

ECONOMIC DEVELOPMENT, GLOBAL BUSINESS STRATEGY, AND INSTITUTIONAL LEGITIMACY: THE MNC AS AN INSTITUTIONALIZED FORM OF NEO-DEPENDENCY

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*Now let us sport us while we may,
And now, like amorous birds of prey,
Rather at once our time devour
Than languish in his slow-chapt power.*

Abstract

The institutional concept of legitimacy is offered as the cornerstone for analyzing the appropriateness of foreign manufacturing entities in emerging economies. After an introductory discussion about economic development and dependency theory, the dominant writings of global business strategy are reviewed and then linked to major institutional frameworks found in economics and sociology and shown to be the source of normative legitimacy for business globalization. However, both the writings and the frameworks limit themselves to developed-economy orthodoxy, i.e. firm performance instead of economic development. This myopic perspective ignores the growing discontent with globalization and lends itself to the institutional charge of illegitimacy. In particular, it ignores the prevailing condition of neo-dependency found in MNC manufacturing subsidiaries within most emerging economies and neglects the broader societal concern for national economic development. Given the multiple levels and perspectives for institutions and their legitimacy, our reviews reveal that MNCs with emerging-economy subsidiaries operate with 'narrow' institutionalized legitimacy (labeled organizational legitimacy). But at the societal level, where legitimacy is 'broad' (labeled societal legitimacy), MNCs suffer a legitimacy deficit due to the dilemma presented by neo-dependency. With findings from an empirical study of maquiladora plants in Mexico reflecting MNC operations at the micro level, a hypothesis indicative of neo-dependency is tested. Finally, an augmented institutional framework is proposed that allows for a more inclusive model of global business strategy with a broader perspective on legitimacy.

INTRODUCTION

ECONOMIC DEVELOPMENT and DEPENDENCY THEORY

Guillen (2001) in a comparative institutional analysis of development in Argentina, Korea, and Spain specified six fundamental models, similar to those noted by Hunt (1989), for national economic development. They are:

- 1.Dependency**—an oppressive view of globalization that requires government remedies
- 2.World-System**—an oppressive view of globalization that requires systemic changes
- 3.Modernization**—a convergent view of globalization evolving through basic stages
- 4.Late Industrialization**—a convergent view of globalization needing a developmental state
- 5.Neoclassical**—a convergent view of globalization using quick, market-oriented changes
- 6.Comparative Institutional**—a positive view of globalization respecting national practices

Guillen contends that the first two models, dependency and world-system, are similar with a pessimistic view of a *glass ceiling* being imposed on the developing countries by the developed world. However, the next three models, modernization, late industrialization, and neoclassical, are quite optimistic with their focus on how the developing countries can catch up economically with the developed nations. Nevertheless, the problem with the optimistic models is their homogenizing push toward global convergence and standardized development paths, i.e. all nations and development remedies become alike. Though there are outspoken proponents of global homogenization (Levitt, 1983), its opponents (Stiglitz, 2002) can speak even louder given their much greater number. Thus, the preferred development model, as postulated by Guillen, is the comparative institutional one. It alone allows the emerging economies to catch up while maintaining their distinctive and favorable differences. Guillen thinks that his three national studies validate his preferred model. Nonetheless, he does note (2001: 222-223) that none of the three countries has achieved the income level of the developed nations and that, “*On the one hand, the three countries remain 'dependent' on the most advanced core economies, albeit in different ways.*” For him, Spain and Korea have supposedly offset their dependency somewhat with outward direct foreign investment and indigenous R&D, respectively. Though there exist these non-dependent indicators that one can point to, the pessimistic issue of dependency still remains very real as evidenced by Guillen’s own data—the disappointing ratios of inward to outward direct foreign investment and of royalty payments to royalty receipts.

Dos Santos (1970: 231) defined dependency as “*...a situation in which the economy of certain countries is conditioned by the development and expansion of another economy to which the former is subjected....*” Writing in the prestigious **Foreign Policy** journal, Velasco (2002) felt compelled to discuss dependency theory at length and then to dismiss it as others have (e.g. Packenham, 1992) on macro-economic grounds. No correlation between the GDPs of the developed and emerging economies can be found, and the evidence for deteriorating terms of trade in the emerging economies has not been consistently demonstrated. Nevertheless, Velasco does not think that global integration is the solution to economic development, either. As he notes, for every Chilean success story, there are *two growth disasters*. Such failures are both unwelcome plus injurious and underscore the increasing attention to and frustration with 1990’s economic

development concepts, especially the Washington Consensus or neo-liberalism (see Blustein, 2002, and Dunning, 2003).¹ This essential point has been poignantly made in the case of Argentina (Kristof, 2002) where the Washington Consensus was religiously adhered to and then resulted only in deleterious outcomes until recently when it began to discard the Washington Consensus principles. In fact, Bolivia with its early acceptance of the Washington Consensus principles and very recent electoral rejection of them may provide a better example of the dependency outcomes that Dos Santos and other *dependistas* accept as being obvious.

The staying power of dependency theory is due in part to its pessimistic viewpoint that reflects current reality remarkably well in most, but not all (contemporary China and India are two major exceptions), emerging economies. As we argue herein, the problem with dependency theory is not its unrealistic perspective, but its level of analysis, i.e. macro, which has historically been utilized to examine and reject it. As demonstrated below in detail, a more conceptually compelling variant of dependency theory— what we call neo-dependency² cannot be so easily dismissed, especially in the case of wholly-owned offshore outsourcing in pursuit of low-cost labor in non-prominent countries, i.e. those lacking the economic clout of Brazil, Russia, India, and China (the BRIC phenomenon). Neo-dependency will be defined herein similar to Dos Santos' dependency but with one major exception—the neo-dependent firms and sectors of an emerging economy are subject to the *institutionalized routines* of MNCs from the developed economies and hence constrained in their own development by MNCs with controlling interests through their direct foreign investments. As we show in the

¹Many experts (Buckley and Ghauri, 2004; Chidambaram, 2005; London and Hart, 2004; Ricart, et.al., 2004) have noted this decade-long shift in attitudes toward the role of MNCs in economic development. Dunning's edited book (2003) on Responsible Global Capitalism offers one alarming signal that traditional economic development ideas emphasizing the MNC are indeed in trouble. Perhaps, no one has captured the dramatic shift better than Vernon(2001, 509) in his final paper. In his opening remarks, he comments on Fukuyama's (1992) audacious pronouncement made early in the 1990s about the end of history. To quote Vernon, "*Fukuyama wants the reader to believe that a basic issue in political economy has at last been settled—that, whatever else political scientists may have to quarrel about, they should accept history's verdict of the superiority of a society based on liberal democratic principles and open markets. Today, at the close of the millennium, Fukuyama's 1992 surprises, repeatedly raising basic questions about how well we understand the societies whose behavior we are being asked to predict...And they have generated many new cautions about joining in the mantra regarding the superiority of open markets and democratic societies as an adequate foundation for a new compact between big business and national governments.*"

² We do not wish to enter into a protracted discussion and debate about the world capitalist system, dependency theory, its many manifestations, and their endless nuances. Nevertheless, we do believe that there is a conceptual and empirical argument for asserting that the relationship between the headquarters and subsidiaries in an MNC operating in non-prominent countries is one of dependence and that the relationship has observable outcomes that can be tested as hypotheses, which we do with the Mexican Maquiladora Program (MMP) data. This verifiable condition we have labeled neo-dependency in deference to dependency theory as originally proposed by Miller, Crespy and Becker (1992). We are not attempting to construct a grand, macroeconomic theory as Frank (1967) did to explain underdevelopment in the emerging economies. Though such an undertaking is commendable, our intent aims to focus attention on the micro level where economic activity and transactions are designed and implemented and not on the macro level where aggregated data can only reflect factual measures that those transactions did occur.

following sections, the global business strategy literature has provided normative legitimacy for such neo-dependent routines; however, our review of the seminal literature on institutions and legitimacy reveals it to have a broader purview than simple organizational legitimacy. The broader notion of legitimacy, i.e. societal legitimacy, gives rise to concerns about MNC illegitimacy fomenting neo-dependency, which we examine through the illustrative case of the Mexican Maquiladora Program (MMP). After discussing the literature reviews and the MMP findings, we conclude by arguing that issues of MNC institutionalized control and legitimacy must be addressed by those who wish to contend that national economic development, with its long-term, “*slow-chapt*”, view toward sovereign and societal outcomes, is still compatible with the MNC and its short-term fixation, “*at once our time devour*”, on immediate gratification.

