Manag Int Rev
DOI 10.1007/s11575-017-0324-0

Management International Review

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RESEARCH ARTICLE

The Effect of Corporate Political Activity on MNC Subsidiary Legitimacy: An Institutional Perspective

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Received: 29 October 2016 / Revised: 21 June 2017 / Accepted: 3 August 2017

Abstract MNC subsidiaries engage in a variety of corporate political activities to gain legitimacy in the host country. Based on institutional theory, our study examines five types of strategies that MNC subsidiaries pursue to gain legitimacy in foreign markets. Using data from Australian subsidiaries of MNCs operating in different industries, and whose parents originate from 28 different countries, we find that mimetic isomorphism strategy has the strongest effect whereas information strategy has no effect on subsidiary legitimacy. The other three strategies, namely, financial, constituency building and relational have strong to moderate effects on subsidiary legitimacy. In addition, we show that multiple CPA strategies are essential and work together synergistically to contribute to the legitimacy of MNC subsidiaries. Our paper provides empirical support to the widely recognized need for MNC subsidiaries to engage in different types of CPA to legitimize their operations in diverse institutional contexts across the globe.

Keywords Institutional perspective · Corporate political activity · Legitimacy · MNC subsidiary

1 Introduction

Multinational corporations (MNCs) employ a range of market and non-market strategies to succeed and grow in international markets. In international business (IB) research, scholars largely focus on the market-related strategies of multinational firms (MNCs) and how these strategies deliver superior customer value and performance in competition with local and foreign firms. It is increasingly

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Published online: 21 August 2017

recognized, however, that MNC subsidiaries do not operate in a vacuum, "but in specific social, cultural, and political contexts" (Okhmatovskiy 2010, p. 1039). As MNC subsidiaries operate across diverse institutional contexts, they manage their broader external environments through institutional strategizing that are broadly referred to as non-market corporate political activities (CPA) (Marquis and Raynard 2015). Although the study of CPA has its origins in the political literature (e.g., Mitchell et al. 1997), increasingly, IB and management scholars acknowledge that institutional pressures affect MNC subsidiary activities and formally incorporate CPA strategies in theoretical models of organizational effectiveness (e.g., Blumentritt and Nigh 2002; Shirodkar and Mohr 2015b; Wan and Hillman 2006). The need for non-market activities to achieve MNC subsidiary goals is also growing in practice (Rodriguez et al. 2006), as illustrated by the following example of Amway in China:

> *Whereas a long-term focus under private-ownership helped Amway ride through years of underperformance in China, "just as important was Amway's ability to sell itself to officialdom. The firm's senior managers got to know regulators and informed them about the differences between pyramid schemes and established direct sellers … Amway (also) sponsored a fellowship that sent rising stars of the Communist Party to Harvard's Kennedy School of Government, with a handy stopover at Amway's headquarters in Ada, Michigan" (Economist* 2016*, p. 49*).

Similar examples of CPA by firms to gain favour from governments are found in developed countries, as indicated by the following quote in the context of the gambling industry in Australia.

> *… the (gambling) industry does not leave regulation to chance: it donates lavishly to both big political parties and to independent politicians. "This corrupts governance," argues Andrew Wilkie, an independent MP who instigated the attempt at federal regulation in 2012" (Economist* 2017*, p. 22*).

Prior CPA studies have drawn on different perspectives from various academic disciplines to focus on the environmental and firm level drivers of CPA (Getz 1997, 2002; Hillman et al. 2004). Although there is a good understanding of the drivers of CPA and the different types of CPA pursued by firms, relatively less attention is paid to the outcomes and the potential benefits of CPA (Getz 1997; Hillman et al. 2004; Ozer 2010). Empirical evidence regarding the relationship between CPA and firm performance is mixed and not always positive (Rajwani and Liedong 2015). This indeterminate financial outcome linked to CPA has mainly been attributed to its "unique strategic nature" (Hadani 2012). Over the years, studies have speculated that CPA leads to legitimacy, however, traditional CPA and IB studies have not paid sufficient attention to the issue of strategic use of CPA for shaping subsidiary legitimacy (Hillman and Hitt 1999; Hond et al. 2014; Nell et al. 2015). For example, whereas Luo (2001) recognizes the need for legitimacy, it does not tell us how firms should go about gaining it. Legitimacy, like market share, has to be earned through firm actions (Kostova and Zaheer 1999). Echoing the above, institutional theory posits that firms need to broaden their mandate beyond achieving superior financial and market-related performance, and focus on other non-financial goals such as legitimacy that are considered important for MNC subsidiary survival and success in host countries. Accordingly, our paper extends Luo (2001) and Kostova and Zaheer (1999) by showing empirically how the different types of CPA and their adaptation within the local environment support MNC subsidiaries in gaining legitimacy in the host country.

Legitimacy is defined as "a generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions" (Suchman 1995, p. 574). As legitimacy is a socially constructed perception of propriety about an entity such as a multinational firm, it is essentially "a conferred status" (Singh et al. 1986). Literature on legitimacy posits that obtaining the support and endorsement of external stakeholders is key to gaining legitimacy (Meyer and Scott 1983; Suchman 1995). Accordingly, conferring legitimacy does not occur spontaneously, but rather is an effect of social judgement by different stakeholders through conscious thought and attention via the institutionalisation process (Rueede and Kreutzer 2015). Certainly, in most countries, government remains the most influential stakeholder controlling critical resources and opportunities, and shaping the regulatory framework (Chan and Makino 2007; Hillman and Wan 2005). For that reason, by strategically engaging in CPA, MNC subsidiaries can successfully maintain positive government relationships and gain legitimacy to access vital resources, operate productively, and create value for the firm and its diverse stakeholders (Reast et al. 2013).

Since MNC subsidiaries are evidently of foreign origin, they face circumstances significantly different from domestic firms and have different priorities with respect to the strategic use of CPA as compared to their domestic counterparts in the host country (Wöcke and Moodley 2015; Zaheer 1995). To overcome the liability of foreignness, a subsidiary may seek to build positive perceptions of itself through a variety of legitimacy seeking actions, including CPA (Boddewyn and Brewer 1994; Nell et al. 2015; Suchman 1995; Wöcke and Moodley 2015; Zaheer 1995). For example, MNC subsidiaries often employ strategies intended to influence the public policy environment in a manner favourable to the firm (Baysinger 1984). However, competing in the public policy environment is not easy, as improper implementation of accepted practices can heighten tensions with the host government and society (Lawton et al. 2013; Rajwani and Liedong 2015; Wöcke and Moodley 2015). Another potential downside of subsidiary CPA is that it is more sensitive to ethical issues than market strategies, as the nonmarket setting has a murkier aspect where fraudulent ways can be the prevalent mode (Doh et al. 2012; Mantere et al. 2009; Rajwani and Liedong 2015). It has been observed in the non-market strategy literature that "institutional contradictions create a context where a particular nonmarket strategy may lead one stakeholder group to confer legitimacy to the firm but meanwhile may lead another group of stakeholders to withdraw its legitimacy" (Mellahi et al. 2016, p. 154). As CPA inevitably faces widely contradictory nonmarket and corruption circumstances and remains "unseen" (Hadani 2012; Windsor 2007), any public awareness of MNC subsidiaries' CPA involvement in a host country can raise ethical questions that can have negative repercussions on the reputational goals of the company. Thus, all else being equal, the need for MNC subsidiaries to seek legitimacy in host countries becomes more complex and controversial than for local firms (Hillman et al. 2004; Lux et al. 2011; Rajwani and Liedong 2015). Presented with such confounding institutional environment, it becomes evident that traditional CPA strategies alone may not be sufficient to attain legitimacy in a host country (Mellahi et al. 2016).

Accordingly, we extend the study of legitimacy with a neo-institutional (or institutional sociology) perspective that emphasises the need for isomorphism with established and prevalent practices or norms within the firms' institutional environments (Doh et al. 2012; Kostova and Roth 2002). From a neo-institutional viewpoint, societal actors have discernible influences on firms' conduct (Doh et al. 2012), which compels firms to pursue adaptive strategies (De Villa et al. 2015) and mimic the activities of competitors in the host nations. By adopting a configuration of multiple adaptive and transformative strategies, subsidiaries both adapt to and shape the institutional environment of host nations. Such an integrated approach enables subsidiaries to engage in conduct that constitutes "appropriate" behaviour as well as facilitates engaging with key stakeholder groups to influence what constitutes "appropriate" behaviours as the criteria for legitimacy (Greenwood et al. 2011; Scott 2014). As the mechanisms underlying sociological institutionalism are fundamentally similar in both organizational and political fields (Beckert 2010), subsidiary CPA strategies are "inextricably and inexorably linked to traditional strategic rationales and approaches" (Doh et al. 2012, p. 23). Against this background, the key research question that we aim to address in this study is—how do the various CPA strategies of MNC subsidiaries contribute to the goal of achieving MNC subsidiary legitimacy.[1] To the best of our knowledge, no study explicitly tests the legitimacy effect of diverse CPA strategies.

