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EFFECTIVE SOLUTION?  
AN EXPLORATORY STUDY IN A  
SAMPLE OF SPANISH MNCs**

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Jaime Bonache Pérez\* y José Pla Barber\*\*

Abstract

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A common claim in the literature of expatriation is the one referring to the high costs of expatriation. In this paper, on the basis of transaction cost literature, we show how limited this approach is. In particular, we consider a set of costs that, although ignored in traditional expatriation literature, must be accounted for when an MNC is deciding on whether to recruit expatriates or local managers in its subsidiaries. These costs include selection, training and performance evaluation costs. We also formulate a series of hypotheses around the situations in which the total costs of recruiting expatriates are lower than those generated by local managers. We then test these hypotheses in a sample of 124 Spanish MNCs. The results of the study allow us to explain the apparent contradiction that, although businesses have a need to reduce costs, they continue to employ apparently costly practices such as expatriation.

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**Key words:** Expatriation, transaction cost theory, international human resource management

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## INTRODUCTION

One of the key decisions that multinational companies must make is whether to select local or expatriate personnel to manage their foreign subsidiaries. In the face of this choice, the predominant trend in MNCs seems to be ethnocentric (Maryhofer and Brewster, 1996). This effectively is the case in Japanese companies, in which, according to a survey by Koop (1994), 75% of their subsidiaries' directors are expatriates. But it is also the case in European and U.S. MNCs, in which expatriates occupy 54% and 51% of senior management posts, respectively.

Although the ethnocentric orientation is predominant in MNCs, there are certain obvious problems associated with it. It is noted, for example, that it creates problems of adaptability to foreign environments and cultures, leads to high failure rates, has a discouraging effect on local management morale and motivation, increases the "foreignness" of the subsidiary, and may involve high transfer and salary costs. As regards the latter problem, international assignments seem to be an "expensive" option for an enterprise. It is estimated that for more than 75% of companies, the costs of expatriates amount to more than 3 times that of local employees (The Conference Board Europe, 1996).

If we focus only on costs, we must ask ourselves the following question: If local personnel are a much cheaper recruitment option, then why is it that, in a business context defined by the need to cut costs, multinational companies continue to make such intensive use of international assignments?

This paper analyzes this question from the perspective of the transaction cost theory. After explaining why this theoretical perspective is particularly suited to examining this question, we analyze the overall costs, above and beyond the purely salary-related costs to which traditional expatriate literature limits its attention, that are implicit in management personnel recruiting in subsidiaries, and we formulate a series of hypotheses around the situations in which the total costs of recruiting expatriates are lower than those generated by local managers. We then test these hypotheses in a sample of 124 Spanish MNCs. The results of the empirical study lead us to conclude

that in MNCs that have a limited international base, are not very innovative and have adopted a global strategy, the expatriate solution can prove to be a more cost-effective staffing option.

## **TRANSACTION COSTS AND STAFFING DECISIONS IN MNCs**

The question we pose in this paper is why, in a business context where the pressures to cut costs are steadily increasing, do MNCs continue to use the apparently costly solution of sending expatriates to their international operations? In other words, why do they rely on the organization and not the local job market to recruit management personnel for the subsidiary?

Thus posed, the question is similar to the one raised by Coase (1937), which laid the foundations for the theory of transaction costs (TCT): if markets are so efficient in making transactions, why do organizations exist? The similarity between the two questions is not purely accidental. As Williamson states (1990), the TCT can be applied to any situation in which an exchange takes place.

In the case that interests us here, this exchange is the one defined by an employment relation in a multinational subsidiary. In this relationship, the employee contributes human capital and behavior (Wright et al., 1994) in exchange for a series of rewards. By human capital, we refer to the knowledge, experience, skills and abilities inherent in the employee. We also include behavior because, as Wright et al (1994) assert, employee human capital does not provide value to the firm unless it is utilized through employee behavior. The question is whether the employee is from Headquarters or, conversely, whether he/she is recruited from the local market.