THE GLOBAL BUSINESS STRATEGY LITERATURE INSTITUTIONALIZING NEO-DEPENDENCY

We begin our discussion of neo-dependency and economic development by reviewing the salient management writings on how to manage an MNC in this current era of globalization. As we show with this review, the case for neo-dependency via the MNC follows from these writings and will be viewed as the normative legitimacy justifying such dependency. Our decision to examine the MNC instead of macro-economic indicators, e.g. trade flows, offers a very different perspective on economic development, and it addresses the level-of-analysis weakness in dependency theory that was identified by Pakenham (1992). Our review, which we now summarize, reveals that *micro-level practices as promulgated in the foundation global strategy literature do reflect a preferred condition of neo-dependency in emerging-economy subsidiaries found in non-prominent nations, especially those involved in outsourcing efforts.*

The chosen micro-level focus is consistent with Guillen (2001) who emphasized the importance of social actors at the firm level and also with Porter (1990) who underscored the relevance of micro-level actors in the development of world-class industries. Furthermore, this level of analysis is in keeping with the seminal idea of institutional practices and routines that Nelson and Winter (1982) have developed to show how firms and strategies must evolve if they are to survive. It also fits concisely into the transaction-cost modality of institutional thinking (Williamson, 1985) and the OLI (ownership-location-internalization) paradigm that are popular among international business scholars. In addition, it is in line with the main thrust of neo-liberalism, i.e. the Washington Consensus, and its belief in the rightness of individual actors, whether they be firms or persons. Finally, micro-level analysis has clearly been at the forefront in the writings of those scholars who laid the foundation for global business strategy (GBS) in the 1980s, which now permeates the neo-liberal contribution to national economic development.

The GBS literature can be categorized as either prescriptive or descriptive in its discussion of subsidiaries in emerging economies. The early literature, to be discussed first was primarily prescriptive (though based on solid empirical efforts according to its creators) and relegated subsidiaries from emerging economies to a role of no, or at best,

little importance. Furthermore, it advocated their dependence on headquarters in the Triad (Ohmae, 1987) and demonstrated indifference to the economic development of the nations where the subsidiaries resided. To substantiate this contention, we have surveyed the major foundation works that focused on GBS (please see Table 1 below). The selected books were chosen because their authors demonstrated an early and strong influence (e.g. Roth & Morrison, 1992, used the authors of three of the books for 25 percent of their references) and are still influencing research agendas for international business strategy (e.g. Blumentritt & Nigh, 2002; Vermeulen & Barkema, 2002; Katsikeas, Samiee & Theodosiou, 2006). A second reason for choosing to review these prominent and influential books was the comprehensive coverage that the authors were able to give the complex topic of global business strategy. An exception to this would be Porter's (1986) lengthy article on configuration and coordination for an international value chain. A third reason for picking these particular authors' books was their international perspective, i.e. both U.S. and non-U.S. MNCs were examined as they struggled to develop and implement global strategies.

Table 1.
Annual Number of Citations per Author(s) in the Social Sciences Citation Index
1990 1991 1992 1993 1994 1995 1996 1997 1998 1999 2000 2001 2002 2003 2004

Ohmae (2 books)	10	17	14	15	15	7	10	10	7	9	4	13	8	7	5
Prahalad & Doz	16	16	17	16	19	18	21	14	17	17	26	18	11	19	15
Bartlett & Ghoshal	8	25	21	31	34	40	47	40	39	37	51	41	43	55	53
Yip	-	-	1	3	2	2	4	7	3	6	10	9	6	6	15

The disadvantage of focusing on books stems from the breadth of coverage that the book format allows. Such breadth can result in conflicting statements that may result in ambiguity. To overcome that disadvantage, we will use direct quotes from each of the writers. Though it may be somewhat cumbersome, it will allow the reader to see that our interpretation of each writer is grounded in the writer's own words and not in errant paraphrasing of his words.

In 1985 and 1987, Kenichi Ohmae's books—Triad Power and Beyond National Borders were published and provided the foundation that revealed his thinking. Ohmae, the renowned Japanese business strategist often mentioned in the early years of globalization, had a view of the world that is especially noteworthy because of his emphasis on the Triad. Apparently, the new reality of markets was in the Triad, which had, according to Ohmae, 630 million inhabitants. Assuming a world population of over five billion people in the 1980s, there were 4.4 billion people (87% of the world) excluded from the Triadian race. What should happen to them? Ohmae was vague about that. He indicated that 'trickle down' was no longer the reality in OECD countries, but

beyond that historical group of 24 developed nations he was silent. Ohmae deemed it imperative that a business firm operate throughout the Triad with only limited attention paid to non-Triad countries. His view of how to organize the MNC vis-à-vis emerging economies could best be visualized by looking at his JUE (Japan, United States, Europe) Tetrahedron found on page 96 (Ohmae, 1987, who cited McKinsey & Company as the original source). It placed MNCs from Europe, Japan and the United States in the center and everything else on the periphery.

According to Ohmae, *"Seeking to globalize by expanding into countries of little or no strategic importance is simply unproductive dissipation of corporate energy. That means that companies should be far more selective with their investments in developing countries"* (1987: 97). For Ohmae, investments in developing countries were for production sites and not for markets. As could be seen in his JUE diagram, emerging economies with their subsidiaries on the periphery were to be dominated by the MNCs from the developed economies.

Also appearing in 1987 was the book by C.K. Prahalad and Yves L. Doz--The Multinational Mission: Balancing Local Demands and Global Vision—a still much cited work as revealed in Exhibit A. The authors of this book did provide a balanced view of the demands on the MNC. Those demands were expressed as economic, political, and organizational imperatives. The demands presented the constraints through which the MNC must navigate as it strives toward its global vision. The global vision, i.e. the necessary, worldwide perspective of MNC managers, was a recurring theme of theirs and in all the GBS literature. It has been a theme that assumed the eventual globalness of business activities and provided much of the legitimating rhetoric (Suddaby and Greenwood, 2005) needed for globalization.

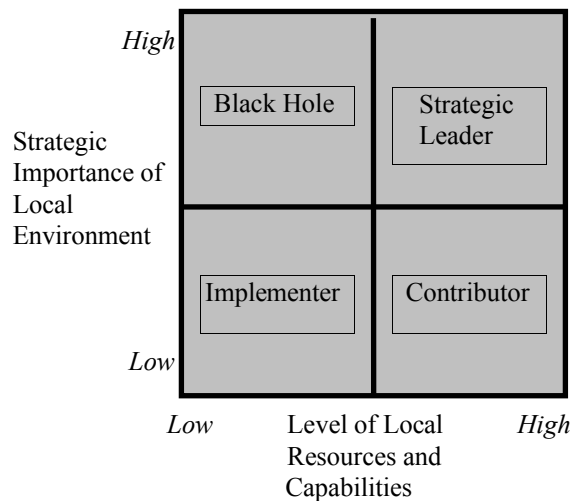
Prahalad and Doz devoted an entire chapter to host government demands and policies. Nevertheless, local governmental demands, discussed early in the book, seemed to wane in importance as they attempted to maximize the firm's resources by balancing between the local and the global. The necessary balancing attempt was best symbolized by their integration-responsiveness grid, the cornerstone of their framework. According to them, proper use of the grid with its equal emphasis on global integration and local responsiveness should yield the best results for the firm. Nevertheless, as explained and operationalized by Prahalad and Doz, implementation of the grid was the task of senior management. It was responsible for the headquarters-subsidary relationship, which would be manifested through the strategic needs of control, change, and flexibility. These three needs were at the center of global strategic management, which must be controlled by upper management.

