interviewee (ConCo 2) this kind of wage policy was a norm in labour-intensive companies. This was confirmed by reports in public media and extant research (e.g., Cooke, 2004).

Secondly, the HQ's bonus policy of ConCo was that no bonus was paid if the whole corporation made a loss. This was the so called "killing factor" (ConCo 2). This was considered extremely demotivating for employees, especially workers because their wage was very low and a bonus would top up the total pay to some extent. The workers had not been paid a bonus for a couple of years because the whole MNC suffered a continuous loss. The HR manager was very frustrated with this situation at the time of interview in 2009:

When there has been no bonus for long time employees feel discouraged. They think there is no difference in doing well or badly. (ConCo 2)

This policy was finally amended by the HQ in 2010 when the last interview was conducted. The new policy was that the global target counted only for 50 per cent, i.e., if the corporation's result was unprofitable the workers were still entitled to 50 per cent of the bonus.

Thirdly, the HQ of ConCo recently adopted a flat salary structure. Employees were grouped into broader salary categories. For example, the entire manual workers were grouped into a broad category with little differentiation in wage levels. According to the HR manager of ConCo there were three different types of manual workers- line leader, key operator and general worker. The line leaders had more responsibilities and played more important roles than the other types of workers and the same logic was followed in terms of key operator versus general worker. Quite a few line

leaders had worked for the company for a long time, as the HR manager described,

These people [line leaders] have been here since the establishment and they have gained substantial experience in the production lines. They play a key role in ensuring punctual delivery and good quality. They are very valuable to us. We don't want to lose them. But in the new structure the difference in pay between a line leader and a normal worker is really small. (ConCo 2)

These line leaders had progressively upgraded their salary level over the years. The subsidiary saw that the flat salary structure would act as a demotivation factor to these workers because applying the new structure would mean lowering their salary level. What ConCo did was to keep the old salary level for the existing line leaders and applied the new structure only to key operators and normal workers. This somewhat eased the problem but the narrow gap between key operators and normal workers remained.

IndCo2 met some challenge of applying minimum wage policy for workers as well. For example, the shop-floor workers were not satisfied with their pay and caused some disruptive incidents in the factory. There was some resistance to performance-based pay rises from middle managers. The HR manager reported,

Last year we introduced differentiated salary increase policy for managerial staff based on the results of their performance. They got different increases in their salary. It was not successful. They were not happy with that. Some came to me and asked why they have got different salary rise from others. (IndCo2 2)

As reported earlier, IndCo2 perceived a disadvantage of its location in recruiting and retaining managers. A minor modification was made to the salary standard for managers and key personnel. In the situation where some key positions were needed the subsidiary could adjust the salary standard to a higher level within the HQ-specified 20 per cent. The HQ's policy allowed for a fluctuation of 20 % below or above the median salary of the region where subsidiary was located.

The misfit in ServCo was reported in the bonus policy. According to the corporate bonus plan only managerial staff enjoyed a bonus. The HQ also

specified a performance-based bonus. Following this principle any extra pay outside the normal salary was regarded as a bonus, thus ought to be paid against performance. This was somewhat at odds with employee expectation for some kind of bonus, especially before the Chinese New Year. The general manager commented as follows:

Of course, it would be nice to give something before the Chinese New Year. But people would take this as a bonus. We have a bonus policy, which is always performance-based. Therefore we don't pay the 13th month salary, because that would contradict our principle in a way. (ServCo 1)

The 13th month salary meant that an employee who had worked for a full year was automatically paid one extra month's salary. This was a prevailing practice in China and local employees expected it from employers. The subsidiary did not see this restrictive incentive policy a problem for China. The general manager stated,

We pay more than average. We have rather high base salary. (ServCo 1)

This meant that their salary level was higher than other companies that were operating locally. The subsidiary adopted a high salary and restricted bonus practice which was consistent with HQ's policies. This was likely due to the homogeneous and highly educated employees. ServCo was a service company. Because of the nature of business, the bulk of employees consisted of experts and specialists. Administrative staff was minimal. In addition, the existing personnel were mostly leaders and key individuals who were crucial for the start-up of the new business unit. The next step would be to recruit more normal engineers. This policy might meet more challenge in the future.

EquCo1 and IndCo3's global policy concerned only the bonus scheme for higher level managers. The interviewees of these two companies (EquCo1 1, EquCo1 3 and IndCo3 2) reported that the global bonus scheme was suitable for the subsidiary and implemented accordingly. The salary and bonus practice for the other employees was defined by the subsidiaries.

It is worth noting that although the case subsidiaries of standardization adopted the transferred practice without modification or with minor

modification they had some locally designed element(s) of compensation practice (and some other HR practices as well). The locally designed practices existed also in the case subsidiaries of localization. This will be described below.

### *Localized practice versus locally designed practice*

The findings described in this section show that most subsidiaries were able to gain some exceptions from the HQs or modify the transferred compensation practice in situations of misfit. The findings also show that the HQs-transferred compensation practice consisted of only part of the subsidiary compensation practice. The data indicate that outside the area of HQs-transferred practice the subsidiaries had considerable freedom to design their own practices and this was the terrain the subsidiaries had much room to utilize the institutional resources to serve their own interest. For example, the 13th month salary was widely adopted by the subsidiaries including IndCo2 and ConCo that were apparently not able to modify the HQs' practice. The 13th month salary was paid to all employees and served as a sort of bonus. The subsidiaries used this locally prevailing practice to increase the incentive for employees by going around the HQs' policy territory. A number of other forms of bonus were adopted by some subsidiaries as well, e.g., best monthly employee prize in ConCo and IndCo3 and best quality prize in IndCo1 and MecCo. Further, the benefits practice formed part of the total compensation practice, i.e., compensation and benefits were normally bundled together. The data revealed that benefits practice was totally under subsidiary discretion. As Chapter 5 described, China's institutional environment was such that the Chinese government encouraged enterprises to provide extra benefits or benefits of a higher standard. The subsidiaries adopted, to a varying extent, some extended benefits in e.g. commercial insurance, health checks, free meals, transportation and company car, and/or higher standards of social benefits in e.g. medical insurance, pension insurance and housing funds. IndCo2 provided a housing fund even though the local regulation did not require it. These benefits served as a complement to the formal salary and bonus. In this way the subsidiaries tried to create an attractive compensation package that would appeal to employees and increase employee commitment. This evidence indicates that

localization of compensation practice should be looked at in connection with benefits practice because benefits practice had similar purpose of motivating and retaining employees. Apart from the benefits practice discussed above, many subsidiaries attempted to improve employee retention by providing extensive training (e.g. IndCo1, IndCo2, EquCo2, ServCo and ConCo), or creating a fair and equal work environment (e.g. EquCo1, IndCo3 and IndCo1). These findings show that employee retention could be actualized through other means than compensation practice alone.

### 6.3. QCA Analysis on Compensation Practice

In the previous section, I described the findings on the causal conditions and the outcome, based on which I calibrated the set-membership of the cases. Now this information is transferred to a data matrix (Table 6.8) below:

**Table 6.8** Data matrix for QCA analysis

Caseid	High labour market mobility	Unattractive location	Weak HQs monitoring	Strategic role of subsidiary	Outcome: Localization
IndCo1	1	0	0	1	1
EquCo1	0	0	1	0	0
IndCo2	0	1	0	0	0
EngCo1	1	1	1	1	1
EquCo2	1	0	1	0	1
EngCo2	1	0	0	1	1
MecCo	0	1	0	1	1
ServCo	0	0	1	0	0
ConCo	1	1	0	1	0
IndCo3	0	0	0	1	0

As the table shows the top row lists the four conditions and the outcome. The most left column is case identification (caseid) denoted by the pseudonymous names of the case subsidiaries. All the ten cases are included.

### 6.3.1. Truth Table

I transform the data table (Table 6.8) into a truth table by using the software fsQCA (Ragin and Davey, 2009). Table 6.9 below displays the truth table.

**Table 6.9** Truth table of the Boolean configurations for localization of compensation practice

Caseid	High labour market mobility	Unattractive location	Weak HQs monitoring	Strategic role of subsidiary	Outcome: Localization
EngCo1	1	1	1	1	1
EquCo2	1	0	1	0	1
IndCo1, EngCo2	1	0	0	1	1
MecCo	0	1	0	1	1
IndCo2	0	1	0	0	0
IndCo3	0	0	0	1	0
EquCo1, ServCo	0	0	1	0	0
ConCo	1	1	0	1	0

This truth table displays only the configurations corresponding to the observed cases. As the table shows, two rows have multiple cases. IndCo1 and EngCo2 share the same combination of conditions that leads to [1] outcome. EquCo1 and ServCo have the same combination of conditions which leads to [0] outcome. This is already a step forward to data reduction, from the initial total ten confirmations to eight configurations. There are four different configurations for [1] outcome and [0] outcome respectively. No contradictory configuration, i.e., the same combination of conditions representing both the [1] outcome and [0] outcome, occurs.



### 6.3.2. QCA Analysis of Presence of the Outcome- Localization

#### *Analysis of necessary conditions*

Before proceeding to analyzing sufficient conditions I test necessary conditions. As described in Chapter 3, a causal condition is necessary when the outcome is present the condition always occurs, i.e., no case may show the outcome without the condition. In the set relationship, the cases that exhibit the outcome are a subset of the cases that all exhibit the condition. When evaluating possible necessary conditions it is recommended to use consistency score 0.90 as the threshold (Ragin, 2009; Schneider and Wagemann, 2012). The results of necessity analysis of this study show that the consistency score is below 0.90 (see Appendix 5). Thus, there is no necessary condition for localization ([1] outcome). In effect, the number of cases is small in this study. This cutting point is less meaningful here than for a larger number of cases.

#### *Analysis of sufficient conditions*

As recommended by Ragin (2008b) I perform the standard analysis with the software (Ragin and Davey, 2009). The result suggests four configurations in the complex solution as shown in Table 6.10 below. The score of both the consistency and the total coverage of the solution terms are 1 (see Appendix 6).

**Table 6.10** QCA complex solution for localization

Solution terms	Cases covered
1) hlmm*unallocation*whqmonitor*ssr +	EngCo1
2) hlmm*~unallocation*whqmonitor*~ssr +	EquCo2
3) hlmm*~unallocation*~whqmonitor*ssr +	IndCo1, EngCo2
4) ~hlmm*unallocation*~whqmonitor*ssr	MecCo

Note:

hlmm = high labour market mobility

unallocation = unattractive location

whqmonitor = weak HQ monitoring  
ssr = subsidiary strategic role  
\* = the logical AND  
~ = absent state of the condition  
+ = the logical OR

As noted earlier, a complex solution is produced from the minimization of the configurations that have empirical cases. The complex solution for the outcome of localization consists of four solution terms that correspond to the five cases which are indicated in the right column of Table 6.10. Each solution term may be seen as a sufficient path leading to the localization of compensation practice. This shows multiple paths to the same outcome. Further, all the terms are combinatorial conditions, i.e., conjunctural, which indicates that no single condition is found to be sufficient for the outcome. These two features together indicate the notion of multiple conjunctural causation (see Section 3.2).

The four configurations in Table 6.10 inform that localization is observed in the following circumstances:

- 1) The subsidiary operates in an unattractive location, experiences a pressure of high labour mobility, experiences weak monitoring from the HQ and has a strategically important role in the MNC organization. This situation corresponds to the case company EngCo1.

Or

- 2) The subsidiary operates in an attractive location, experiences a pressure of high labour mobility, experiences weak monitoring from the HQ, and has no strategic role in the MNC. This is the situation of case company EquCo2.

Or

- 3) The subsidiary operates in an attractive location, experiences a pressure of high labour mobility, experiences strong monitoring from the HQ and plays a strategic role in the MNC organization. Two case companies, IndCo1 and EngCo2 fall into this situation.

Or

- 4) The subsidiary operates in an unattractive location, experiences no pressure of high labour mobility, experiences strong monitoring from the HQ and is strategically important in the MNC organization. Case company MecCo is found in this situation.

Now I interpret these configurations in terms of the theoretical framework I constructed in Section 2.5. Regarding the host country institutional context, the four configurations in Table 6.10 indicate that the need for localization comes from the demand of the host country institutions. I factor the two conditions of host institutions and present the four configurations in a slightly different way shown in Table 6.11 below.

**Table 6.11** QCA solution terms with factored host country conditions

Solution terms	Cases covered
1) hlmm*unalocation*(whqmonitor*ssr) +	EngCo1
2) + 3) hlmm*~unalocation*(whqmonitor*~ssr + ~whqmonitor*ssr) +	EquCo2, IndCo1, EngCo2
4) ~hlmm*unalocation*(~whqmonitor*ssr)	MecCo

Note:

hlmm = high labour market mobility

unalocation = unattractive location

whqmonitor = weak HQ monitoring

ssr = subsidiary strategic role

\* = the logical AND

~ = absent state of the condition

+ = the logical OR

As the table shows the need for localization stems from either both high labour mobility and unattractive location as in the case EngCo1 or one of them as in the cases EquCo2, IndCo1, EngCo2 and MecCo. This seems to indicate that the condition for the occurrence of localization is that the subsidiary experiences a pressure from at least one of the sources – high labour market mobility and unattractive location.

In a similar manner as with the conditions of host country context, I factor the conditions of MNC organizational context and obtain the following configurations (Table 6.12):

**Table 6.12** QCA solution terms with factored MNC organizational conditions

Solution terms	Cases covered
1) whqmonitor*ssr*(hlmm*unallocation) +	EngCo1
2) whqmonitor*~ssr*(hlmm*~unallocation) +	EquCo2
3) + 4) ~whqmonitor*ssr*(~hlmm*unallocation + hlmm*~unallocation)	IndCo1, EngCo2, MecCo

Note:

hlmm = high labour market mobility

unallocation = unattractive location

whqmonitor = weak HQ monitoring

ssr = subsidiary strategic role

\* = the logical AND

~ = absent state of the condition

+ = the logical OR

As Table 6.12 shows, regarding the MNC organizational context, three types of combinations of conditions seem to entail the occurrence of localization: weak HQ monitoring and strategic role of subsidiary, weak HQ monitoring and non strategic role of subsidiary, or strong HQ monitoring and strategic role of subsidiary. This finding reveals the power relationship between the MNC HQ and the subsidiary and the subsidiary capability to adjust the HQ's compensation policy when it is unsuited to the local context of host country. In order to understand how these power relationships work with the contextual pressures of host country and produce the result of localization I proceed to identifying the causal mechanism through within-case analysis.