This employment relation is characterized by two factors that make it a complex type of exchange. On one hand, unlike virtually instantaneous transactions (e.g., when the subsidiary acquires furniture for its offices), the employment relation is long term. Secondly the relation is uncertain, as many contingencies may arise throughout its duration.

From the organization's perspective, the potential problem it faces is that this exchange may not be efficient, i.e. if the people selected do not have the required human capital or do not display the appropriate behavior. For those who must make the recruiting decision, this problem is a possibility due to the convergence of two factors. They are rationally bounded; they have limited information on individuals and cannot anticipate everything that might happen throughout the relationship. In addition, employees have the potential for acting opportunistically. This is the term, which according to Moran and Ghoshal (1996) constitutes the vision of this theory with regard to human nature. Williamson uses it to refer to types of behavior such as lying, stealing, cheating and calculated efforts to mislead, distort, disagree, obfuscate or otherwise confuse (Williamson, 1985). In our context, it means that prospective employees may try to hide information that reveals they do not have the knowledge, experience and skills required for the job and/or behave incongruously with the organization's objectives. According to Williamson and Ouchi (1981), not all individuals are opportunistic, but some are. The problem is that it is practically impossible to separate a priori those who are from those who are not.

Increasing the effectiveness of this employment relation will result in transactions costs for the organization (Jones and Wright, 1992). These refer to the costs incurred to ensure that the employee meets the requirements for the job and, once recruited, to provide incentives and ensure that he/she behaves as desired. Since we are analyzing the employment relation, we will call these transaction costs "employment costs". Therefore, employment costs are the negotiation and monitoring costs required to ensure that the employment relation is forthcoming.

On the basis of Jones and Wright (1992), we can associate these employment costs with specific human resource policies. This will give us four basic types of costs:

1. Selection and recruitment costs. These are all costs incurred by the organization on negotiating with the subsidiary's prospective managers and overcoming adverse selection. This issue concerns the tendency of prospective employees to overemphasize the level of knowledge, experience and skills they possess in order to maximize their returns from the firm (Jensen and Meckling, 1976).

2. Training and socialization costs. These are the costs associated with developing the skills and competencies of the subsidiary's managers, and with learning the organization's rules, values, policies and procedures.
3. Compensation costs. These are costs targeted at attracting, retaining and motivating the subsidiary's managers.
4. Costs of monitoring and evaluating the subsidiary's managers. These are the costs the organization would incur on verifying that behavior is not opportunistic. These would include costs of visits of HQ managers to the subsidiary, managerial time spent on supervision, and costs of implementing appraisal and feedback systems.

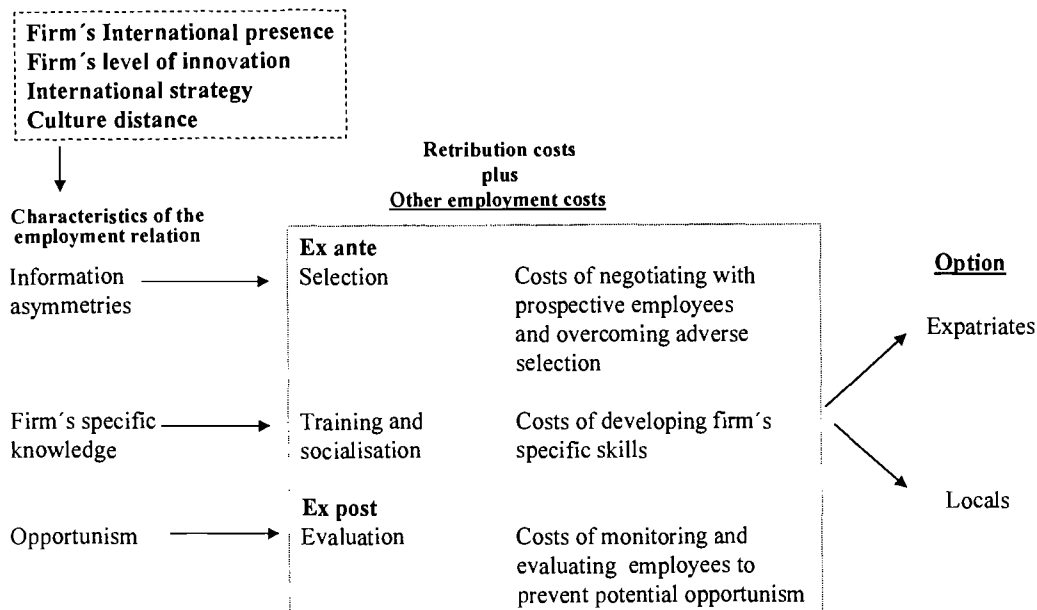
The basic premise of transaction cost economics is that transactions will tend to take place in a manner that minimizes the combined costs of the transaction. If we apply this thesis to our scenario, we see that, when deciding whether to recruit a local manager or an expatriate, the organization will consider the total transaction costs associated with each of these two options and will choose the most effective one (the one that minimizes these costs).