"Control is the essence of implementation...Control is established by headquarters over subsidiaries in order to manage global integration of an interdependent network of operations... Strategic control is more subtle. It involves the assignment of strategic missions to subsidiaries... Both aspects of control-global integration and strategic coordination - are at the heart of the relationships between headquarters and subsidiaries... In effect, the ability of headquarters to influence the

actions of subsidiaries is a function of the nature of dependencies built into the multinational network... The dependency of subsidiaries on headquarters for resources technology, export markets, or management and financial resources facilitates control. The dependency of a subsidiary can take one of several forms" (1987: 160-61, emphasis added).

Building on these earlier writings and their own research (primarily nine case studies), Christopher Bartlett and Sumantra Ghoshal (1989) authored a major book (still used after multiple revisions as a textbook with cases in many graduate international management courses) wherein they advocated the transnational solution. Briefly stated, the solution recognized that *dynamic interdependence is the basis of a transnational company that can think globally and act locally* (Bartlett and Ghoshal, 1988: 69). To think globally and act locally, the global company must simultaneously pursue three goals-- worldwide efficiency, national responsiveness, and technological adaptability. To make these goals more manageable, Bartlett and Ghoshal (1989: 106) recommended that global corporations utilize a simple, four-cell matrix for classifying national subsidiaries. Each national subsidiary should be expected to contribute to the global business endeavor on the basis of its generic classification within the matrix taken from their book and shown here as Figure 1.

Figure 1. Generic Roles of National Organizations



In terms of the generic roles, two could be expected to make a contribution to a product development effort. Those two were: the strategic leader and the contributor. Only a few national subsidiaries would be able to fulfill the leader or contributor roles, and the great majority of the national subsidiaries must be relegated to the implementer role, i.e. a follower selling products developed in other countries. The black hole role pertained to a very limited number of countries, e.g. China and India, so it would not be relevant for most national subsidiaries. The fact that China and India represented such a

large proportion of the world's population provided them with a special classification in the TNC (transnational corporation) world view.

According to Bartlett and Ghoshal, the implementer role would be: *“Characteristic of many subsidiaries in the developing countries of Latin America, Africa and Asia as well as the national organizations in Canada and in the smaller European countries... These national organizations cannot contribute much to the strategic knowledge of the firm. They do not have access to critical information; they do not control scarce resources. Fundamentally, they are implementers - deliverers of the company's value added. Their task is not unimportant, however. The implementers make it possible to capture economies of scale and scope that are critical to most global strategies”* (1989: 109). In strategic military terms, the developing countries are the expendable foot soldiers of a general's conquering army.

A few years later, George Yip's book (1992), **Total Global Strategy**, turned the lowly foot soldier into an even lower canine. He advocated that most industries were becoming global and that business firms, to be successful, must do as the book's title indicates, i.e. develop a comprehensive global strategy. In order to do that, the global company must undertake several actions. First, it must understand its capabilities and its industry's global drivers. Having done that, it should next manipulate the global strategy levers as specified by Yip. Pulling those levers required the MNC management team to select globally strategic countries worthy of market participation by the company. To accomplish this, Yip borrowed from the BCG (Boston Consulting Group) matrix and classified countries as wildcat, star, cash cow, or dog. *Dog countries were to be avoided by the MNC*. Though he never specified which countries were dogs, his discussion of lead countries (page 44)—*“Lead countries can be easily identified as those in which the most important product or process innovations occur”*—revealed that emerging-economy subsidiaries were not going to be leading the MNC. At no point in the book did Yip explicitly exclude emerging economies from the development of the MNC's global strategy. If such a nation was strategically important (highly unlikely as a market but quite possible as a production factor), then it deserved to be included in the global strategy.

To enact a global strategy, Yip advocated (1992: 185): *“one of the most effective ways to develop and implement a global strategy is to centralize authority so that all units of the same business around the world report to a common global sector head”*. He augmented the proposed centralization with the notion of a global team that was responsible for the success of the global strategy. The members of the team (6-8 people) were individuals with critical functions found in the lead or strategically important countries. For Yip, a global strategy would almost always relegate emerging-economy subsidiaries to an insignificant or “dog” role.

To summarize, the authors of these four influential works recommended and prescribed, i.e. rhetorically legitimated, global strategies for Triadic MNCs that emphasized the importance of developed economies while neglecting emerging economies (with exceptions for China and India) and prescribing complete dependence of MNC subsidiaries. Were such recommendations describing MNC reality? Did their prescriptions reflect existing practices in the MNCs? The answer appeared to be

affirmative. Ohmae's recommendations came from his work as a senior partner with the international consulting firm McKinsey & Company. The Prahalad and Doz prescriptions were based on a six-year research study that included interviews with more than 500 top executives from over 20 MNCs. Bartlett and Ghoshal developed their transnational solution after conducting 236 interviews with MNC managers during a five-year period. The research effort was centered on nine MNCs from the European Community, Japan, and the United States. Yip's recommendations were from a five-year study involving interviews with more than 50 senior executives at 23 of the Triad's largest MNCs. Based on their extensive research efforts involving MNC headquarters and the similarity in their findings, there was and still is no readily apparent reason to doubt that their recommendations for headquarters control were grounded in so-called "best practices."

In the paragraphs above, we reviewed the (classic) writings for GBS. Next, we want to mention briefly more recent articles that have appeared in two leading and germane business journals—the **Journal of International Business Studies** and the **Strategic Management Journal**. Both journals have devoted considerable attention to the complex topic of the headquarters-subsidiary relationship. The articles, with one exception (Rugman and Verbeke, 2001), are empirically based and purportedly designed to be analytically descriptive. Nevertheless, they are clearly influenced by the classic GBS literature. All cite (except for Kim, et al., 2004; Robins, et al., 2002) one or more of the authors from the foundation writings. Interestingly, these two exceptions actually mention dependence in their titles and do explore power relationships between superiors and inferiors. However, none of the other articles' authors (Bjorkman, et al., 2004; Cantwell and Mudambi, 2005; Frost, et al., 2002; Hewett, et al., 2003; Kim, et al., 2003; Rugman and Verbeke, 2001; Tsang, 2002; Watson, 2000) appears willing to make power or dependence the explicit focus of their work. In spite of this reticence, their writings clearly corroborate the existence and the salience of the *control relationship* between MNC headquarters and subsidiaries.

Rugman and Verbeke (2001) present the conceptual arguments for including subsidiaries in the building of firm-specific competencies *for the benefit of the firm*, and they do note the contingencies that will impact the development of such competencies across the firm's network of subsidiaries. The other studies augment the Rugman-Verbeke position by developing and testing hypotheses about the headquarters-subsidiary relationship. Generally speaking, with the exception of Tsang (2002) who examines the relationship in Chinese ventures, these organizational researchers present positive results concerning the relationship and its functioning. Without fault, these reported studies do not question the purpose or legitimacy of the relationship and always assume that its existence is *for the exclusive benefit of the firm*.

Subsidiary autonomy, the antidote to micro-dependence, can occur, but it is a rarity in emerging economies and even then only in a full-fledged operation and not a manufacturing concern—our principal focus. This caveat is pertinent to the Robins, et al. (2002) research which examined joint venture operations in Mexico based on a listing in the Mexican AmCham Directory that would preclude plants in the maquiladora sector. In spite of their broader focus, Robins, et al. (2002: 896) noted that "*the key empirical insight to emerge from this study is that a balance of ICV (international cooperative*

venture) *dependence and independence is important to the success of strategies for emerging economies*". Less dependence and more independence may be needed, but as discussed and examined by Edwards, et al. (2002) in Malaysia, it probably will not happen even when it is encouraged by special governmental programs. Subsidiary dependency, particularly in networked manufacturing entities found in non-prominent emerging economies, is an inescapable fact of life in MNCs with integrated networks.