### *Identifying causal mechanisms*

The strength of QCA is lies in the ability to identify the combinations of conditions that lead to a given outcome. As De Meur et al. (2009: 160) point out, "it describes the conditions that are present or absent when an outcome is observed or not observed". QCA by design does not describe the process behind the conditions. To open the "black box" of causal mechanism leading to

the outcome it requires within-case analysis on the process (Brady and Collier, 2010; George and Bennett, 2005; Gerring, 2010; Mahoney, 2004). What is valuable in QCA techniques is its intimacy with the cases and visibility of the cases throughout the analysis (Shalev, 2007). This allows for in-depth analysis of underlying processes.

As described in the findings in Section 6.2.2, the need for localization comes from some kind of misfit between the HQs-transferred practice and the Chinese local context. More specifically the central issue of localization was to adjust the HQs' policy to tackle the high labour mobility and disadvantages caused by location. Returning to the cases the data show that the modification of HQ's practice in IndCo1, EngCo2 and MecCo (configuration 3 and 4) all involved a negotiation between the subsidiary and the HQ. In EngCo2 the negotiation was carried out by the China management team who coordinated all the units in China. The HR director described the process as follows:

When we feel difficult to implement the HQ's global policy like this salary policy, we propose our own percentage for the salary increase. The HQ usually comes back with a different [lower] figure. Then, we collect more information. We show more evidence that the HQ's idea does not quite meet the situation here. If there is still a disagreement at the end we China management will make the final decision. (EngCo2 2)

In IndCo1 the bonus level was negotiated between the general manager of the subsidiary and the HQ in Finland. A similar situation was observed with MecCo. The general manager of MecCo stated,

There are always hard negotiations concerning budget issues. This is directly related to the pay rise. In the end, we normally got the percentage we proposed. (MecCo 1)

A common characteristic is that these case companies negotiated the "terms" of implementation and were able to gain some concession from the HQs, despite the HQs' tight centralized policy (strong HQ monitoring). This indicates a power position of the subsidiaries. As the data show, this powerful position was entailed by the strategic role of the subsidiary within the MNC.

In configuration 1, EngCo1 encountered pressures from both high labour mobility and unattractive location. Consequently, the need for adjusting the transferred practice was greater than IndCo1, EngCo2 and MecCo. The strategic position of EngCo1, not only operating in a big and growing market but also being an R & D centre and technology leader seemed to give EngCo1 a significant position in the whole MNC. This was supported by the fact that EngCo1 succeeded, without hard negotiation, in a number of modifications and exceptions in bonus level, salary standard and special bonus plan for high potentials. In addition the data also indicate a supportive attitude from the HQ in modification of the standardized compensation policy by the subsidiary. This is reflected in the “China specific” policies that were enjoyed by EngCo1 and seemingly not by subsidiaries of other countries. This favorable attitude of HQ was apparently due to the strategic importance of the subsidiary. In the second configuration EquCo2 was seemingly in the disadvantageous position in terms of power relationship with the HQ because it had no strategic role in the MNC. On the other hand lack of HQ’s monitoring of the implementation of the transfer apparently provided the subsidiary with some freedom as well. The subsidiary could prioritize to implement some elements of the practice over the other elements according to its own need. This subsidiary autonomy seems to reflect the ethnocentric policy of the parent company or the lesser importance of the subsidiary to which HQ might pay less attention than to those subsidiaries that are strategically important. Table 6.13 below summarizes the mechanisms of localization through the within-cases analysis on these four configurations.

**Table 6.13** Causal mechanisms for localization

Causal mechanism	Configuration	Case
Common interest between subsidiary and HQ	hlmm*unalocation*whqmonitor*ssr	EngCo1
Subsidiary autonomy	hlmm*~unalocation*whqmonitor*~ssr	EquCo2
Negotiation process	hlmm*~unalocation*~whqmonitor*ssr ~hlmm*unalocation*~whqmonitor*ssr	IndCo1, EngCo2 and MecCo

### 6.3.3. QCA Analysis of the Absence of the Outcome- Standardization

The same procedure of QCA analysis is repeated for standardization of compensation practice as it is with the localization of compensation. The notion of necessity for the absence of the outcome is the same as that for the presence of the outcome. For absence of the outcome (standardization), a causal condition is necessary when the absence of the outcome occurs, the condition always appears. The result of the necessity test shows that the consistency score is below 0.90 for all the causal conditions (see Appendix 7). This indicates that no individual causal conditions are found to be necessary for the standardization of compensation practice. Having conducted the standard analysis on sufficient conditions I obtain the complex solution that consists of four solution terms as displayed by Table 6.14 below. The scores of consistency and the total coverage of the solution terms are 1 (see Appendix 8)

**Table 6.14** QCA complex solution for the standardization of compensation practice

Solution terms		Cases covered
1)	$\sim hlmm * \sim unallocation * \sim whqmonitor * ssr$	IndCo3
+		
2)	$\sim hlmm * \sim unallocation * whqmonitor * \sim ssr$	EquCo1, ServCo
+		
3)	$\sim hlmm * unallocation * \sim whqmonitor * \sim ssr$	IndCo2
+		
4)	$hlmm * unallocation * \sim whqmonitor * ssr$	ConCo

Note:

hlmm = high labour market mobility

unallocation = unattractive location

whqmonitor = weak HQ monitoring

ssr = subsidiary strategic role

\* = the logical AND

~ = absent state of the condition

+ = the logical OR

The four minimum formulas in Table 6.14 indicate four different possible causal paths to the standardization of compensation practice. These configurations cover total five cases as shown on the right side of the table. The four configurations can be understood as follows:

The standardization of compensation practice is observed in the circumstance where

- 1) A subsidiary lacks the pressure from high labour mobility, operates in an attractive location, experiences strong HQ monitoring, and possesses a strategic role in the MNC organization. This situation corresponds to the case IndCo3.

Or

- 2) A subsidiary lacks the pressure from high labour mobility, operates in an attractive location, experiences weak HQs monitoring, and lacks strategic role in the MNC organization. This situation corresponds to the cases EquCo1 and ServCo.

Or

- 3) A subsidiary lacks the pressure from high labour mobility, operates in an unattractive location, experiences strong HQs monitoring, and lacks strategic role in the MNC organization. This situation corresponds to the case IndCo2

Or

- 4) A subsidiary experiences pressure from high labour mobility, operates in an unattractive location, experiences strong HQs monitoring, and possesses strategic role in the MNC organization. This situation corresponds to the case ConCo.

Looking across the cases it is apparent that in the first and second configurations the institutional factors are absent. This tells that there was a lack of driver at the subsidiary side to modify the HQ's practice. The case data indeed show that the subsidiaries perceived little opposing pressures between the high labour mobility in the local market and the HQs mandatory policy. For EquCo1 the HQ's policy involved bonus schemes for only senior level managers, thus the compensation practice for majority of the employees was outside the scope of the HQ's global policy. IndCo3 was similar to EquCo1 in that HQ's global policy in salary and bonus applied only to rather limited groups of employees, namely high level managers and to some extent middle



managers as well. For ServCo the high salary practice somewhat compensated the absence of bonus. The bonus policy, though somewhat mismatched to employee expectation, did not seem to cause real problem. As analysed earlier, the homogeneous characteristic of the employees – highly educated and highly skilled – seemingly contributed to implementing standardized practice.

The interesting cases are IndCo2 and ConCo where counter pressures to the transferred practice existed. The most interesting case is ConCo with the fourth configuration. ConCo encountered the challenge of both high labour turnover and unattractive location. There were a number of misfits between the HQ's global policy and the local institutional context. In spite of the great needs ConCo felt to adjust the HQ practice it failed to make any major modification. The unsuitable elements of the transferred practice, such as minimum wage, no profit no bonus and flat salary structure had to be implemented. Looking at the MNC organizational context, the subsidiary operated in a large growth market. Theoretically it should be strategically important within the whole MNC and possess some power capability in relation to the HQ, as it is shown in most of the localization cases. However, this is not the case with ConCo. The data clearly show that ConCo failed to utilize the external institutions as a power resource. One key reason seemed to be that the whole MNC had suffered from bad economic performance and was in deep crisis. The MNC was under major restructuring and the tight salary and bonus policy were part of the restructuring programme. The other reason seemed to relate to the labour intensive nature of the industry where cost effectiveness is of the utmost importance and has a bigger impact on compensation practice. Or it might relate to the electronics sector where performance driven strategy could be prevailing more than in other sectors.

## **6.4. Localization of the Performance Management Practice**

### **6.4.1. Transfer of HQs' Performance Management Practice**

In the nine case companies (number 2 to number 10 in Table 3.1) except EquCo1, a standardized form of appraisal evaluation was developed at the HQs and transferred to all the units for global use. The structure of the appraisal

template was similar among the companies. It normally included four parts: appraisal of past performance, competence evaluation or discussion, a personal development plan and target setting for the next year. The measurement of performance was quantitative with a grade, e.g. 1 to 5, or percentage. There were also global guidelines or instructions on how to conduct the appraisal and to use the forms. Some parent organizations (e.g. those of ServCo and ConCo) had also a requirement for standardized appraisal language, i.e. the evaluation discussion ought to be conducted in English and the forms ought to be filled in English. The superior and subordinate were to carry out annual or bi-annual discussion to review the performance, set the objectives for the next year, and agree on the personal development plan. In EngCo1 and ServCo there was also a mid-year follow-up discussion session to adjust the objectives of current year or improvement plan. In EquCo1 according to the HR manager there was no template transferred from HQ. The subsidiary was supposed to design the evaluation form itself.

Two tendencies were observed from the data. One was the enlargement of employee groups who were covered by global performance appraisal. Often the practice was first introduced to high level managers and gradually extended to lower levels of managers, and then, to other employees. For example, in EngCo1, EquCo2, and MecCo, this practice was initially applied only among managers; then, it expanded to professionals and staff. Very recently it became applicable to all employees in EngCo1 and EquCo2. In EngCo2 the HQ's policy of 100 per cent coverage of performance management was just introduced at the time of interview. The other was the tendency of linking performance to pay. It was apparent that the bonus was most likely to be linked to the performance in one way or another. Performance was measured by an individual/ personal target, or both individual and group targets. The linkage of the salary rise to performance seemed to be less extensive than the linkage of the bonus to performance. Overall, there was an increasing emphasis by HQs on using standardized performance management practice globally. Table 6.15 summarizes the key findings described in this section.

**Table 6.15** Transfer of standardized performance management practice

Case	Transferred practice and its applicability
EquCo1	A policy framework
IndCo2	Standardized template and instructions, applying to managers
EngCo1	Standardized template, instructions and detailed guidelines, applying to all employees
EquCo2	Standardized template and instructions, applying to all employees
EngCo2	Standardized template and instructions, applying to managers and professionals
MecCo	Standardized template and instructions, applying to managers
ServCo	Standardized template and instructions, applying to all employees
ConCo	Standardized template and instructions, applying to all employees
IndCo3	Standardized template and instructions, applying to managerial employees

#### **6.4.2. HQs Monitoring on Implementation**

While all the nine case companies had HQ-transferred performance management practice in place the interview data revealed that the extent to which this practice was mandated by HQs or was an option available for subsidiaries varied across these cases. Also, how HQs monitored the implementation varied across the cases. Table 6.16 below shows the key findings on these two issues.

**Table 6.16** HQs monitoring on implementation of standardized performance management practice

Case	Mandatory nature	HQs monitoring
EquCo1	Non-mandatory	No monitoring
IndCo2	Non-mandatory	No monitoring
EngCo1	Mandatory	Little oversight on the implementation
EquCo2	Mandatory	Strong
EngCo2	Mandatory	No monitoring
MecCo	Non-mandatory	No monitoring
ServCo	Mandatory	Moderate
ConCo	Mandatory	Strong (Reporting to HQ and modification to the standardized policy was strictly restricted)
IndCo3	Mandatory	No monitoring

As Table 6.16 indicates, the majority of case subsidiaries perceived or experienced rather moderate monitoring by HQs of the implementation of this practice. Most case subsidiaries felt a considerable freedom on how they could carry out the performance appraisal and discussion. According to the interviews with EquCo1 and IndCo2 there seemingly was no mandatory requirement from the HQs. In the interview when asked about HQ standardized policies and practices, performance management was not mentioned initially and it appeared later during the interview that there was such a practice in the corporation. This was further confirmed by the corporate reports. The HR manager of IndCo2 commented in comparing with the early experience which the interviewer had gained through working in an American MNC:

Y (name of the MNC corporation) is flexible. It is not centralized. The corporate does not seem to advocate [the performance management practice]. The US company was very results oriented. It was also very centralized from the top HQ down to the bottom. When I worked there we had quite a number of global policies in e.g., HR and finance, strongly pushed by the HQ straight down to the subsidiary. Here I do not see this. (IndCo2 3)

In EngCo1 although the global performance management policies were transferred with detailed operational instructions the monitoring of implementation process seemed to be inadequately exercised, at least seen by the general manager:

We have this yearly performance appraisal. There should be actions taken to poor performers and to make them improve. If they do not improve we should consider moving them to another job or dismissing them. Many countries did not implement this... The HQ promotes this policy but there is little control. Then, there is no standardized implementation. (EngCo1 1)

The interviewee was seemingly critical of the HQ's inconsistency between the written policy and the actual implementation, which might result in unfairness between subsidiaries and lack of effectiveness of this policy. In EngCo2, MecCo, and IndCo3 the practice was also mandatory but implementation was dependent on individual subsidiary own action, somewhat similar to EngCo1 in this respect. In addition the policy was of a framework type and rather general in nature.

