STRATEGIC PERFORMANCE MEASUREMENT AND CULTURE IN THE MULTINATIONAL CORPORATIONS

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ABSTRACT

A major challenge facing many U.S. based Multinational Corporations (MNCs) is the evaluation of foreign strategic business units (subsidiaries). The way an organization evaluates and measures performance determines the motivation behind the decisions and actions of a subsidiary's manager. Failure to consider the strategic objectives of this subsidiary or the culture identity of its management is an error many MNCs commit when they export the evaluation systems of the parent company to the foreign units. When developing control systems to evaluate the performance of an international subsidiary – and rewarding its managers – companies must design performance measures that consider the impact of business unit strategies and cultural differences.

INTRODUCTION

Multinational organizations operate as global businesses with global work forces. The challenges of managing these diverse operations in diverse environments have never been greater. The considerations of cultural differences are particularly important when the management of the foreign operations is delegated to host country personnel. All too frequently, multinational corporations mistakenly evaluate their performance using some financial measures such as Return on Investments (ROI), Residual Income (RI) or Economic Value Added (EVA), regardless of the business unit strategy. This can lead to management control systems that result in suboptimal decision making, conflicting corporate and foreign subsidiaries objectives, and a negative impact on morale. Return based measures play a role in evaluating performance but used improperly, they perpetuate a short – term orientation and may be inconsistent with the cultural preferences that motivate the local manager.

Strategic Objectives

Although there are broad agreements that some form of performance measurement system is an important component of organizational control, there is no general model that provides a precise prescription of such a system. Different organizations will be pursuing different strategic objectives operating in different environments with different technologies and so will require different performance measures (Otley, 1987; Simons, 1990; and Fitzgerald et al, 1991). Common to all systems is the need to decide what performance measures to use, how to set targets for those measures and what rewards are to be associated with the achievements of performance targets. The strategy for a foreign operation is dependent on its mission and the consideration of environmental opportunities, internal strategies and the resources available to accomplish its goals and objectives [9].

Three approaches to control system design that foster goal congruence are: situation specific, universalistic, and contingency [8]. The situation – specific model views each situation as unique, so application of general rules is not possible. Universalists argue that an optimal control system design will be effective in all settings. The contingency approach, which has become the prominent paradigm, is positioned between these two extremes. It suggests that the appropriateness of the control system depends on the business setting (like the situation – specific approach), but generalization (universalistic

approach) can be made across similar settings. If the mission or the competitive strategy of the foreign unit varies across divisions within the organization, the control system must be modified to capture the relevant performance measures and motivate the foreign managers accordingly [21].

Strategic mission or business unit strategies are commonly grouped into the following areas: build, hold, harvest, and divest [12]. Competition strategies include: low cost, differentiation, focus, defender, or proprietor [18].

Strategic Mission

The mission of an international business unit is related to life cycle concepts. A build mission implies the goal of increasing market share and typically applies to any foreign operation with low market share in a high-growth industry. In order to build a competitive advantage it may be necessary for the manager to sacrifice short-term earnings and/or cash flow. Also, a build strategy implies an increase in production, which results in additional use of firm's resources. Performance measures that focus mainly on profit and return would be in conflict with the overall mission of the foreign unit. The manager therefore should be evaluated and rewarded primarily on achieving a targeted increase in sales or market share, with profitability measures (with a great deal of slack) a secondary objective.

The hold strategy applies to a unit with a high market share in a high-growth industry. Though profit oriented accounting performance would be appropriate, non-financial measures also should be incorporated, such as customer service, maintaining market share and quality measures.

The goal of a harvest unit is to maximize short-term cash flow and earnings at the expense of market share (high market share, low-growth industry). These earnings can then supplement other business units that may be in build strategies. To align management decision making with the harvest strategy, the control system should evaluate performance using one of the conventional return measures, such as ROI, RI or EVA. Measures of cash flows also may be appropriate. Profit and return have a much tighter acceptable range and should be adhered to strictly.

In a low-market-share, low-growth industry, the unit's strategy may be to divest through a process of slow withdrawal or outright sale. The appropriate control system at this stage is unique to the particular situation.

