FACING THE LIABILITY OF ORIGIN: EMNE SUBSIDIARIES IN DEVELOPED COUNTRIES

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Paper presented at the 6th Copenhagen Conference on: 'Emerging Multinationals': Outward Investment from Emerging Economies, Copenhagen, Denmark, 11-12 October 2018

Abstract

For some years now, EMNEs (Emerging Market Multinationals) have increased their international presence dramatically. However, their cross-border expansion is not exempt from drawbacks. EMNEs are likely to possess an inherited negative image, making it more difficult for these firms to successfully operate in advanced economies. The present paper analyses how EMNE subsidiaries in developed countries can overcome the effects of liability of origin. To explore this, we adopt a mixed approach combining quantitative and qualitative methods on a sample of EMNE subsidiaries settled in Germany, United Kingdom, France, Italy, and Spain. We find that developing good relationships with local partners and headquarters gives deeper insight into the local and corporate dynamics for adaptation, enabling to increase subsidiaries' levels of both external and internal legitimacy. The later, in turn, raises their level of decision-making power, which is necessary to better respond to isomorphic pressures and makes them less likely to suffer discrimination from their local partners. As a result, the main contribution of this paper is the creation of an original model that assesses EMNE subsidiaries' levels of embeddedness, legitimacy and autonomy to explain how they combat their liability of origin in developed countries.

Keywords: EMNE, subsidiaries, liability of origin, legitimacy, institutional theory

1. Introduction

For some years now, EMNEs (Emerging Market Multinationals) have increased their presence not just in emerging countries but in most of the developed countries as well (Cuervo-Cazurra and Ramamurti, 2014; Luo and Tung, 2007; Yang and Deng, 2017). According to the UNCTAD (2016), the value of cross-border M&As and greenfield projects from emerging countries has risen dramatically in just 12 years (2003-2015) (greenfields by 97.81% and M&As by 616.75%). Furthermore, in 2015, 63.83% of the total value of cross-border M&As was invested in developed countries, and 40.12% in the European Union, which established this region as a serious destination for EMNE's FDI (Foreign Direct Investment) (UNCTAD, 2016).

In spite of this upward trend, there are significant differences at both institutional and cultural level between developed and emerging countries which make it particularly difficult for EMNEs to adapt to the new environment (Meyer et al., 2014). On the one hand, new entrants have to make considerable efforts to overcome their lack of host-country knowledge, learn the rules of the game in developed countries, and familiarize themselves with local customs in order to compete more effectively with both local and other foreign players. On the other hand, the inherited negative image of EMNEs often makes it more difficult for them to be successful in developed countries (Bartlett and Ghoshal, 2000; Pant and Ramachandran, 2012). This cross-border disadvantage, called liability of origin, is exclusive to EMNEs; stakeholders in developed countries are likely to have an unfavourable opinion of firms from emerging countries because of the insufficient institutional development of their countries of origin (Bartlett and Ghoshal, 2000). The assumptions regarding the poor level of EMNEs in terms of product quality, service, R&D, safety measures, and so on, create this negative perception about investments from emerging countries to developed markets (Yu and Liu, 2016). Consequently, EMNEs in developed countries suffer discrimination from customers and suppliers as these local agents may have serious doubts about their competitiveness (Yu and Liu, 2016).

Faced with this challenging scenario, it is necessary to reflect on the way how EMNEs can effectively solve these conflicts in developed countries. Accordingly, this study raises the following research question: How can EMNEs mitigate this liability of origin in these markets? Responding to this question is extremely important given the growing interest on EMNEs in the International Business (IB) literature and their increasing direct investment in developed countries.

Few studies to date have analysed this issue, especially from the subsidiary perspective. This point is of particular relevance since subsidiaries of EMNEs located in developed countries are the visible face of these corporations in these settings and are thus the ones that experience the effects of liability of origin at first hand. Only a few studies descend to the EMNE's subsidiary unit of analysis (see, e.g., Panibratov, 2015; Nguyen and Larimo, 2015; Yu and Liu, 2016), although they restrict the analyses to few cases coming from a particular emerging country.

Our study aims to narrow this gap by investigating from the Institutional Theory perspective and based on a wider empirical scope, how subsidiaries can reduce their liability of origin in developed countries. Applying the concept of network embeddedness (Andersson et al., 2007; Uzzi, 1996), we argue that developing good links with local partners and headquarters gives deeper insight into the local and corporate dynamics for adaptation, enabling to increase subsidiaries' levels of both external and internal legitimacy. The later, in turn, raises their level of decision-making power, which is necessary to better respond to isomorphic pressures and convince local customers and suppliers that their behaviour is not necessarily different from that of other local firms. To explore this we adopt a mixed approach combining quantitative and qualitative methods on a broader sample in a variety of settings. Fundamentally, we apply a PLS-SEM method to estimate the hypothesized model based on a sample of 116 EMNE subsidiaries, from a vast range of emerging countries, located in five developed European countries (Germany, United Kingdom, France, Italy and Spain). Moreover, our qualitative results, obtained from ten cases through in-depth interviews with managers of EMNE subsidiaries, corroborate the quantitative findings and also provide more comprehensive and enlightening information on this phenomenon.

As a result, the main contribution of this paper is the creation of an original model that assesses EMNE subsidiaries' levels of embeddedness, legitimacy and autonomy to explain how they combat their liability of origin in developed countries. More specifically, we find that higher levels of subsidiaries' internal and external embeddedness increase their levels of internal and external legitimacy respectively, which together favour a greater degree of subsidiary autonomy and makes them less likely to suffer discrimination from their local partners.

2. Theoretical Framework

According to the Institutional Theory, the effect of liability of foreignness (Buckley and Casson, 1976; Zaheer, 1995) is even more accentuated in the case of EMNEs entering developed countries, because of the higher distance between home and host countries (Klossek et al., 2012; Si and Liefner, 2014; Wong, 2012). When operating in developed host markets, EMNEs have greater difficulties than other much institutionally closer foreign firms in understanding the dynamic of local business (Meyer et al., 2014). This greater unfamiliarity with the legal and regulatory frameworks, business practices and cultural values that enable business transactions, boosts liability of foreignness, increasing the costs of doing business overseas and worsening performance (Kostova and Zaheer, 1999).