This opens up the possibility that, if we do not confine our attention to salary-based costs, expatriates may represent a more cost-effective staffing option in certain situations. The question then can be posed as follows: When are the employment costs of using expatriates lower than those of using local nationals?

Figure 2 shows the model that allows us to respond to this question. It includes the transaction costs that must be considered when deciding between expatriate or local managers, the employment characteristics that determine whether these costs will be higher or lower, and the situational factors that, in turn, influence these characteristics. In each situation, the organization will consider the benefits of each option, net of their respective transactions costs, and adopt the one it deems most effective.

In addition to salary costs, we have included selection, training and evaluation costs as part of employment costs, dividing them into “a priori”, which are those costs incurred to ensure that the individual has the required human capital, and “a posteriori”, the purpose of which is to motivate and assure the desired behavior.

**Figure 1: A model of the recruitment decision in MNCs**



By employment relation characteristics, we refer to a series of factors that, as we will indicate below, influence the sum of the transaction costs. These factors are as follows:

1. Information asymmetries: this is the extent of the knowledge the organization has on the candidate's qualifications and potential behavior. The less information it has, the greater will the efforts be that it must make to negotiate with candidates and overcome adverse selection (the greater will the selection costs be).
2. The firm's specific knowledge: this is the extent of the knowledge the candidate must possess on the organization's procedures, management policies or culture. If this knowledge is important, the organization will have to incur training and socialization costs in order for the individual to acquire these specific skills.

3. Opportunism: this is the degree of trust the organization has in the extent to which the candidate will meet the terms of the agreement. The lower this level of trust is (the higher the expectations are of opportunistic behavior by the candidate), the higher will the cost of evaluation be for verifying that the candidate's behavior is in line with the organization's objectives.

It should be noted that these three elements pose fewer problems in the case of expatriates. Expatriates tend to be recruited from the organization proper (Nauman, 1992; Maryhofer and Brewster, 1996). This means that, on one hand, the organization already knows their qualifications and performance, at least in its own market, and therefore possesses more information on them. Secondly, as they have experience inside the firm, they have already acquired the organization's specific knowledge, skills, rules and values. Finally, opportunism is influenced by what Moran and Ghoshal (1996) describe as the "feeling for the entity", which represents the individual's assessment of the organization. In the case of subsidiary managers, expatriates are usually trustworthy employees who are assigned to foreign operations to represent the organization's interests (Nhorria and Ghoshal, 1994). This means that they are employees who have internalized the organization's rules and values, and thus Headquarters can be sure that their behavior will be instrumental (not opportunistic). Consequently, in those situations in which these three elements are most important, it can be assumed that the organization will choose to recruit expatriates.

