Cultural Diversity, Strategic Alliance Configurations, and Ecological Innovations of MNEs

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Introduction

Multinationals are increasingly involving in "ecological innovation" not only because they are forced by national and international laws, but also because the adoption of environmental management strategies improves firms' image in the customer´s mind and at the same time provides opportunities for business organizations. In this study, I regard ecological innovation as "innovations that consist of development of new or modified processes, practices, systems and/or products which contribute to environmental sustainability" (Oltra & Jean, 2009). Previous studies on the topic have demonstrated that environmental sustainability of firms may strengthen their economic goals (Wood & Jones, 1995; Etzion 2007; Calza et al., 2017). Even if environmental management may not perhaps increase profitability in the short term, it could create economic payoffs in the long term (Hart & Ahuja, 1996).

In order to engage in ecological innovation, MNCs can incorporate environmental issues into their strategies through strategic alliances (Lin & Darnall, 2010). Ecological strategic alliances are often voluntary collaborations between firms in regards to sharing, and conducting joint research and development of products and technologies to meet environmental protection requirements Gulati, 1998; Lin & Darnall, 2010). While previous research has recognized the importance of strategic alliances, these studies have traditionally focused on

assessing the economic aspects of interfirm relationships (Mitchell & Singh, 1996). Strategic alliances, however, can be formed to cope with environmental issues such as alternative energy, waste management, and recycling (Lin & Darnall, 2015). Thus it is important to understand how firms establish strategic alliance to facilitate ecological innovation to cope with environmental issues.

In addition, recently ecological innovation is becoming an important topic for both in practice and in academia (Schiederig, Tietze, & Herstatt, 2012). Most studies have tested the linkage between this type of innovation and firm performance (Cainelli et al., 2013; Benito & Benito, 2006). Other studies have focused on the specific determinants of ecological innovation at the firm level including internal factors, external factors and environmental regulation (Kesidou & Demirel, 2012). Particularly in the innovation management field, there are only a few scholars who have conducted research related to new product and service development of ecological innovations (Lin, 2012; Stadtler, & Lin, 2019). To fill this literature gap and to provide a framework for ecological innovation in international business, this study is aimed at answering the following question: *What is the relationship between cultural diversity, alliance types and ecological innovation performance in strategic alliance? How do control strategies by alliance partners moderate these relationships?*

In the next sections, I will discuss theoretical foundation of the study, and then we develop our propositions and model of the study. In the last section, we elaborate the results, our contributions, and suggestions for further study.

Dynamic capabilities and Ecological innovation

Previous research shows that there is strong link between Dynamic Capabilities (DCs) and innovation of firms. DCs (e.g. Teece et al., 1997; Halfat et al., 2007; O'Reilly and

Tushman, 2008; Teece, 2018) refer to firm-level abilities to build, integrate, coordinate internal and external resources. The concept of DCs is based on resource based views (Barney, 1986, 1991) which explains that competitive advantage of firms can be achieved on the basis of their novel bundles of resources and capabilities. DCs are emphasized on learning organization (Zollo & Winter 2002), and are embedded in the firms (Helfat & Peteraf, 2003). According to Zahra, Sapienza, Davidsson (2006) unsuccessful use with current capabilities and major change of environment play crucial roles for trigger the development and the use of DCs.

Rothaermel and Hess (2007) have posited that DCs of firms are driven by three different perspectives including the individual, the firm, and network level perspectives. At the individual level, they propose that intellectual human capital and scientists are sources for innovation. At the firm level, they posit that continuing investment on R&D capabilities is necessary and is positively related to a firm´s innovative output. At the network level, it is suggested that firms can improve their capabilities through external investment, including via alliances or acquisitions. According to Brezinik and Hisrich (2014), the concept of innovation capabilities is complementary to that of dynamic capabilities. According to Teece (2018), DCs are involved in innovation strategy formulation of firms. Strategic alliances in ecological innovation are mainly used by organizations to gain resources, and technological and competitive advantages by combining existing knowledge and capabilities and/or creating new ones in the favour of environmental sustainability.