EMNEs' liability of foreignness is even more acute because of country-of-origin effects (Bartlett and Ghoshal, 2000; Marano et al., 2017; Nguyen and Larimo, 2015; Panibratov, 2015; Pant and Ramachandran, 2012). According to Moeller et al. (2013), the country-of-origin information has a significant impact on the quality perception of a product/brand as well as the corporate reputation in the host country. Consumers of developed countries usually expect poorer features from products or services associated with EMNEs, due to the lack of maturity of the institutions in emerging countries, which in turn often results in low legal quality requirements. In this regard, EMNEs are likely to possess an inherited negative image, making it more difficult for these firms to successfully operate in advanced economies.

The IB literature has labelled these negative perceptions of EMNEs expanding into developed economies as liability of origin (Bartlett and Ghoshal, 2000; Pant and Ramachandran, 2012). This concept is defined as the additional disadvantage that EMNEs tend to suffer (compared with other foreign multinational enterprises from advanced economies), simply because they belong to an emerging economy (Bartlett and Ghoshal, 2000). While liability of foreignness can be associated with any MNE, the liability of origin and specifically, the disadvantages due to the perceived weakness of the home country's institutions, are particularly associated with EMNEs.

Local stakeholders often have negative stereotypes towards firms from other institutionally and culturally distant countries, which are influenced by their perceived underdevelopment (Marano et al., 2017; Moeller et al., 2013; Nguyen and Larimo, 2015; Yu and Liu, 2016). In this regard local stakeholders may be concerned about the levels of technological development, quality of products or services, accountability and trustworthiness of EMNEs, and hence be reluctant to interact with them. Host public administrations may also be reluctant to attract EMNEs' inward investment simply because of the lack of confidence in their capabilities or due to geopolitical considerations (Yu and Liu, 2016): for example, the fear that extracting resources from the host country might damage its economic infrastructure and possibly even threaten its national security (Cui and Jiang, 2012; Meyer et al., 2014). Hence, EMNEs in developed countries could be seen as 'Trojan horses' stealing knowledge from local partners, and therefore local stakeholders might see these foreign investments in an unfavourable light.

3. Hypotheses development

In order to overcome the liability of origin in developed host countries, EMNEs have to gain external legitimacy and make themselves known in the new environment, demonstrating their competitiveness and seriousness in doing business abroad. Subsidiaries located in these host countries are the organizational units responsible for undertaking this assignment, since they are the ones in closest contact with the new environment and local stakeholders. A useful way to earn credibility in the host country is by knitting networks with local partners in order to share information and establish constant interactions. These relationships are conceptualized as external embeddedness, and are defined as close relations between a subsidiary and its local business partners (Andersson et al., 2007; Uzzi, 1996). EMNE subsidiaries with close relationships have the chance to grasp and better understand the specific needs of new local stakeholders. Using this information in a smart way, they are able to deploy effective adaptation measures to enhance their acceptance in developed host countries, and thus establish external legitimacy (Kostova and Zaheer, 1999; Peng et al., 2008). For instance, through constant communication with customers, subsidiaries can convince them of their products' quality and their ability to deliver on time, thus overcoming customers' potential negative preconceptions of EMNEs. Therefore, by maintaining these close relationships in which frequent exchanges of information and concerns abound, subsidiaries build up a mutual trust with their local partners (Andersson et al., 2002; Uzzi, 1996), improving their reputation and corporate image in the local community. Thus, arguably, the possession of a high level of external embeddedness by these subsidiaries can translate into a good external legitimacy (see **Fig.1**). Hence, we posit:

> **H1.** The greater the external embeddedness of EMNE subsidiaries, the greater their external legitimacy in their developed host countries.

It can also be assumed that EMNE subsidiaries with a high external legitimacy due to their good local reputation and their acknowledgement among their local stakeholders are less likely to face the problem of liability of origin. EMNE subsidiaries which are unable to adapt appropriately to the developed country are in a worse position to combat this problem successfully; this means that local stakeholders will continue to view these firms negatively due to their inability to meet the host-country requirements (Kostova and Zaheer, 1999). Given these obstacles, EMNE subsidiaries are especially interested in gaining a favourable reputation in the host country as quickly as possible. Only once these subsidiaries have achieved legitimacy with their customers or suppliers, they will overcome the initial negative stigmatization caused by their status as belonging to EMNEs. As a result, their country of origin would no longer be a matter of importance, since stakeholders will be more interested in the positive things rather than in the nationality of these corporations. Therefore, as depicted in **Fig. 1**, a significant reduction in the liability of origin can be expected through a higher degree of external legitimacy. This leads us to propose the following hypothesis:

> **H2.** The greater the external legitimacy of EMNE subsidiaries, the lesser the effect of their liability of origin in their developed host countries.

Not only do EMNE subsidiaries have to focus on building cohesive relationships with their host-country stakeholders, but they also have to develop and maintain close interactions with other units within their own corporation and especially with the parent company. The intensity of the frequency, depth and quality of these relations (Ciabuschi et al., 2014; Hallin et al., 2011) is what the IB literature terms internal embeddedness. As internal close links increase, the good understanding between the two parts will rise (Gulati and Sytch, 2007). Over time, these good relations will deepen the engagement between managers and employees, which in turn will help to develop a mutual trust (Andersson et al., 2002) that improves subsidiary-headquarters interaction. Moreover, the alignment with the parent firms' cultural values, such as certain corporate customs or more appropriate ways of expressing things, will strengthen the emotional and communication ties between subsidiary and headquarters. Indeed, cultural proximity will be crucial for the frequency of interactions since it improves understanding (Harrison et al., 2000), and increases the levels of collaboration between the two (Li et al., 2016), achieving by this way greater access to scarce organizational resources and receive more support (Kostova and Zaheer, 1999; Zaheer, 1995). Thus, subsidiaries gain internal legitimacy through a high level of internal embeddedness in order to obtain their headquarters' support. Therefore, we posit:

> **H3.** The greater the internal embeddedness of EMNE subsidiaries, the greater their internal legitimacy with respect to their headquarters.

Because of the great institutional differences between developing and developed countries, EMNE subsidiaries face great challenges in attempting to give a simultaneous response to both external (host country) and internal environments (the EMNE corporation) (Kostova and Zaheer, 1999). These environments, which are often quite different from one another, can simultaneously exert isomorphic pulls on EMNE subsidiaries, in what has been described as the 'isomorphic conflict' (Forsgren, 2013). Therefore, a balance has to be struck between the two pressures in order to achieve appropriate levels of external and internal legitimacy and thus, ensure the EMNE's success in the host country.