Though most of the international business (IB) literature stresses the need for subsidiary dependence, not all IB scholars share this view, especially those dealing with much more recent international phenomena. Some do recognize that dependence can be counterproductive with unwanted outcomes. Such viewpoints can be found in Child et al. (2003), London and Hart (2004), Luo and Peng (2003), Rugman and Verbeke (2003, and Zanfei (2005). However, the research by Child and colleagues plus that done by Luo and Peng is relevant primarily to China and not generalizable beyond transition economies as their authors note. The contribution made by Rugman and Verbeke is from a transaction-cost perspective and assumes that the proper goal for the subsidiary is profit maximization for the parent corporation³. Using more inclusive assumptions, the writings of London and Hart and of Zanfei are much more reflective about the proper role of emerging economy subsidiaries and do advocate, if economic development is the goal, a different and independent role for such subsidiaries.

Nevertheless, additional evidence of subsidiary dependency can be found in Michael Porter's (1990) massive study of global industries, which also corroborates the likelihood of dependency in the state of affairs between MNCs and their subsidiaries in emerging economies⁴. Due to this, Porter has taken a position critical of MNCs and argued that they foment dependency and provide no development impetus in emerging economies. He contended: "*Competitive advantage in developing countries tends to be almost exclusively in industries where natural resources, cheap labor, locational factors, and other basic factor advantages provide a fragile and often fleeting ability to export. Dependence on such industries, where exports are invariably sensitive to price, leaves the nation vulnerable to exchange rate and factor cost savings*" (page 675).

In brief, the type of MNC-subsidiary dependency studied and described by recent researchers and prescribed-legitimated by Ohmae, Prahalad & Doz, Bartlett & Ghoshal, and Yip offers corroboration for the organizational image detailed two decades ago by Morgan (1986: 302-303). He notes:

"Recent research has suggested that the activities of many, multinationals, particularly those operated from the United States, are highly centralized,

³ We wish to thank one of the reviewers for pointing out the works of Child, et al., Luo and Peng, and Rugman and Verbeke. They do open up the possibility of the relationship between headquarters and the subsidiary becoming less controlling or dependent. However, as with the mea culpas of the GBS literature we find that the Child et al. article was cited five times, the Rugman and Verbeke piece 13 times, and the Luo and Peng paper 55 times between 2003-06. Furthermore, Luo and Peng noted their findings should not be generalized beyond the context of transition economies. Thus, they are constrained to the situation found in the former communist countries.

⁴ Porter (1990) primarily tracks MNCs from the triad. MNCs from non-triad countries would have by default different reporting and power relationships, see for example Bacardi from Bermuda and Cemex from Mexico.

their foreign subsidiaries being tightly controlled through policies, rules, and regulations set by headquarters... Their staff are often allowed very little influence on key decisions affecting the subsidiary. The resources of the multinationals are also usually managed in a way that creates dependency rather than local autonomy. . . Centralized administration tends to replace the interplay of market forces. Or, as business historian Alfred Chandler has put it, "the visible hand" of management replaces the "invisible hand" that Adam Smith saw as guiding competitive market economies. Whenever we examine the multinationals, therefore, we are quickly brought face to face with their monolithic power. Of all organizations, they came closest to realizing Max Weber's worst fears with regard to how bureaucratic organizations can become totalitarian regimes serving the interests of elites, where those in control are able to exercise power that is "practically unshatterable." Simply put, the name of the multinational game frequently becomes control, control, control."

Morgan's statement may seem overly harsh, but even Prahalad appears to have realized that so much MNC control fosters not only neo-dependent but also unproductive practices and routines. In a later article, *The End of Corporate Imperialism* (Prahalad and Lieberthal, 1998: 70), he and his co-author state in their discussion of emerging markets that "as a result of this imperialist mind-set, multinationals have achieved only limited success in those markets... The more we understand the nature of these markets, the more we believe that multinationals will have to rethink and reconfigure every element of their business models". The need to *rethink and reconfigure* is in the future tense; thus, Prahalad is confirming that for now—1998—imperial control or neo-dependency is the modus operandi of the MNC⁵. Bartlett and Ghoshal (2000) also have updated their thinking about the role of the emerging-economy subsidiary within the MNC constellation. We label both these later contributions *mea culpa*(s) and note that, using the SSCI as an indicator of scholarly influence, one finds the Prahalad and Lieberthal article has been cited a total of 17 times through 2004 and the Bartlett and Ghoshal piece has been cited a total of three times in the same time period since its publication. This contrasts impotently with the robust 280 and 565 citations, respectively, for their original publications wherein they, particularly Bartlett and Ghoshal, advocated neo-dependent activities for those subsidiaries found in all but the largest and most fortunate emerging economies—China and India. As we discuss next, these neo-dependent practices and

⁵ Prahalad (2005) has recently, however, cited about a dozen case studies of local firms and MNCs penetrating the bottom of the pyramid, most of which are of non-triad origins. The emergence of this new phenomenon seems real, but it should be viewed from a realistic perspective. Upon review of the 2005 Fortune Global 500 list of Corporations, we find 35 firms are from the emerging economies (Brazil-3, China-16, India-5, Malaysia-1, Mexico-2, Russia-3, Saudi Arabia-1, Taiwan-2, Thailand-1, and Turkey-1). Twenty-two (63%) of the 35 companies are in the bottom half of the 500 group, and the four that rank in the top 100 are state-owned oil companies and utilities. Any celebration over the rise of private-sector corporations from the emerging economies seems premature, if not contrary to the facts, as of 2005.

routines gained their normative institutional legitimacy from the GBS literature that these early writers so ably provided.

INSTITUTIONAL THEORY: ORGANIZATIONAL VERSUS SOCIETAL LEGITIMACY

Institutionalism has a very long and broad history, particularly in the disciplines of economics, political science, and sociology. With the published working paper by the National Bureau of Economic Research (Easterly & Levine, 2002) and the earlier edited volume by Harriss, Hunter, & Lewis (1995), we can safely assume that institutions are also critically important in national economic development. In addition, the World Bank (2002) has emphasized the critical nature of institutions to development in its World Development Report—**Building Institutions for Markets**. The International Monetary Fund (2003) has also provided support for an institutional mindset toward economic development in its publication sub-titled **Growth and Institutions**. Given the primacy now of institutions to economic development and their long-standing relevance to business organizations, there is a sound rationale for exploring how the institutional concept of legitimacy can be utilized to shed a clearer light on the linkage between global business strategies and economic development. Due to the need for brevity, we will only discuss the institutionalist links between global business strategy and two of the disciplines, economics and sociology.

From the economics perspective, the works of North (1990) and Williamson (1985) are most instructive. North has provided the insight that there are macro-institutional rules for conducting economic exchanges. When the rules are written and enforced as laws, they can be considered formal and legitimate. Legitimacy flows from the fact that the sovereign, with its paramount power, has promulgated and implemented the rules. Legitimate rules give stability to economic transactions across society and, if efficiently constructed, reduce the costs of uncertainty. For him, there is no guarantee, though there is much concern, that the rules will be efficient, *“I abandoned the efficiency view of institutions. Rulers devised property rights in their own interests and transaction costs resulted in typically inefficient property rights prevailing. As a result it was possible to account for the widespread existence of property rights throughout history and in the present that did not produce economic growth”* (page 7). North’s interest in property rights reflects a neo-liberal viewpoint centered on the economy at the national level; however, his conclusion that institutions need not reflect efficient rules is unavoidable and germane to MNCs with emerging-economy subsidiaries.

Williamson, on the other hand, believes that governance structures (his preferred term) for firm-level exchanges will be efficiently constructed, hence legitimate. The legitimacy of institutional governance structures necessary for conducting economic transactions results from their assumed efficiency. Institutionalized governing structures will be efficient because managers making choices about such structures will find it in the firm’s interest to search for and adopt structures that benefit the firm financially. Management’s desire to earn pecuniary awards for the firm will guarantee the development of efficient institutional structures for transacting the firm’s business.

Williamson's efficiency—with its inherent legitimacy in the for-profit firm—has been a major influence on much of the business scholarship analyzing the MNC. Furthermore, there is a presumption, contrary to North's findings, that efficiency and its benefits at the firm level will translate into efficiency and benefits at the societal level, i.e. that which is legitimate at the firm level will also be legitimate at the national level. This major difference in the institutional thinking of North and Williamson is crucial to understanding how legitimacy will be seen and evaluated distinctly, and often times contrarily, depending on one's viewpoint.