Proposition development and Framework of the study

Drawing upon the foundations of dynamic capabilities described above, this study examines how cultural diversity and different types of strategic alliances have an impact on ecological innovation. Cultural diversity´s consequences in this study are divided into two

types - cultural synergy and cultural conflict. Types of strategic alliances are categorized as: exploration vs. exploitation alliances, foreign market focused vs. domestic market focused alliances, competency oriented vs. legitimacy oriented alliances, and business related vs. non business related alliances. Control strategies are further divided into broad control and focus control. Below section is a detailed discussion on the development of the propositions related to this chapter.

Cultural Diversity

Cultural diversity is defined as differences in the national cultural background of partners in the alliance (Elia et al., 2019). Cultural diversity has been argued to lead to either cultural synergy or cultural conflicts (Globocnik et al., 2019). Cultural synergy in an alliance enriches the capability of the partnership to innovate by positively influencing the operations of the partnership (Mihaela, 2014). Previous research has noted that cultural diversity can be beneficial for innovation within organizations by way of providing different ideas and new concepts from different members of different cultures. Especially, it may offer new methods and ways of how to cope with environmental issues, and help generate innovative capabilities for organizations (Birkinshaw et al., 2008; Russo & Fouts, 1997).

In contrast, cultural diversity can also result in cultural conflicts. Cultural conflict can distort expectations about the other partner's behavior (Ye et al., 2013). This causes problems in communication and negotiation between partners. In addition, it could have an impact on daily activities of the alliance. Thereby, it reduces an alliance´s ability to work toward innovation. This is also because cultural diversity which leads to cultural conflict reduces the effectiveness of a partner´s focus on ecological innovation, since partners have to spend much

time on resolving conflicts rather than on creating or innovating on the ecological aspects of the business. As a result, I propose that:

Proposition 1a: Cultural diversity resulting in cultural synergy tends to be associated with higher levels of ecological innovation.

Proposition 1b: Cultural diversity resulting in cultural conflict tends to be associated with lower levels of ecological innovation.

Alliance Types

Exploration versus Exploitation

Alliances can be categorized into exploration and exploitation types (Yamakawa *et al* 2011). Exploitation refers to organizational learning or product development by making new combinations of 'existing' knowledge, whereas exploration refers to learning by looking for and experimenting with 'new' knowledge. Exploration alliances combine complementary competencies from heterogeneous partners to build stronger DCs for the alliance (Mamédio et al., 2019) and thus it triggers innovation for new product development. Innovation stimulated by exploration alliances is often related to more radical and novel or creative changes to products and operations. These innovations, in turn, enable firms to initiate change from their current environmental practices, to pre-empt regulatory mandates and to adopt proactive environmental strategies for a competitive distinction (Li & Darnall, 2010). By contrast, exploitation alliances tend to emphasize on the use of things already known rather than the creation of new knowledge, or things that might become new products for firms (Levinthal & March, 1993). These firms, therefore, are less likely to adopt proactive environmental strategies.

Proposition 2: Exploration alliances tend to be associated with more ecological innovation than exploitation alliances

Domestic-market-focused versus foreign-markets-focused alliances

Previous studies (e.g. Nguyen & Larimo, 2009) have suggested that the focus strategy (domestic market vs. foreign market) of international alliances can have an effect on the alliance operations and performance. In domestic-market-focused alliances, the products of the alliance are mainly sold in the domestic market. On the other hand, in foreign-market-focused alliances, the products of the alliance are mainly sold in foreign markets.