The interviews show that EquCo2, ServCo and ConCo experienced closer monitoring and more persuasion from the HQ than the other case subsidiaries. The interviewee of EquCo2 stated the following:

The framework of performance discussion and appraisal is global. It has an identical format for everyone in the whole corporation. It should be done according to that. (EquCo2 1)

In ServCo and ConCo, for example, there was a reporting system on the results of performance evaluation. In addition, in ConCo the appraisal evaluation from the template to the discussion language ought to follow the standardized procedure. Under the HQ's restriction it was almost impossible to modify any element of the practice even if it was not suitable to the subsidiary condition. This point will be further described in the findings on the outcome of localization.

#### **6.4.3. Outcome of Transfer: Localization**

The data show that the extent to which the transferred practice was implemented by the case subsidiaries differed considerably. EquCo1 and IndCo2 were distinctive in that this practice was not executed. They are best categorized as outlier cases. In the case of EquCo1 the top management had decided to implement performance management and the HR manager was responsible for preparing the task. However, the other Chinese subsidiary of the same MNC had been implementing this practice for a long time. The HR manager of EquCo1 explained that conditions were different in EquCo1 and that it was not ready for the practice:

Performance appraisals must be linked to financial reward and benefits; otherwise they do not make much sense. Furthermore they must be linked to training opportunity and employee personal development. (EquCo1 3)

Apparently the perceived difficulty in linking performance result to bonuses and the lack of capability to provide training to employees who would need development were the obstacles to implementation of this practice. Nonetheless the subsidiary had decided to implement the performance appraisal and the appraisal template was under preparation in the HR department. The corporate group consisted of three loosely connected business lines which had been merged from different companies. The other subsidiary mentioned earlier belonged to another business division. The lack of consistency among subsidiary units in the practice might be due to different tradition in the original organizations. The business divisions had been rather independent in HR policies and business issues. At the time of the interview, the corporation was undergoing global restructuring. The business director explained the situation as follows;

Instead of having many companies in one country, only one Z (name of the MNC corporation) company will be formed. There will be one company with one country manager under whom will be human resources, IT, communications, finance, legal and support functions for all different business areas. So it means everything will be in accordance with the Z standards and practices. (EquCo1 2)

IndCo2 was similar in that the corporate group was formed by four business divisions which came from two different original MNC companies. The HR policies and practices had previously been under the HR organization of divisional HQs in different countries. The corporate HQ's HR organization was rather new. The HR manager stated the following:

We have this [performance appraisal form] from the corporation. But I can tell you we are not using it. (IndCo2 3)

According to the HR manager the subsidiary top management lacked a strong desire for performance-based management practice.

The key findings on the outcome of transfer of performance management in the seven subsidiaries that had implemented this practice are presented in Table 6.17 below.

**Table 6.17** Outcome of the transfer of HQs' performance management practice

Case	Appropriateness of the HQ's practice	Outcome of transfer
EngCo1	Misfit: the practice was not vigorous enough	Localization: A new, major element, forced ranking was added to the standardized practice.
EquCo2	Misfit: individual appraisal	Localization: Appraisal discussion with some employees was carried out in group or by telephone instead of supposed individual personal meeting.
EngCo2	Fit	Standardization: Practice implemented without modification.
MecCo	Fit	Standardization: Practice implemented with some elaboration to one evaluation criterion.
ServCo	Fit	Standardization: Practice implemented without modification.
ConCo	Misfit: English as appraisal language, forced ranking	Standardization: Practice implemented without modification despite the misfit.
IndCo3	Fit	Standardization: Practice implemented without modification.

EngCo2, MecCo, ServCo and IndCo3 regarded the HQ's appraisal form and guidelines as suitable for the subsidiary context. In EngCo2, ServCo and IndCo3 the performance appraisal followed the standard template from the HQ and applied to the groups of employees according to the requirement. The HQ appraisal system was not modified during implementation. The director of IndCo3 stated,

We have the appraisal template for management positions. It is globally standardized, not modified for China. Basically it is related to the bonus system.  
(IndCo3 1)

In fact, the evaluation items were rather generic and were therefore applicable across units world-wide. The broad framework of performance evaluation sometimes required some inputs from the subsidiary in order to make it operational in local contexts. For example, MecCo reported that one evaluation item was cooperation with customers. It had to add a specific description on how this item should be evaluated, what counted as cooperation.

The appraisal discussion was considered as a channel of communication between superior and subordinate where subordinates had a chance to tell their own expectation on job preference and career development. This part of the performance management system appeared to be positively perceived by employees. The positive attitude of Chinese employees to appraisal was reported by a number of case subsidiaries.

EquCo2, EngCo1 and ConCo reported some minor misfit between the HQ's practice and subsidiary context. In EquCo2 the individual appraisal method met some difficulty. When the appraisal practice was introduced to lower level employees a problem arose. Some supervisors had many subordinates or the superior and subordinates worked in different locations. Individual, face-to-face discussions became practically difficult. Thus, a modification was made to the appraisal procedure that the evaluation meeting was held in groups for some employees, i.e. one superior had several subordinates in the same discussion session. This made implementing the practice more feasible and acceptable. The effectiveness of the discussion might be questionable in this context and some evaluation discussions might be more of a formality. When I wanted to look at a completed evaluation form the



HR manager of EquCo2 told her colleague to bring one “with some content,” meaning not one with little content. The message was that some forms were not completely filled in or had little substance. Nonetheless, this modification was applied primarily to the lower level employees whose targets were mainly group targets and whose personal development seemed not a priority of the discussion.

The misfit perceived by EngCo1 was a different kind. The subsidiary wanted to have a more “vigorous” performance management than the one from the HQ. EngCo1 added the forced ranking element to the HQ’s practice although the HQ did not require it. This “enhanced” performance management practice was fully initiative of the Chinese subsidiary. The HR director for China reported the following:

Last year we introduced the concept of so-called ‘forced ranking’, forced distribution for the first time. You know the normal distribution curve? We have adopted this type of forced, preprogrammed distribution. Someone should be in the bottom 5. Someone should be in the top 10. So, bottom 5 means no increase in salary, nothing. It means you need to find a job outside. (EngCo1 3)

This modification of standardized HQ practice was not for the purpose of adapting to the local institutions or employee expectation. Rather it was the belief of the top management team that rigorous performance management would produce good financial results. As the interviewee of EngCo1 noted,

This [forced ranking] is China only. X (name of the MNC corporation) world-wide never enforced any [forced distribution]. We introduced it ourselves. We are ‘stupid’ to implement it. That’s why our performance is very good. ... This year our performance is the best in the history. (EngCo1 3)

A similar view was also held by the top manager in EquCo2 and ServCo. However, some HR managers stated that performance management would lose much of its meaning if the company does not have resources for training and not provide opportunities for development. Employees would become disappointed and could eventually lose motivation at work.

ConCo seemed to have the most misfits between the HQ-transferred practice and local context. One problem was the HQ’s’ requirement for normal

distribution of the evaluation results. The HQ required that there should be 10 per cent of the employees who would receive points below 40 in performance evaluation (100 were the full points). The HR manager reported:

This was extremely difficult. You must give some people points below 40 after they have worked for a year. We have been raising this issue to the global HR. I have complained about it to the HQ for two years. And all our department managers dislike it. Nevertheless, the HQ is insistent on this. (ConCo 2)

Additionally, this forced distribution was almost impossible to operate technically because in the workshops workers had both individual targets and group targets. The points would easily exceed 40 when the group target and a few personal targets were met.

The other problem in ConCo arose from using English as the appraisal language, which was required by the HQ. The difficulty was caused by lack of English language proficiency among the professionals. The interviewee commented,

Currently in China there are relatively few engineers who possess good English skills. We have difficulty in recruitment to find technically competent people with good English. It is very difficult for them [the engineers] to use English in discussion. (ConCo 2)

Although ConCo was not able to alter the appraisal language officially it translated the appraisal evaluation form into Chinese, and used it as an unofficial version.

It is evident in the data that the language use and associated problems for some employees reported by ConCo above are not an exception, but a rather common issue among the case subsidiaries. For example, some interviews revealed that language affected employees' opportunities in training and career advancement. English language proficiency was a great advantage in this respect. Many management training programmes and all training for high level managers were conducted in English. Employees who were proficient in English were given priority in participating in training programmes and in turn

had more opportunities for progression along the managerial ladder. The HR manager of EngCo1 commented as follows:

Departments should identify potential talents according to certain criteria. If they have good English skills we will send them to the global leadership programme. (EngCo1 5)

In practice, the employees who lacked English proficiency were excluded from higher management positions in the subsidiary. As one HR manager described it,

Many engineers here have good technical competence, but their English is not so good. When the promotion opportunity comes we cannot give them the position if they do not understand English, because we often need to contact the HQ and our customers who are international companies. We cannot allocate an interpreter for them. (ConCo 3)

The same HR manager even advised the children of his relatives as follows:

If you want to work in a foreign company, the shortcut to success is to have good English. Even if you are not very competent technically you will have more opportunities than others if your English is good. (ConCo 3)

To summarize, the analysis of the data in this chapter revealed that firstly, the propensity of transfer from the HQs to the case subsidiaries varied across the HRM practices. The transfer of practices in compensation, performance management and training and development was more common than the transfer of practices in recruitment and selection. No transfer was found in benefits and employee representation practices. Secondly, compensation and performance management practices encountered the most conflicting pressures between the HQs' standardized policies and the Chinese local context. Furthermore, different HRM practices were found to be susceptible to different kinds of host country pressures and to varying demand for standardization within MNC organizations.

Thirdly, the most important findings in terms of the research question, four configurations were identified to lead to the localization of compensation

practice. The configurations explain why localization occurs under combinations of four conditions- labour market mobility, location, HQs monitoring, and strategic role of subsidiary, in their presence or absence. These multiple conjunctions indicate alternative pathways to achieve localization of HRM practice in foreign subsidiaries. The high labour mobility in China was one main driving force for the localization of compensation practice (and for adaptation of a wider range of other HRM practices). An unattractive location tended to generate a greater need for localizing the compensation practice than an attractive location. Subsidiaries that played a strategic role possessed certain power capability, which in turn were likely to succeed in modifying HQ's practice; however, strategic role alone was not deterministic to localization.

Fourthly, the conditions of labour market mobility and location showed no relevance to the localization of performance management practice. Finally, a few other factors such as expatriate, especially the changing values of Chinese employees were found relevant to adapting the HQ-transferred practices to the Chinese environment.

## 7. Discussion

The research question of this study is “How can localization of HRM practices be explained by a configuration of institutional factors and power relationships between subsidiary and headquarters?” The theoretical interest is the combinatorial effect of institutions and power relationships between HQ and subsidiary of MNC on the outcome of cross-national transfer of HRM practices. The study sought to identify what combinations of institutional and organizational factors contribute to the outcome of localization of a given HR practice. With crisp set QCA, an explanatory model was built to investigate the compensation and performance management practices across a number of case companies. Four causal paths of localization were identified in compensation practice. The causal mechanisms were investigated through further analysis within individual cases. A number of other findings related to localization were revealed from the data, e.g. variations of propensity of transfer across the HR practices and complementarity of locally designed practices to localized practices.

In the following, I first summarize the key theoretical assumptions of this study. Then, I discuss the findings in light of the guiding theories and relevant literature. The discussion covers such issues as configurational explanations of the localization of compensation practice, host country effect, country-of-origin effect, localization of HRM practices in China and localization as a process.

### 7.1. Configurational Explanations of the Localization

This study views localization of HRM practices as an outcome of cross-border transfer of HQ practices from the home country of the MNC to the host country of the subsidiary. Following Ferner and Tempel (2006; also Ferner et al., 2005), cross-border transfer of HRM practices is seen as a movement of practices across national institutional domains. The MNC subsidiary operates under

condition of institutional duality and faces both the institutional terrain of the multinational company and that of the host country where it operates (Kostova, 1999; Kostova and Roth, 2002). The differences in national business systems between countries imply that the practices that generate in one national business system may not be suited to another national business system. The different institutional environments under which the subsidiary operates are likely to exert rival pressures on transferring HR practices from the parent country to the host operations. This, in turn, creates tension between implementing the HQs' global policies and meeting the divergent demand of the host environment. In this regard, localization of HRM practices is conceptualized as the subsidiary modifying the HQ-transferred practices to fit the local context.

However, institutions are not deterministic in that the power capability of MNC actors such as HQ and subsidiary is likely to influence the HR practice transfer within the MNC (see, e.g., Edwards and Kuruvilla, 2005; Ferner et al., 2012). This power perspective argues that MNC actors influence the process of practice transfer by drawing on institutional resources they possess. This process in turn impacts the dissemination and adoption of the transferred practice. Subsequently, the transferred practices are likely to be modified during the course of implementation. This study set out to investigate how the working of institutions with the power relationship between the HQ and the subsidiary leads to the outcome of localization of HRM practices.

According to the theoretical assumptions of institutionalism and power relations within MNCs, I identified six causal conditions: labour law, labour unions, labour market mobility and location, HQs monitoring and strategic role of subsidiary. The first four conditions are institutional factors of the host country. The last two conditions are factors of power capability of MNC actors: HQ monitoring is a factor of the power capability of HQ and strategic role of the subsidiary is a factor of the power capability of subsidiary. With these conditions I built an explanatory model to examine the outcome of transfer of two practices: compensation and performance management.

For compensation practice the results show that out of the total ten cases examined five have localization and five have standardization. The findings on the conditions show that there was no impact from labour law and labour unions. Thus, the model was modified to consist of four conditions: labour

market mobility, location, HQs monitoring and strategic role of subsidiary. Four different combinations of conditions are identified to lead to the localization of compensation practice. In all these four paths no single factor is found to result in the localization. Instead, localization occurs under the influence of multiple factors. Firstly, the configurations show it is the combination of the four conditions, labour market mobility, location, HQs monitoring and strategic role of subsidiary, in their presence or absence that produces the outcome of localization. This confirms the conjunctural causation of causal complexity. Secondly, the four different configurations demonstrate that there are alternative pathways to the localization. Different configurations of conditions can lead to the same outcome of localization, depending on the constellation of the presence and absence of the conditions. This confirms the multiple causality of causal complexity in social phenomena.