In our model, we have also indicated four situational factors that influence the relative importance of each of these elements. These factors are the level of the company's international expansion, their focus on innovation, the type of international strategy used, and the cultural distance between Headquarters and the subsidiary. As these factors influence employment characteristics, they affect the sum of employment costs and, accordingly, the recruitment option (expatriate versus local national). We formulate below a series of hypotheses regarding the most economically effective recruiting option in each of these situations.



### Extent of International Expansion

The literature has noted a series of advantages involved in using local managers, including the following: (1) They speak the language, understand the culture and local political system, and generally belong to the social élite of the subsidiary's country, which allows them to improve market penetration and eliminate the adaptation problems of expatriates and their families (Hamil, 1989); (2) They provide for continuity of the subsidiary's management and thus avoid frequent expatriate substitutions, often accompanied by unjustified management changes in the subsidiary; (3) They allow for major salary cost savings, thus providing a margin to pay premiums that attract the best local candidates; (4) They enhance motivation and career opportunities of local personnel, since the subsidiary's senior management positions are not reserved for headquarter employees; (5) They increase the firm's acceptance in the target country. Local governments and organizations often argue that foreign employees take away jobs from local citizens. This point of view is the basis for legislative initiatives that require multinationals to establish joint ventures with local enterprises or limit the number of foreigners in the subsidiary (Grosse and Kujawa, 1988); (6) Locals represent the subsidiary's viewpoints and conditions in the headquarters' decision making processes.

Let us assume that the firm, having become convinced of these advantages, decides to recruit local managers. Now the question is: how does it recruit them? If the company is a newcomer on the international scene, its lack of knowledge of local job markets and the fact that it does not have a base of local candidates that already work in the company make this a risky, debatable recruiting option. In order to overcome adverse selection and reduce information asymmetries, it will have to invest more time and resources in the selection of possible candidates (trips to the subsidiary's country, managers' time spent on this task, ads, employment agency expenses, checks that the candidates fulfill qualification requirements, etc.). Furthermore, local recruited candidates may have to familiarize themselves with the company's products and procedures, which will require an investment in their training and socialization with the

resulting costs. Finally, to prevent potential opportunism of “unknown” people already in the organization, it will also probably incur higher evaluation costs (frequent trips to the subsidiary, closer supervision, design and implementation of auditing systems, etc.). On the other hand, this series of costs are drastically reduced when “trustworthy” personnel already working in the firm are recruited, or as the company acquires a higher level of international expansion.

Since the costs of employing local managers tend to decrease as the level of a company’s international expansion increases, we propose the following hypothesis:

H1: The lower the level of a company’s international expansion, the more it will use expatriates.

#### Degree of Technological Innovation

From the standpoint of the theory of transaction costs applied to the international arena (Buckley and Casson, 1976; Rugman, 1981; Hennart, 1991), it could be expected that the degree of technological innovation is in some way associated with a greater use of expatriates, since they help to mitigate the perceived risk of possible opportunistic behavior by non-company people hired from local markets.

Nevertheless, in a recent work, Baron and Kreeps (1999) explain how an organization’s degree of technological innovation heavily influences the predominant type of jobs in the organization. These authors distinguish between star jobs and guardian jobs, and claim that star jobs predominate in very innovative companies. These are the jobs in which a bad performance is not too bad, but a good performance is very good for the firm. A star job would be one held by a manager who runs a subsidiary that has very little dependence on headquarters’ products, brand image and procedures, and where the essential thing is to develop new products or management processes highly tailored to the local market.

A guardian job is one in which a good performance is only slightly better for the firm than an average performance, but a bad performance is a disaster. A guardian job would be one held by a manager of a subsidiary whose function is to represent the organization

before a series of global customers and in which the organization's reputation is a valuable asset. Subsidiary managers in the financial industry typically belong to this category.