In the case of alliances of firms or multinational corporations (MNCs) focusing on the domestic (or home) market, the requirements of environmental protection from domestic authorities are usually made familiar by the local government; and these requirements should have been adopted or followed by domestic-market focused alliances to meet with legal requirements of the market to get licenses for their operations. Thus, in this case, such firms or MNCs do not need to innovate any more for this aspect. This reduces domestically focused firms' or MNCs' motivations to innovate ecologically. On the other hand, alliances that focus on foreign markets need to use their DCs to innovate more to meet with the new or changing requirements of various foreign markets (Teece, 2018) on the environmental aspect, alongside the requirements concerning environmental issues from their home markets. In order to enter foreign markets, firms also often have to build a good image in because corporate reputation can be a significant asset or liability (Roberts & Dowling, 2002). This provides an incentive for firms to utilize their DCs to carry out ecological innovation in their operation in foreign markets (Rönnegard, 2015).

Proposition 3: Foreign market focused alliances tend to be associated with more ecological innovation than domestic market focussed alliances.

Business related vs. non-business related alliances

Business relatedness of alliance partners is regarded as a key factor determining alliance performance (Xu & Lu, 2007). Non related alliances refer to the types of alliances where the core business of each of the partner is different. Due to this, non-related alliances are argued to be less likely to benefit from MNCs´ (or partner's) existing knowledge. According to Anand *et al.*(2010), business activities that MNCs are involved are often related to DCs in alliances so they have to press more on the DCs to innovate themselves to meet with the local requirements of ecological aspects. In addition, in non-related alliances, partners may often have different backgrounds with different management and technical know-how. Thereby, there is much more room for partners´ skills and management know-how to interact and have synergic effect and these are good foundations for building their DCs for innovation. On the other hand, in related-business alliances, the two partners of the alliance often have the same kind of products or similar products. Thus, partners can easily agree and transfer their knowhow to the alliance for production. As a result, when partners are business related, the alliance will receive ready standard of formula for the production process. Thereby, there is not much new input and the need for alliances for building new capabilities. Therefore, such alliances do not have enough capabilities to innovate in order to meet the ecological requirements for their products. Based on above discussion, I propose that:

Proposition 4: Non business related alliances tend to be associated with more ecological innovation than related business alliance.

Competency-oriented vs. legitimacy-oriented alliances

Alliances could be further divided into competency and legitimacy oriented alliances (Lin, 2012). Competency-oriented alliances allow members to improve their learning ability. This kind of alliance integrates complementary competencies from partners (Lin & Darnall, 2010) and links more to business rather than environmental issues. As such, in this kind of alliance, alliance managers have their priority to reduce costs, generate more revenue, or improve the effectiveness of business. The resources or capabilities of this type of alliance are likely to be reserved for other areas of innovation rather than for ecological issues. On the other hand, the legitimacy-oriented alliances are typically under pressure of legal of local markets to improve existing practices or even refining their current routines (Barringer & Harrison, 2000) towards being environmental friendly. As such, the financial returns associated with ecological innovation may not be seen clearly in the short term performance of the alliance, yet, the benefit of ecological innovation may come later to the long term performance of the alliance. Therefore, legitimacy-oriented alliances can help corporate managers to have more support from alliance partners to focus their resources for ecological innovation. As a result, I propose that:

> *Proposition 5: Legitimacy-oriented alliances tend to be associated with more ecological innovation than competency-oriented alliances*

Equity Versus Non-Equity alliances

Non-equity alliances, which have received much less investment from partner firms, are aimed to maintain their independence and flexibility so that they can respond quickly to changing market conditions (Linnarsson & Werr, 2004). On the other hand, equity alliances get much more resources and investment commitment from their partner firms, and therefore

have more resources for building stronger capabilities in R&D. At the same time, ecological innovation often requires greater resource commitments to initiate significant changes in processes or entirely new production technologies (Hart & Ahuja, 1996). Similarly, According to Culpan (2008), for knowledge exploration in an alliance context, firms need equity participations in the creation of new products and technologies. R&D intensity is often argued to be positively correlated with firms' adoption of proactive environmental strategies (Arora & Cason, 1996). Equity alliances thus are able to use their current capability and competencies or even utilize their DCs to create new competence (Teece, et al., 1997) that are required for ecological innovation development. Thus, they are more likely to facilitate firms to pursue more ecological environmental strategy.