In terms of the theoretical interest of this study, firstly, the findings of the study show that the effect of host institutions on practice transfer is likely to be played out by the power relationships between HQ and subsidiary (see Ferner et al., 2005; Ferner et al., 2012). Subsidiaries may be able to deploy host institutions as resources to circumvent HQs' institutionalization of HR practice in situation of conflicting interest with their HQs. For example, IndCo1, EngCo1, EngCo2 and MecCo were able to utilize the demand of local institutions – the pressure of high labour mobility and/ or an unattractive location as a power resource and modified HQ's transferred salary and/bonus practice. These subsidiaries were operating in a key market and/ or being an R & D unit within the MNC which were the crucial resources for the success of the MNC. This indicates that a subsidiary that plays a strategic role within the MNC is likely to possess some power capability. The contrasting case is IndCo2. Although the company faced pressure from its unattractive location, the lack of a strategic role in the MNC combined with HQ's strong monitoring of transfer resulted in standardization, i.e., the transferred practice was implemented without major modification. This finding confirms the study of Festing et al. (2007) who show that subsidiaries that possess critical resources such as big market size and R & D function were able to gain exceptions from HQ's rule. It also affirms the argument that subsidiaries may achieve power over resources (Ferner et al., 2012; Festing et al., 2007). However, the findings also indicate that strategic role does not necessarily ensure that subsidiary's

power capability materializes. Strategic role alone is not decisive in localization. Also, whether a subsidiary adopts a localized practice or a standardized practice can be affected by the overall strategic orientation of the MNC. The case of ConCo can be understood as a cost-driven strategy of the MNC organization. This may be related to the low value-added business of the sector where cost competitiveness is of great importance. Therefore, the compensation policy of the MNC organization can be regarded as largely driven by the HQ's cost-efficiency strategy. This left little room for ConCo to negotiate.

Secondly, the findings confirm the study by Ferner et al. (2005) that transfer is likely to involve a negotiation process where the subsidiary and the HQ negotiate the "terms" of transfer. The study shows that negotiation is found to be one of the mechanisms that lead to the localization of compensation practice. The cases IndCo1, EngCo2 and MecCo are examples of this. These subsidiaries were able to mobilize the host institutions as resource to bargain with the HQs and reach a balance in HR practice transfer between the interest of the subsidiary and the MNC organization. This finding supports the argument of Ferner et al. (2012) on the interplay between power and institutions on the outcome of transfer. The localization of these case subsidiaries may be seen as similar to the scenario where the subsidiary possesses power over resources to negotiate with the HQ on the transferred practice and make the practice more acceptable in the local context (Ferner et al., 2012). In this respect, negotiation on the basis of power capability due to the strategic status is regarded as the causal mechanism that links the conditions to the outcome of localization. The finding further shows that the negotiations with HQs were often carried out by the top management of the subsidiary, rather than the HR manager of the subsidiary.

Thirdly, the findings show that there are other mechanisms than negotiation that may link the conditions to the localization. The case of EngCo1 indicates a common interest between the subsidiary and the HQ in the China operation. EngCo1 was operating in a key market and undertaking some global functions such as R & D. These were an integral part of the corporate strategy. EngCo1's initiatives to modify the transferred compensation practice were supported by the HQ. The findings also indicate that although strategic role of subsidiary proves to be an important condition for localization it is not



always required for localization. As the case EquCo2 shows localization can also occur in the absence of a strategic role combined with weak HQ control over transfer. The mechanism linking the conditions to the outcome is subsidiary autonomy. HQ adopted a decentralized policy that enabled the subsidiary to adjust the HQ practice. In this case the transfer did not seem to involve a negotiation between the subsidiary and the HQ.

For the localization of performance management practice no direct impact was found from the four causal conditions of host country context. The localization was neither driven by the constraint of labour regulations and trade unions, nor by labour market mobility and sub-national institutions. The data revealed that subsidiary top management belief in and employee attitudes to performance management seem to be highly relevant to the ways the case companies reacted to the transfer of this practice. These findings indicate that it requires some other conditions to explain the localization of performance management practice.

In terms of sector of subsidiaries this study could not draw a clear linkage between the types of sector and patterns of localizations/ standardization. The data reveal some distinction between the subsidiaries in service (ServCo) and telecommunication sector (ConCo) and the subsidiaries in more traditional industry. ServCo and ConCo seem to stand out from the other subsidiaries in terms of extensive coverage of HQ's practices and strong monitoring by HQ. The standardization of both compensation and performance management practices in these two subsidiaries can be regarded as relating largely to HQ's centralized and performance oriented policies. The high centralization and performance driven HR policies might be more common in the service sector and electronics/ telecommunication sector than in the more traditional manufacturing sectors.

## **7.2. Host Country Effect**

### **7.2.1. Legal Framework**

This study shows a lack of coercive isomorphism (DiMaggio and Powell, 1983) from the Chinese institutions. Literature suggests that host country legislation

and labour unions are likely to be strong coercive pressures faced by subsidiaries of foreign MNCs (e.g., Brewster, 1995; Brewster, Sparrow and Vernon, 2007; Budhwar and Sparrow, 2002; Doz et al., 1981; Gooderham et al., 1999; Rosenzweig and Singh, 1991; Rosenzweig and Nohria, 1994). The findings of present study show that the two conditions derived from legal framework of employment – national labour law and labour unions – had no direct impact on the localization of compensation and performance management practices. No competing pressure was found from either the Chinese labour regulations or labour unions for the HQs-transferred practices. The reason is that the Chinese labour regulations stipulate the minimum requirements of pay related issues such as minimum wage, overtime pay and on time payment of wages. The main problems in China have been such issues as firms paying wages below minimum standards and failing to pay wages and overtime compensation. Protecting the basic rights of workers has been the key issue which the Chinese labour legislation aimed to combat<sup>14</sup>. The practices examined in this study concern salary standards, pay rises and bonus schemes. The salary standard of the HQs of case companies (except the two cases IndCo2 and ConCo for operative workers) was to follow the local level. Often this local level was benchmarked with the foreign sector, meaning that the salary standard was much higher than the minimum wage, and even often higher than the local Chinese firms. The pay rise and bonus were beyond the issues stipulated by the laws. In the context of this study, localization is not the issue of complying with basic requirements of the laws.

In terms of the absence of influence of labour unions, this study confirms the existing literature in general. Firstly, among the ten case companies upon which compensation is examined, four had a union or a worker representative. Among the total thirteen cases some form of employee representation (a labour union or an employee representative) was found in seven subsidiaries. This level of propensity is much in line with some other studies and reports that show the unionization rate of foreign companies in China was from 20 to 50 per cent (e.g., EIU, 2008; Hewitt, 2004, in Dessler, 2006). Secondly, the roles of unions were primarily in employee well-being, entertainment, helping employees who had family or personal difficulties. None of the unions in the

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<sup>14</sup> Only very recently, issues such as discrimination and sex harassment at work began to be regulated by law.

four case subsidiaries was found to be involved in determination of salary and bonus. This finding of no involvement of labour unions in compensation practice is not a surprise. It confirms the general picture of the union status of foreign companies in China reported by existing studies (e.g., Ding et al., 2002; Zou and Lansbury, 2009). For example, Zou and Lansbury (2009) note that Korean multinational company HMC was able to introduce a performance-based promotion scheme for production workers in its Beijing factory whereas this practice was strongly resisted by the union of the company in the home country and the seniority-based pay system had to be maintained. The finding of the present study contrasts to the work of Almond et al. (2006) on subsidiaries of US MNCs in Germany, Spain, UK and Ireland. They show that the performance-based pay transferred from the US HQs encountered opposition from trade unions in most of these countries.

The reason for the lack of influence of labour unions in China is that the industrial relations system of China is very different from that of Finland. Theoretically labour unions enjoy legal status in China. They are entitled to negotiate with employers on wages, working conditions and other issues relating to employee benefits. In general the negotiation is to be carried out at enterprise level. Yet, the labour union law of China also stipulates that labour unions are voluntary organizations. This implies that enterprises do not have to have a union in house. In addition, there is lack of employer associations in China. Although some form of three-party negotiation was reported in some local regions there is no such a tripartite system in China (Shao, Shen, Nyland and Zhu, 2009) as the one in Finland.

The present study also confirms some research on transfer of MNC HRM practices from mature market economies to other transition economies. For example, Festing and Sahakians (2010) show that subsidiaries of German MNCs encountered very limited legal constraints in Central and Eastern Europe in implementing Western compensation practices. Vo (2009) shows that the openness of the Vietnamese institutional environment facilitated transplanting the practice of fast career track of the US MNCs to subsidiaries in Vietnam. This seems to indicate that the finding of the present study on the lack of regulatory pressure has general implications for transferring HR practices of Western MNCs to transition economies. The formal institutional constraints in transition economies seem to be much less significant than those

in the highly regulated, mature market economies. A high degree of openness can be expected in transition economies. Apart from the fact that Chinese labour laws are to some extent less restrictive to employers than the labour laws in the West, the patchy enforcement of regulations in general has been a key factor behind this freer environment (see Vo, 2009 for the case of Vietnam). Further, there have been considerable variations in the government surveillance of regulations across regions and cities. Also, the Chinese system has traditionally relied on administrative governance by bureaucracies rather than by legislation. The legal system has a rather short history in China (see the discussion in Chapter 3). It is worth noting that the labour environment in China has been moving towards to a more regulated direction recently, especially since 2008 when the Labour Contract Law and a series of other new labour regulations were promulgated (see, Lu, 2009). It can be expected that in the future the institutional distance in labour and employment regulations will become shorter between China and the West.

#### **7.2.2. Labour Market System**

The present study systematically examined the localization of compensation practice of MNC subsidiaries from labour market perspective. The findings demonstrate that the generally existed high labour mobility was one main driving force for the localization of compensation practice. In the past 30 years China's labour system has transformed from a highly centralized, government-controlled labour administration to a free labour market. Both the employer and employee have the freedom to choose each other. Short-term labour contract replaced lifetime employment. This reformed labour system has much encouraged loose employment relationship between employer and employee. Meanwhile, the continued high growth of China's economy has resulted in an increasing shortage of qualified professionals, managers and skilled workers. The high scarcity of skills intensified competition in the labour market and pushed the salary level up sharply. This promoted a job-hopping mentality which in turn further facilitated labour mobility. The findings of this study show that the key issue in the localization of compensation practices was retention: to have the total pay package (salary, bonus and other incentives)

competitive in the labour market. The elements of the HQs' practice, such as using the median salary level of the region/city as the salary standard, the MNCs' standardized bonus levels and pay rise levels often fell below the competitive level in the local labour market. As the findings indicate, the localized practice was often a higher level of pay rise and/or a higher level of salary standard than those of the HQ, or special bonus arrangement that was lacking in the HQ's practice. The findings of this study on retention problem, especially retaining managerial and skilled technical employees by offering higher pay partly confirms existing studies on HRM of foreign MNCs in China (e.g., Goodall et al., 2007; Walsh and Zhu, 2007). The present study further demonstrates that the compensation practice may be used as means of retention. This supports Lam, Chen and Takeuchi (2009) who found that retention-oriented compensation practice has a positive effect on employee commitment to the firm and on reducing an employee's intention of turnover. The present study further shows that adjustment to the HQ's pay practice was not the only means to tackle the retention problem. A number of case subsidiaries included the 13th salary and benefits which were outside the HQ-transferred practice in the compensation package. Some subsidiaries opted for other means of retention than pay policy such as training, career development and a fair work environment.

The high labour market mobility in China points to the particular characteristics of the Chinese labour market system. According to Whitley (1999) and Hall and Soskice (2001), in 'short-termist' business systems or liberal market economies there tends to be a high inter-firm mobility of employees. This is primarily due to the lack of long term investment in training by firms. They rely heavily on the external market to acquire skills, resulting in a weak tie between employer and employee. However, in China the high labour mobility is largely due to a shortage of skills and the resultant war for talent. The present study indicates that most case companies provided substantial training to employees and this did not necessarily warrant low employee turnover. As some of the interviewees commented, once some employees had been trained and become competent and experienced, their market value increased and the chance for them to leave also became higher. They often became the targets for poaching by other companies, both international and domestic Chinese. Vo's (2009) study of two MNCs (one US and one Japanese)

in Vietnam shows that although the Japanese MNC emphasized building employee skills with extensive training it had higher employee turnover than the US MNC. One key reason was the slow promotion of Vietnam employees to managerial positions in the Japanese company. The high labour mobility in China is also due to the urbanization process that has been accelerating over the past two decades. Massive numbers of people have migrated from rural areas to cities for jobs. These migrant workers are highly mobile for economic and social reasons. They were labeled the “flowing population” in China. The characteristics of the Chinese social system (see Chapter 5) and the income-based motive for work resulted in their weak commitment to the workplace<sup>15</sup>. The discussion above suggests that the labour market characteristics of China are not only a question of coherence between dominant business systems such as state, financial system and labour market institutions, as typically suggested by comparative institutionalism (e.g., Hall and Soskice 2001; Whitley, 1999). The Chinese labour market reflects the complex configuration of the legal system, development stage, urbanization, social security system and economic growth. This complex, turbulent labour market presents a very different context from the labour market of Western countries where the market economy is mature and socio-economic development is much advanced.

### **7.2.3. Sub-national Institutions**

This study explicitly examined the impact of sub-national institutions on cross-national transfer of HRM practices, which has been largely neglected by extant research. The transfer of compensation practice was found to be affected by sub-national institutions. No effect of sub-national institutions was found on the transfer of performance management practice.