The type of job post to be filled affects the time and resources invested in candidate selection and evaluation. For a star job, the costs of a hiring error are small relative to the upside potential from finding an exceptional individual. Therefore, the organization will be less concerned with problems that information asymmetries and opportunism could cause during recruiting, and will therefore be willing to assume a higher risk in its decisions. On the contrary, in non-innovative organizations in which managers hold guardian jobs, it will be essential to ensure that the candidate fulfills the required qualifications and that his/her performance is not detrimental to the organization's global reputation or image. In this case, the higher salary costs that the company incurs on recruiting "trustworthy" employees with a long track record inside the company may compensate for the costs that would be involved if the company made a selection error.

Since the costs of employing local managers tend to decrease as a company's degree of technological innovation increases, we propose the following hypothesis:

H2: The higher a company's focus on innovation, the less it will use expatriates.

### International Strategy

There are two basic ways for multinationals to compete on the market: country to country, or on a global basis. In the latter case, the MNC's presence in foreign markets is often justified by its possession of firm-specific knowledge that provides it with a competitive advantage over local firms (Hymer, 1976; Teece, 1986). This advantage allows it to offset the disadvantage resulting from its foreign status (compared to local enterprises, MNCs are less familiarized with the national culture, the structure of local industry and other aspects of doing business in a specific country). On the other hand, these MNCs usually maintain a high degree of interdependence between their units, so that whatever one unit does impacts the organization's other units.

The type of international strategy affects the costs of training, selecting and evaluating its subsidiaries' managers. First of all, if the subsidiary competes on the basis of standard firm-specific knowledge, it is assumed that the skills of Headquarters' employees also apply to the subsidiary. Such knowledge and skills are often only obtainable in the firm and only after a long time. Furthermore, the level of knowledge about the firm, its operations, its personnel, its traditions, etc., required for higher-level positions, such as those considered in our case, is likely to be much greater and therefore more costly to acquire (Baron and Kreeps, 1999). Therefore, it is logical and rational that the company will want to amortize the training costs of its national employees in other destinations, instead of training a new local manager in those skills.

On the other hand, management jobs in interdependent units generally require making decisions that span other units of the corporation. Therefore, the costs of error of those higher up in the hierarchy are very high. This implies a greater aversion to the risk involved in recruiting personnel on which less information is available, and also in the potential opportunism that this personnel may display. Under these circumstances, the higher costs related to expatriate managers may be compensated by the savings resulting from lower selection, training and evaluation costs.

Therefore, since the costs of employing local managers are higher in global strategies, we propose the following hypothesis:

H3: Companies with a global strategy will make more use of expatriates than companies that compete country to country.

#### Geographical Area (Cultural Distance)

A multinational basically has two different but complementary mechanisms available to it for controlling its subsidiaries' performance: centralization and formalization. Centralization refers to the extent to which decisions, such as new product introduction, product design changes or production process changes, are made in headquarters. Formalization, on the other hand, depends on the existence of a well-defined set of rules and procedures that regulate tasks and the way to react to different situations. This mechanism limits a subsidiary's decision-making autonomy, but it also decreases the

headquarters' direct involvement in the subsidiaries, as direct control is replaced by rules and procedures.

When there is a great cultural distance between headquarters and the subsidiary, these two control mechanisms are not effective, since they amount to a kind of straightjacket that prevents the subsidiary from confronting the political, legal, economic or cultural complexity of its environment (Nohria and Ghoshal, 1994).

To address this issue of control in very culturally distant units, we can propose some recruiting options. The cultural difference between Headquarters and Subsidiary increases information asymmetries and the potential for opportunism. Therefore, if local managers are recruited, the company would incur higher selection, training (e.g., sending these managers to Headquarters to improve communications between both units) and evaluation costs. On the contrary, the higher salary costs that the company would have to pay on sending a "trustworthy" manager to act as an interpreter and secure Headquarters' interests in the subsidiary (Boyacilliger, 1990) could offset the costs the company would incur to overcome the possibility of opportunism and adverse selection. Since the costs of employing local managers tend to increase as the cultural distance between Headquarters and Subsidiary increases, we propose the following hypothesis:

H4: The greater the cultural distance, the more the organization will use expatriates.