However, as many authors have pointed out, it would be difficult for subsidiaries to achieve full external and internal legitimacy simultaneously (Kostova and Zaheer, 1999). On the one hand, according to Li et al. (2016), the increase in a subsidiary's internal legitimacy brought about by raising the level of institutionalization of their headquarters' practices and by narrowing internal interaction makes the external legitimacy process more challenging. Subsidiaries which are internally integrated and also wish to be accepted by local actors in the host country must be fully aware that some parent firms' practices can be in conflict with local ones. An excess of internal with respect to external legitimacy will not help to combat the negative perceptions of local stakeholders towards EMNEs' investments. Local players would consider that foreign subsidiaries are not doing enough to adapt to the developed host country and hence, this situation would not resolve the effect of the EMNE's liability of origin. On the other hand, EMNE subsidiaries that prioritize achieving external legitimacy at the expense of internal legitimacy, are also mistaken. In such cases, headquarters may be increasingly far away from their subsidiaries, even reaching a point where they would not identify them as members of the same corporate group. As a result, these subsidiaries will progressively lose the confidence of their headquarters and subsequently the necessary endorsement to be successful in the host country.

Consequently, subsidiaries need to achieve both types of legitimacy to fulfil internal and external requirements. Specifically, it could be expected that subsidiaries that have gained external legitimacy report satisfactory results in the local market, and so the parent company has more confidence in their competitiveness and potential for obtaining higher profitability in future. Accordingly, as the parent company feels proud of the performance and the image of the foreign subsidiary, it will be more satisfied and more committed to it, ascribing major legitimacy to this unit. Hence, we argue that good external legitimacy will increase the level of internal legitimacy. We therefore hypothesize that:

> **H4.** The greater the external legitimacy of EMNE subsidiaries in their developed host countries, the greater their internal legitimacy with respect to their headquarters

Subsidiaries achieving the correct level of internal legitimacy increase the confidence of the parent company in their capabilities, and thus obtain greater recognition of their responsibility; this in turn increases their decision-making power. When a subsidiary gains internal legitimacy within the corporation it attracts more attention and resources, and also receives greater freedom to manage them. This refers to its decision-making power: that is, the extent to which subsidiary managers are able to make decisions without headquarters' involvement (Roth and Morrison, 1992). In this regard, until the subsidiary has achieved a satisfactory level of legitimacy from its parent firm, the latter exercises great control over it and does not allow it to make many decisions by itself.

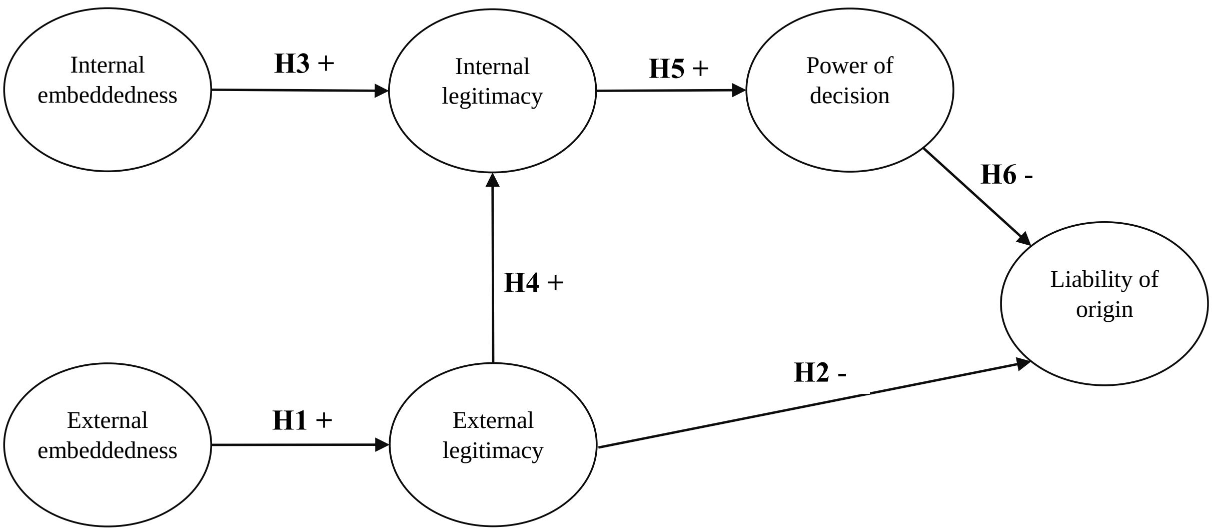
A subsidiary's good reputation and mutual trust with the parent company leads to greater autonomy. Subsidiaries' managers can assert their valuable local market knowledge to convey to their headquarters that they are the best qualified to make decisions about local resources (Cavanagh et al., 2017; Schüler-Zhou and Schüller, 2013). Once the headquarters' trust is won, EMNE subsidiaries enjoy some leeway to decide about the resources assignment and the different strategies for expanding business in the host country. This leads us to the following:

> **H5.** The greater the internal legitimacy of EMNE subsidiaries in the eyes of their headquarters, the greater their decision-making power.

The possession of greater autonomy enables subsidiaries to behave in their host countries like any other local company. This is because the possibility of making decisions freely allows subsidiaries to blend better into the host country (Yeheskel et al., 2004). Accordingly, delegating decision-making power provides an opportunity for EMNE subsidiaries to differentiate themselves from their parent company and overcome the possibly negative perceptions towards the latter (Luo, 2003; Wang et al., 2014). By acting as local firms, subsidiaries would avoid being labelled pejoratively. More autonomous local managers can more easily undertake measures to raise transparency, improve accountability in order to reduce EMNEs' liability of origin (Luo and Tung, 2007). Further, Nguyen and Larimo (2015) and Wang et al. (2014) have already suggested that foreign subsidiary autonomy is one of most important mechanisms for overcoming EMNEs' home-country disadvantages after foreign entry. Therefore, we argue that EMNE subsidiaries with higher decision-making power will provide an improved response to their host environment, by mitigating stereotypical judgments that in turn reduce their liability of origin (see theoretical model in **Fig. 1**). Hence:

> **H6.** The greater the degree of EMNE subsidiaries' decision-making power, the lesser the liability of origin suffered by EMNE subsidiaries in their developed host countries.