Our paper makes three theoretical contributions to the CPA literature in international business. One, we contribute to the organisational sociology perspective of institutional theory by showing how subsidiary CPA can manage relationships with relevant stakeholders in host nations to gain an important non-financial outcome for MNC subsidiaries, namely, subsidiary legitimacy. In particular, our study extends the CPA literature in IB by examining the effect of both adaptive and transformative approaches to gain legitimacy (Dorobantu et al. 2017). Two, we discuss the concepts of essentiality versus equifinality of CPA strategies and demonstrate with examples how the different CPA strategies are complementary and work synergistically to reinforce each other in enabling the subsidiary to gain legitimacy in host countries. Three, our study contributes to the debate on optimal distinctiveness (Zhao et al. 2017). That is, the need for MNC subsidiaries to reconcile the contradictory prescriptions of mimetic isomorphism in institutional theory versus innovation in strategic management (Birkinshaw and

[1] For simplicity in exposition, and to avoid confusion with the different labels and models of CPA that (a) theoretically (but not empirically) distinguish between strategies and approaches (Hillman and Hitt 1999), or (b) use the terms "strategy" and "approach" interchangeably (Dorobantu et al. 2017; Luo and Zhao 2013), we refer to the five CPA strategies/approaches that we examine in our paper under the common umbrella term of CPA.

Hood 2001; DiMaggio and Powell 1983; Kostova et al. 2008; Kostova and Zaheer 1999).

Methodologically, we test both individual and joint effects of different types of CPA with primary data from MNC subsidiaries operating in different industries within a single country, Australia, a geographic region that has remained unexplored (Rajwani and Liedong 2015). Moreover, we collect the data through a large-scale mail survey, a method that is infrequently employed in empirical CPA studies (Rajwani and Liedong 2015). In addition, while the endogeneity bias has been acknowledged in IB research (Reeb et al. 2012), our paper is one of the very few to test it in the context of CPA in IB (e.g., Shirodkar and Mohr 2015a). Finally, from a managerial perspective, we offer a larger practical toolkit for MNC subsidiary managers to carry out their legitimacy enhancing activities, while managing the complexities and contradictions of innovation and imitation in market and non-market activities respectively.

The remainder of the paper is structured as follows. In the next section, we draw on institutional theory to develop hypotheses regarding the effects of different types of CPA strategies on subsidiary legitimacy. Next, we discuss our method including data collection through a large-scale mail survey of MNC subsidiaries operating in Australia, the measures we use to operationalize our constructs, and the results of our analysis using multiple regressions. Finally, we discuss our results highlighting the paper's contribution to CPA research and practice and suggest some outstanding issues for future research.

2 Theory and Hypotheses

Institutional theory explains why MNC subsidiaries, facing institutional unfamiliarity in host countries and stigma of foreignness, are motivated to act in socially responsible ways (Kostova and Zaheer 1999; Zaheer and Mosakowski 1997). By engaging in activities that assist local communities, subsidiaries can gain legitimacy which becomes significant in an organisation's history as it can reduce regulatory stringency and intensify institutional support (Kostova and Zaheer 1999; Oliver 1996). According to Scott (1995, p. 45), legitimacy is "a condition reflecting cultural alignment, normative support or consonance with relevant rules or laws". Thus, legitimacy reflects the opinion of key stakeholders who observe the firm's behaviour and assess if its presence in society is socially desirable and aligned with established institutional norms, values and beliefs (DiMaggio and Powell 1983; Suchman 1995). In the context of MNC subsidiaries, the two important stakeholders who accord legitimacy are: (1) government actors who establish, change and enforce relevant rules and laws, and (2) societal and community members who uphold cultural norms of conduct (Young and Makhija 2014). With MNC subsidiaries operating in diverse institutional contexts and exposed to heterogeneous stakeholder expectations, subsidiaries aim to both abide by and shape/reshape the institutional environments for establishment and maintenance of legitimacy (Hillman and Wan 2005). Thus, firms adopt a range of strategic responses to address key stakeholders' expectations and influence their perceptions about their legitimacy (Oliver 1991; Scherer et al. 2013; Zhao et al. 2014). In this study, we examine the effects of five CPA strategies on subsidiary legitimacy, namely, financial incentive, information, constituency building, mimetic isomorphism and relational.

Based on the logic of institutional change, institutional theory suggests three types of legitimacy-seeking strategies for MNC subsidiaries, namely, financial incentive, information, and constituency building (Dorobantu et al. 2017; Hillman and Hitt 1999; Luo 2001). The *financial incentive strategy* aims to directly sway policy makers with incentives such as financial contribution to political parties or candidates. Subsidiaries following the *information strategy* target political decision makers by initiating discussion at the national, state, and local level, and furnishing information on research results and viewpoints on reports to government. When adopting the *constituency building strategy*, subsidiaries engage in grassroots mobilisation, public relation or advocacy advertising in the media, and press conferences on public issues, with the aim of exerting indirect pressure on policy makers through the support of the general public and voters.

In addition, based on the idiosyncratic social and cultural expectations within a given institutional field, the normative logic of the neo-institutional tradition in institutional theory requires MNC subsidiaries to respond to institutional pressures by following a mimetic isomorphism strategy to gain legitimacy (Barreto and Baden-Fuller 2006; Doh et al. 2012; Oliver 1997). *Mimetic isomorphism strategy* refers to the tendency of organisations to model themselves on other organisations "when goals are ambiguous, or when the environment creates symbolic uncertainty" (DiMaggio and Powell 1983, p. 151).[2] Institutional theory suggests that organisations within the same institutional field overcome the ambiguity "between acceptable and unacceptable behaviour" by adopting similar strategies to achieve legitimacy (DiMaggio and Powell 1983; Meyer and Rowan 1977; Scott 1995). Taking into account the ethical issues in CPA and the uncertain environment, it is especially important for MNC subsidiaries to pursue an adaptive approach to CPA through mimetic isomorphism strategy to gain legitimacy (Dorobantu et al. 2017; Hillman and Wan 2005; Lawton et al. 2013; Wöcke and Moodley 2015).

Although the idea of mimetic isomorphism strategy for legitimacy is intuitively appealing, scholars query the empirical usefulness of legitimacy given its characteristics of being a highly abstract construct that describes organisational outcomes instead of being examined as an empirical phenomenon in its own right (Deephouse and Suchman 2008; Suddaby et al. 2017). On the other hand, institutional researchers argue that while new components of legitimacy are conceptualised, few are tested empirically (Deephouse and Suchman 2008; Suddaby et al. 2017). We believe our empirical validation of the usefulness of mimetic isomorphism to gain legitimacy provides a stronger foundation for the neo-institutional view of institutional theory.

[2] Although DiMaggio and Powell (1983, p.150) consider their isomorphism "typology is an analytic one; the types are not always empirically distinct", our paper empirically tests the relationship between subsidiary isomorphism strategy and legitimacy within the broader CPA framework.

Finally, the *relational strategy* of developing relationships over time with policy makers is considered a good investment, and which becomes helpful when any issues arise in relation to MNC subsidiary operations in the host country (Hillman and Hitt 1999; Keillor and Hult 2004). Within a given institutional environment, long-term collaborative engagement with government stakeholders can lead to creating trust “between the suppliers and demanders of public policy” (Hillman and Hitt 1999, p. 829). In this way, through an adaptive relational approach to CPA, MNC subsidiaries can be seen to be part of the social structure, affirming their place in the institutional field to gain legitimacy (Doh et al. 2012; Dorobantu et al. 2017). Hillman and Hitt (1999) also observe that the long-term political relational strategy is not extensively examined in the CPA literature, perhaps due to its potential unethical association.

Overall, our conceptualisation of the five strategies is based on the premise that the IB situation is complex where both the ”distinct” types of CPA strategies under the Hillman and Hitt (1999) model as well as the adaptation strategies within the host environment need to be incorporated within a single integrated model to comprehensively examine the effects of different types of CPA on subsidiary legitimacy. Our five CPA strategies encompass both transactional (in response to specific or salient issues) as well as relational (across issues and over time) approaches of CPA, and which have a direct influence on subsidiary legitimacy, as hypothesised below.