## **METHODOLOGY**

### **TARGET POPULATION OF STUDY AND FINAL SAMPLE**

This work is part of a broader study on internationalization of Spanish enterprises in which both exporting firms and multinational companies took part<sup>1</sup>. Here we will refer solely to the subsample of multinational firms. These companies were selected from the international files of a database set up by Bun & Bradstreet. This database included 498 multinational companies whose head offices were 100% Spanish. These companies can be considered as the most active Spanish enterprises in international markets.

A postal survey was the instrument used to gather information. Questionnaires were sent to the selected companies, either addressed to the company presidents or, in some cases in which their names were not available, to the head executives. The first mailing to all selected companies was made in June, 1997. Within three months we received 74 replies, after which we again mailed the questionnaires to those companies that had not responded. The process was concluded with a total of 134 valid replies, which amounts to a real response rate of 26.9%.

## VARIABLE MEASUREMENT

### Dependent Variable

To determine the extent to which a company is using local or expatriate managers, the questionnaire included the following question: "What percentage of managers in charge of international operations are Spanish?" In view of the sample distribution (Table 1), which shows that most companies are amassed at the two extremes, and following the same methodology used in other studies in the field of international business (Stopford and Wells, 1972; Anderson and Coughlan, 1987; Gomes-Casseres, 1989; Hennart, 1991), we have created a dichotomous variable for which the cutoff point was a rate of international managers of Spanish nationality of more than 95%. A percentage below the cutoff point means that the company has at times resorted to the market to hire managers. A higher percentage means that this function is fully internalized in the company.

**TABLE 1: % OF EXPATRIATES**

<b>% of expatriates</b>	<b>N</b>	<b>%</b>
Between 0-50	38	28.3
Between 50-95	25	18.6
More than 95	71	52.9

As we can see, 52.9% of the companies prefer to use expatriates. As we noted in the introduction, this high percentage of expatriate use is entirely consistent with results obtained in other studies on other nationalities (Koop, 1994).

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<sup>1</sup> For a more detailed description of the methodology used, see Pla Barber (1998).

## **Independent Variables**

### **Level of International Expansion**

Traditionally, the number of subsidiaries and the percent of manufacturing done outside the local market have been variables associated with a higher degree of corporate development in the international arena (Johanson and Vahlne, 1977, 1990; Luostarinen, 1994). To encourage replies and based on experience gained in previous studies indicating a low level of foreign expansion by Spanish companies, we introduced the following intervals:

**TABLE 2: FOREIGN EXPANSION**

<b>Analysis Value</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>
% manufacturing abroad	0%	Between 1%-9%	Between 10-29%	More than 30%
No. of subsidiaries	1	Between 2 & 5	Between 5 & 10	More than 10

In order to homogenize both results, we constructed an index (IMPL) for each company, based on the sum of the values of the two variables and divided by 2. This method of constructing indexes is similar to the one used by Anderson and Coughlan (1987) and Kobrin (1994). The alpha coefficient is 0.51, positioned between the generally accepted values for the exploratory stages of research (Nunnally, 1978).

### **Degree of Technological Innovation**

Based on Kim and Hwang (1992), the innovation variable was measured by an index (INNV) constructed in a way similar to the previous case. This variable involves an appraisal, on a five-point Likert scale, of the following statements (alpha coefficient: 0.64):

- The degree of technological innovation existing in the company.
- The level of complexity of products/services or processes involved in international operations.
- The innovative level of products/services or processes involved in international operations.

## International Strategy

In order to measure the global or multi-domestic nature of the international strategy guiding company operations (ESTR), and following a methodology similar to the one used by Leong and Tan (1993), a dichotomous variable was introduced that very concisely reflected the role that foreign subsidiaries play in the company. Managers had to choose one of the following two statements; the variable was assigned value 1 if the first statement was selected, and value 0 if the second was selected.