This study identifies two levels of sub-national institutions and their effect on the localization of compensation practice. The transfer of the HQs’ compensation practice, use of local market salary level as a salary standard, was challenged by both regional and intra-regional differences. First, the minimum wage level and the market salary level were higher in Shanghai

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<sup>15</sup> However, there is an attitudinal shift in the new generation of migrant workers. They adapt more quickly to urban ways than their parent generations and have less intention to return to rural life (see, *businessweek*, 30 July 2013; Miller, 2012)

(Yangtze River Delta) area than in Beijing-Tianjin region. This attracted people moving from the region of lower wage to the region of higher wage. This was especially true for the rural migrant workers who are very sensitive to wage levels in their job selection. This is evidenced by the problem of retaining operative workers in MecCo and ConCo where the local salary level was applied. Second, there were (there are still) intra-regional differences between Shanghai and the surrounding smaller cities in wage level, socio-economic development and living standard. This resulted in Shanghai being more attractive than the smaller cities around it in terms of employment. Smaller cities especially lacked attraction to managers and highly skilled employees. This is evidenced by the cases of EngCo1 and IndCo2.

As described in Chapter 4, economic reform in the past 30 years has significantly increased the economic and legislative power of the sub-national governments at the provincial and municipal level. Local governments (provincial and municipal) have substantial power to design economic policies and have responsibility for local regulations. The minimum wage standards and social welfare standards are regulated at the provincial and municipal level. The minimum wage affects the general level of labour market price of the respective province or city. The economic policy of various regions and cities influences the living standards and level of social welfare locally. The locational characteristics discussed above directly affect the variation of workforce availability in different local labour markets. A majority of the case companies had multiple units in various locations in China. The same HQ practice was not necessarily suitable for all locations in China. Further, due to the variations of regulations in social benefit standards across provinces and cities, different units could have very different benefits practice although they were all operating in China.

Since the case companies were all located in the greater Beijing area and the greater Shanghai area further analysis is warranted of the sub-national embeddedness of international HRM in the dominant national business system of China. Both Beijing and Shanghai are located on the east coast, the most developed region of China. They are the two largest cities<sup>16</sup> in China. The variations are very small in terms of the level of social and economic

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<sup>16</sup> Shanghai and Beijing are municipalities directly under the central government of China. This means that they have the same status as a province in terms of authority power.

development. However, the overall business environment in Shanghai can be regarded to be more dynamic than in Beijing. Shanghai Pudong is the largest special economic zone in China although not the first one. It has been the experimental site for a number of market-oriented policies on economic and social reform. For example, the Shanghai Free Trade Zone launched in September 2013 made it the largest free trade zone in China (BBC, 29 September 2013; Xinhuanet, 20130930). Within the zone regulations in eighteen sectors, ranging from finance to shipping were liberalized. Shanghai is the most important financial centre in mainland China. It is highly popular as a destination of FDI due to these locational advantages. The fact that Shanghai hosted two thirds of Finnish FDI in China while Beijing and Guangzhou together hosted only one third shows the locational advantages of Shanghai over Beijing. The variations in the business systems between Shanghai and Beijing are partly due to historical reasons as well. Shanghai has been an industrial and commercial centre while Beijing has been a political centre. Shanghai has been much more and earlier exposed to foreign business due to its big harbour and colonial status after the Opium War while Beijing has been much more protected from foreign influence.

In fact, the locational advantage is even more obvious for Shanghai compared with smaller, less developed cities. The differences between Shanghai and its surrounding smaller cities demonstrate the variations in the capacity for skills development and control systems in sub-national context (see Almond, 2011). Shanghai has an obvious advantage in the production and reproduction of human resources. This is evidenced by several case subsidiaries cooperating with local universities in study programmes and recruiting graduates directly from higher educational institutions. MNCs themselves contribute to skill development through cooperation with local educational institutions. MNCs themselves create a pool of human resources in the local labour market. One piece of evidence is that the HR managers of several case subsidiaries who were interviewed had worked for US or Japanese MNCs before. The other example is that an important source of engineers and technical specialists for EngCo1 was a few large US MNCs that were operating in the same region.



### **7.3. Country-of-Origin Effect**

#### **7.3.1. Generally Low Propensity of Transfer and Tendency of Decentralization**

This study identified some effects of country of origin. One is the general tendency of moderate pay (salary standard, pay rise and level of bonus). This was found in most HQs' pay policy across the cases. Downplaying extrinsic rewards was also evident generally in the HQs' compensation practice, e.g., it was not common to have particular high pay for key personnel. The conservative style of Finnish MNCs contrasts with the bold practices of US MNCs that tend to have large wage gaps between top and bottom levels of the workforce and high pay for high performers (see, e.g., Farley, Hoenig and Yang, 2004; Walsh and Zhu, 2007). These features of Finnish MNCs can be regarded as reflecting the Finnish management culture that is rooted in the dominant social norm of equalitarian philosophy. There has been strong policy and social pressure to minimize income gaps in Finland. Yet, the study shows that it is in compensation issues where the most misfits existed between HQs' practice and the Chinese context. The elements of HQ pay practice were not quite suited to China's tight labour market with high labour mobility and fierce competition. They also somewhat conflicted with the values of Chinese employees who expected a high reward for their work. Finnish managers found it challenging to cope with Chinese employees' expectation for extrinsic reward as recognition of their achievement and performance. The small pay rise found in a number of Finnish HQs policy might also originate from the routine of operation in the home country. In Finland the annual salary rise has been two to three per cent. Also, the labour market price of Finland has been much more stable compared with China. In China wage levels have been rising much faster partly due to rising income and partly due to the tight labour market. Nonetheless, many case subsidiaries tried to accommodate to the Chinese environment through e.g. modifying HQ practice and/or designing locally adapted practices.

The second country of origin effect is the tendency to decentralize HRM. This study shows that in general relatively few HR practices were transferred, especially in mandatory form. No transfer was found in practices on benefits

and employee representation among any of the cases. Transfer of some elements of recruitment and selection practice was observed in a minority of the cases. Compensation and performance management practices exhibit the highest propensity of transfer across the cases, followed by training and development. Even in the four HR practices where transfer was involved, often only some elements of a given practice were transferred, not the entire practice. The subsidiaries had considerable freedom to design local practices or elements of the practices outside the HQ-transferred practices. This was evident even in the compensation practice that had relative strict control by most HQs. For example, the 13<sup>th</sup> month salary used by all the ten subsidiaries except ServCo was a local practice; the salary and bonus for operative workers in all the cases (except IndCo2 and ConCo) were under the subsidiaries' full control. The bonus practice for other lower levels of employee was also fully designed by a number of case subsidiaries.

The third effect is the moderate or weak control by the HQs. This is evidenced firstly by the low number of mandated practices. Only for the compensation practice did the HQs of most case companies have a mandatory requirement for the salary standard, pay rise and bonus scheme. In about half the case companies, performance management was not mandated by the HQs. For training and recruitment there were few mandatory requirements from the HQs. Further, the levels of the subsidiary organization effectively covered by HQ practices were generally managerial employees except in ServCo and ConCo, though some variations were observed across the cases. Secondly, the HQ's enforcement of the transfer was generally moderate or weak. Except for compensation practice where over half of the case subsidiaries experienced strong HQ monitoring, the subsidiaries perceived rather moderate or no overt monitoring from HQ of practices. For example, the implementation of performance management was largely left to the subsidiary management (except ConCo). This seemed to contribute to the variety of outcomes: some subsidiaries implemented the practice without modification (EngCo2, ServCo, ConCo, IndCo3); some subsidiaries implemented it with some modification (EngCo1, EquCo2, MecCo); and some did not implement it at all (EquCo1 and IndCo2). EngCo1 even added forced ranking into the practice, which was not recommended by the HQ. As the general manager of EngCo1 stated, "*There is a standardized policy but no standardized implementation*". This statement

captured the general situation across the cases though the comment was about EngCol's own MNC organization. The findings on performance management practice seem to indicate that implementation was largely due to subsidiaries' own initiative rather than forced by the HQs.

The findings of this study contrast to some studies of US MNCs. For example, Almond and Ferner (2006) show that in broad terms US MNCs have a consistent pattern of global standardized and formalized policies in a number of HR areas such as management career, workforce diversity, collective representation, compensation and performance management. Almond et al. (2006) further demonstrate that pay and performance management tended to be highly centralized among most case-study firms of their sample of US MNCs. In particular, performance management systems were highly centralized and had a high degree of cross-national uniformity. Further, explicit or implicit forced ranking was relative common. Almond et al. (2006) posit that these characteristics reflect the dynamics of country of origin arising from the entrenched concept of a free market for labour centred on the notion of 'employment at will' and the emphasis on individual pay for performance in the USA. The pursuit of relatively strong global standardized policies by US MNCs may indicate the USA's dominant economic power and big domestic market. According to Smith and Meiksins (1995), dominant economies are powerful to exercise influence on the 'best models' of production and technology and best practices of management across the world. They are likely to create dominance effects. These characteristics of US MNCs contrast with the tendency to decentralization and the lack of a consistent pattern of HQ control among the Finnish MNCs. The relative decentralized HR policies and high autonomy of subsidiaries of Finnish MNCs can be regarded as being embedded in the highly coordinated business systems in the home country. The resolution of varying interests tends to be handled through coordination and negotiation among various interest groups. Further, Finland is a small economy with a small domestic market. Finnish MNCs are not likely to have a dominance effect.

### **7.3.2. Dynamics of the National Business System and Internationalization of HRM**

This study indicates that in some respect Finnish MNCs are moving towards Anglo-American models of human resource management. The findings show that the number of HQ global policies has increased over years and the application of HQ practices has gradually enlarged. Apart from operative workers and in some subsidiaries also other lower level employees, a range of employees were subject to some elements of the HQ practice in compensation, performance management, and training and development. This indicates the tendency towards centralization of HR policies in large Finnish MNCs. The widespread transfer of compensation and performance management practices and increasing use of performance-based pay found in this study show that the internationalization of HRM of Finnish MNCs follows, to some extent, the Anglo-American models (see e.g., Almond et al. 2006). This is in line with the literature on growing emphasis on performance and financial results among large European MNCs (e.g., Ferner, 2000; Ferner and Quintanilla, 1998). The finding on the tendency towards HQ control of the salary budget is also consistent with the tight control of labour costs through formal budget setting and review process, the typical feature of US and UK MNCs (e.g., Almond and Ferner, 2006; Edwards et al., 1996; Marginson et al., 1993).

Indeed, the traditional industrial relations and the concept of equality in Finland have been much challenged by the ongoing globalization of the business environment (see, Morgan, Whitley and Moen, 2005) where economic result is much emphasized in business organizations. Finland is typically regarded as the Nordic model of industrial relations and HRM (Lilja, 1998; Linderberg, Manson and Vanhala, 2004). Yet in recent years the traditionally high membership rate of trade unions has been steadily decreasing. The national level collective bargaining has switched to industrial level and is further moving towards company-level corporatism (Lilja, 1998). Talent management is exercised as a common practice among large Finnish MNCs (see, Mäkelä, Björkman and Ehrnrooth, 2010). These changes suggest a sign of Anglo-Americanization of the economic system and industrial relations (see Tainio and Lilja, 2003).

One main reason suggested by Tainio, Huolman and Pulkkinen (2001) is the strong impact of foreign ownership in Finnish companies. Since mid-1990s

major Finnish companies have been integrated into the global financial market (Tainio et al., 2001). Foreign institutional investors have brought an Anglo-American shareholder oriented business value and a whole new owner-driven management culture into Finnish companies (Moen and Lilja, 2001). One clear change is in managerial incentive practice. There has been increasing use of outcome-based compensation with typical forms of stock options and equity holding as means of bonding management to shareholders' interest (Tainio et al., 2001). Company executives have increasingly enjoyed huge bonuses and salaries. As a result, the gap in pay between company senior managers and the rest of the employees has become bigger. Option schemes have become more common, firstly for top management, then for key personnel and even all employees (Tainio et al., 2001). Large scale national surveys show that performance related pay is more common in Finland than in the UK where the unions and collective bargaining are apparently weaker than in Finland (Vernon, 2005). Even academic remuneration in Finland has moved from a tenured civil servant system towards individualistic, performance-related compensation (see Peltonen and Vaara, 2012, p73). Laurila (1999) even claims that foreign investors have brought about changes not only in Finnish management culture, but also in the whole Finnish business system.

The move towards an Anglo-American business culture is evident also in some other CMEs with highly regulated industrial relations such as Germany (Deeg, 2005; Edwards, T., Gunnigle, Quintanilla and Wächter, 2006; Lane, 2005). Deeg (2005: 39) suggests that the German financial and corporate governance systems have moved on to a new path that incorporates substantial elements of a liberal market model. For example, the traditional commercial banking based on long term relations with large firms has changed to investment banking where the relationships between the bank and the firm is more contractual (deal-based) (Deeg, 2005). Shareholder value has become increasingly prevalent in Germany. According to Lane (2005), the influence of the stock market has been considerable on managerial attitudes, strategies and structure of large German firms. The strong presence of American MNCs in Germany has gradually changed the landscape of traditional industrial relations. Many US MNCs have chosen HR and industrial relations practices that depart from the German norms, for example, opting out of the sector-level collective bargaining and the vocational training system (Edwards et al., 2006; Muller,

1998). The American innovative HR practices have been cited as ‘best practices’ and increasingly spread in Germany (Edwards et al., 2006). One example is the increasing use of pay for performance. According to the Cranet surveys Germany is among the top rankings of 16 European countries in use of pay for performance (Brewster et al., 2007). The findings of the present research on Finnish MNCs are similar to some studies on German MNCs (e.g., Ferner and Quintanilla, 1998; Ferner et al., 2001; Lane, 2005). For example, Ferner et al. (2001) show that a majority of German MNCs in their case study introduced some sort of international policy of linking reward to performance.