Proposition 6: Equity alliances tend to be associated with more ecological innovation strategies than non-equity alliances.

Moderating role of control on the relationship between alliance configuration and ecological innovation

Previous research (e.g., Inkpen & Currall, 2004; Luo, 2007) has shown that partner control strategies have a direct influence on the learning environment (Makhija & Ganesh, 1997) and therefore it may either stimulate or reduce innovation activities in alliances (Labitzke et al., 2014). The main purpose of partner control is to attain predictability and critical information on alliance operations through established rules (Makhija & Ganesh, 1997), thus, it protects the partner firms' interests and influences innovation activities of alliances (Sartor & Beamish, 2014).

Xu and Lu (2007) find that parent control has a positive interaction effect on technological knowledge creation in alliances. This is because in alliances, members not only

learn about environments but also about their partners as they are from different organizations. This learning process can provide new knowledge which increases the capacity of members to cooperate and acquire the knowledge they need to perform ecological innovation. Previous studies (e.g. Beamish & Lupton, 2016; Nguyen, Larimo, Ali 2016) suggest that depending on alliance types, partners firms will have suitable control strategies to help to increase alliance performance. Partner firms can control their alliances through either 'broad control' or 'focused control' (Geringer & Hebert, 1989). The partner firms can choose to have a broad control and attempt to exercise control over the entire range of the IJV's activities, or they can have a narrow (or focused) control and devote their control activities to the performance dimensions that they consider to be critical (Geringer & Hebert, 1989; Groot & Merchant, 2000). Broad controls can help partners to lead the alliances to go exactly to the place that the partners want it to be. However, with broad control by partners, there will be much less room for the operations to be flexible and much less room for trying and testing new ideas and thus reduce its DCs to function as well as its creativity. On the other hand, with narrow controls, partner firms can allows the operations of alliances to have more space to strengthen their flexibility and thus stimulate DCs to innovate especially in ecological aspect (Georgsdottir & Getz, 2004). As a result, I propose that:

> *Proposition 7: Control strategies by partner firms moderate relationship between cultural diversity, alliance types and ecological innovation performance such that focused control strengthens the positive relationship while broad control weakens it.*

Discussion and Conclusion

In increasingly challenging global economies, firms that sustain their competitive advantage through ecological innovation will be able to stay ahead of their competitors. In this

chapter, I discussed the role of cultural diversity and alliance types on the relationship with ecological innovation in multinational strategic alliances. I further discussed the moderating role of parent control on these relationships. Based on our arguments and discussion, I conclude that exploration, foreign market focused, legitimacy oriented, non-related business and equity alliances tend to be associated with more ecological innovation than exploitation, domestic market focused, business related, competency oriented, and non-equity alliances. In addition, cultural diversity between partners can increase level of ecological innovation in the alliance, if the result of cultural diversity between partners is cultural synergy. In contrast, if the result of cultural diversity is cultural conflict, cultural diversity can reduce the level of ecological innovation. I, in addition, conclude that right control by partner firms can strengthen the relationship between alliance types, cultural diversity and ecological innovation.