In terms of the institutions that govern the transactions between MNC headquarters and their subsidiaries, the Williamson perspective contends that the managers of the MNC will construct institutions that govern transactions efficiently for the firm. North, on the other hand, sees no guarantee that these institutionalized transactions will be efficient for society. In fact, he argues in his discussion of institutional change that organizations may struggle to preserve inefficient (from the societal level) institutions:

“Institutions, together with the standard constraints of economic theory, determine the opportunities in a society. Organizations are created to take advantage of those opportunities, and, as the organizations evolve, they alter the institutions. The resultant path of institutional change is shaped by (1) the lock-in that comes from the symbiotic relationship between institutions and the organizations that have evolved as a consequence of the incentive structure provided by those institutions and (2) the feedback process by which human beings perceive and react to changes in the opportunity set” (page 7).

As discussed below, the MMP may well be efficient and legitimate for governing economic transactions within the MNC from Williamson's viewpoint, but that efficiency may not accrue to Mexican society from North's perspective. In light of its decades-long existence, the Program is very likely locked-in with its current MNC beneficiaries arguing both for the efficiency and stability of their maquilas (the plants themselves) in spite of doubts (from those focused on economic development) about its societal impact or national legitimacy (this term is explained below).

If economists see institutions as the rules and governance structures for conducting exchanges, then sociologists perceive them as the routines or practices that result in exchange stability across a population of organizations. Regarding sociology and its sub-discipline of organization theory, the writings of DiMaggio and Powell (1983) and Scott (1995) offer an in-depth view of how sociologists conceptualize institutions. For them, institutions represent the isomorphic practices and routines that occur across a group of organizations. Addressing the observed patterns and routines, DiMaggio and Powell (1983: 148) wanted to know *why there is such startling homogeneity of organizational forms and practices?*

If a similar organizational practice is found to exist among a set of business firms, then that practice can be classified as an institution that is supposedly legitimate. Legitimacy emerges solely from the acceptance of practices across multiple sites or firms. For example, Guler, Guillen, and Macpherson (2002) have shown, at the global level, that isomorphism does happen in terms of quality practices as exemplified by the ISO 9000

certificate. The adoption of ISO 9000 by thousands of businesses since the late 1980s represents a global institution. For sociologists, the question of ISO 9000 efficiency is not germane—only the undisputed fact that the practice with its mandatory routines exists among so many firms matters. The mere observation of isomorphic practices denotes acceptance and assumes legitimacy for that practice. For sociologists, an efficient governance structure does not necessarily render an institution legitimate, nor does a rule from the sovereign always equate to legitimacy; however, the observation of a common practice across a set of firms does reveal a stable institution, whatever the source of its legitimacy.

To tie together the divergent notions of the above institutionalists and to link them with the already discussed practice of MNC control over dependent subsidiaries, the economics-based work of Nelson and Winter (1982) is helpful. Though their approach is grounded in micro-economics and the efficiency objective, it clearly moves beyond traditional neo-classical economics. For them as for many sociologists, institutions are best observed at the firm level or across firms within an industry. The institutions of interest are referred to as routines and can include almost any and all the repeated behaviors in organized firms. Nelson and Winter rely on the biological metaphor of genes to explain the existence (not the legitimacy) of routines, which are very enduring organizational behaviors. Given the lasting nature of these genetic routines and the ubiquitous condition of environmental change, some organizations will survive, depending on their routines and the changing environment to be confronted, and others will fail. Nelson and Winter's model of the firm is rooted in evolutionary ideas from biology and is quite deterministic in its outlook. Nevertheless, it does allow us to understand that MNCs, when viewed with the GBS literature in mind, have become large organizations with institutionalized routines and structures that create and lock-in dependence in their emerging-economy subsidiaries. If the global environment wherein the MNCs operate shifts, e.g. away from the 1990's preference for a global economy based on the individual focus of neo-liberalism and toward a newer preference for a global economy emphasizing developing-nation economic development (the current Doha round of WTO negotiations is a clear example of this), then MNCs with neo-dependent routines may find themselves in institutional jeopardy and routinely buffeted by latent and divergent claims for legitimacy.

Legitimacy, from the viewpoint of institutions at the organizational level, can be better understood by first referring back to how DiMaggio and Powell (1983: 150-152) conceptualized institutionalization. It is organizational isomorphism (their primary concern) and is caused by three mechanisms: coercive, mimetic, and normative. As quoted here, their descriptions for these three terms in reference to institutional change are critical to comprehending institutional legitimacy (a secondary concern for them).

“Coercive isomorphism results from both formal and informal pressures exerted on organizations by other organizations upon which they are dependent and by cultural expectations in the society within which organizations function.

Not all institutional isomorphism, however, derives from coercive authority. Uncertainty, is also a powerful force that encourages

imitation. When organizational technologies are poorly understood... when goals are ambiguous, or when the environment creates symbolic uncertainty, organizations may model themselves on other organizations. A third source of isomorphic organizational change is normative and stems primarily from professionalization... We interpret professionalization as the collective struggle of members of an occupation to define the conditions and methods of their work, to control' the production of producers,' and to establish a cognitive base and legitimation for their occupational autonomy."

Their view of legitimacy, as a function of isomorphism, regards it as either being a compelling force, an imitative response, or the appropriate professional behavior. For DiMaggio and Powell, normative isomorphism is explicitly tied to legitimacy and is readily observed in the appropriate behaviors of the profession—the GBS literature is one manifestation of normative institutional change for globalization.

Later, Scott (1995), building on earlier work in sociology and drawing from institutional writings in economics and political science, developed an integrative model for institutions that gave more emphasis to legitimacy. In Scott's view, an institution is a complex phenomenon that consists simultaneously of carriers, pillars, and itself, e.g. the Mexican Maquiladora Program. The nominal institution receives support from its three pillars, regulative, cognitive, and normative, which are in turn nurtured by carriers, e.g. structure and activities. For Scott, each pillar offers and carries its own type of legitimacy. Regulative legitimacy generally flows from the formal rules; cognitive legitimacy for businesses usually stems from rational efficiency; and, normative legitimacy primarily emanates from the right behavior. Though Scott's conception of an institution is distinct and more refined than that of DiMaggio and Powell, the institutional overlaps are clear. In addition, his perspective on legitimacy appears to be consistent with Suchman's (1995) comprehensive synthesis of the organizational literature on legitimacy. The latter's "three primary forms of legitimacy," pragmatic, cognitive, and moral equate roughly, but more broadly, to the legitimacies of Scott's three pillars. More importantly, Scott's emphasis on three pillars with three distinct types of legitimacy contributes to a metaphorical appreciation of institutional legitimacy as a construct whose strength will vary depending on the pillar(s) supporting it.

By utilizing an expanded notion of institutional pillars with distinct types of legitimacy, an evaluation of organizational routines becomes clearer. Such an evaluation brings into light the multi-faceted concept of legitimacy that under girds an institution. It allows us to see that legitimacy for MNC control practices (neo-dependency) in emerging-economy subsidiaries is not just a question of the cognitive pillar and transaction efficiency as espoused by Williamson. It is also an issue for the normative pillar where the difficult question of rightness can be raised about the legitimacy of an institutional practice. By raising the question of rightness, it brings into the foreground critical points of view that will cause additional questions to be asked about the formal rules of the regulative pillar that supports such a 'doubtful' institution. Following North's thinking, this emerging skepticism (see Dunning's edited volume, 2003, regarding global capitalism) shines considerable light on the enforceable rules of the sovereign because it

is the sovereign that grants regulative legitimacy. In a democratic government, which Mexico now has (Krauze, 2006), those rules are subject to the elected representatives of the voters, who now have a say in matters of institutional legitimacy. Thus, an efficient MMP, to be fully legitimate, needs MNC cognitive acceptance, voter normative acceptance, and elected representative regulative acceptance. This idea that legitimacy will have varying degrees of acceptance or strength is discussed by Suchman (1995: 585) who notes, “...frictions among pragmatic, moral, and cognitive considerations seem most likely to arise when larger social institutions either are poorly articulated with one another or are undergoing historical transitions.” As noted below, such frictions clearly exist in the case of NAFTA and the MMP given the inherent contradiction between the two international institutions⁶.