Figure 1. Hypothesized model



4. Methodology

In order to establish how EMNE subsidiaries can mitigate their liability of origin in developed European countries, the analysis adopts a mixture of quantitative and qualitative methodologies. Drawing on the research framework, we first conducted a survey in order to obtain empirical evidence to contrast our research hypothesis. Later on, we complement these quantitative results with a case-study methodology to know "how" things happen (Yin, 2003).

4.1. Quantitative study

<u>Population and sampling</u>

We identified our target population in the *Analyse Major Databases from European Sources* (AMADEUS), including the most important European developed countries in terms of nominal GDP (IMF, 2016). To ascertain the emerging country of origin of the multinationals we selected 39 countries[1] whose real GDP growth rates, according to the IMF (2016) for the period 2007-17, were above 4% for at least three periods. Then, we defined foreign-owned subsidiaries whose parent firms were located in the targeted emerging countries which held at least 50.01% of their shares. This criterion was used to ensure that the EMNE exercised an absolute control over the European subsidiary.

A preliminary list of 3,021 foreign-owned subsidiaries from emerging countries were identified in Germany, France, United Kingdom, Italy, and Spain. We reduced the number of EMNE subsidiaries to 1,413 by establishing several strict criteria in order to identify the population relevant to our research: a) non-active and holding companies were excluded; b) discrepancies caused by errors in foreign shareholder's origin were eliminated; c) firms owned by personal shareholders were omitted; d) subsidiaries founded after 2014 were eliminated since we want to ensure sufficient experience in the host country. Then, a sample of the population was obtained by means of the non-probabilistic sampling technique called proportional quota sampling. First we chose the relevant stratification, in this case certain fixed characteristics such as subsidiaries' business sector, their host country and the origin of their headquarters, and divide the population accordingly. Second, we carefully calculated a quota for each stratum based on the proportion of the selected characteristics amongst the 1,413 EMNE subsidiaries. Finally, after estimating the number of firms needed in each stratum, we selected non-randomly subsidiaries to take part in our research until each of these quotas was filled. This meant that our sample was as representative as possible of the population being studied. This process provided us with a final sample of 746 firms.

<u>Data collection and characteristics of the sample</u>

[1] Argentina, Bahrain, Brazil, Bulgaria, Chile, China, Colombia, Costa Rica, Czech Republic, Ecuador, Egypt, Hong Kong, Hungary, India, Indonesia, Kazakhstan, Korea (South Korea), Kuwait, Latvia, Lithuania, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Qatar, Romania, Russia, Saudi Arabia, Singapore, South Africa, Taiwan, Thailand, Turkey, Ukraine, United Arab Emirates, Uruguay and Venezuela

In a telephone pre-screening we requested that the potential respondent should be the CEO, general manager or someone in a position of responsibility within the subsidiary because this person would have a wide knowledge and overall vision of the firm. Based on the information obtained from the phone calls, we sent online questionnaires to the potential respondents. One round of reminders was sent to all target respondents when necessary. Following data collection over a four-month period (from November 2016 to February 2017), replies were received from 127 respondents, of which 116 were found to be usable. We obtained a net response rate of 15.55%, which is relatively satisfactory in surveys with high-level executives as respondents.

The t-statistic was used to test the non-response bias for both the number of employees (in log scale) and age (log scale), and the Chi-square test for the subsidiary origin (classifying the following emerging regions: 1= Asia, 2= Latin America, 3= Middle East, 4= Eastern Europe), as the nominal variable. The results showed no significant differences between responding and non-responding subsidiaries at a 5 % significance level (*p*-value=0.826; *p*-value=0.675; *p*-value=0.142, respectively) and so we can conclude that non-response bias did not represent a problem in our study.

Our final sample is diverse in terms of industry, size, age and origin (for more details, see **table 1**).

Table 1. Sample characteristics

Description	Percentage	Description	Percentage
Industry-sector		**Subsidiary origin**	
Machinery and equipment	13.79	China	25.00
Chemical	11.21	India	24.14
Automotive components	9.48	Turkey	12.93
Fabricated metal products	8.62	Brazil	11.21
Rubber and plastic products	7.76	Mexico	11.21
Basic metals	7.76	South Korea	6.03
Wholesale trade, except for motor vehicles and motorcycles	6.90	Poland	5.17
Pharmaceutical	5.17	Czech Republic	2.59
Food products	3.45	Chile	1.72
Other non-metallic mineral products	3.45	**Entry mode**	
Electrical equipment	3.45	Acquisition	82.76
Others	18.96	Greenfield	17.24
Technology and knowledge-intensity industry classification (Eurostat's criterion based on two-digits NACE)		**Subsidiary size (No. of employees)**	
High-technology manufacturing	5.18	< 50	20.68
Medium high-technology manufacturing	43.97	50–100	17.24
Medium low-technology manufacturing	28.45	101–200	35.35
Low-technology manufacturing	9.48	201–500	18.97
Knowledge-intensive services	0.86	> 500	7.76

Less knowledge-intensive services	12.06	**EMNE subsidiary age**	
Subsidiary location		3–5 years	27.59
Spain	28.44	6–10 years	52.59
Germany	23.28	11–15 years	10.34
United Kingdom	18.97	16–20 years	5.17
Italy	15.52	> 20 years	4.31
France	13.79		

Survey questionnaire and measures

We designed our survey's questions according to an exhaustive literature review of EMNE subsidiary-headquarters relationships, in order to identify a suitable group of variables that might play a role in the liability of origin. We also took steps to reduce ex ante common method variance bias: a) we assured all respondents that their data would be treated confidentially (Harzing, 1999); b) we designed a relatively brief online questionnaire occupying only four screenshots; c) we varied the series of the responses (e.g., strongly disagree to strongly agree; not at all to very much; and very unsatisfied to very satisfied) (Podsakoff et al., 2003).