Despite the converging tendency of Finnish MNCs to international HRM practices represented by Anglo-American models, some national traits of Finnish MNCs remain. As this study shows, even though some HR practices look similar e.g., performance-based pay and performance appraisal, how these are transferred by the Finnish MNC HQs and carried out at their foreign subsidiaries bear a distinctive Finnish character. As the early discussion shows, the Finnish ways are integrated into the dominant HRM practices. This produces a sort of international HRM practices with Finnish characteristics (see Ferner et al., 2001 on German MNCs).

#### **7.4. Evolving National Business Systems in China and Localization of HRM Practices**

The previous section discussed the dynamics of country-of-origin effect on international HRM of Finnish MNCs. The case of China in this study illustrates how the Chinese national business systems have evolved and how the changes affected the localization of HRM practices over time.

This study shows that the Chinese business system has been undergoing fundamental changes for over three decades. In the early stage of China’s transition (1978 - early 1990s), the pace of reform was slow. There was strong institutional continuity in the economic system marked by the high level of central planning and in the labour market system marked by state control of labour supply and restriction of labour movement. These institutional arrangements posed considerable challenges to foreign companies in hiring, firing and setting wages and pay. The “Hukou” (residence registration system) prohibited free movement of the workforce geographically and the personnel

file system prevented inter-organizational flow of employees (Tsang, 1994; Zhu and Dowling 2000). The deep rooted “iron bowl” (lifetime employment) as both system and legacy made dismissal of excessive workforce difficult, and the “iron wage” (equalitarian remuneration) tradition was an obstacle for foreign companies to introduce performance-based reward systems (Child, 1994; Laaksonen, 1988). The strong institutional and organizational continuity in HRM practices existed not only in Chinese state-owned enterprises, but also in Chinese-foreign joint ventures (Goodall and Warner, 1997). The central issue of localization was conformance to this restricted environment.

In the later reform period (from the mid-1990s up to 2010 of this study) the Chinese institutional environment has become much more liberalized. The business systems have become very open, much more deregulated than those of mature market economies. This is evidenced by the findings that the regulatory institutions had no direct effect on HQ-transferred compensation and performance management practices and had a rather limited constraining effect on the six HR practices in general (except the benefits practice). This openness of business systems in China enabled the case subsidiaries to conduct their desired HR practices, e.g. performance appraisal and performance-based pay. These findings are similar to Vo’s (2009) study that shows US MNCs were successful in introducing fast career track practice in Vietnam though it was contradictory with the traditional norms. As Almond et al. (2005) suggest, applying innovative HR practices is easier in less actively regulated business and employment systems than in highly regulated systems. The subsidiaries of Finnish MNCs were operating in a freer environment in China than in Finland. This allowed them to apply a wider range of HRM practices than in the home country.

This, however, did not mean that the need for localization has reduced. As the findings revealed, there was a strong need to modify the HQs’ compensation practice. The Chinese labour market was characterized by an increasingly severe shortage of skills and a high inter-organizational flow of employees. The competition for skilled professionals and experienced managers has resulted in speedy increases of salary, thus further encouraging frequent shifting between jobs. The key issue in localizing the HQs’ compensation practice was accessing and retaining talents and skills in such a dynamic environment. The need for local adaptation, making practices suited

to local conditions, existed in almost every HR practice such as recruitment, selection, benefits, training and development.

One salient change brought about by the transformation of business systems in China and by globalization is the changing values of Chinese workforce. This study indicates that Chinese employees are moving away from to some extent the traditional collectivism and equalitarian philosophy. There is a tendency towards greater appreciation of extrinsic rewards and personal achievement. This finding supports some existing studies (e.g., Fang, Zhao and Worm, 2008; Faure and Fang, 2008; Leung, 2008) that show a similar tendency towards these emerging values in today's Chinese society that contradict the old ones. In this respect work values of Chinese employees can be regarded as an important driving force for local adaptation. However, the impact of the changing values on the HRM of foreign MNCs in China has received relatively less attention in existing research. Many studies have focused on the impact of the structural and formal institutional changes.

Another significant change is the increasing heterogeneity of the Chinese workforce. The study shows that urban workers, rural migrant workers, professionals, managers, women employees and male employees, and employees of different generations exhibited diverse motives and attitudes to work, careers and financial rewards. For example, generation is a particularly prominent issue in China. The fact that people who were born in the 1970s, 1980s and 1990s are labeled post-70 generation, post-80 generation and post-90 generation reflects the distinction between generations by every decade since the commencement of economic reform in the late 1970s. The findings demonstrate that younger generations have high expectations not only for economic reward, but also for fast careers. Studies on other transition economies such as Russia (Karhunen, 2007), Estonia (Heliste, Karhunen and Kosonen, 2007) and Vietnam (Vo, 2009) show similar findings. The findings of the present study also reveal that Chinese younger generations are more open to express their personal desire and more willing to exhibit individual personality. This is similar to the finding of Kommonen (2011) who studied Chinese colour values and showed how the young Chinese, unlike their parents, express themselves with colours, showing their personality and difference from others. The experienced younger professionals and competent managers, especially those with foreign language proficiency and foreign experience, are



highly desirable to foreign MNCs. These people have the capability to mobilize their competence and exert influence on HRM practices; for example, the retention bonus and special pay practice for key personnel as found by this study.

The findings of this study on the changing values and diversification of the Chinese workforce point to the limitations of national culture approach (e.g., Hofstede, 1980). This approach has faced increasing challenge and scrutiny recently (e.g., Fang, 2010; Leung, Bhagat, Buchan, Erez and Gibson, 2005; McSweeney, 2002; Söderberg and Holden, 2002). This approach views culture as homogeneous values and traits within a nation. Based on this approach Chinese culture has been uniformly described as exhibiting collectivism, large power distance and high hierarchy. It also tends to overlook sub-cultures in terms of different groups such as different age groups and professional groups as shown by this study. Furthermore it is static, viewing values as constant characteristics of national mindsets (Ferner et al., 2005) and fails to capture the dynamic nature of culture. The findings of this study on the changing values and diverse values of Chinese employees show that the assumption of national culture is inadequate for explaining the Chinese context and limits research on managerial practices (see e.g., Sackmann and Phillips, 2004). As discussed above, the traditional norm of collectivism is being challenged by individualist values and the traditional homogeneous Chinese culture is moving towards diverging values represented by various social groups. These changes are significant in the Chinese context because not long ago China was a totally closed country and the cultural values were overwhelmingly uniformed. Not only economic transition, but globalization, foreign direct investment and telecommunications technologies (the Internet as the most salient) all bring about an ever fast changing environment for Chinese people.

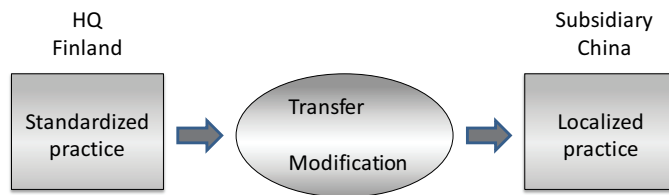
While China has been undergoing rapid transformation of economic and social systems path dependency is evident. The influence of the central planning regime on HR practices is apparent. This study observed that enterprises are expected to play a bigger social role in China than in Finland. For example, the social security system in China is usually covers only minimum standards. Enterprises are supposed to contribute to employee welfare more than the minimum standards. The study shows that many case

companies exceeded the minimum standards and even extended some benefits to employee family members, e.g. medical insurance. The housing fund is a typical transition phenomenon where enterprises have the responsibility to subsidize employees in purchasing apartments after the system of free allocation of housing was completely abolished in late 1990s and early 2000s. These benefits practices can be regarded as path dependence on the pre-reform central planning system where state-owned enterprises functioned as mini welfare states. Although the significance of traditional values is decreasing some deeply rooted values persist. For example, the study revealed that equalitarian thinking was still common among lower level employees. The variable pay (bonus) for workers in most case companies was in fact a part of normal wage. The bonus was paid as long as the job duty was performed and work disciplines were followed. The level of bonus was quite unified as well among the workers. Chinese employees still regard the workplace as important in personal life. They see the workplace as part of their social life, not only a place to work. This is evidenced by the findings of extensive social activities organized by a number of case companies such as birthday parties, outings, holiday trips, entertainments and sports. The finding on the importance of enterprises' role in socialization can be seen as the legacy of Danwai (work unit) that acted as a social institution to which member staff were closely bound for their work life and personal life (see Knight and Song, 2005). The roles of social responsibility and socialization of enterprise discussed above are important in increasing employee commitment and reducing voluntary turnover in China.

## **7.5. Localization as a Process**

The present study regards the central issue of localization of HRM practice as MNC subsidiary response to host country institutional demands under multiple institutional pressures. In the course of practice transfer from HQs the subsidiaries are seen as facing opposing institutional pressures from host country institutions on the one hand, and from MNC corporate influence (Kostova and Zaheer 1999; Prahalad and Doz, 1987; Rosenzweig and Singh, 1991; Westney, 1993) and the parent country-of-origin effect on the other hand

(Ferner, 1997; Ferner and Quintanilla, 1998). In the situation of misfit of HRM practices of MNC HQ to the Chinese context, subsidiaries modify their HRM practices to suit the local conditions. Based on this logic, localization is defined as a subsidiary's modification of HQ-transferred HRM practices to respond to the local institutional environment. Subsequently localization was examined by contrasting the HRM practices implemented by the subsidiary with the originally transferred standardized practices of MNC HQs. Thus, localization involves modification of HQ practice. This is an important difference from the existing research, where localization is equated with being similar to local firm practices and investigated by comparing subsidiary practices with those of local companies/host country (e.g., Björkman and Lu, 2001; Gunnigle et al., 2002; Lu and Björkman, 1997; Myloni et al., 2004; Rosenzweig and Nohria, 1994). By examining subsidiary modification to HQs' transferred standardized practices the present study is able to unveil the process of localization. Figure 7.1 below illustrates the process of localizing MNC HQ practice.



**Figure 7.1** Localization process

As Figure 7.1 shows, localization is the process that involves transfer of standardized HR practice from HQ and modification of the practice by the subsidiary. For example, among the eight case subsidiaries where HQs' compensation practice was not quite suited to the local Chinese conditions, five subsidiaries modified the unsuitable elements of the practice by setting a higher pay level and/or higher salary rise, or initiating additional incentive schemes. This resulted in a localized practice and led to the outcome of localization. The other three subsidiaries instead implemented the transferred practice without modification or with minor modification. They primarily pursued the HQ's standardized practice, leading to the outcome of standardization.

The re-conceptualization of localization enabled this study to go beyond the simplistic measure of resemblance to parent/local practices with perceptual data (see the call by Björkman et al., 2008). The present study provides a fine-graded understanding of subsidiary HRM practice- what is localized, what is not localized and what is locally designed. This study demonstrates that resemblance to the parent practice, which is regarded by the conventional literature as standardization, does not necessarily indicate that the subsidiary adopts the standardized practice of MNC organization. For example, although some recruiting methods such as Internet Portal and headhunter and the selection method of interview used by the case subsidiaries were the same as in their parent company, the HQs of most case companies did not transfer these practices to their subsidiaries in China. Although the subsidiaries had similar ways of recruiting and selecting employees as their parent company it was not the result of adopting HQs' standardized practices. These practices may be regarded as imitations of prevailing international HRM practices. Furthermore, the study shows that though these practices looked the same between the subsidiaries and their parent companies the purpose of using them was quite different. For example, as the finding revealed, in China through the Internet the subsidiaries were able to collect the maximum number of job applicants. The Internet was used in recruiting as a strategy to tackle the difficulty of finding suitable candidates, the severe competition in the labour market and the rather low rate of qualified candidates among applicants. In Finland, using the Internet in recruiting was mainly for reasons of efficiency and cost saving, whereas qualified employees were relatively easy to obtain in the labour market. The Internet as a recruiting channel was much more important in China than in Finland. These differences in the purpose and importance of using the same practice reflect the different institutional context between China and Finland.

In the same vein, resemblance to the local HRM practice, which is perceived as localization in the prevalent literature, may not be the result of localizing the HQs' practice. This study revealed a number of subsidiary-initiated practices; for example, the direct intake of recruits of graduates from local universities and colleges, the monthly/ quarterly bonus for lower level employees, the thirteenth-month salary, and the higher standard/ extended benefits to employees in a number of case subsidiaries. These practices were

defined by the subsidiaries locally, geared to take into account the Chinese institutional, social-economic and cultural context. These HR areas were outside the scope of the HQs' standardized practices. The decentralization of these HR issues to subsidiaries can be seen as a sort of Finnish way of doing things influenced by the parent country of the MNCs, Finland.

By investigating what is transferred from the HQs and how the HQs' practices fit the local context, this study is able to uncover the competing pressures between isomorphism emanated from the HQs and local demands from the host institutions in the transfer process. It shows that there are considerable variations in institutional and organizational influences across HRM practices. The compensation practice exhibits most obvious conflicting pressures between HQ policy and the local context across the case subsidiaries. The practices in performance management and recruitment and selection showed less conflicting pressures. Training and development revealed little/ no conflicting pressure. This indicates that different HRM practices are likely to be subject to a different extent of institutional and HQ pressures.

By examining localization through subsidiary modification of the HQ-transferred practices this study provides nuanced findings on localization and standardization. It showed that in the cases of localization subsidiaries often modify some part of the HQs' practice while maintaining part of the practice unchanged. Further, there are also often locally designed elements in the same practice. In the cases of standardization there are also locally designed elements in a given practice. This demonstrates that standardization and localization are not an either/or issue. A given HR practice of subsidiary can be inclusive of both localized and standardized elements, and often locally designed elements as well, as typically in the case of compensation practice and performance management practice. Furthermore, subsidiaries are not homogeneous. For the same practice some subsidiaries adopted HQ's standardized one and some adopted a localized one as shown by the study in the compensation and performance management.



## 8. Conclusions

This chapter first presents the contributions of the study. Then, it highlights the managerial implications for business communities- Finnish and non-Finnish companies. The chapter ends with discussion on the limitations of the study and suggestions for future research.