Though there now exist some 2800 maquilas in the MMP with more than one million employees, that size does not necessarily render it fully legitimate. Focusing just on the normative pillar, in a recent critique of administrative science, Hinings and Greenwood (2002) raised the fundamental question about legitimacy—legitimate, or right, for whom? Too often in the past fifty years, the question has been defensively answered as legitimate for business vis-à-vis the cognitive pillar and rational efficiency. Hinings and Greenwood have contested that answer and signaled that in the future legitimacy must be given broader consideration through the use of more comprehensive and better integrated frameworks⁷. In line with their thinking, we propose that legitimacy can be viewed simultaneously as 'narrow', labeled organizational legitimacy, and 'broad', termed societal legitimacy. The former has been discussed above, and the latter is reviewed next.

A scholarly presentation outlining a broader framework for legitimacy can be found in Jost and Major (2001). In an edited book, they reveal and discuss the concept of societal legitimacy from its roots in antiquity to its current status in academic research looking at social behavior across multiple settings. Though insightful, their effort was not intended for those of us who study business organizations in emerging economies. Nevertheless, their book does have a broad section on Institutional and Organizational Processes of Legitimation, which is instructive. Elsbach (2001) contends that organizational legitimacy resides primarily in the minds of relevant stakeholders. Their perceptions of legitimacy are based on a universal appreciation for fairness. In her thinking (influenced by detailed studies of organizational crises), the responsibility for being perceived as fair

⁶ There is an inherent contradiction between a free trade area like NAFTA and a free trade zone or export processing zone, which the MMP represented, being located in the same geographical space. From a free trade perspective, the latter is totally redundant to the former. Thus, the Mexican negotiators of NAFTA agreed to eliminate the MMP by the year 2001. As we have indicated, the Program had always had its strident critics; thus, the Mexican trade negotiators apparently saw little reason to keep it in place given its 'uselessness' within NAFTA. However, the Mexican maquiladora associations did not see it as useless (it exempted them from income taxes), and they have prevailed in the political wrangling that has kept the Program alive, and once again expanding in employment numbers.

⁷ We have selected an institutional legitimacy framework to examine questions about the neo-dependency of MNC practices in emerging-economy subsidiaries. Other frameworks could have been used. For example, Alexander, et.al. (1987) developed a value framework for evaluating the social impact of MNCs across countries. The stated purpose of their framework was to clear up much of the confusion between the modernization and dependency schools about the impact of MNCs upon national societies.

belongs with the organization, which should manage its legitimacy (a standard, though questionable position, taken by many management scholars). To do that, it must deal with how it is perceived, i.e. as rational and/or as understanding in its exercise of fairness. Organizational legitimacy, if it is to be gained and held, must recognize and manage both these characteristics if it is to overcome stakeholder questions and doubts about it.

Tyler (2001) expands on this dual connection between legitimacy and fairness by expounding on the notion of procedural justice—the institutional application of due process to societal decisions. He makes a strong point that fairness is not about perceptions of distributive justice with equitable outcomes for all. Instead, it resides in the consistent application of procedural justice by authorities and institutions. Its application, if deemed successful, should not result from “command and control strategies.” Such approaches generally fail according to Tyler. The most recent research on legitimacy indicates that it is perceived as fair when people, the subjects of institutional decision-making, feel respected by, and hence identify with those making the decisions. This identity results in respect for and obliging loyalty to the institution and its decision makers who are more likely to be perceived as fair. As Tyler states (2001: 419), “...it is feelings of obligation (i.e., of what one ought to do) that are central to legitimacy.” In his research of U.S. citizens and their perceptions of legitimacy for the U.S. Congress, the variable that far exceeds all others in its explanatory power of institutional legitimacy is the one labeled *quality of treatment*, that is, treatment with respect.

More specific to emerging nations, The World Bank (2002: 6-7) has examined the complex issue of institutional legitimacy within the economic context of emerging economies and has noted that “*the balance between markets and state power, and between business and social interests, is a delicate one in the course of institutional development.*” Achieving this balance is not easy and requires considerable skill in developing effective institutions that necessarily include internal enforcement mechanisms. In other words, institutional legitimacy for society requires the judicious application of power in the balancing of interests and the enforcement of rules. Otherwise, an imbalance will arise and provide a solid basis for perceptions of illegitimacy.

Thus far, our perspective on institutional legitimacy has been rooted in the economics and sociology disciplines; nevertheless, other social scientists, especially in political science, also view it as a touchstone for testing institutions. Writing about the legitimacy of actions taken by nations, Tucker and Hendrickson (2004: 18) have espoused themes similar to those reviewed above. They wrote—

“Legitimacy arises from the conviction that state action proceeds within the ambit of law, in two senses: That action issues from rightful authority, that is, from the political institution authorized to take it; and second, that it does not violate a legal or moral norm. Ultimately, however, legitimacy is rooted in opinion, and thus actions that are unlawful in either of these senses may, in principle, still be deemed legitimate. That is why it is an elusive quality. Despite these vagaries, there can be no doubt that

legitimacy is a vital thing to have, and illegitimacy a condition devoutly to be avoided."

To summarize, our viewpoint on institutional legitimacy is an integration of what others from various disciplines have noted about this concept. It should not be viewed as a unitary phenomenon; it is much more complicated than that. At a minimum, an institution rests on three pillars—the regulative, the cognitive, and the normative—each with its own distinct flavor of legitimacy. In addition, each legitimacy flavor has its own particular way of being perceived by the diverse stakeholders in a national society. As implied below, the perceptual qualities of particularity and diverseness complicate judgments about legitimacy.

ECONOMIC DEVELOPMENT AND VERTICAL LINKAGES THE CASE OF MEXICO'S MAQUILAS

From the broader Mexican perspective, both the MMP (created in 1965) and NAFTA (established in 1994) are societally legitimate if they contribute to national economic development—an obvious and often stated desire by Mexican political and business leaders. This same broad desire across developing nations is underscored by Dunning's **Making Globalization Good** (2003), which repeatedly emphasizes that global capitalism now suffers from illegitimacy due to serious deficiencies that put its long-term continuation as the dominant economic paradigm for the earth in jeopardy. As Stiglitz notes in his chapter (2003), one of the major problems with past development efforts has been the creation of employment within enclaves or projects, which can be subject to charges of illegitimacy. Enclaves can be viewed as economic endeavors (often showcase impressive) with links to a developed economy(ies) but with very limited linkages into the developing nation itself. In essence, there is a lack of vertical linkages, for example, between the foreign subsidiaries in an export processing zone and the domestic producers of raw materials and the national buyers of finished components. Enclaves may create employment and provide large, modern exemplary facilities in a developing nation, but they do little to stimulate and create value-added within the national economy, outside their limited geographical space.

In terms of national economic development, the requisite need for legitimate vertical linkages with their accompanying domestic value-added has been noted and discussed by numerous writers with a development perspective. In a critical **Trade and Development Report** (UNCTAD, 2003), the lack of vertical linkages and technology development in countries participating in production-sharing programs receives special attention due to the slowdown in the value added from many of these countries. The importance of domestic value added to national economic development has been highlighted by Gereffi (2003) in a United Nations publication entitled— "The Global Apparel Value Chain: What Prospects for Upgrading by Developing Countries." In the context of the apparel-textile industry, the countries that have advanced the most economically during the past fifty years, i.e. the East Asian nations, are those which captured an increasing amount of the value added within their own domestic industry.

Through national vertical linkages, they were able to move beyond being simply assemblers of clothing for the markets in the developed nations.