Based on the literature review, we identified the measures best suited to meet the specific requirements of our research purpose. The questionnaire included 30 items, which correspond to six constructs: The 'external embeddedness' (7 items) and 'internal embeddedness' (2 items) constructs were measured by adapting the scales of Ciabuschi et al. (2014) and Hallin et al. (2011), which focus on the frequency of communication and the degree of valuable knowledge gained by subsidiaries through business relationships with major external and internal stakeholders. The 'external legitimacy' variable (6 items) was operationalized in line with Hsu (2012) and Zheng et al. (2015) to reflect both reputation and acknowledgement of the firm among local suppliers and customers. The 'internal legitimacy' (2 items) was adapted from Hsu (2012) to measure the subsidiaries' degree of acceptance by their headquarters. To quantify 'power of decision' (8 items), we adopted measures from Dimitratos et al. (2014), Edwards et al. (2002), Ghoshal and Nohria (1989) and Taggart (1997) that determine the capability of a subsidiary to make eight important decisions. Finally, the 'liability of origin' construct (5 items) measures the potential discrimination suffered by the EMNE subsidiaries in their developed host countries merely due to their belonging to a corporation from an emerging country. Since, to our knowledge, there are no scales for measuring this kind of liability, we created an original construct based on the existing literature that investigates the subject from a qualitative perspective (Moeller et al., 2013; Nguyen and Larimo, 2015; Panibratov, 2015). In addition, several control variables associated with liability of origin are included in the model to manage possible biases. The list of items for each measurement scale is presented in **table 2**.

Table 2. Constructs and measures

Construct/indicator	Definition
External embeddedness (EE)	**Respondents assessed the strength of the following aspects in the interaction with their following local partners.**
	(1= very low interaction (yearly); 5= very high interaction (weekly))
• EE1	• Frequency of communication with suppliers
• EE2	• Frequency of communication with customers
• EE3	• Frequency of communication with public administrations
• EE4	• Frequency of communication with research centres or universities
	(1= not at all; 5= very much)
• EE5	• Valuable knowledge acquired from suppliers
• EE6	• Valuable knowledge acquired from customers
• EE7	• Valuable knowledge acquired from research centres or universities
Internal embeddedness (IE)	**Respondents assessed the strength of the following aspects in the interaction with their headquarters.**
	(1= very low interaction (yearly); 5= very high interaction (weekly))
• IE1	• Frequency of communication
	(1= strongly disagree; 5= strongly agree)
• IE2	• Good understanding
External legitimacy (EL)	**Respondents assessed to what extent they feel their subsidiaries are valued by the following local partners.**
	(1= not at all; 5= very much)
• EL1	• Acknowledgement from suppliers, based on the maintenance of a good relationship
• EL2	• Acknowledgement from customers, based on the maintenance of a good relationship
• EL3	• Acknowledgement from public administrations based on the maintenance of a good relationship
• EL4	• Acknowledgement from research centres or universities based on the maintenance of a good relationship
	(1= strongly disagree; 5= strongly agree)
• EL5	• The subsidiary has a good reputation among suppliers
• EL6	• The subsidiary has a good reputation among customers
Internal legitimacy (IL)	**Respondents assessed to what extent they feel their subsidiaries are valued by their headquarters.**
	(1= strongly disagree; 5= strongly agree)
• IL1	• The subsidiary has a good reputation with its headquarters
	(1= very unsatisfied; 5= very satisfied)
• IL2	• The headquarter is satisfied with the subsidiary's business performance

Power of decision (PD)	**Respondents indicated how decisions are made regarding the following business operations carried out by the subsidiary.**
	(1= decided by headquarters without consulting subsidiary; 5= decided by subsidiary without consulting headquarters)
• PD1	• Formulating the annual Budget
• PD2	• Purchasing activities
• PD3	• Sales and distribution
• PD4	• Regional marketing
• PD5	• Hiring and firing of the subsidiary's workforce
• PD6	• Manufacturing process (modifying the production methods)
• PD7	• Manufacturing process (increasing/decreasing level of production)
• PD8	• Monitoring and controlling quality of products/services
Liability of origin (LO)	**Due to the fact that the main shareholder of their subsidiaries is from an emerging country, respondents assessed the following aspects.**
	(1= strongly disagree; 5= strongly agree)
• LO1	• Differences in treatment in the relationships maintained with suppliers
• LO2	• Differences in treatment in the relationships maintained with customers
• LO3	• Brand acceptance by local consumers is more complicated
	(1= not at all; 5= very much)
• LO4	• Negative perception of the quality of the products or services among local customers
• LO5	• Discriminatory treatment by public administrations in relation to local competitors and to other foreign MNCs from developed countries
Control Variables	
• Entry mode	• Takes values of 1= greenfield investments; 0= acquisition
• Subsidiary's age	• Number of years a subsidiary is held by an EMNE (natural logarithm)
• Subsidiary's size	• Number of subsidiary's employees (natural logarithm)
• Subsidiary's origin	• Nominal variable for emerging regions (Asia, Latin America, Middle East, and Eastern Europe)
• Industrial effects	•Takes values of 1= high-tech or medium-high-tech , 0= low-tech or medium-low-tech (Eurostat's criterion)
• Subsidiary's degree expats	• Degree of use of expatriates (1= not at all; 5= very high)

4.2. Qualitative study

Case selection and data Collection

Ten cases were selected from the database of 116 firms collected through the survey questionnaire as usable responses were received. We followed non-probabilistic criteria (Eisenhardt and Graebner, 2007) to ensure the selection of subsidiaries with (1) headquarters located in all emerging country regions (Asia, Latin America, Middle East, and Eastern Europe); (2) operations in both service and manufacturing industries; and (3) a variety of entry modes to the host country. **Table 3** summarizes the profiles of each of these cases.

Data were collected through in-depth, personal, semi-structured interviews (conducted between November 2016 and March 2017) that lasted on average 90 minutes. All the interviews were recorded and transcribed, and the crucial aspects of the interviews highlighted and divided into different sections (Yin, 2003). The structure of the interviews was similar to the quantitative survey but aimed to attain a deeper understanding of the hypothesized causal relations. Accordingly, unlike the online questionnaire, the questions of personal interviews were open-ended for respondents.