2.1 Mimetic Isomorphism Strategy

MNC subsidiaries are subject to host nation’s socio-political and cultural environment pressures due to the idiosyncratic local conditions in which they operate (Rosenzweig and Singh 1991; Westney 1993). While all firms are exposed to the influence of a host country’s particular institutional environment, foreign subsidiaries are subject to more challenges in a host country compared to domestic firms due to their “liability of foreignness” (Hymer 1976; Zaheer 1995). When confronted with such institutional constraints, institutional theory suggests that organisations are motivated to pursue social adaptation for gaining legitimacy (DiMaggio and Powell 1983). For MNC subsidiaries, variations in institutional environments add uncertainty in foreign operations, which in turn affects their strategy decisions. In the face of uncertainty, a core mechanism for institutional adaptation is mimetic isomorphism, that is, copying or following other similar/large/successful organisations (Haverman 1993). Drawing on this logic, institutional theory suggests that mimetic isomorphism in political activity is one way for MNC subsidiaries to obtain favourable public opinion and legitimacy.

Subsidiaries face hurdles from political institutions such as changes in the identity of policy makers, or amendment to policies in response to CPA by host country competitors. When such policy changes are of concern to MNC subsidiaries, these firms face ambiguity about political participation in the public policy domain. Due to their foreign ownership, subsidiaries fear criticism and controversy if perceived to be participating in the politics of the host country (Hansen et al. 2004; Walker 2012). There is uncertainty in the choice of political behaviour that a subsidiary should adopt, wherein its behaviour is viewed to be legitimate (Kostova and Roth 2002). In such situations, looking at actions of others can provide clues about possible strategic choices (Bonardi and Keim 2005). Also, mimetic behaviours strengthen the importance of social processes as it stimulates the use of social comparison as the basis for making decisions (Haunschild and Miner 1997). Thus, drawing on the above, the logic of mimetic isomorphism indicates that subsidiaries are likely to favour copying and adopting the contemporary CPA strategies of their successful competitors and reflexively enacting them as their own, as widespread adoption essentially legitimises such behaviours (DiMaggio and Powell 1983; Westphal et al. 2001). In other words, imitating the political strategies of local competitors provides a simpler pathway for foreign subsidiaries to gain legitimacy in the host country. Hence, it is expected that subsidiaries are more likely to resort to mimetic CPA behaviours to attain legitimacy, as this reflects conforming to accredited organisational behaviour of interest representation in public policy making domain. It is therefore hypothesised that:

H1: Mimetic isomorphism strategy has a positive effect on subsidiary legitimacy.

2.2 Relational Strategy

In addition to the strategies that deliver immediate gain in legitimacy, MNC subsidiaries also engage in long-term strategies that help the subsidiary in moving up the legitimacy trajectory. These involve building relationships with key decision-makers in the public policy domain, so that the subsidiary can tap into the contacts that are already in place when the need arises (Hillman and Hitt 1999). Whereas Luo (2001) argues that the need for relationships is more salient in an environment where formal institutions are weak, we believe relationships are valuable universally in gaining trust and credibility and building legitimacy for the MNC subsidiary irrespective of the institutional characteristics of the host country. However, arguably, the importance of relationships may vary between weak and strong institutional contexts. Hillman & Hitt (1999, p. 829) theorise that long-term collaborative engagement with government stakeholders can lead to creating trust "between the suppliers and demanders of public policy".

Engagement between the firm and external stakeholders occur at multiple levels in the MNC, including both individuals and groups in the firm, and with people located in the subsidiary as well as the headquarters of the MNC. It is also important that the subsidiaries engage with public policy across a broad range of areas that are of interest to the political establishment including health, education, employment, training, arts, culture, sport, infrastructure, etc. (Kim 1988; Luo 2001). Active participation in public policy across diverse domains can provide subsidiaries with multiple opportunities to develop relationships over time. It is naturally expected that policy makers and "regulators will favour those firms that appear to want to work with them and can be seen to be professional and reliable" (Coen and Willman 1998, p. 36). Thus, through relational strategy, subsidiaries can facilitate their on-going involvement in the public policy arena, obtain the support of key stakeholders, and enhance their legitimacy in the host nation (Wang and Qian 2011). On the other hand, there could be potential downsides of relational strategy if it is viewed as unethical by some constituents in society. However, to the extent that these activities are open, legal and transparent, their overall impact is likely to be positive. We therefore hypothesise that:

H2: Relational strategy has a positive effect on subsidiary legitimacy.

2.3 Financial Incentive Strategy

Political parties and politicians require dependable sources of finance for election campaigns (Schuler et al. 2002). Direct contributions to political parties or decision makers can consolidate subsidiaries' position with key political actors as credible and trustworthy suppliers of necessary funding (Schuler et al. 2002). CPA literature also suggests that soft money contributions can aid in swaying legitimacy in favour of donors and help mitigate any negative public image (Alakent and Ozer 2014). By appointing individuals with direct political experience as managers, directors, consultants, or hiring political decision makers' relatives (Getz 1993; Hillman et al. 1999), subsidiaries can build goodwill among a diverse group of external stakeholders who can be effective allies in the social construction process of projecting a positive image about the subsidiary. Additionally, developing connections with the host government by offering pro bono services can facilitate dealing with the regulatory bodies as well as understanding and responding to both the cognitive and normative domains of the institutional environment. Such activities, from an institutional viewpoint, can help in building social legitimacy.

However, an alternative viewpoint holds that financial contributions to political parties and election campaigns can create close political connections between firms and public policy decision-makers leading to undue and unfair influence in a country's politics and policies (Claessens et al. 2008). IB literature acknowledges that political connections and preferential access to finance is unethical and related to CPA corruption that can distort honest public debate on important policy issues, thereby diverging from the public interest (Chen et al. 2010). While political financing can be a matter of concern for MNC subsidiaries, it may be unavoidable due to host country institutional or competitive pressures (Lawton et al. 2013). Notwithstanding these issues, as our opening examples illustrate in the context of Amway in China and the gambling industry in Australia, the reality of firms contributing to all political parties to gain political legitimacy and patronage is widespread in both developing and developed countries. To the extent these activities are carried out legally, openly and transparently, the positive effects are likely to outweigh the downsides of financial incentives. Overall, therefore, we argue that by managing their key stakeholder's requirements and/or demands through financial incentive strategy, MNC subsidiaries can create linkages with influential public policy makers and rely on their support to establish or enhance subsidiaries' acceptance in the host country. The above discussion leads to the following hypothesis:

H3: Financial incentive strategy has a positive effect on subsidiary legitimacy.

2.4 Information Strategy

In the non-market political arena, policy makers generally operate in uncertain environments and need reliable and useful information about the policy desires of their constituents (Schuler et al. 2002). Elected politicians and policy makers come from different backgrounds, and listen to many points of view before making a decision. At the same time, they need timely information. Therefore, in dealing with government, where varied, incomplete, self-serving or even distorted information exists, MNC subsidiaries seek to educate policy makers and officials by providing reliable and sought after information. In this way, the subsidiary can be perceived by policy makers as credible and trustworthy. Such exchanges between subsidiaries, policy makers and government officials are pivotal in earning organisational legitimacy from one of the important stakeholders in the host nation.

Information strategy is essential for MNC subsidiaries in providing policy makers with informed arguments that are based on studies commissioned or research conducted by the firm or government. The depth and quality of knowledge received by policy makers from the subsidiaries can be utilised for constructive policy making. Subsidiaries that provide quality information to policy makers, e.g., political, technical, or economic assessment, are likely to be more 'heard' and considered credible (Hillman and Hitt 1999). In the process, subsidiaries can gain reputation as being valuable and reliable sources of information (Schuler et al. 2002). With institutional theory viewing governments as principal actors in establishing norms through coercive or regulatory methods (DiMaggio and Powell 1983; Oliver 1997), and with legal constraints being a crucial source of the legitimisation of organisation (Halliday et al. 1993), MNC subsidiaries can employ information strategy to communicate and convince policy makers of their adherence to the regulatory framework and thereby establish and enhance their legitimacy. Thus, MNC subsidiaries have the motivation to engage in information strategy to enhance their acceptance by their salient stakeholder that has the power to confer legitimacy, and which could favourably affect the subsidiaries in the regulatory domain as well as in the social sphere (Kostova and Zaheer 1999). It is therefore hypothesised that:

H4: Information strategy has a positive effect on subsidiary legitimacy.