In a broader sense, the argument for domestic value added through national vertical linkages has also been made by many, e.g. Moran and Ghoshal (1999), Ocampo (2001), Sachs (2000), and Zanfei (2005). All contend that national economic development cannot occur without the availability of technology that enables national learning and innovation. The latter will require domestic business entities that can undertake new activities as suppliers and buyers to the MNCs. For this process to occur, the types of investments made in the local economy become crucial. As noted by UNCTAD (2000: 20)—

“There can be a significant economic difference between “high quality” FDI (with strong forward and backward links to the domestic sector, with a strong export orientation or with high skills or technology spillovers) and “low quality” FDI (with few linkages with the domestic sector and so on).”

In 1965, Mexico established its Border Industrialization Program (later renamed the Maquiladora Program) in order to foster economic development and employment growth along the Mexico-U.S. border—the initial export processing zone (EPZ). As such, it has evolved substantially as an institution over the years as we briefly note in the following sentences. It was predicated on (then evolved into) specific clauses in the U.S. Tariff Schedule (later, NAFTA, which stipulated the demise of the MMP in 2001) and on special rules (later, enforceable laws) promulgated in Mexico. The bi-national rules permitted U.S. materials (later, foreign materials) to enter Mexico (first along the border then throughout the whole country) without being subject to Mexican duties, to be assembled (later, manufactured and designed) in MNC-owned plants there, and then to be re-exported to the U.S. subject only to a U.S. duty on the value added in Mexico. By 2000, after thirty-five years of incremental changes (including the now permitted sale of maquiladora production in Mexico) and when the Program reached its zenith, there were more than 3800 registered maquilas employing 1.3 million people. Approximately half of Mexico’s exports to the U.S. now (2006) emanate from maquilas (the NAFTA stipulation never took effect due to Mexican government intervention); thus, many would judge it a success based on that single criterion. However, this single measure of exports is only an indirect measure of economic development—the original intent of the Program. It does not reflect vertical linkages or institutional legitimacy, in the broader sense, for the maquilas and their MNC parents.

The MMP, built around earlier Program rules purportedly designed to foment economic development in Mexico, has been implemented, nevertheless, by MNCs utilizing institutionalized routines that import in semi-finished materials and export out finished goods. Such strategic routines with their cognitive legitimacy for managers require subsidiary practices predicated on headquarters control and would, as specified by the normative GBS literature, result in a situation of neo-dependency for manufacturing units operating within an emerging economy like Mexico. Assuming that the latent construct of neo-dependency does exist in Mexican maquilas and that the rules-routines institution for the MMP still exists, we would expect to find low levels of economic

development when measured as established vertical linkages at the micro level. To reiterate, this predicted outcome ought to be present because the MNC with its global outsourcing strategy has relied on its subsidiary(ies) in the Mexican EPZ for firm-level enhancement while ignoring the establishment of vertical linkages and the broader legitimacy derived from national economic development.

To examine this likelihood empirically, a research project exploring maquiladora institutionalization (rules and routines) was begun in 1999 and finished in 2001 prior to the economic downturn in the United States and the Mexican maquiladora sector. In the above review and discussion of the GBS literature, there has been an implicit assumption of MNC homogeneity. For expository purposes, we have assumed that all MNCs with foreign subsidiaries are alike, i.e. operating with a similar degree of neo-dependency. Of course, that assumption is too simplistic. Based on the earlier work of Wilson (1992), and the more recent writings of Carrillo and Hualde (1997), we know that MNCs with maquilas do differ. They are not all equally dependent upon headquarters. The first generation of plants involved assembly operations following the specific orders of headquarters in the United States. Then in the 1980s, maquiladora plants started to appear that combined assembly with manufacturing. In the 1990s, some maquilas began to mix assembly with manufacturing and design & engineering. According to Carrillo and Hualde, maquilas can be categorized as first (assembly), second (manufacturing), or third (design & engineering) generation operations. The later generations are thought to be and arguably ought to be more independent in their operations than was the first. Both Wilson (1992) plus Carrillo and Hualde have indicated that higher generation plants should be more integrated into the Mexican economy. Such integration, i.e. vertical linkages with Mexican operations, is a direct indicator of economic development. By allowing for the possibility of this generation effect upon the institutionalized routines of MNCs with maquilas, we state our main hypothesis as:

H: Subject to the generation effect, maquilas will exhibit a low degree of vertical relationships with Mexican suppliers and buyers.

To test this hypothesis, a stratified, random sample of 36 maquilas from eight cities was selected using a structured interview method with the top manager at each facility⁸. Because the research was being funded by the State of Texas, the six principal border cities along the Mexico-Texas border were chosen along with two northern interior cities, Monterrey and Ciudad Victoria. The strata for the sample were the main maquiladora industries—automotive, electrical products, electronics, and textile-apparel. For data analysis purposes, electrical products and electronics were later combined into a single group. Ninety percent of the firms selected and contacted agreed to participate in the study. Comments were solicited from the manager about the planning methods, structures, and routines (indicative of the generation) practiced in each maquila. To

⁸ The first author received support for these efforts in 1999 by a University Research Enhancement Grant from the State of Texas and in 2001 by a grant from the Texas Center for Border Economic and Enterprise Development. He gratefully acknowledges their encouragement and assistance.

assess better this latter construct, a plant tour was requested at the end of each visit. In addition, data were gathered for each plant regarding its turnover rate, remuneration—both starting and average wages, and percentage of purchases from Mexican suppliers and sales to Mexican buyers. The data shown below for assessing the effect of maquiladora generation upon vertical linkages should be both valid and reliable. There is little reason to doubt the generation measure reported by the manager and verified in the plant tour, and the percentages for domestic purchases and sales were readily provided by the managers given that this is a statistic also reported to the Instituto Nacional de Estadística, Geografía, e Informática (INEGI) on a periodic basis. Finally, interviews were also conducted with local maquiladora association officials in order to understand the specific context for the plants in each maquiladora city.

To analyze the hypothesis, the rankings for vertical linkages between the maquilas and their Mexican buyers/suppliers are examined. The results from the maquilas which provided data on Mexican inputs and outputs are shown in Table 1 as numerical scores on the non-parametric Wilcoxon test. Traditionally, the linkages have been quite low (in the 5% range for the maquiladora population using INEGI's historical data). They are somewhat higher for the sample; however, and more importantly, there is a significant impact of maquiladora generation upon those linkages for this particular sample of plants. The more advanced, or later-generation, maquilas do link up more with Mexican firms.

This positive generational relationship with vertical linkages—an indicator of economic development—is substantial and significant. As generations increase within a maquila, the direct relationship with vertical linkages becomes apparent—higher generations beget greater in-sourcing and vice-versa. Thus, the hypothesis is supported for this sample of maquilas. Yet in terms relative to economic development, the degree of vertical linkages is quite low.

Table 1: Maquiladoras and Vertical Linkages with the Mexican Economy

Plant Generation	Maquiladora Inputs Score	Maquiladora Outputs Score
First Generation (n=14)	9.2	8.8
Second Generation (n=16)	13.4	13.4
Third Generation (n=6)	18.8	20.2
Wilcoxon Test	Significance at $p < .10$	Significance at $p < .05$

DISCUSSION AND CONCLUSION

As demonstrated above, the non-parametric statistical test supports the hypothesis and reveals the importance of maquiladora generations for increasing vertical linkages between the maquilas and Mexican firms. The significantly reduced level of vertical linkages in lower generation maquilas exposes the latent neo-dependency condition legitimated normatively by the global business strategy literature and indicates that maquilas with the most basic or first-generation routines contribute the least to Mexico's

economic development. Therefore, many of the maquilas in this study (39% are 1st generation, 44% are 2nd, and 17% are 3rd), when evaluated from the perspective of vertical linkages contributing to economic development, could be critically viewed as examples of MNC neo-dependency and weak contributors (see Figure 2) to Mexico's continued development. From the broader, societal perspective, such a judgment would then cast doubts on their institutional legitimacy and raise questions about their societal value.