### 8.1. Contributions

#### 8.1.1. Institutional Analysis of Practice Transfer within the MNC

This study contributes to the literature on institutional analysis of international transfer of HRM practice. It demonstrates that the outcome of the transfer is affected by a configuration of institutions and the power relationships between HQ and subsidiary. More specifically, the outcome of transfer is shown to result from a combination of labour mobility, location, monitoring by HQ and strategic role of the subsidiary. None of these factors alone plays a decisive role. Moreover, different constellations of these conditions may lead to the outcome of localization/ standardization. This indicates the possible alternative paths to the same outcome. The four causal conditions- labour mobility, location, monitoring by HQ and strategic role of the subsidiary- are derived from the theories and literature and empirically verified with the data of this study. Hence, the causal paths to localization identified by this study are considered generalizable to the transfer from other coordinated market economies to China or to other transition economies.

The findings of different types of outcome of transfer, localization and standardization highlight the interplay between institutional forces and power relationships of HQ and subsidiary on practice transfer. From the subsidiary point of view, those that play a strategic role within the MNC are likely to

possess some power capability in relation to the HQ (see Ferner et al., 2012; Festing et al., 2007). The subsidiaries may mobilize the host institutions as a resource to negotiate with the HQs on the 'terms' of transfer (see Ferner et al., 2005). The outcome is likely to be a modified practice from that of the HQ and the modified practice becomes more suited to the local context. Subsidiaries that lack power capability are likely to follow the HQ's mandate for the transfer. In this regard, the institutional effect is played out by the power resources which the HQ and subsidiary are able to deploy.

The study demonstrates the limited applicability of institutional theory in explaining the coercive pressure (DiMaggio and Powell, 1983) of the Chinese legal framework of employment. Labour laws and labour unions are found to exert no direct constraint on transfer of HQ compensation and performance management practices. In general, the impact of Chinese labour laws and labour unions on HRM practices are rather moderate compared with the strong coercive pressure of labour laws and labour unions suggested by the literature for the Western context (Brewster, 1995; Gooderham et al., 1999; Rosenzweig and Nohria, 1994). This may be explained by the relatively new labour legislation in China that permits a more open and free formal institutional environment than in Western countries.

On the other hand, the study shows that Chinese labour market conditions have significant influence on transfer of compensation practice and are highly relevant to the localization of this practice and local adaptation of a wider range of HRM practices (such as recruitment, selection, training and development). As evidenced by this study, the particular characteristics of Chinese labour market conditions, the scarcity of skills, fierce competition, rapid rising wages and the changing values of Chinese employees combined with high labour mobility present a very different context from that of Finland and mature market economies in general. The Chinese labour market poses considerable challenges and puts pressure on subsidiaries to localize HQ-transferred HR practices or formulate their own practices to adapt to the local context. However, labour market conditions have largely been neglected in the analysis of host country influence on subsidiary HRM practices (see, Festing and Sahakians, 2010). This may be due to the fact that much research has been conducted in the context of the stable nature of the market in mature, developed economies. Neglect of labour market conditions meant that an



important source of influence on local adaptation of HRM practices in China would be missed.

Sub-national institutions have received increasing attention in international HRM study (e.g., Almond, 2011; Edwards and Kuruvilla, 2005; Ferner and Tempel, 2006). Yet, empirical research remains scarce. The study shows that transfer of compensation practice is challenged by the variations in minimum wage and labour market price across the regions and cities of China. The sub-national variations in availability and development of skills, social welfare standards and quality of life create locational advantages/disadvantages across the provinces and cities. This has a wider implication for local adaptation of a number of HR practices such as recruitment, compensation, benefits and training and development. The business systems in China and other transition countries should be understood in the heterogeneous sub-national context of economic growth, social system, development stage and urbanization process within the dominant national system. Accordingly, MNCs are likely to face more prominent sub-national influences on their HRM practices in China than in their home countries.

#### **8.1.2. International Human Resource Management Study**

The study complements existing literature on localization. The present study conceptualizes localization of HRM practices as adjusting HQs-transferred practices to fit the local context. It measures localization by examining subsidiary's modification to the HQs-transferred practice. These go beyond the conventional conception of localization as resembling the practice of local companies/host country and measuring localization by comparing subsidiary practices with those of local companies/host country. The revised conception of localization enables the present study to produce new insights into localization. This study demonstrates that localization (and standardization) is a process affected by multiple institutional and organizational factors. The interplay of host and home country factors and power relations within the MNC shape the ways how subsidiaries localize HQ-transferred practices.

As most of the research so far has tended to be vague in conceptualizing and analysing institutions, the present study de-composes institutions into

specific elements such as labour law, trade unions, labour market mobility and sub-national institutions (location) showing how each impacted or did not impact on a particular HR practice. Existing studies focus on the average impact of institutional or organizational factors across subsidiaries while this study shows that the same institutional or organizational factors have varying effects across subsidiaries and a similar external environment does not necessarily result in resemblance in organizational behaviour and management practice. Furthermore, the existing studies emphasize the average degree of localization or standardization across subsidiaries. This study, however, uncovers the variations between subsidiaries in pursuing either localization or standardization.

In addition, the study provides fine-grained results on individual HR practices. Different HR areas (the six under examination in this study) are shown to be susceptible to different kinds of host-country pressures. For example, recruitment, selection and compensation are exposed to pressures of labour market mobility, sub-national institutions and employee values; benefits practice is primarily susceptible to national and local regulations. HQs impose isomorphism at varying extent across HR practices as well. In general, there is stronger pressure for implementing HQs' standardized compensation practice than performance management practice. Training and development has the least pressure from the HQs. Consequently, the pressure for localization varies across the practices; for example, there is greater pressure for compensation than performance management. This pressure also varies across different levels of the subsidiary's organization and groups of employees; for example, there is a greater pressure for adapting practices at lower levels of the organization and for highly desirable employees than there is at higher levels of the organization and for some other groups of employees. This study further shows that within the same practice there can be both standardized element(s) that are suited to the local context, not modified from HQ practice and localized element(s) that are not quite suited to the local context and subsequently modified from HQ practice. This indicates that localization and standardization can be inclusive in the same HR practice. In addition, subsidiaries may have their locally designed elements outside the scope of HQs' unified policy.

The present study contributes to our knowledge of Finnish MNCs in terms of HR practice transfer and control mechanisms. This study shows that

human resource management of Finnish MNCs exhibit some distinctive Finnish features. In general, relatively few HR practices were transferred to China, especially in mandatory form. Finnish MNCs also exhibit the tendency to decentralize HRM policies. Subsidiaries have much authority to design and decide HR practices for a majority of the six HR practices investigated in this study. The control over transfer seems to be rather moderate, with the exception of compensation practice. These characteristics of Finnish MNCs can be regarded as being embedded in their national context. However, the tendency of Anglo-Americanization is evident in the frequency of transferring compensation and performance management practices among the large Finnish MNCs. Compensation policy is increasingly under budget control and directed to enhancing performance. The enforcement of HQs' salary and bonus practice is also stronger than other practices. These findings indicate the tendency to convergence of Finnish large MNCs to dominant international HRM practices, importantly in the area of compensation and to some extent, performance management. The study demonstrates that the nationally determined behaviour of Finnish MNCs is not static but evolving (see, Ferner and Quintanilla, 1998; Ferner et al., 2001). Also, the Finnish way of doing things is integrated into international HRM and mediates the pressures of host-country institutions and globalization. This gives rise to the dynamics of the country-of-origin effect.

### **8.1.3. The China Study**

This study offers fresh insights into the localization of the HRM practices of foreign MNCs in China. The current Chinese institutional environment is very different from that of the early reform period (1978 – early 1990s). China has shifted from a centrally planned to a market-based economy after reforms of over three decades (the World Bank, 2012). This means that market-based mechanisms have largely replaced central planning and bureaucratic control of economic activities. The findings of this research show that the early constraints encountered by foreign enterprises from local authority interventions in human resources practices (Child, 1994; Goodall and Warner, 1997; Tsang, 1994; Zhu and Dowling 2000) have become history.

The liberalized employment environment during the later reform period (mid-1990s to 2010) enabled foreign subsidiaries to pursue Western HR practices. On the other hand, an increasing shortage of skills as well as accessing and retaining talent have become the main HR issues facing MNCs in China. The findings of this study demonstrate that the central issues of localization are predominantly concerned with how to recruit, retain and develop Chinese employees so that foreign subsidiaries could maintain sustainable growth. The empirical evidence of this study shows substantial differences in institutions, cultures, labour market conditions and social system between China and Finland. These account for the need for the subsidiaries to adopt localized practices. Meanwhile, operating in a more open and freer institutional environment also provided opportunities for Finnish MNCs to introduce HQ practices such as salary grading, performance appraisal for career development and performance-based pay, as well as design innovative practices adapted to the local environment. In this respect, MNCs contribute to the development of human resources and management practices in the host country.

#### **8.1.4. Methodology in International Business Research**

The application of Qualitative Comparative Analysis in this study is innovative in IB research. One methodological distinction of this study, compared with statistical method in general, is the emphasis on the combinatorial effect of causes. The use of QCA has enabled this study to explain the localization or standardization of HQs' HR practice in configurations of the causal conditions, rather than in individual factors. The other distinction is the ability to keep causal complexity. Alternative paths to localization have been explored and permitted, rather than just looking for one best model. The findings on multiple paths to the localization and combinatorial explanations for the various paths can be considered having wider implication for the use of a configurational approach such as QCA in business, organization and management study (see Fiss, 2007; 2009).

This study may be seen as an example of how QCA may be applied in international HRM research and in IB and IM research in general. The rapid

growth of QCA applications in management studies in recent years indicates the high potential of this method in business studies (Rihoux et al., 2013). Yet, so far, the majority of QCA applications have been conducted in social and political sciences. In existing QCA applications, units of analysis tend to be at macro and meso levels such as state and social group, and causal conditions and outcomes are generally calibrated with numerical data. This study shows how QCA analysis may be conducted at sub-organizational level (HR practices and subsidiaries of MNCs). The present research also shows how conditions and outcome may be calibrated with qualitative data of interviews and documents. As this study demonstrates, combining QCA with qualitative case study, a popular research strategy in IB, allows an extensive iteration between theory and rich empirical data throughout the research project (Rihoux and Ragin, 2009; Schneider and Wagemann, 2012). This gives much leverage for theorizing from case studies and producing nuanced findings.

## **8.2. Managerial Implications**

This study will potentially benefit the internationalization of Finnish companies and non-Finnish companies as well. The importance of China as a foreign investment location for Finnish companies has increased steadily over the past two decades. China has become an important destination for Finnish foreign investment and is Finland's fastest growing market (Formin, 2010). The latest information shows that Finnish companies employ totally over 70,000 people in China (BOFIT, 3.5.2013). This makes China the second most important country for Finnish foreign operations in terms of number of employees (BOFIT, 3.5.2013). As one of fastest growing economies in the world, China provides extremely promising opportunities for Finland and Finnish businesses. The latest survey reveals that 72 per cent of Finnish companies operating in China plan to increase investment in the future (FBCS, 2012). The strategic importance of China for European companies has been increasing (EUCCC, 2012). China has been undergoing a fundamental economic transition and continuous changes in all spheres of society. This presents a very different institutional and cultural environment from Finland and other developed European countries. This implies the importance of

understanding human resources management for the Finnish companies that already operate in China and those that intend to expand to China. This research systematically examined compensation and performance management practices and more generally other four HR practices (recruitment and selection, benefits, training and development and employee representation). The subsidiaries under investigation were Finnish-owned units in China in manufacturing sectors (twelve companies) and service sector (one company).

The results of this study are expected to assist Finnish companies in better understanding the differences between China and Finland and the consequent impact on people management in the Chinese context. The results are also considered useful for other European companies with business interests in China. For example, the fast changing environment in legislation, the developing phase of socio-economic conditions, as well as the diverse, changing norms and values of Chinese employees in China influence a wide range of HR issues: how local employees are recruited and selected, how important are compensation and benefits and what role the two practices play in retention and performance, the nature of training needs, and how training and development may affect the commitment of local employees to companies. For example, the Chinese labour market is characterized by keen competition for competent managers and specialists, a severe skills shortage, high inter-organization flow of workforce, and high salary expectations. In combination, these mean that recruitment, retention and rewards are of high priority for HR management, which is different from Finland. In this respect, the results of this study are supported by the survey involving over 500 European companies in China (EUCCC, 2012) and the survey on Finnish companies in China (FBCS, 2012).

The Chinese workforce is much more diverse in education background, professional attitudes and work-related values than the workforces in Finland and other mature market economies. Managing human resources in China requires attention to the various needs and expectations of different employee groups. For example, the influence of the generation phenomenon at the workplace is particularly strong in China because of the fundamental changes brought about by the economic reform in the past thirty years. The labels post-70 generation, post-80 generation and post-90 generation are indicative of the fast pace of generational change in China. The post-80 generation and post-90

generation represent young people who seek individualist achievement. They are highly motivated to learn and take new challenges at work, at the same time expecting fast career tracks and high rewards as well as valuing a good working environment.

Recently, the Chinese employment system has been moving towards a more regulated environment after the liberalization of the labour market in the 1990s and 2000s. The Labour Contract Law enacted in 2008 and a series of complementary laws and regulations have assured issues of employee relations a more prominent position on enterprise agendas. Finnish and other foreign companies operating in China should follow this trend.

The results of the study on the Finnish MNCs provide knowledge of the suitability of MNC parent practices to the Chinese context, which may be useful for the decision makers in HQs. This study shows that compensation, i.e. salary standard, pay rise and bonus schemes, has been the biggest stumbling block in terms of HQs' practice in the Chinese context. They are more prescriptive in nature. When standardized practices are highly prescriptive they tend to be problematic for local adaptation. On the other hand, when HQ policies are in the form of a general framework and broad guidelines, they tend to have higher adaptability. In this situation, subsidiaries have more room to decide on the substance of the practices and adapt them to the local context. When subsidiaries are involved in developing the practices, the parent policy is more likely to be suited to the local context. Furthermore, the pace of changes in the institutional and cultural environment is much faster in China than in Finland. With HQs located in Finland it is crucial to understand the dynamics of business system in China when making policies at corporation level. In all, the study provides a better appreciation for differences in people management and for developing "best practices" that fit the Chinese environment.