Table 3. Information on the ten EMNE subsidiaries analysed

Company	Headquarter origin	Year of entry into Spain	Entry mode	Activity sector	Interviewees
Accord Healthcare, S.L.	India	2009	Greenfield	Wholesale pharmaceutical products	General manager
Ceilhit, S.L.U.	Czech Republic	2010	Acquisition	Radiant heating production	General manager
Cosco Shipping Lines Spain, S.A.	China	1999	Greenfield	Shipping and related extension services	General manager
Ekol Spain Logistics, S.L.	Turkey	2014	Greenfield	Transport and logistics	Development manager Spain
Huayi Compressor Barcelona, S.L.	China	2012	Acquisition	Compressors and condensing units manufacturing	Human Resources manager
Motherson Sintermetal Products, S.A.	India	2011	Acquisition	Automotive components manufacturing	General manager
SQM Iberian, S.A.	Chile	1988	Joint-venture	Wholesale fertilizers	General manager
Stabilit, S.L.U.	Mexico	2000	Greenfield	Plastic laminates manufacturing	Human Resources manager
Unión Químico Farmacéutica, S.A.	India	2011	Acquisition	Pharmaceutical manufacturing	General manager
UPL Iberia, S.A.	India	2006	Greenfield	Seeds and crop protection products manufacturing	General manager

5. Results

5.1. Quantitative results

Structural Equation Modelling (SEM) using Partial Least Squares (PLS) was applied to analyse the quantitative data collected (Chin, 1998; Wold, 1985). Specifically Smart PLS Version 2 Software (Ringle et al., 2005) was used. This technique is more suitable than covariance-based models due to the exploratory character of the study and its usefulness when the relationships between variables have not been addressed before (Chin, 2010). Also, the PLS approach to SEM is particularly suited for conditions when data are not normally distributed and for small sample sizes (Hair et al., 2011).

Analysis of measurement model

Regarding the psychometric properties of the measurement model, we found sufficient confidence that it is reliable and valid[2]. First, individual item reliability was above the minimum value of 0.707, except for items PD7 (0.6657), EL5 (0.6932), EL6 (0.6086), and LO5 (0.6270). We decided to retain these items because they exceeded the minimum admissible value of 0.55 suggested by Falk and Miller (1992). However, three items of the external embeddedness construct (EE3, EE4, EE7) and two of the external legitimacy (EL3, EL4) scales were eliminated because their loadings did not meet this minimum acceptable value.

Second, the composite reliability ranged from 0.8435 to 0.9318 in all latent variables, exceeding the recommended value of 0.7 for internal consistency reliability (Hair et al., 2010). Further, all Cronbach's alpha exceed the minimum value of 0.7, except for Internal embeddedness (0.6808). However, we found support for the reliability of the measures since Cronbach's alpha assumes that each item makes an identical contribution to the latent variable and underestimates internal consistency reliability (Chin, 1998).

Third, the average variance extracted (AVE) values in our study vary from 0.5490 to 0.8286, thus passing the threshold value (0.5) that Fornell and Larcker (1981) recommend. Finally, all constructs differed substantially from each other, since the AVE for each latent variable is much larger than the squared correlation between two latent variables, thus achieving discriminant validity (Fornell and Larcker, 1981).

In addition, we check for common method variance bias using the Podsakoff et al.'s (2003) ex post approach. The amount of the variance in the items, explained by their latent variables (on average 0.6827) was significantly higher than those explained by the common method factor (on average 0.1331). Further, the overall pattern of significant/insignificant paths did not change. These results suggest that the common method bias does not represent a threat in our study.

[2] Detailed analyses of the psychometric properties of the measurement model are available upon request from the authors.

Analysis of structural model

Regarding the structural model evaluation, we found that our research model is well suited to explain the relationships. First, the model convey a very satisfactory level of predictive capacity, since the R^2 value for the final latent variable, i.e., ‘liability of origin’, suggest that 60% of the variance can be explained by the model, while the rest dependent variables exceed the 27.5%. Also, the Q^2 statistics (Geisser, 1974; Stone, 1974) is greater than zero for the four endogenous latent variables, providing support for the model’s predictive relevance.

Finally, we determined the significance level of the path coefficients using a resampling bootstrap procedure with 5000 subsamples (Chin, 1998). As can be observed in **table 4** which summarizes the results, ‘liability of origin’ was directly and negatively influenced by both ‘power of decision’ (β=–0.2896, *t*=4.1346) and ‘external legitimacy’ (β=–0.5534, *t*=9.1680), which in their turn, were directly and positively influenced by the ‘internal legitimacy’ (β=0.5242, *t*=8.8321) and ‘external embeddedness’ (β=0.6792, *t*=14.9765) respectively. Moreover, ‘internal legitimacy’ was also positively related to ‘internal embeddedness’ (β=0.5299, *t*=5.4139) and influenced by ‘external legitimacy (β=0.2004, *t*=2.8897). In conclusion, all the hypothesis in the conceptual model (H1 to H6) are significant and supported at the 1% level of significance. With regard to the control variables, we only found a significant positive relationship for ‘subsidiary degree expats’ on ‘liability of origin’ (β=0.2375, *t*=3.8284).

Table 4. Analysis of structural model

Effects on endogenous variables	**Path coefficient**	**Standard Error**	**t-value (bootstrap)**	R^2	**Stone-Geisser** Q^2
Effects on External legitimacy				0.4613	0.2530
• External embeddedness	0.6792***	0.0453	14.9765		
Effects on Internal legitimacy				0.3736	0.2939
• Internal embeddedness	0.5299***	0.0979	5.4139		
• External legitimacy	0.2004**	0.0694	2.8897		
Effects on Power of decision				0.2748	0.1171
• Internal legitimacy	0.5242***	0.0594	8.8321		
Effects on Liability of origin				0.6061	0.3355
• External legitimacy	-0.5534***	0.0604	9.1680		
• Power of decision	-0.2896***	0.0700	4.1346		
Control variables on Liability of origin					
• Entry mode	-0.0281	0.0814	0.3456		
• EMNE subsidiary age	0.0106	0.0744	0.1428		
• Subsidiary size	0.0575	0.0739	0.7782		
• Subsidiary origin	0.0729	0.1035	0.7044		
• Subsidiary degree expats	0.2375***	0.0620	3.8284		
• Industry effects	-0.0275	0.0656	0.4193		

Note: ****p* < 0.001; ***p* < 0.01; **p* < 0.05 (based on a Student *t*(4999) distribution, two-tailed test

5.2. Qualitative results

By studying the experiences of the ten EMNE subsidiary managers in the host country (see **table 3**), we aim to provide a deeper understanding of the causal relationships which were previously demonstrated. Accordingly, we compile the following narrative qualitative evidence that illustrates and nuances our tested hypothesis.