To shed an optimistic light on this dilemma for outsourcing MNCs, we propose the following matrix to portray the potential contribution of MNC subsidiaries to national economic development in the emerging-market context of non-prominent nations. In Figure 2, we illustrate the contribution that outsourcing MNCs can make through the creation of later-generation subsidiaries and the formation of human capital. The latter, though not a construct developed and measured herein, is closely linked and crucially essential to the creation of third-generation maquilas. As originally espoused (Becker, 1964), human capital formation focused primarily on its development in the public domain, i.e. schooling and years of education. Nevertheless, more recently it has been considered as a phenomenon that also occurs in the private sector as a result of efforts from both the employee and the company. Miyamoto (2003) has discussed such efforts in terms of a Virtuous Circle that can occur from foreign direct investment. For example, we know of one maquiladora operator, specializing in complex engine components, that encourages and pays its employees to obtain advanced degrees. Though the education benefits the employee as much as the company, the latter feels strongly enough about this matter that it has based its human resource practices around knowledge management coupled with its third-generation operations.

Briefly, we reveal in Box 1 of Figure 2 the empirical finding that first-generation operations contribute only in a very shallow manner to vertical linkages and economic development. In Boxes 2a and 2b, we note that greater development contributions do flow from enhanced vertical linkages and human capital, but alone these two changes are incomplete in terms of maximizing economic development. It is only at the level depicted by Box 3 where we see the emergence of the third-generation stage with its significantly greater number of vertical linkages. This desired outcome results from MNC decisions to re-institutionalize their outsourcing operations in emerging economies. These institutional changes require new practices or routines vis-à-vis human capital formation and national vertical linkages. Though such changes assume a high degree of optimism about outsourcing, we believe they, being descriptive of third-generation maquilas, are harbingers for global or world-class operations in emerging economies *and* for national economic development via the MNC.

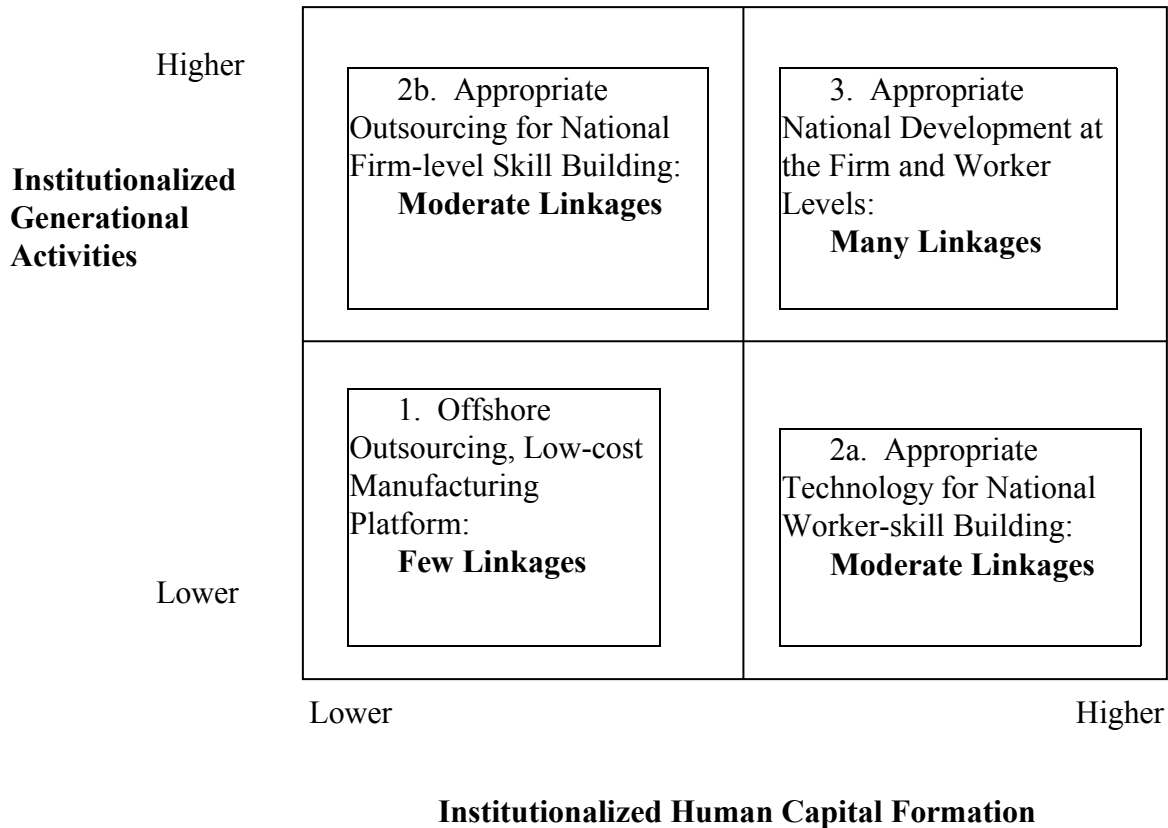


Figure 2. Re-Institutionalizing MNC Subsidiaries in Emerging Economies for National Economic Development Outcomes as Vertical Linkages

Though the positive institutional changes highlighted by Figure 2 seem warranted, a prudent observer may see them in a more pessimistic light. When we view institutions and their legitimacy across the full range of academic disciplines that encompass institutional theory, we note, as detailed in the above reviews, that legitimacy in the eyes of many business scholars and practitioners has been viewed in the narrow, organizational sense. We would argue that the fuller, societal view is much more representative of reality. Institutionalism is not confined, as the GBS literature assumes, to that narrow region amply covered by Williamson and transaction-cost economists. They have done good work, but other scholars, with valid research supporting their views, have shown that institutional legitimacy is multi-faceted and needs to be treated as such. In addition to its rational or economic face, it also has regulative or political and normative or societal faces. The latter are not mere facades and should not be ignored by MNCs. In addition, North’s notion of institutional lock-in deserves more attention as we consider the institutional rules-routines needing to be changed by MNCs in emerging economies.

To help legitimize those changes, the institutional ideas coming from The World Bank need to be given more attention and emphasis by institutional scholars who can provide the necessary normative legitimacy for business practitioners operating in emerging economies. With that legitimacy, practitioners can begin to utilize outcome indicators that reflect not only the efficiency of institutions but also their efficacy from a developmental perspective.

In conclusion, by utilizing an expanded notion of institutional legitimacy and then assessing it with both business and development indicators, we can more readily deal with the neo-dependency issue and the threat it poses. Given that it is an issue or threat, the results shown herein indicate that it can be addressed by MNCs willing to undertake changes in routines and practices, i.e. third generation maquilas or their equivalents in the more robust Asian countries. Whether it will be addressed is a question for practitioners to confront, but they (and some clearly are) must be aware that political leaders and voters in democracies, e.g. Mexico in July 2006, have undoubtedly been addressing the legitimacy question by asking legitimate for whom? Both the MMP and NAFTA were initiated and developed in a less democratic Mexico, i.e. before the election of 2000. Thus, they do suffer from a lack of normative and regulative legitimacy in a democratic nation (especially the MMP whose value was little appreciated by the Salinas administration when it agreed in the NAFTA negotiations to let the MMP be terminated in 2001). In this newer context, the long-term fate of maquila-like operations presents a real challenge, especially when considered in light of the recent reformist governments across the region—Lula in Brazil, Chavez in Venezuela, Morales in Bolivia, Kirchner in Argentina, Correa in Ecuador, Ortega in Nicaragua and the vitriolic closeness of the 2006 Mexican Presidential election—which though having seriously challenged the neo-liberal model of development have still not replaced it (Lyons, 2006). To address this new challenge effectively, business firms must be willing to accept fundamental changes in institutionalized practices. That, unfortunately, is easier to say than to do. Nevertheless, as already noted, numerous scholars have advocated this position. Though there are many reasons to doubt the likelihood of institutional change, it can be done. Perhaps, as suggested by Zanfei (2005) it should be mandated by governmental policy makers. A few maquilas have clearly shown that routines can be altered. It is not only a responsible change for industry to make, but it is also a responsible direction for future researchers to track if the challenges of neo-dependency and societal legitimacy are to be truthfully confronted.

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