2.5 Constituency Building Strategy

MNC subsidiaries face multiple stakeholders that confer legitimacy. As legitimacy is socially constructed, "created subjectively" but "possessed objectively" (Suchman 1995, p. 574), MNC subsidiaries have to address various stakeholders' expectations in a host country. From a stakeholder perspective, with some being more important than others, managing stakeholder heterogeneity and balancing their interests are key to subsidiaries being conferred the legitimacy status by multiple societal actors (Mellahi et al. 2016; Scherer et al. 2013). To manage this process efficiently, subsidiaries often respond to the "consistency of societal expectations" (Scherer et al. 2013). Literature on legitimacy states that organisations both align with external societal expectations as well as influence the perceptions of stakeholders to create, maintain or redeem legitimacy in a host nation (Scherer et al. 2013).

Constituency building involves efforts to educate and inform constituents at the grassroots level on local issues and encourage people's participation in resolving these issues. By mobilising constituent stakeholders through education programs on issues, subsidiaries can develop goodwill and a base of dependable supporters. Further, since policy makers and elected officials listen and respond to grassroots feedback to get elected or to serve the constituents' interests (Lord 2003), favourable social judgement towards MNC subsidiaries by grassroots constituents who possess the power to confer legitimacy can translate into conferring of legitimacy by all stakeholders. Strategies to influence the perception of stakeholders include creating a positive public image through public relations advertising, or by varying or controlling the views of key stakeholders such as policy makers through press conferences on public policy issues and advocacy advertising. By pursuing the constituency building strategies of advertising campaigns and strategic public relations, subsidiaries can create a positive reputation among various stakeholders including continued patronage, as well as alter any unfavourable perceptions in the eyes of the "beholders of legitimacy" (Zimmerman and Zeitz 2002). From the above discussion, we hypothesise that:

H5: Constituency building strategy has a positive effect on subsidiary legitimacy.

In sum, following institutional theory, we propose five strategic pathways for MNC subsidiaries to gain legitimacy in host countries, namely, mimetic isomorphism strategy, relational strategy, financial incentive strategy, information strategy, and constituency building strategy. We next discuss the method we use to test our hypotheses.

3 Method

3.1 Sample and Data Collection

Our sample of MNC subsidiaries is drawn from one host nation, Australia, a context that remains unexplored in CPA studies (Rajwani and Liedong 2015). As per the 2016 World Investment Report, Australia ranks among the top 20 host countries for foreign direct investment (FDI) in 2015. Even during the period 2008/2009, when the data was collected, Australia's global FDI inflows increased although there was an overall downward trend of FDI inflows across the globe due to the global financial crisis (World Investment Report, 2009). These statistics signify that Australia, with a mid-size, open economy having significant FDI inflows, is an important and appropriate country setting to investigate MNC subsidiary CPA. Additionally, by selecting a single host country context, we are better able to test our theory of MNC subsidiary CPA and legitimacy after controlling for extraneous factors that may add noise to our data (Amine and Cavusgil 1986). We capture diversity in our focal variables by (a) collecting data from MNC subsidiaries operating across a broad cross-section of industries including manufacturing, wholesale, and other services, and (b) examining MNCs with parent headquarters located in 28 different home countries (see Appendix 2). Our sample thus provides a new perspective on the CPA phenomena, as prior studies are mostly based on US-origin MNCs or US-based MNC subsidiaries. Appendices 1 and 2 include the distribution of our sample by industry and by home country of the parent headquarters respectively.

We used a self-administered questionnaire survey to collect data from top executives of MNC subsidiaries operating in Australia, including Chief Executive Officers, Managing Directors, Directors, Presidents, General Managers and Head-External Affairs. Such an approach is consistent with research on strategic management and CPA that uses single informants (e.g., Aragón-Sánchez and Sánchez-Marín 2005; Wan and Hillman 2006). Nearly 80% of the survey responses are from the top executives, with the remaining respondents holding senior managerial positions such as Public Relation Manager, Marketing Manager, Commercial Development Manager or Project Manager. The top and senior management positions of our survey respondents gives us confidence that our data is from interested and informed participants and of a high quality. The mean age of our respondents is 48 years and their average experience in the subsidiary is 9 years, which further suggests that the respondents have a relatively good understanding and knowledge of their subsidiary's strategy and are in a position to provide valid and reliable responses to the survey questions.

The responses to questions were mainly based on five-point Likert scales. Questionnaire items were derived from the literature (see Appendix 3 for details of the sources of the items used to measure the constructs in our extended theoretical model of CPA). The questionnaires were mailed with an explanatory cover letter to 3330 MNC subsidiaries operating in Australia. The list of MNC subsidiaries was obtained from a Dun and Bradstreet database and includes all identified MNC subsidiaries operating in Australia, therefore minimising potential bias. Excluding the subsidiaries that were unwilling to participate and/or for which the questionnaire was not applicable, the survey sample was reduced to 2776. The final number of returned responses was 217, of which 3 were rejected due to missing responses. The net usable sample size is 214, representing a response rate of 7.7%, which is comparable with that reported in several published studies including Dawson and Dickinson (1988) and Dikova (2009), and expected in large mail surveys with response rates of 5–10% (Alreck and Settle 1995; Stock et al. 2000). A recent CPA related study by Shirodkar and Mohr (2015b) has a similar response rate to ours (n = 105, 10.24%). Interestingly, their study was also open ended without prior contact with or endorsement by industry associations. In contrast, we speculate that the high response rate in Hillman and Wan (2005) (n = 169, 35% of the corporations sampled and 22.5% of the subsidiaries) was due to the fact that "survey endorsement came from the American Chamber of Commerce (AmCham) EU

Mission in Brussels, Belgium, to maximise response rate" (Hillman and Wan 2005, p. 329).

Further, from a qualitative perspective, the low response rate may also be due to the sensitive nature of the information sought from the MNC subsidiaries, as indicated by comments from the subsidiaries who responded without completing the questionnaire such as "data too confidential to release", "the level of detail could not be provided", and "rather not disclose the information". Our experience of data collection is in line with Lawton et al.'s (2013, p. 100) observation that "empirically it is not a straightforward process" as CPA is a "sensitive and often discreet activity and firms are justifiably reluctant to provide access to information on their endeavours. There are therefore significant practical limitations to data acquisitions".

We carried out a number of statistical analyses to test if our sample is representative of the population of MNC subsidiaries in Australia. Following Dikova (2009), we carried out t-tests comparing the mean age, size, and sales of the responding subsidiaries with a random sample of subsidiaries in the population. The results with three sets of random samples of the same size as the responding sample show no statistical difference between the two groups. Second, we compared the industry distribution of our responding subsidiaries with that of the subsidiary population in Australia. All industry sectors in the subsidiary population are represented in our response sample (see Appendix 1). Thus, the analyses indicate that our MNC subsidiary sample adequately represents the population of MNC subsidiaries in Australia. Additionally, of the 214 usable subsidiary responses, 208 are from wholly-owned MNC subsidiaries and six have missing data on ownership. Thus, there is practically no variance in our sample arising from ownership characteristics.

3.2 Measures

3.2.1 Dependent Variable

Our dependent variable is subsidiary legitimacy. This construct reflects the extent to which subsidiary conduct is perceived to concur with society's expectations for business behaviours and outcomes (Johnson et al. 2006; Wood 1991). Based on the earlier works on legitimacy (such as Dowling and Pfeffer 1975; Ryan et al. 1987; Singh et al. 1986; Zimmerman and Zeitz 2002), we measure subsidiary legitimacy with three items that reflect acceptance and endorsement of subsidiary behaviour (see Appendix 3 for details).

3.2.2 Independent and Control Variables

Following institutional theory, we explain subsidiary legitimacy with the five strategies of mimetic isomorphism, relational, financial incentive, information, and constituency building. Mimetic isomorphism is measured with three items derived from the literature (Haverman 1993; Schoonhoven et al. 1990). The four measures of relational strategy are obtained from Blumentritt (1999) and Hillman and Hitt

(1999). The measures for financial incentive (3 items), information (7 items), and constituency building (4 items) strategies are based on Hillman and Wan (2005). We test our hypotheses by controlling for variables that have been identified in prior studies as related to CPA. Our choice of controls, namely, subsidiary age, subsidiary size, related diversification and industry concentration, is guided by Hillman et al. (2004) and Hillman and Wan (2005). Subsidiary age and size reflect host country experience and visibility respectively and are considered important factors that affect subsidiary legitimacy (Hillman and Wan 2005). Additionally, we control for subsidiary-parent country distance by using the World Bank Governance Indicators (Kaufmann et al. 2003). We first compute the overall average governance score across the six governance dimensions for each of the 28 parent countries and the subsidiary country, Australia. Next, the subsidiary-parent country distance is calculated as the absolute value of the difference in the overall average governance score between Australia and each of the 28 parent countries. To control for industry fixed effects, we include two industry dummies, namely, manufacturing and wholesale (see Appendix 3 for the measures used to operationalise each variable).