In order to adapt to host countries and reduce liability of origin, the EMNE subsidiaries interviewed try to establish good relationships with local stakeholders. Information and resource exchange through close interaction seems important to them in consolidating long-term relationships with customers, contributing to achieving mutual trust (this goes in line with Andersson et al., 2002; Uzzi, 1996). In the words of SQM Iberian's general manager *"The relationship with our customers is very close. We have built strong bonds of confidence over the last few years. We really have brought positive things to each other; for example they have always given us very good feedback that has helped us to improve our products and we have provided them with technological skills that have enable them to export more. So our growth has gone hand in hand with their growth"*. Further, in these win-win relationships not only technical information or other feedback flows occur; there is also the possibility of sharing contacts by opening up new market opportunities. And he adds: *"Within these close relations, we have provided our clients with new contacts in Latin American countries where we have a strong presence, so that they can set up new businesses. In this way, we have earned the respect and acceptance of our clients"*. Moreover, subsidiaries make their customers and suppliers feel especially valued by communicating the importance they have for the company. For example, Huayi celebrates a customers' and suppliers' day every year in Barcelona. They invite them to their facilities, explain the latest improvements at the factory, offer them dinner and go to see a professional football match. By means of these social activities, a climate of mutual confidence is built up, which increases the level of acceptance among local agents and in turn improves the reputation of EMNE subsidiaries in the host country.

Enhancing this reputation enables achieving external legitimacy as one way of shifting host-country stakeholders' attention away from the previous negative stereotypes, thus reducing the liability of origin. In this respect, the general manager of Accord reported: *"Once you have already proven that because of being an Indian firm you are no worse than other companies from Germany or France, that is, when you can demonstrate to others that your products are good and effective, so your Indian origin is no longer a problem"*. This also appears to be the case of Ceilhit, as the Spanish subsidiary currently has no problem with local suppliers and customers in spite of belonging to a Czech group. After years of hard work, this subsidiary has been able to show its competitiveness at local market, thus gaining a good reputation and this acknowledgement enables the company to remove all possible misgivings about the quality of its products due to its origin.

The interviewed subsidiaries also highlighted the importance of headquarters' acceptance since they need their support in order to boost the business in the host country. To this end, they forge close links with headquarters through frequent communication and good understanding (corroborating Ciabuschi et al.'s (2014) findings). Cosco Shipping is a good example of this; the Spanish subsidiary has a good relationship with its Chinese parent firm and together they have generated an atmosphere of mutual appreciation. Moreover, to quote the development manager of Ekol in Spain: *"The frequent and good communication that we maintain with our Turkish headquarters has helped us to gain their acceptance. We have shown an interest in Turkish values and even learned a few words in Turkish…this has brought us closer to our headquarters"*. Furthermore, Ekol is keen to integrate into the MNC group they belong: *"Our multinational's corporate slogan, 'One Ekol', arose from a comment made by our subsidiary's general manager at a meeting attended by all the subsidiaries and the Turkish headquarters. During the meeting, various general managers referred all the time to 'my' subsidiary, but our local general manager said 'we should say 'we' instead of 'my'…' as a result, we coined the slogan 'One Ekol' which really symbolizes the excellent relationship we have with our headquarters"*. This illustrates how subsidiaries that care about forging good relationships with headquarters can earn their appreciation and trust. In addition, mutual cooperation between subsidiaries and headquarters is driven by the frequent sharing of internal information and knowledge (Ciabuschi et al., 2014, Ferraris et al., 2018), which improves the subsidiary's reputation in the eyes of its parent company. For example, Stabilit maintains a very fluent relationship with its headquarters, and they provide each other with knowledge and resources concerning production activity. Some Stabilit engineers have gone to Mexico to set up projects and production lines designed at the subsidiary; and in turn, Mexican engineers came to Spain in 2005 to implement a new acrylic manufacturing line. Thus, this mutual exchange of knowledge and constant good communication improve the Spanish subsidiary reputation with the Mexican headquarters.

In order to gain internal legitimacy, the analysed subsidiaries not only take care to build close relationships with headquarters, but also try to win them over by demonstrating their their good local business performance. EMNE subsidiaries can achieve good internal legitimacy by showing clear evidence of their high external legitimacy in developed countries in Europe, driven by their good reputation among local stakeholders and their outstanding performance. In words of the development manager of Ekol in Spain: *"The fact that in our sector we have a very high acceptance and good corporate image, particularly among customers and suppliers, has certainly enhanced our reputation with our headquarters since the Turkish managers feel very proud of us"*. The general manager of Accord corroborates the above: *"Our legitimacy with the Indian parent company is also the result of our good performance in the market, and therefore the positive outcomes obtained are fruit of our success with our customers"*.

In conditions of good foreign business performance and close corporate relationships, the parent company builds up confidence in its subsidiaries and is more likely to delegate more power of decision. Indeed, the studied cases point gaining reputation in front of headquarters as a key requirement for enjoying greater autonomy when making decisions in the host country. In the words of the general manager of Accord: *"The* *prize for our past hard work is the autonomy we currently have to operate in the local market"*. This hard-won autonomy is visible in many corporate functions such as commercial or production areas. The general manager of SQM Iberian said *"for example, at the commercial level we have a spectacular degree of autonomy and this is so because the Chileans are happy with us"*. In the case of Stabilit we see the same situation: *"We have enough freedom to make decisions such as withdrawing the product from the market, so they trust our opinion fully, because they are really satisfied with our results"*. Moreover, subsidiaries have not just won the option to decide about distributing or withdrawing products, but their headquarters' commitment gives them full and complete freedom to negotiate important agreements with suppliers or customers, as is the case with Ekol. Even more interestingly, is the great autonomy of UQUIFA that could make the decision to acquire other companies in the host countries.

The fact that EMNE subsidiaries have the chance to make their own decisions in many functional areas in the company can ease their adaptation in developed countries in Europe. Subsidiaries' managers can make decisions in order to bring their subsidiaries more into line with other local firms, and are in a better position to do so than the parent company from the emerging country. That seems to be the case in Accord Healthcare, since they have freedom to hire whom they want; their recruitment of local people, who come into immediate contact with customers like European laboratories, has really helped them to combat possible prejudices arising from their Indian origin. The idea behind this is that the presence of local faces in these subsidiaries increases the sensation that these firms are no different from other local firms. Moreover, subsidiaries' decision-making power is also necessary to convince local customers and suppliers that their behaviour is aligned with local practices. According to the general manager of UPL Iberia: *"Having a great autonomy and making important decisions regarding the development of products or enlargement of distribution agreements enable us to offer faster solutions and supplies to our customers, thereby avoiding any perception of late delivery time…so our local partners regard us as a local firm"*. Further, after being acquired by an EMNE, Motherson Sintermetal had to assure local agents that the new Indian owners would continue to allow the Spanish subsidiary to make its own decisions.