Competitive Strategies

A foreign unit with a low-cost competitive strategy attempts to achieve lower costs relative to competition. Typical low-cost actions include taking advantage of economies of scale; learning curve effects; reducing customer service, research and development, advertising, and/or sales force; and maintaining a stable product line. Strict adherence to cost standards through variance analysis and other measures of operating efficiency, such as cycle time and inventory turnover, would be appropriate measures to evaluate and control performance in this competitive environment. Further, Thompson and Strickland, suggest that significant cost advantages can emerge from an analysis of an entity's internal and external value chain [20]. Low-cost participants must be careful, however, because the market place will still demand a minimum level of product quality and functionality.

A differentiation strategy focuses the unit manager's attention on brand loyalty, customer service, product design and technology. The goal is to create a product that customers view as unique and exclusive. Product innovation is critical. To create uniqueness, the unit is likely to have a more diversified set of products or functionally superior products compared to a low-cost competitor and it

must invest in research and product development, technology; marketing and customer service. Achieving a target ROI does not measure process effectively within this strategy while traditional financial measures still play a role, non-financial performance measures such as quality, on-time deliveries, customer satisfaction and number of new products to market, must be emphasized.

A unit with a focus strategy targets a narrow competitive market within an industry segment. The specific objectives could be either low cost or differentiation. Design of the control system must be tailored to the selected objective.

A unit with a defender strategy engages in limited product/market research, have limited product lines, and have a stable environment. Defenders compete through cost and quality control. This strategy is consistent with the features of the hold and harvest missions. ROI, RI and EVA may be effective control measures if they are incorporated with variance analysis, operating efficiency measures and quality variables.

Prospector units, similar to differentiators, compete by focusing on market development, new product development, and searching (prospecting) for market opportunities. These units are often in a build strategic mission. Profit-oriented measures would not capture progress toward goals and objectives. The number of new products to market, customer satisfaction, quality, sales from products developed in the last year and market share would evaluate and control the manager more appropriately.

Culture

Most of the multinational companies use local management talent to operate a foreign subsidiary rather then relying on “imported” expatriates [16]. U.S. MNCs frequently export the home country control system to the host country unit but fail to consider the import of cultural differences. Effectiveness of the management control system depends on whether the local manager of the unit perceives the control system as aligned with the shared values maintained in the host-country [11]. Hofstede defined culture as “the collective programming of the mind that distinguishes the members of one category of people from those of another [13]. In perhaps the most extensive and most frequently cited research conducted with respect to cultural differences, Hofstede identified five underlying cultural dimensions – power distance, uncertainty avoidance, individualism versus collectivism, masculinity versus feminity, and confusion dynamism – and assign scores on them to more than 50 countries [14].

The potential exists for conflict in preference across cultural factors within the same country. In a high uncertainty- avoidance culture, the manager’s preference would be for a high-control with a fixed performance rewards. If the country also scores high on individualism, however, a tight budget control would conflict with the manager’s preference for independence and performance-based rewards. When factors conflict within a single culture, the control system should target congruence with the dominant cultural dimension as well as align with business strategy.

CONCLUSION

Managerial performance evaluation employing multidimensional financial and non-financial measures has been advocated for decades [7]. However, there are divergences between generally accepted theory and current MNCs practices regarding international and domestic managerial evaluation. Among others, Choi and Czechowicz [5] and Barkowoski [2] suggest that home and host country managers should be evaluated using different criteria due to economic, political and cultural differences in their operating environments.

The differing importance of performance evaluation criteria among countries has implications for MNCs with both native-born and foreign-born managers in a subsidiary. If a Canadian based MNC has both Canadian and Japanese managers in a subsidiary, each group will have different expectations about their performance evaluations given their country's prevailing culture. Each group of managers may also make decisions based on their culture imprint. However, if the MNC can align its measurements metrics with the corporate strategy and in the same time managers align their values with that of their organizations we will insure MNC goal congruence and maintain managerial morale and discourage dysfunctional behavior while addressing the cultural differences among the managers.

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[21] The Contingency model proposes that, in addition to mission and competition strategy, other contingent factors include the external environment, technology firm diversification and size, and the ability to observe effort and output. In this paper, the authors' concern is in the impact of strategy and culture.