3.3 Potential Biases

3.3.1 Non-response and Common Method Biases

Although surveys are common in IB research, there are some concerns about potential biases since the data for both the predictor and criterion variables are collected from the same respondent with a single survey instrument. To address these concerns, we examined our data for two common types of biases: non-response bias and common method bias. Following Armstrong and Overton (1977) and Lambert and Harrington (1990), we test for non-response bias by comparing the characteristics of early wave (n = 141) and late wave (n = 73) respondents. Early wave respondents are MNC subsidiaries that returned completed questionnaires in response to the initial survey and two follow up reminders. To increase our response rate, we resent the original survey questionnaire and two follow up reminders to the non-respondents almost five months after the start of the initial survey to avoid the December–January summer break period in many organizations in Australia. We received a further 73 completed questionnaires and these are referred to as late wave respondents, and deemed to be representative of the characteristics of non-respondents. The *t* tests (Table 1) show no significant differences between the two groups of respondents on subsidiary age, size, assets, and sales, indicating no response bias at least on these characteristics.

Using a uniform five-point Likert scale across measures can be a source of common method bias (CMB). In keeping with past studies, we overcome potential CMB at the instrument design and data collection stage by minimising ambiguity in the design of our questionnaire, maintaining simplicity and avoiding complex syntax, and assuring confidentiality and anonymity to the respondents (Chang et al. 2010; Podsakoff et al. 2003). In addition to the data collected from our survey, we use secondary data to measure subsidiary-parent country distance as a control variable, as recommended by Chang et al. (2010). After following all procedural

Table 1 *T* test results for response bias

	Early response sub-sample: mean (sd)	Late response sub-sample: mean (sd)	t value
Subsidiary age (years)	21.23 (17.45)	24.24 (22.39)	−1.08
Subsidiary size (number of employees)	215.03 (587.40)	300.78 (756.62)	−0.91
Subsidiary assets (A$, million)	138.16 (927.65)	207.57 (877.77)	−0.45
Subsidiary sales (A$, million)	105.87 (248.80)	166.30 (391.46)	−1.35

sd standard deviation

remedies related to questionnaire design, we use Podsakoff et al.'s (2003) proposed single-common-method-factor approach to statistically test for CMB for a post-survey analysis. Exploratory factor analysis (EFA) of our model variables extracted five factors that accounted for 69% of the total variance, with the first factor extracting 39% of the total variance. A substantial degree of CMB is considered to be present if either (a) a single factor emerges from the EFA, or (b) one general factor explains "the majority of the covariance among the measures" (Podsakoff et al. 2003, p. 889). Since our EFA produces neither a single factor nor a general factor, CMB is unlikely in our data. "A final technique that could be used to control statistically for method bias is the instrumental variable technique" (Podsakoff et al. 2012, p. 564), and which we discuss below.

3.3.2 Endogeneity Bias

IB research is susceptible to the presence of endogeneity bias arising from three sources: omitted variables, measurement error and reverse causality (Bascle 2008; Jean et al. 2016; Reeb et al. 2012). To overcome the problem of omitted variables, we include seven control variables in our model, namely, subsidiary age, subsidiary size, related diversification, industry concentration, subsidiary-parent country distance, manufacturing dummy, and wholesale dummy (Hillman et al. 2004; Hillman and Wan 2005). Next, we overcome the potential problem of measurement error by: (a) writing the items clearly and providing well-defined instructions to the survey respondents on how to complete the questionnaire, (b) using multiple valid items to measure each construct reliably, and (c) creating factor scores for each set of items used to measure our constructs, and using these factor scores as inputs for our multiple regression models (Nunnally and Bernstein 1994). The third source of endogeneity is reverse causality, from the dependent to the independent variable, and which we address indirectly with our endogeneity tests (Bascle 2008).

One of the most common methods to test endogeneity is the two-stage least squares (2SLS) regression with instruments. However, for the endogeneity test results to be reliable, the instrument must satisfy two key criteria—validity and strength. Validity means the instrument must be logically related to the endogenous explanatory variable but not to the dependent variable, and strength means the relationship must be empirically strong (see Bascle, 2008 for details). We use the construct of CPA resourcing as the instrument for our 2SLS regression. In our study, CPA resourcing is the extent to which the subsidiary has a formal government relations department with dedicated employees and budgets to carry out the government relations activities. The subsidiary's government relations department enables the firm to execute the CPA strategies that it aims to undertake to gain legitimacy in the host country (Schuler 1996). On the other hand, since a firm's internal resources are unlikely to be visible to outsiders, other than through its CPA strategy, one would not expect the subsidiary's CPA resourcing by itself to affect its legitimacy in the country in which the firm operates. We therefore consider CPA resourcing to be a valid instrument for our 2SLS regression model. We measure CPA resourcing with three binary (yes/no) items: subsidiary has a formal government relations department, a budget is allocated for government relations work, and employees are wholly assigned to government relations activities. We next create a single CPA resourcing construct score by aggregating the scores for the three measures.

Consistent with our hypotheses and our OLS estimation strategy, we test five different models using the 2SLS approach in Stata (models 1a to 1e), one for each type of subsidiary CPA strategy, followed by tests of endogeneity for each regression. We use the same instrument, CPA resourcing, for all five models of CPA for consistency and comparability across the models. As shown in Table 2, in the first stage regression, our instrument (CPA resourcing) is significant in all five models, with t-values ranging from 1.89 ($p = 0.06$) to 8.73 ($p = 0.00$). The instrument therefore satisfies both the validity and strength criteria and can be regarded as a good instrument for our 2SLS regression. Following both the OLS and 2SLS regressions, we carry out tests of endogeneity for each of the five CPA strategies. As shown in Table 2, all five tests of endogeneity are not significant. The p-values for the Durbin test range from 0.42 to 0.89, and those for the Wu–Hausman

Table 2 Two-stage least squares (2SLS) regression with CPA resourcing as the instrument variable: First-stage regression and tests of endogeneity

	Model 1a	Model 1b	Model 1c	Model 1d	Model 1e
Instrumented predictor variable (CPA)	Mimetic isomorphism strategy	Relational strategy	Financial incentive strategy	Information strategy	Constituency building strategy
First-stage regression results					
Unstandardized coefficient	0.13	0.48	0.52	0.51	0.42
Std. error	0.07	0.06	0.06	0.06	0.07
t value	1.89	7.59	8.71	8.73	6.45
p value	0.06	0.00	0.00	0.00	0.00
Tests of endogeneity					
Durbin (score) Chi square (1)	0.13 ($p = 0.71$)	0.08 ($p = 0.78$)	0.22 ($p = 0.64$)	0.65 ($p = 0.42$)	0.02 ($p = 0.89$)
Wu–Hausman F(1,203)	0.13 ($p = 0.72$)	0.07 ($p = 0.79$)	0.21 ($p = 0.65$)	0.62 ($p = 0.43$)	0.02 ($p = 0.89$)

test range from 0.43 to 0.89. Since the null hypotheses for these tests are that the predictor variables are exogenous, a non-significant result indicates that the null hypotheses cannot be rejected. In other words, the five CPA strategies are exogenous, and we can retain and focus on our OLS results for further discussion (Papies et al. 2016).[3]

4 Results

We first carried out a descriptive analysis of our data, followed by measurement model analysis. The hypotheses were tested with multiple regression analyses. Table 3 provides the means, standard deviations and correlations for the thirteen variables in our model, including one dependent variable, five independent variables, and seven controls. The six variables (excluding controls) measured with multiple items all have good measurement properties. All variables with multi-item measures have good convergent validity, as reflected in acceptable values of average variance extracted (above 50% for all variables except financial incentive strategy at 49%) and composite reliability (above 0.70 for all variables). Similarly, all our multi-item variables have adequate discriminant validity, as the square root of average variance extracted for each variable (the diagonal entries in bold in Table 3) is greater than its correlation with all other variables (the off-diagonal elements in the corresponding rows and columns in Table 3) (e.g., Venaik et al. 2005). Finally, all measures have good loadings with their respective variables indicating measurement reliability (see Appendix 3 for details).

To test our hypotheses regarding the effectiveness of different types of strategies in gaining legitimacy, we used multiple regression analysis. Table 4 presents the regression results. Variance inflation factor (VIF) results show no VIF is greater than 10, indicating that multicollinearity is not an issue for our data. Model 0 is the baseline model with the control variables only. Models 1a to 1e test the hypothesis regarding the effect of each of the five CPA strategies on subsidiary legitimacy, after controls. For completeness, we also tested the model with all strategies (model 2).