The foregoing managerial implications may extend to foreign MNCs that operate in other transition economies such as the Central and Eastern European countries, the independent states of the former Soviet Union as well as East Asian countries. These countries have undergone similar changes from a socialist central planned system to a market economy and share a similar context with China in economic growth, labour market conditions, industrial relations, sub-national variations and fast changing values of workforce.

### 8.3. Limitations and Future Research

The causal paths identified in compensation practice are considered to be valid for a particular type of HR practice, compensation practice, and in a specific context of transfer from a coordinated market economy to a transition economy. As shown by this study, different HR areas tend to be susceptible to different kinds of host country pressures. For example, the conditions of labour market mobility and location proved to be irrelevant to localization of performance management practice. Also, different HR areas tend to be subject to a different extent by HQs' pressures for global standardization. Additionally, the conditions of labour market mobility and location are derived from the institutional differences between China and Finland. This limits the context of host country to a transition economy and home country to a coordinated market economy. These limitations open the possibility for further research investigating combinations of conditions for localization/ standardization of other HR practices. For example, business strategy, beliefs of subsidiary top management and attitudes of employees seem to be relevant for performance management practice. An investigation of localization of this practice can be conducted with a combination of the above-mentioned factors. The education system can be highly relevant for training practice in addition to labour market mobility and location. In addition, an investigation could be conducted on a practice where HQs impose little mandate and HQ practice is a kind of general framework, such as the training and development practice in this study. In this circumstance implementation of HQs' practice requires a substantial input of the subsidiary. The localization is likely to take the form of the integration of the HQ practice rather than modification of it.

The condition HQ monitoring is derived from the power source of formal authority of the HQ. This implies the HQ's power capability is limited to that of formal bureaucracy. HQs possess other sources of power as well, e.g. controlling tangible and intangible resources and simulating corporate culture and values. HQs may use other means to influence the transfer process, such as communication and networking. The strategic role of the subsidiary is measured by the key market and R & D function of the subsidiary and therefore power capability of subsidiary is limited to this scope. Obviously subsidiaries may possess other competence or resources, for example market



competitiveness, management skills, product and technology (e.g., Birkinshaw, 2000; Festing et al., 2007). A future study may examine the power capabilities of HQ and subsidiary enacted by other sources as mentioned above. Further, some other factors such as business strategy, presence of expatriates and employee values were found relevant for localization but were not included into the conditions due to the limited number of conditions required by the QCA method. Future research may include these factors into the analysis of localization.

Some methodological limitations need to be addressed. First, the use of dichotomies has some cost in terms of simplifying the data. Crisp-set QCA does not capture the fine-grained categorization of conditions and outcome. For example, the standardization cases are not totally uniform. Some minor modification(s) of HQ's practice existed in a few cases. Categorising the cases into the two groups of localization and standardization might give the impression that the outcome of transfer is either localization or standardization. While acknowledging a loss of information by dichotomization I should note that any generalization from empirical inquiry involves some degree of simplification, be it quantitative or qualitative (King et al., 1994: 42). Simplification enables the researcher to extract parsimonious patterns from complex cases. As Rihoux et al. (2013) argue, dichotomy provides the simplest operationalization of relevant difference and therefore gives strong analytic leverage in terms of parsimony. The emphasis of this study is on different types of outcome rather than degree of the outcome. In this respect, the use of dichotomy is suited to the purpose of the research. In addition, the localization or standardization of a particular practice in this study concerns only some element(s) of the practice and/or some groups of employees. The entire practice such as compensation and performance management exercised by the case subsidiaries often consisted of both transferred elements and locally designed elements. This is already a hybrid form, not an either-or.

Second, the study suffers from a lack of interviews with the HQ representatives. The data on HQ-transferred practices and the control over the transfer were collected from only the subsidiaries. This means the findings on the practice transfer and the localization of the compensation and performance management practices are based on the subsidiaries' views only. The same is true for the findings of monitoring by HQ. What was transferred and what was

localized are judged by the subsidiaries' own reports. The subsidiaries might interpret HQs' mandatory versus non-mandatory requirement in favour of their own interest. The subsidiaries might use the power of meaning (Ferner et al., 2012) to prevent or facilitate the transfer process. The power capability of the subsidiary could have been more fully explored had interviews been conducted with representatives of the HQs. Additionally, interviews with the HQs would provide first hand information on the HQs' views of mandatory/ optional nature of transferred practices and how transfer was monitored. This would then produce a more rigorous measure for the condition of HQs monitoring and the outcome of localization.

A final remark on the possible future research is in place. This study has shown that the shortage of skills, high competition for talent and work-related values contributed to the high labour mobility in China. But how language affects employee voluntary turnover has received little attention in existing research. This study shows some cases where technically competent employees were excluded from global training programmes and promotion opportunities due to their inadequate proficiency in English. This confirms the recent research on language and career in MNCs. For example, studies show that the common corporate language creates a glass ceiling and makes vertical career progression difficult for those who do not possess the necessary language competence (Neeley, 2012; Peltokorpi and Vaara, 2012; Piekkari, Vaara, Tienari and Sääntti, 2005). Piekkari and Tietze (2012; also Swift, 2011) argue that language used at the workplace shapes and steers perceived opportunities for career mobility and advancement. This can be regarded highly relevant for MNCs operating in China given the particularly high employee turnover. Thus, the possible effect of a common language on career mobility can be a potential future research area of international HRM in China.

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# Appendixes

## Appendix 1 Summary of the total interviews

Case company	Place of interview	Time of interview	Interviewee	Number of interviews
IndCo1	Shanghai	19 Sept. 2008	General manager	2
		2 March 2010		
		19 Sept. 2008	HR deputy manager	1
		2 March 2010	HR manager	1
EquCo1	Shanghai	24 Sept. 2008	Deputy general manager	1
		18 Sept. 2008	Functional director	1
		18 Sept. 2008	HR manager	1
IndCo2	Jiangsu	22 Sept. 2008	Asia-pacific president	1
		18 May 2007	HR/Admin. manager	1
		18 Sept. 2008	HR manager for China	1
EngCo1	Jiangsu	25 Sept. 2008	General manager	1
		22 Nov. 2007	Finance director	1
		23 Sept. 2008	R & D director	1
		26 Sept. 2008	HR director Asia-pacific	1
		25 Sept. 2008	HR manager	1
		23 Sept. 2008	Project Director	1
EquCo2	Shanghai	22 Sept. 2008	East Asia president	1
		25 May 2007	General manager	1
		22 Sept. 2008	HR manager	1
	Finland	20 June 2006	Sales manager	1
EngCo2	Shanghai	22 May 2007	China vice president	1
		3 Jan. 2007	General manager	1
		16 Sept. 2008	HR manager for China	1
MecCo	Beijing	7 Jan. 2009	General manager	1
		12 Jan. 2009	HR manager	2
		8 March 2010		
ServCo	Helsinki Beijing	4 Feb. 2009	China President	2
		13 Feb. 2009	HR manager for China	
ConCo	Beijing	26 July 2006	Asia-pacific president	1
		13 Sept. 2006	General manager	1
		21 Jan. 2009	HR manager	2
		24 Feb. 2010		
IndCo3	Shanghai	25 Sept. 2008	Business director	1
		16 Sept. 2008	HR direct for China	2
		1 March 2010		
EquCo3	Shanghai Helsinki	6 May 2007	General manager	2
		11 Aug. 2008		
IndCo4	Shanghai	24 Sept. 2008	General manager 1	1
		3 March 2010	General manager 2	1
		24 Sept. 2008	HR manager	2
		3 March 2010		
EquCo4	Shanghai	17 Sept. 2008	General manager	2
		17 Sept. 2008	HR manager	
Total				43

## Appendix 2 Interview guide

### 1. China's institutional environment

Example questions:

- What are the state and local laws and regulations that are relevant to HR issues?
- How do these regulations impact on your HR policies and practices?
- What are the changes in HR practices after the new law was enacted?
- How do the authorities monitor and enforce the laws and regulations?
- What qualifications are required for professional jobs?
- How are the qualifications regulated and who are entitled to provide them?

### 2. HR functions and practices

Example questions:

- Can you please tell about the functions of your HR department?
- How do you recruit and select people?
- How do you deal with employee turnover?
- How do you define salaries and bonus?
- What benefits does your company provide?
- What training do you conduct?
- Can you describe the performance management policies?
- Does your company have a labor union/ worker representative?
- When and how was it established?
- What does it do?
- How employees react to the HQ's practices?
- How do you implement these policies/ practices?

### 3. HQs policies and practices

Example questions:

- Can you tell about the global policies and practices from the HQs?
- Which of them are mandatory and which are not?
- How are they implemented in your company?

Interviewee background and company information are collected with a separate form.

### Appendix 3 List of the documentary data

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## Appendix 4 Comparisons between the Labour Contract Law and the Labour Law

Items	Labour Contract Law	Labour Law
Use of written labour contract	Required (article 10).  Labour contract must be concluded within 30 days of commencement of work (article 10).	Required.  Not required.
Consequences for employment without a written labour contract	Employer pays twice of the salary (article14); employment relationship is deemed as permanent if the employment has lasted for one year without a contract (article14).	No rule.
Conditions for applying open term labour contract	After two fixed term contracts with the same employer; or for employees who have worked for 10 years at the same employer (article14).	For employees who have worked for 10 years.
Severance pay for not renewing the labour contract	Yes (article 46).  One month salary for one year employment; half month salary for half year (article 47).	No rule.  No rule.
Probation period	Maximum 6 months (article19).  No probation if the contract is less than three months; 2 months for the contract of 1 – 3 years; 6 months for the contract over 3 years (article19).	Maximum 6 months. Not specified.
Employee participation in making company rules	An employer has to discuss with the labour union or with all employees or employee representative(s) when making or revising company rules or significant matters concerning employee direct interests, such as remuneration, working hours, rest and vacation, work safety and hygiene, social insurance and welfare, training, work disciplines, and workload, etc.  An employer should publicize the decisions on company rules or inform the workers (article 4).	No rule.

Role of labour union	<p>Employer has to inform in advance the labour union of the reason for dismissal of an employee (article 43).</p> <p>The union has the right to request the employer to correct the dismissal decision if the union deems it inconsistent with the law, regulation or the terms of the labour contract (article 43).</p>	<p>Not required.</p> <p>The union has the right to interfere the inappropriate dismissals.</p>
Regulations on agency workers	Obligations of temporary worker agency and hirers (article 57-67).	No rule.
Consequence for non-compliance	Economic compensation and penalties, with specific amount. E.g. an employer will have to pay twice the amount of the wage if it fails to sign an open term contract with the employee (article 82); under conditions of failing to pay overtime work, severance compensation, or paying wages under minimum requirement, the employer is obliged to pay 50 to 100% additional compensation to the employee (article 85).	Economic compensation and penalties, but there is no rule on how much.
Role of governments (Surveillance and inspection)	<p>Surveillance and inspection of the local governments are stipulated specifically.</p> <p>A list of inspected items is provided (article 74).</p> <p>Roles of government authorities in surveillance are much more emphasized.</p>	<p>Roughly stipulated that local labour authorities shall supervise and inspect employers in abiding by the laws and regulations.</p> <p>Role of authorities are weakly presented.</p>

Based on the Labour Contract Law (enacted on 1 January 2008) and Labour Law (enacted on 1 January 1995) of People's Republic of China

## Appendix 5 Results of the necessity test for the outcome of localization

Condition	Consistency	Coverage
hlmm	0.80	0.80
~hlmm	0.20	0.20
unallocation	0.40	0.50
~unallocation	0.60	0.50
whqmonitor	0.40	0.50
~whqmonitor	0.60	0.50
ssr	0.80	0.67
~ssr	0.20	0.25

## Appendix 6 Coverage and consistency of solution terms for localization

	Raw coverage -----	Unique coverage -----	Consistency -----
ssr*~whqmonitor*unallocation*~hlmm	0.200000	0.200000	1.000000
ssr*~whqmonitor*~unallocation*hlmm	0.400000	0.400000	1.000000
~ssr*whqmonitor*~unallocation*hlmm	0.200000	0.200000	1.000000
ssr*whqmonitor*unallocation*hlmm	0.200000	0.200000	1.000000
Solution coverage: 1.000000			
Solution consistency: 1.000000			

Note:

hlmm = high labour market mobility

unallocation = unattractive location

whqmonitor = weak HQ monitoring

ssr = subsidiary strategic role

\* = the logical AND

~ = absent state of the condition

+ = the logical OR

## Appendix 7 Results of the necessity test for the outcome of standardization

Condition	Consistency	Coverage
hlmm	0.20	0.20
~hlmm	0.80	0.80
unallocation	0.40	0.50
~unallocation	0.60	0.50
whqmonitor	0.40	0.50
~whqmonitor	0.60	0.50
ssr	0.40	0.33
~ssr	0.60	0.75

## Appendix 8 Coverage and consistency of solution terms for standardization

	Raw coverage -----	Unique coverage -----	Consistency -----
ssr*~whqmonitor*~unallocation*~hlmm	0.200000	0.200000	1.000000
~ssr*whqmonitor*~unallocation*~hlmm	0.400000	0.400000	1.000000
~ssr*~whqmonitor*unallocation*~hlmm	0.200000	0.200000	1.000000
ssr*~whqmonitor*unallocation*hlmm	0.200000	0.200000	1.000000
Solution coverage: 1.000000			
Solution consistency: 1.000000			

Note:

hlmm = high labour market mobility

unallocation = unattractive location

whqmonitor = weak HQ monitoring

ssr = subsidiary strategic role

\* = the logical AND

~ = absent state of the condition

+ = the logical OR







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