6. Discussion and conclusions

This study demonstrates the rationale behind the ways in which EMNE subsidiaries located in developed countries are able to mitigate their liability of origin. It has been found that the setting of subsidiaries' external and internal embeddedness (in the host country and in the multinational corporation) has a significant positive influence on their external and internal legitimacy respectively, and in turn, increases their power of decision and reduces their liability of origin. The results of our hybrid analysis support the conceptual model presented. Hence, to the best of our knowledge, this article is the first contribution in the EMNE stream of literature to examine empirically the relationships between these elements.

Previous studies have mainly focused on laying the theoretical foundations of liability of origin suffered by EMNE in developed countries (Bartlett and Ghoshal, 2000; Luo and Tung, 2007; Pant and Ramachandran, 2012) rather than offering a full empirical examination of the phenomena (some exceptions are Nguyen and Larimo, 2015; Panibratov, 2015; and Yu and Liu, 2016). Thus, our study is one of the few to assess whether EMNE subsidiaries (regardless of their specific country of origin and if they are acquired or greenfield) suffer liability of origin in developed countries in Europe, and how they might dilute it. Moreover, as far as we know, we present the first attempt to shape the construct of EMNE liability of origin by establishing a preliminary scale of five items which should be considered and possibly refined in further empirical works.

This research corroborates the importance of establishing dual network embeddedness for foreign subsidiaries (Achcaoucaou et al, 2014; 2017), particularly for EMNEs, since it helps them to achieve dual legitimacy. Prior research has suggested that it is difficult to achieve adequate levels of both simultaneously (Kostova and Zaheer, 1999; Li et al., 2016). However, this article shows that subsidiaries' external legitimacy increases their internal legitimacy, confirming a positive relationship between them. So far, no relationships, either positive or negative, have been demonstrated between achieving a good reputation in the host country (external legitimacy) and achieving greater parent firm satisfaction (internal legitimacy); and what is more, there is no empirical evidence of which kind of legitimacy comes first. So the qualitative study in this paper sheds light on the direction of this causal relationship and offers some clues to explain the logical sequence set out in the theoretical model. A good internal reputation in the eyes of the headquarters does not come automatically by itself; on the contrary, demonstrating host-country success takes time. Only when the subsidiary gains a good reputation in its host market will it become a lucrative business for the EMNE, improving its internal legitimacy at the corporation. Hence, EMNE subsidiaries have to earn internal legitimacy by showing their high degree of adaptation in the foreign environment, making parent companies feel proud of them.

Finally, our data stress that subsidiaries which enjoy greater autonomy suffer less liability of origin. Earlier studies such as Wang et al. (2014) and Nguyen and Larimo (2015) confirmed that EMNEs which perceive serious institutional constraints in their countries of origin are more likely to delegate more autonomy, particularly in the case of acquired subsidiaries, in order to distance them from the negative image associated with their country-of-origin. However, we did not find differences between acquired and greenfield subsidiaries. To explain the negative relation between subsidiaries' autonomy and liability of origin, we suggest that subsidiaries with more power of decision are able to blend better into the developed host country (Yeheskel et al., 2004). Indeed, our control variable 'subsidiary degree of expatriates' indicates that when subsidiaries are closely controlled by local managers they suffer less liability of origin. Furthermore, our qualitative findings show that greater autonomy not only enables the subsidiary to offer a quick response to its local partners, but also helps to allay fears about the possibly drastic changes caused by EMNE subsidiary acquisitions.

In the light of these results, this study offers several implications for academics and practitioners. On the one hand, with regard to theoretical implications, the inclusion of embeddedness and legitimacy at both internal and external levels reflects the importance of the quality of the subsidiary's relationships with its parent company and with host-country stakeholders. Previous work examining the issue has focused the attention on explaining the main drivers of this liability of origin and has given some clues about how the subsidiary should interact with its local partners in order to mitigate its effect (Panibratov, 2015; Yiu and Liu, 2016), but has neglected the key role of the parent-subsidiary relationship. EMNE subsidiaries need to maintain close links not just with local partners, but also with the parent company, since only the parent company can grant them the greater autonomy they require to reduce this liability. Indeed, our results contribute to the literature by highlighting the role played by greater subsidiaries' autonomy in mitigating liability of origin. Following on from the studies by Nguyen and Larimo (2015) and Wang et al. (2014), our findings show that a high degree of autonomy allows subsidiaries to mimic local companies' behaviours, thus avoiding prejudices and stigmas. In the light of our results, future empirical studies on liability of origin should consider subsidiaries' autonomy as a key feature.

With regard to managerial implications, our results show that the appointment of EMNE expatriates to control foreign subsidiaries' operations in developed countries is counterproductive, since our results demonstrate that it increases the liability of origin. Hence, EMNEs should be aware of this and should try as far as possible to appoint local managers to direct their subsidiaries in order to enhance their local acknowledgement. Local subsidiary managers know the host-country dynamics better than expatriates from emerging countries and are 'familiar faces' to local stakeholders, which helps to neutralize negative country-of-origin effects and increases sales.

Finally, this study has some limitations which at the same time are the source of possible opportunities for future research. Our study focuses on Europe as the target host region for emerging countries' FDI. However, it would be interesting to compare results with other developed regions such as the United States and Japan, to observe whether their perceptions of EMNEs are actually different. Indeed, we might assess whether EMNEs' liability of origin is larger or smaller between countries that are neighbours in geographical or cultural terms but have different levels of development, e.g., between the United States and Latin American countries, or between Japan and China. The aim would be to establish whether vicinity between countries implies lower liability of origin because of sharing similar culture and geographical region, which can affect the way of gaining legitimacy. Taken as a whole, the model presented here may encourage future studies to incorporate new elements which have not been considered before and may help to explain how EMNE subsidiaries can overcome their liability of origin in different host countries.

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