Model 0 shows that subsidiary age, i.e., experience in the host country, has a negative effect, whereas size has a positive effect on subsidiary legitimacy. It is plausible that the expectations of society from subsidiaries with a longer tenure in the country are greater than that from younger subsidiaries, and perhaps beyond what the older subsidiaries can reasonably fulfil, adversely affecting their legitimacy. Also, older subsidiaries might be complacent in carrying out legitimacy seeking activities, and which may lower their legitimacy in the eyes of potential stakeholders. On the other hand, larger subsidiaries are likely to have more resources to carry out the legitimacy seeking activities, resulting in higher legitimacy than their younger counterparts. Similarly, manufacturing (which

[3] As expected, due to the high standard errors in 2SLS regressions, the CPA strategies are not statistically significant in the second stage 2SLS equations. However, since our endogeneity tests show that our predictor variables are exogenous, and for brevity, we do not include the second stage regression results here, but these are available from the authors.

Table 3 Descriptive statistics, correlations, reliability and validity

Variable	1	2	3	4	5	6	7	8	9	10	11	12	13
1. Subsidiary legitimacy	**0.90**[c]												
2. Mimetic isomorphism strategy	0.50**	**0.86**											
3. Relational strategy	0.19**	0.33**	**0.87**										
4. Financial incentive strategy	0.22**	0.26**	0.53**	**0.71**									
5. Information strategy	0.09	0.21**	0.69**	0.65**	**0.84**								
6. Constituency building strategy	0.19**	0.26**	0.43**	0.48**	0.57**	**0.82**							
7. Subsidiary age[a,b]	−0.21**	−0.18*	−0.15*	−0.02	0.04	−0.05	1						
8. Subsidiary size[a,b]	0.06	0.06	0.10	0.23**	0.31**	0.16*	0.41**	1					
9. Related diversification[a]	0.04	−0.09	0.03	0.07	0.07	0.04	0.05	0.03	1				
10. Industry concentration[a]	−0.05	−0.19**	0.04	0.02	0.10	−0.07	0.05	−0.04	0.25**	1			
11. Subsidiary-parent country distance[a]	0.16*	0.07	0.13	0.10	0.07	0.07	−0.14*	−0.02	0.00	0.12	1		
12. Manufacturing dummy[a]	0.10	−0.01	0.00	−0.01	0.04	−0.09	0.00	−0.03	0.12	0.16*	0.13	1	
13. Wholesale dummy[a]	−0.03	0.00	−0.09	-0.15*	−0.23**	−0.07	0.07	−0.18**	−0.15	0.01	−0.12	−0.52**	1
Mean	2.41	1.89	2.35	1.28	1.86	1.36	1.19	1.74	2.84	3.51	0.42	0.37	0.31
Standard deviation	0.62	0.89	1.03	0.40	0.92	0.56	0.39	0.72	1.48	1.31	0.41	0.48	0.47
Average variance extracted	0.82	0.73	0.75	0.50	0.70	0.67	1	1	1	1	1	1	1
Composite reliability	0.92	0.87	0.92	0.73	0.93	0.89	1	1	1	1	1	1	1

** $p < 0.01$, * $p < 0.05$. All tests are two-tailed

[a] Control variables

[b] Log of age (years) and size (number of employees)

[c] The bold diagonal figures are the square root of average variance extracted. Average variance extracted (second last line in the table) for each multi-item construct is the average sum of squared loadings of the items used to measure each construct (Fornell and Larcker 1981). The factor loadings are included in Appendix 3 (figures in brackets against each item)

Table 4 Ordinary least squares (OLS) regression results for subsidiary legitimacy

Variable	Model 0	Model 1a	Model 1b	Model 1c	Model 1d	Model 1e	Model 2
Constant	0.11 (0.31)	−0.20 (0.28)	0.11 (0.31)	0.19 (0.31)	0.16 (0.32)	0.11 (0.31)	−0.25 (0.29)
Controls							
Age	−0.67*** (0.18)	−0.41* (0.17)	−0.61** (0.19)	−0.62*** (0.18)	−0.66*** (0.18)	−0.63*** (0.18)	−0.38* (0.17)
Size	0.26* (0.10)	0.15 (0.09)	0.23* (0.10)	0.19 (0.10)	0.23* (0.11)	0.22* (0.10)	0.16 (0.09)
Related diversification	0.04 (0.05)	0.05	0.04 (0.05)	0.03 (0.05)	0.04 (0.05)	0.04 (0.05)	0.04 (0.04)
Industry concentration	−0.06	0.00 (0.05)	−0.06 (0.05)	−0.06 (0.05)	−0.06 (0.05)	−0.05 (0.05)	0.02 (0.05)
Subsidiary-parent country distance	0.30 (0.16)	0.24 (0.14)	0.27 (0.16)	0.26 (0.16)	0.29 (0.16)	0.27 (0.16)	0.21 (0.14)
Manufacturing dummy	0.32* (0.16)	0.27 (0.14)	0.33* (0.16)	0.36* (0.16)	0.33* (0.16)	0.37* (0.16)	0.29* (0.14)
Wholesale dummy	0.26 (0.17)	0.18 (0.15)	0.28 (0.17)	0.31 (0.17)	0.29 (0.17)	0.29 (0.17)	0.16 (0.15)
CPA							
Mimetic isomorphism strategy		0.46*** (0.06)					0.44*** (0.06)
Relational strategy			0.13* (0.07)				0.00 (0.08)
Financial incentive strategy				0.19** (0.07)			0.14 (0.08)
Information strategy					0.07 (0.07)		−0.17 (0.10)
Constituency building strategy						0.16* (0.07)	0.09 (0.07)
Adjusted R-square	0.07	0.28	0.09	0.11	0.08	0.10	0.28
F change	3.44**	57.94***	3.90*	8.41**	1.11	5.96*	12.90***

Values are unstandardized coefficients. Standard errors are in parentheses. *** $p < 0.001$, ** $p < 0.01$, * $p < 0.05$. All tests are two-tailed includes mining and construction) subsidiaries have greater legitimacy on average than their non-manufacturing counterparts, perhaps due to their greater role in the Australian economy. Thus, larger subsidiaries and those engaged in the manufacturing, mining and construction industry are viewed more favourably, whereas longer legacy of older subsidiaries hurts their legitimacy.

Next, we look at the results of models 1a to 1e in line with our hypotheses. These models show that four of the five strategies have a significant positive effect on MNC subsidiary legitimacy, albeit the size of the effects on subsidiary legitimacy varies across the different strategies. In contrast, information strategy (model 1d) does not have a significant effect on subsidiary legitimacy ($\beta = 0.08$, $p = 0.29$, not significant). Thus, we find support for four of our five hypotheses. Mimetic isomorphism (model 1a) has the strongest positive effect on subsidiary legitimacy ($\beta = 0.45$, $p < 0.001$), whereas financial incentive strategy (model 1c) has a strong positive effect on subsidiary legitimacy ($\beta = 0.20$, $p < 0.01$). Finally, relational strategy (model 1b) has a moderate positive effect on subsidiary legitimacy ($\beta = 0.13$, $p < 0.05$), as does the constituency building strategy in model 1e ($\beta = 0.16$, $p < 0.05$).

Overall, following Cohen's (1988) qualitative rule of thumb for standardized coefficients, where 0.10 is small, 0.30 is medium and 0.50 or more is large effect size, we can conclude that mimetic isomorphism has a medium to large effect on gaining subsidiary legitimacy ($\beta = 0.45$), financial incentive, constituency building and relational strategies have small to medium effects ($\beta = 0.19$, 0.16 and 0.13 respectively), and information strategy does not have a significant effect on subsidiary legitimacy ($\beta = 0.07$). The corresponding adjusted r-square values (28, 11, 10, 9 and 8%) for models 1a to 1e in Table 4 are consistent with the effect sizes. In addition, we also test the statistical significance of differences in the individual effects of the five non-market strategies on subsidiary legitimacy, after partialling out the control variables (Blalock 1979, p. 425; Lee and Preacher 2013). This test shows that mimetic isomorphism has a significantly higher impact on subsidiary legitimacy than any of the other four strategies ($p < 0.001$), and financial incentive strategy has a moderately stronger impact than information strategy ($p < 0.05$). These are interesting results that have important implications for the design of CPA strategies by MNC subsidiaries, and which we discuss in the next section.