- In my company, activities and innovations developed in subsidiaries are controlled to a large extent from central headquarters.
- In my company, subsidiaries can operate and innovate in their local markets with considerable independence from central headquarters.

## Cultural Distance

The questionnaire identified the first three countries where the company had begun its international venture, and also the three most significant countries at the present time. In most cases, it is observed that on entering a specific area, the second and third targeted markets are concentrated in the same area. Furthermore, in most cases these initial markets are currently still the most significant ones. This fact allowed us to classify companies within a certain geographical zone where most of its operations were concentrated. The following table shows the different categories, and also the number of companies included in each one.

**TABLE 3: GEOGRAPHICAL AREA (Cultural Distance)**

<b>Geographical Area</b>	<b>N</b>
European Union	72
Rest of Europe	4
North America (USA and Canada)	13
Latin America	12
Africa	1
Asia	6



## STATISTICAL ANALYSIS AND DISCUSSION OF RESULTS

In order to verify the most significant factors influencing a company's decision to recruit local managers or expatriates, and given the dichotomous nature of the dependent variable, logistic regression analysis is used (Table 5). Once the model is estimated, the values that this model predicts constitute the probabilities that the option defined by the dependent variable will be used. These estimated probabilities follow a logistic model  $\exp(z)/(1+\exp(z))$ , where  $z$  is a linear function of the independent variables. In each model, the sign of the regression coefficients of the statistically significant variables was analyzed. A positive coefficient means that the independent variable increases the probability of using expatriates, whereas a negative coefficient implies an increased probability of using local managers (Cramer, 1991; Liao, 1994)<sup>2</sup>.

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<sup>2</sup> When variables are categorical, the coefficients of each category should be interpreted in relation to the reference category. The coefficient sign will represent the differential effect of this category in relation to the omitted one on the probability that the dependent variable will equal 1.

**TABLE 5: LOGISTIC REGRESSION**

<u>Variables</u>		Coefficient B ( <i>Statistical T</i> )
IMPL	Level of Expansion	-1.786*** (10.32)
INN	Innovation	-0.771* (2.86)
ESTR	Global Strategy	1.642** (5.97)
AREA <sup>3</sup>	Geographical Area	
(1)	European Union	7.54 (0.05)
(2)	Rest of Europe	7.40 (0.04)
(3)	North America	7.16 (0.04)
(4)	Latin America	7.72 (0.05)
CONST		-4.317
<hr/>		
N		77 <sup>4</sup>
-2 log likelihood		71.3
R <sup>2</sup>		0.43
Chi-square		29.807***

\* p< 0.1; \*\*p< 0.05; \*\*\*p< 0.01

As we can see, the regression analysis validates three of the four formulated hypotheses. The model, which converges after 7 iterations, is highly explanatory, presenting a chi-square of 29.08 (p=0.0001) and a percentage of correctly classified cases of 79.22%.

<sup>3</sup> The reference variable is Asia (6).

<sup>4</sup> This number, lower than the percentage of replies received, is due to the effect of lost cases, as the econometric program eliminates any cases where a gap occurs in any of the dependent variables.

All significant variables have the correct sign. As was expected, a higher level of international expansion is associated with a greater use of local managers. The IMPL coefficient (-1.788) is negative and statistically significant at the level of 0.01. Therefore, the likelihood of using expatriates decreases as the number of subsidiaries and foreign production increase.

In addition, a negative (-0.771) and statistically significant ( $p < 0.1$ ) association is observed between the use of expatriates and the importance of innovation. It seems that when innovation is a major competitive advantage for the company, it tends to be more culturally heterogeneous and greater importance is attached to local managers, not only so that they can better address market needs, but also contribute new ways of thinking and understanding the company.