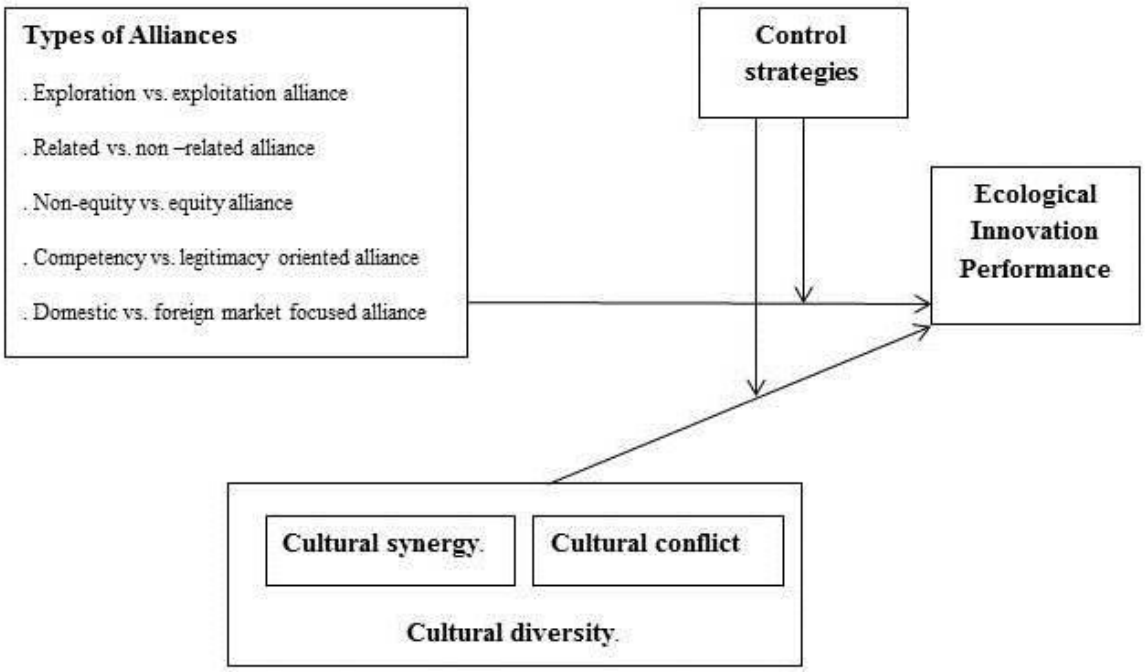

Figure 1. Configuration of Alliance, cultural diversity and ecological innovation

This study has some important implications for research in the areas of firms' dynamic capabilities (Teece et al., 1997; Teece, 2018), strategic alliances, and corporate social responsibility. This study attempts to contribute to these areas by proposing a model that analyses how ecological innovations can be archived through strategic alliances. The study has important contribution for managers. It is critical for firms to choose the right alliance partners or the right type of alliances by knowing what types of alliances are associated with more environmental friendliness. Moreover, knowing that cultural diversity can lead to cultural conflicts, managers can prevent this from happening by e.g. adopting cultural training programs, improving partners' communication skills and thus stimulating cultural diversity to improve cultural synergy (Globocnik et al., 2019) which is one of the important inputs for ecological innovation.

As with many other studies, our paper has several limitations. First, our discussion and conclusion are based on theoretical analysis, thus our model (Figure 1) needs to be validated by empirical data. In addition, Cheah et al., (2018) maintain that there is limited knowledge of innovation especially in service industry such as in retail industry. Thus, future studies can investigate ecological innovation of this industry using our model to see if it holds true. Furthermore, ecological innovation is sometimes initiated by local politicians or non-profit organizations (NGOs). In our study, we do not specify this special kind of strategic alliance where one partner is an NGO or initiated by local politicians. In this study I assume that both partners in the alliances are MNCs. Future studies related to ecological innovation can take into account this special type of strategic alliance. In addition, in the analysis I divided alliances into domestic market focused vs. foreign market focused alliances but in practice, there may have alliances which can focus on both domestic and foreign markets. Similarly, there is also a case that some alliances can be established for both competency and legitimacy oriented. Therefore, future studies can investigate how these special kinds of alliances link to economical

innovations. Finally, ecological innovation requires resource and capability (Hagedoorn & Duysters, 2002) being contributed by partners. In the study, I excluded the discussion of the role of partner´s contributions such as the quality, complementary of the resources. Thus, future research can investigate this issue on ecological innovation in strategic alliance.

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