5 Discussion

Institutional theory considers legitimacy a key requirement for firms to operate successfully in a given environment. In the context of MNCs in particular, the need for legitimacy assumes greater importance due to the additional burden of the liability of foreignness confronted by MNC subsidiaries. Whereas the significance of legitimacy has been recognized in the MNC CPA literature (e.g., Kostova and Zaheer 1999; Luo 2001; Wan and Hillman 2006), it has not been tested formally with data from MNC subsidiaries. Luo (2001) argues that MNC subsidiaries need legitimacy to develop the credibility for building MNC government relations. However, it does not specify the types of activities that MNC subsidiaries need to undertake to attain legitimacy in foreign countries. Legitimacy does not emerge in a vacuum. It is the outcome of a range of non-market strategies that MNC subsidiaries pursue in the environment in which it operates. Of the three sets of factors that shape legitimacy, namely, environment characteristics, organizational actions, and the legitimation process by which the environment builds its perception of the organization (Kostova and Zaheer 1999), our paper focusses specifically on the second factor of organizational actions, albeit the effectiveness of these actions would depend on the other two factors. Our paper thus provides an empirical test of Kostova and Zaheer (1999) and extends Luo (2001) to show how the different CPA strategies support MNC subsidiaries in gaining legitimacy in the host country.

We extend the literature on CPA by acknowledging the significance of mimetic isomorphism for MNC subsidiaries to gain legitimacy in host countries. Due to the liability of foreignness, MNC subsidiaries face additional hurdles for recognition in the host environment. A relatively easy way to get accepted in the host environment is to simply mimic the activities of successful firms in the host country. Combined with the well-recognized CPA strategies of financial incentive, information, constituency building and relational, we examine five types of MNC subsidiary CPA strategies and their impact on subsidiary legitimacy. Although each strategy individually has a significant effect on subsidiary legitimacy, albeit to varying degrees, collectively, only mimetic isomorphism is found to have a large and significant unique effect on legitimacy. Kostova and Zaheer (1999) argue that due to the liability of foreignness, mimetic isomorphism may not be a feasible strategy for multinational firms. Contrary to their thesis, our study shows that mimetic isomorphism is not only feasible but one of the most potent strategies for gaining legitimacy in foreign countries, especially in our sample of MNC subsidiaries in Australia. One plausible explanation for our finding is the evolving nature of the multinational enterprise. In the early literature, MNCs were largely viewed as global corporations, with the subsidiaries merely acting as extensions and appendages of the corporate headquarters whose mandates governed the activities of MNC subsidiaries located in different countries. However, the view of the MNC has evolved from being a global to a transnational corporation, and with it the role of the MNC subsidiary has also changed from being a follower to a leader in its own right (Bartlett and Ghoshal 1986). Given the growing embeddedness of the subsidiary within the host country, it is not surprising that mimetic isomorphism is a strongly significant strategy for MNCs to gain legitimacy in its foreign operations. Since open economies such as Australia have a large number of MNCs operating in the country, the mimetic isomorphism strategy potentially reflects the non-market activities of both foreign and domestic firms in Australia.

To further understand the CPA phenomena in MNC subsidiaries, we found, through a second order factor analysis, that the five strategies can be combined into a single factor representing a composite CPA strategy of MNC subsidiaries, and which has a strongly significant positive effect on subsidiary legitimacy ($\beta = 0.25$, $p < 0.001$). A single overall CPA strategy with five underlying dimensions raises an interesting theoretical and practical question—are the five dimensions of CPA essential and need to be pursued jointly, in parallel, or do they represent a bundle of equifinal strategies. Essential implies that the absence of any of the five strategies would undermine the effectiveness of all the other strategies undertaken by the subsidiary in the CPA mix. Equifinal means different paths can lead to the same outcome (Katz and Kahn 1978; von Bertalanffy 1968). In the context of our study, equifinal implies that the different CPA strategies are substitutes, that is, MNC subsidiaries can pursue any one or more of the five strategies to attain legitimacy. Under the equifinal scenario, absence of a particular CPA strategy would not preclude the MNC subsidiary from benefitting from the other CPA strategies that the firm pursues in the host country. Although we are unable to address the essential versus equifinal question with our survey data, anecdotal evidence suggests that the different components of CPA are essential rather than equifinal in nature.

For example, there are active debates in the Australian community about the merits or otherwise of Chinese investments in Australia across a wide range of industries including mining, agriculture and real estate. Since the legitimacy of Chinese investments is increasingly called into question, Australian governments have imposed a number of restrictions on Chinese investments in recent times. These include, for example, limits on property purchases, increased scrutiny of investments by Chinese state-owned enterprises, and rejection of investment applications to protect the national interest. These policies of the Australian government have created artificial barriers for entry and growth of Chinese investments in Australia.

This is despite the widely known fact that Chinese business interests in Australia often give financial donations to Australian politicians and political parties. However, there is little evidence of Chinese firms engaging in other dimensions of CPA to cement their legitimacy. This limited anecdotal evidence suggests that the five CPA strategies are more likely essential rather than equifinal in nature, and MNC subsidiaries need to pursue all of these strategies to some degree in order to gain legitimacy. Absence of any one of these strategies cannot be compensated by pursuing the other strategies with greater intensity, and is likely to undermine the effectiveness of all the other legitimacy seeking actions undertaken by the firm. It is therefore imperative for Chinese businesses to become more proactive in undertaking other non-financial strategies, including mimetic isomorphism, information, relational and constituency building strategies, in order to gain legitimacy and hence the opportunity to successfully enter and operate their businesses in Australia.

While the potential downsides of CPA are well-recognised in the literature, we find that at least in the Australian context, no CPA strategy has a negative effect on subsidiary legitimacy. This suggests that context is an important variable for testing the model of CPA. We speculate that since CPA in Australia is largely legal, open and transparent, its negative effects are mitigated. Overall, therefore, from a managerial perspective, subsidiary legitimacy gained through simultaneous pursuit of all types of non-market strategies is a sine qua non for MNC subsidiary survival, especially in the context of Australia and perhaps other developed countries, irrespective of its effect on the firm's market performance.

6 Conclusion

The large body of literature on non-market CPA strategy has expanded our understanding of the diverse range of activities conducted by MNCs in host countries. However, the CPA literature gives limited recognition to the organisational sociology perspective of institutional theory and how MNC subsidiaries can manage relationships with relevant stakeholders of a host nation to gain an important non-financial outcome, namely, subsidiary legitimacy. Our paper integrates sociological view of institutional theory with the CPA literature for a comprehensive understanding of CPA implementation and its effectiveness in the IB context. As a result, we contribute to a broader theoretical approach to the management of CPA strategies, which has mainly been analytically categorised and applied. In particular, our study extends the CPA literature in IB by examining the effect of both adaptive and transformative approaches to gain legitimacy (Dorobantu et al. 2017). We also discuss the concepts of essentiality versus equifinality of CPA strategies and demonstrate with examples how the different CPA strategies are complementary and work synergistically to reinforce each other in enabling the subsidiary to gain legitimacy in host countries.

Our study also contributes to the debate on optimal distinctiveness (Zhao et al. 2017). That is, the need to reconcile contradictory prescriptions of imitation versus innovation in institutional theory and strategic management respectively (Birkinshaw and Hood 2001; DiMaggio and Powell 1983). Although more research is needed to jointly examine both market and non-market strategies of MNCs, our preliminary results suggest that firms need to be ambidextrous and adopt a “horses for courses” approach. In other words, MNC subsidiaries need to be innovative to succeed in the marketplace, and concurrently pursue imitation in their non-market activities to gain legitimacy in society.

Methodologically, we test both individual and joint effects of different types of CPA with primary data from MNC subsidiaries operating in a wide range of industries within a single country, Australia, a geographic region that has remained unexplored (Rajwani and Liedong 2015). Moreover, we collected the data through a large-scale mail survey, a method that is infrequently employed in empirical CPA studies (Rajwani and Liedong 2015). In addition, while the endogeneity bias has been acknowledged in IB research (Reeb et al. 2012), our paper is among the very few to test it in the context of CPA in IB.

Finally, from a managerial perspective, we find mimetic isomorphism is one of the most effective non-market CPA strategy for MNC subsidiaries to gain legitimacy. This is in contrast with the fact that MNCs need to focus on innovation to be successful in their market strategies. The need to be innovative in market strategy and imitative in non-market strategies suggests that MNC subsidiaries require organizational leadership that can handle complexity and contradictions with ease, in order to succeed in both market and non-market domains. Further, given the essential and synergistic nature of different types of CPA to gain legitimacy, MNC subsidiary managers need to deploy appropriate organizational resources, capabilities, structures, systems and processes, to execute diverse types of

CPA. MNC subsidiary managers must also recognize the potential downsides of financial incentive and relational strategies and take appropriate steps to mitigate their negative impact, including engaging in these activities in a legal, open and transparent manner.