This fact is also partially confirmed by the variable that reflects the strategy followed by the company. If the subsidiaries depend on and innovations are centralized in the head office, there is a tendency to use expatriates (positive, statistically significant sign). On the other hand, if the nature of the strategy is multi-domestic, whereby the subsidiaries have a certain degree of independence and innovations are usually generated in any part of the organization, the proportion of local managers used is higher. Therefore, the global strategy proves to be a relevant predictor of the degree of internalization of the managerial function in local markets through the use of expatriates.

Finally, the geographical area where the company has most of its operations does not influence the decision to use expatriates or local managers. In accordance with these findings, we consider that cultural distance may be relevant in early investment decisions – where to invest and with what amount of resources, etc. – but once a certain amount of experience has been gained this effect diminishes.

## CONCLUSIONS

A common claim in the literature on expatriation is the one referring to the high costs of expatriates. In this paper, on the basis of transaction cost literature, we have shown how limited this approach is. In particular, we have considered a set of costs that,

although ignored in traditional expatriation literature, must be accounted for when an MNC is deciding on whether to recruit expatriates or local managers in its subsidiaries. These costs include selection, training and performance evaluation costs. We have also defended the premise that in companies with a lower level of international expansion, a lower degree of technological innovation, a global strategy and operations in very culturally distant environments, expatriates can be a cost-effective solution. This explains the apparent contradiction, formulated at the beginning of this paper, of how it is possible, in a business context defined by the need to reduce costs, that companies continue to make intensive use of such an apparently costly solution.

The empirical investigation has confirmed three of our four hypotheses, which illustrates the viability of our approach. The fact that expatriates are more extensively used in companies with a global strategy and a low level of international expansion, two of our study's findings, is consistent with the findings obtained by Edstrom and Galbraith (1977) in the late 70's. On the contrary, the third validated hypothesis in our study, i.e. that expatriates are used less in multinational companies with a higher level of technological innovation, is a finding that, as far as we know, has not resulted from any previous studies on this subject. In view of this, the theory of transaction costs not only makes it possible to confirm findings already obtained from other theoretical perspectives, but also results in new findings that provide sound arguments for defending their potential and interest in this area.

The only unconfirmed hypothesis is the one concerning a diminished use of expatriates when companies operate in very culturally distant environments. Instead, we have found that, at least in Spanish multinationals, the target country has no influence on the recruitment option. A possible reason for this is that the importance of cultural distance starts decreasing as the company acquires a solid international presence. In this case, and in line with what we have defended in this work, information asymmetries and opportunism, two of the factors that generate higher or lower employment costs, are reduced. Companies with a solid international base have already acquired information on how to operate in local job markets, and they also have a local personnel base in their subsidiaries to select the more trustworthy individuals.

The study has some limitations. First of all, we recognize that our framework may be incomplete. Other transaction costs that have not been identified may also be significant to the employment relation in a subsidiary of an MNC (e.g., the costs of enforcing contracts). Secondly, the existence of transaction costs associated with the recruitment decision in multinationals helped us formulate the hypotheses tested in the empirical investigation, but they were not specifically measured. In this respect, we understand that this study is of a merely exploratory nature and should be complemented by other future studies to fill this gap.

In spite of these limitations, we consider that the study points up some interesting elements that do more than shed some light on the apparent contradiction mentioned above. In the first place, the study establishes and explains, from a sound theoretical perspective, an area of management (i.e., expatriate management) that tends to be criticized as a merely descriptive field lacking in analytical rigor. Secondly, it not only integrates a specific international human resource management decision with the company's international strategy, but also jointly considers different human resources policies or decisions; in particular, it demonstrates the influence that other human resource decisions, such as training, compensation and performance evaluation, have on the selection decision. Therefore, it involves the two types of integration (external and internal) that are usually attributed to human resource policies in order for them to be considered strategic. As the need to introduce the "strategic" point of view in expatriate management is a claim made by several authors (Schuler, et al., 1993; Taylor et al., 1996), we consider that this work also makes a contribution in this direction.

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