Notwithstanding these contributions, there are several promising directions for future research to take the CPA field forward and to overcome the limitations of our study. One, subsidiary legitimacy is a complex construct encompassing multiple facets (Suddaby et al. 2017) of which we empirically examine a small subset. Whereas our three measures examine the evaluative aspects of legitimacy in terms of its conformity with the socio-cognitive environment, measuring finer aspects of legitimacy in terms of its properties and processes, and using objective measures would help extend and strengthen the research on the effects of different types of CPA on diverse aspects of subsidiary legitimacy.

Two, it is plausible that the corporate headquarters of the MNC also engages in CPA in the host country, especially if the issues involve large-scale, national level contracts, for example, in the areas of defence and infrastructure. Future research could examine both aspects of CPA, and test which CPA—headquarters or subsidiary—has greater influence on subsidiary legitimacy. Three, the activities of MNC subsidiaries are often legitimized against the baseline of domestic firms. It will therefore be useful to compare and contrast the CPA strategies of MNCs vis-à-vis domestic firms, and estimate the CPA premium that MNCs have to pay to overcome the liability of foreignness in order to achieve the same level of legitimacy.

Four, due to the relatively small size of our sample, we could not slice the data to examine industry-specific CPA strategies and their impact on legitimacy. Future research could focus on a few critical industries, for example, mining, financial services and real estate, and compare and contrast the CPA strategies and their effectiveness in gaining legitimacy across industries. Further, to increase the response rate and sample size for analysis, researchers could get their survey and data collection endorsed by industry associations and MNC parent headquarters. This will not only increase the power of statistical tests but also help in enhancing the generalizability of the study findings.

Five, it will be useful to examine dynamic effects, that is, how the CPA strategies change over time due to changes in the institutional environment arising from globalization of trade and investment flows, and societal expectations about the role of foreign firms in contributing to, rather than just benefiting from, the local economy. Additionally, following Hillman and Hitt (1999), researchers could refine the study of CPA by exploring the extent to which MNC subsidiaries execute the various CPA strategies using transactional, relational or mixed approaches. Further, given political strategies can potentially have both positive and negative effects, depending on the context, and to enhance the generalizability of our results, future researchers could test comparative models of MNC subsidiary CPA with samples from diverse countries, both developed and developing, and spread across different regions of the world.

Six, future research with qualitative in-depth interview data from MNC subsidiary and headquarter managers involved in CPA can help resolve the important question of whether the five dimensions of CPA are essential or equifinal. If the five strategies are equifinal and substitutable (Barney 2001), MNC subsidiaries can focus their resources mainly on pursuing mimetic isomorphism strategy since this strategy has the strongest impact on gaining legitimacy. As a result, subsidiaries can save resources from the other four strategies. On the other hand, if all strategies are essential and complementary, as our anecdotal evidence suggests, firms need to spread their resources in pursuing all dimensions of CPA, with the different strategies reinforcing each other to gain legitimacy. Finally, for a more robust test of endogeneity, we need better instruments to examine the effects of different types of CPA on subsidiary legitimacy in IB.

To conclude, our paper makes a number of important contributions to the MNC CPA literature. We formally operationalize the concept of subsidiary legitimacy and test it with data from MNC subsidiaries. As far as we know, this is one of the first attempts to formally test the important construct of legitimacy that is at the core of institutional theory. We also examine five dimensions of subsidiary CPA strategy and their relative impact on subsidiary legitimacy. With the world economy becoming increasingly globalized through the activities of MNCs, and growing government influence on firm decisions across a wide range of areas, such as taxes, environmental protection, product standards, occupational health and safety, wages and employment conditions, etc. it is important that MNCs proactively pursue different types of non-market strategies, in addition to market strategies, to enter, survive and grow in international markets.

Acknowledgements We would like to thank the editor and the two anonymous reviewers for their constructive comments and suggestions for improving the paper. We would also like to thank Manuel Becerra, Andre Bonfrer, Paul Brewer, and participants at the ANZIBA, AIB and EIBA conferences for useful inputs in the process of developing our paper. Both authors contributed equally in preparing the manuscript. The authors are responsible for all errors and omissions.

Appendix 1: Industries Represented in Our Sample

Industry classification	Number	Percent
Manufacturing (including mining and construction)	79	36.9
Wholesale (including retail trade)	67	31.3
Other[a]	68	31.8
Total	214	100

[a] The "other" category includes the following industries: Professional, Scientific, Training, Administration and Support Services 35 (16.4%); Financial and Insurance Services 9 (4.2%), Transport, Postal and Warehouse 8 (3.7%), Information, Media and Telecom 7 (3.3%), Agriculture, Forestry and Fishing 5 (2.3%), Rental and Real Estate Services 4 (1.9%)

Appendix 2: Parent Countries of our Sample MNC Subsidiaries

Country	Number of subsidiaries
Austria	2
Bahrain	1
Belgium	2
Bermuda	1
Brazil	1
Canada	3
Cayman Islands	1
China	1
Denmark	2
France	12
Germany	15
Hong Kong	4
India	2
Italy	2
Japan	23
Kuwait	2
Liechtenstein	1
Luxembourg	2
Malaysia	2
Netherlands	10
New Zealand	9
Singapore	9
South Africa	2
Spain	1
Sweden	5
Switzerland	15
UK	36
USA	48
Total	214

Appendix 3: Variables and Measures

Variables	Measures	Sources
1. Subsidiary legitimacy	The extent to which subsidiary's behaviour leads to: Justification of strategic choices (0.92)[a] Greater legitimacy within Australia (0.91)	Ryan et al. (1987), Zimmerman and Zeitz (2002)

Variables	Measures	Sources
2. Mimetic Isomorphism Strategy	Indicate the extent to which the subsidiary has followed or adopted (successful) competitors' activities for:	Haverman (1993), Schoonhoven et al. (1990)
	Development of new organisational structure (including dedicated political unit) (0.94)	
	Development of new organisational management (including for government affairs) (0.94)	
	Governmental affairs strategies (0.66)	
3. Relational strategy	Indicate the extent to which the subsidiary agrees with the following:	Blumentritt (1999), Hillman and Hitt (1999)
	Engagement in government affairs is vital to the competitive success of the subsidiary (0.90)	
	Considers political strategies to deal with government as a good investment (in terms of time and money) (0.89)	
	Is generally interested in a variety of public policy issues facilitating on-going political involvement in Australia (0.85)	
	Develops relationships over time so that when issues arise, the contacts are already in place (0.82)	
4. Financial incentive strategy	Indicate the extent to which the subsidiary:	Hillman and Wan (2005)
	Appoints executives who serve in a political position (0.74)	
	Employs individuals with political or professional experience (0.72)	
	Makes financial contributions to candidates or parties (0.66)	
5. Information Strategy	Indicate the extent to which the subsidiary:	Hillman and Wan (2005)
	Develops relations with government at the state level (0.90)	
	Discusses with government at the national level (0.89)	
	Approaches government to support company programs (0.86)	
	Contacts, initiates discussions or provides information (0.84)	
	Includes viewpoints in the reports sent to government (0.80)	
	Engages with government at the local level (0.79)	
	Makes governmental officials aware of research results (0.76)	
6. Constituency building strategy	Indicate the extent to which the subsidiary engages in:	Hillman and Wan (2005)
	Advocacy advertising in the media (0.88)	
	Grassroots political programs (0.84)	
	Press conferences on public policy issues (0.81)	
	Public relations advertising in the media (0.73)	

Variables	Measures	Sources
7. Subsidiary age[b]	How long has the subsidiary been operating in this country	Hillman and Wan (2005), Wan and Hillman (2006)
8. Subsidiary size[b]	Total number of employees working in the local subsidiary	Hillman and Wan (2005), Wan and Hillman (2006)
9. Related diversification[b]	In a given year, indicate the proportion of the subsidiary total sales that are contributed by its largest group of related business	Rumelt (1974, 1982)
10. Industry concentration[b]	Market share of the top four firms in the industry	Schuler et al. (2002), Hansen et al. (2005)
11. Subsidiary-parent country distance[b]	Absolute value of difference between average World Bank Governance Indicator score for parent country and average World Bank Governance Indicator score for Australia across the six governance dimensions.	Kaufmann et al. (2003)
12. Manufacturing dummy[b]	Subsidiaries in manufacturing (including mining and construction) coded as 1, others 0	
13. Wholesale dummy[b]	Subsidiaries in wholesale (including retail trade) coded as 1, others 0	

[a] Figures in brackets are factor loadings

[b] Control variables measured with single items or index

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