# BSM 933 - International Business Lecture 5-7

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#### Internationalisation of firms

- Drivers and processes
  - Product cycle hypothesis (Vernon)
  - Uppsala "psychic distance" model (Johanson and Vahlne)
  - OLI-Eclectic theory (Dunning)
  - LLL-extended OLI theory about internationalisation of emerging market firms (Mathews, Dunning and Lundan)
- Choice of entry mode
  - Greenfield investment vs. acquisitions vs. joint ventures

#### Product cycle hypothesis Construct – I

#### Assumptions

- All developed country firms are similar in the sense that they have access to the same scientific facts and "technology"
- But countries may differ in their ability to translate this knowledge into commercial products; firms in countries like the USA might be better at commercialising scientific knowledge than those in many other countries

#### Early stage of commercialisation

- Producers are unsure about the optimal input mix that they would need to produce the product
- Price elasticity of demand for each firm's product is low and hence firms are not particularly worried about cost differences with other firms
- Successful commercialisation requires resolution of various uncertainties and this in turn requires swift communication among firms, consumers and suppliers

#### Product cycle hypothesis Construct – II

#### Maturing product

- Standardisation of product (which is not inconsistent with attempts at product differentiation)
- This, in turn, opens up the possibility of mass production and economies of scale (at a time when cost considerations are becoming important)

#### Standardised product

- A standardised product can be sold to (and produced in) developing country markets without (significant) disruption in the production process
- Developing countries are generally endowed with cheap labour and this labour can then be used to overcome the informational (and institutional?) problems at the local level, to facilitate the marketing of the product

# Product cycle hypothesis Locational implications – I

- All the issues associated with early stage commercialisation "argue for a location in which communication between the market and the executives directly concerned with the new product is swift and easy, and in which a wide variety of potential types of input that might be needed by the production unit are easily come by".
- If the [maturing] product has high income elasticity of demand or if it is a satisfactory substitute for high cost labour, the demand in time will begin to grow quite rapidly in relatively advanced countries such as those of Western Europe. Once the market expands in such an advanced country, entrepreneurs will begin to ask themselves whether the time has come to take the risk of setting up a local producing facility."
  - Location of production facilities in other [advanced] countries (in part, through *pull* from the countries that have a disadvantage in the trade for the product)
  - Use these overseas locations as launching pads for exports to other countries
  - If economies of scale are sufficiently high in those location, import from those locations to the USA

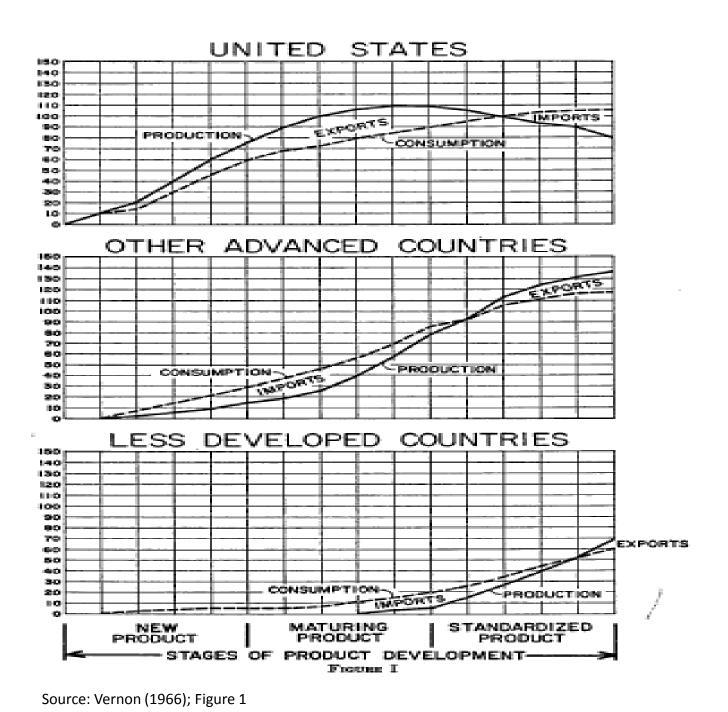
## Product cycle hypothesis Locational implications — II

- Production of standardised products can move to the "south", and capital
  requirements for setting up production facilities are unlikely to deter this exodus
  either because of international or cross-border investments or because capital
  scarcity does not impact all ventures in the developing countries equally
  - Vernon's examples include the generic (i.e., not "high-style") products of the textile industry, and standardised high volume products of the electronics goods industry
  - There are implications for global value chains

# Product cycle hypothesis Visual (and impact)

"The product cycle hypothesis has also attracted considerable attention among international trade theorists .... Paul Krugman (1979) developed a simple model of trade in which new goods are produced in the industrialized North and exchanged for old goods produced in the South. .... Krugman (1979) specified a very simple form of technology transfer, with new goods becoming old goods at an exogenous rate. .... Grossman and Helpman (1991a, b) developed models in which purposeful innovation and imitation gave rise to endogenous product cycles, with the timing of production transfer being a function of imitation effort exerted by firms in the South."

Antras, P. (2005). Incomplete contracts and the product cycle, *American Economic Review*, 95(4): 1054-1073.



#### Product cycle hypothesis Revisited

- Changes since the 1950s and 1960s
  - MNEs have global networks, and increasingly the first port of call outside the home country is not to a culturally or institutionally familiar location
  - There is considerable institutional (and environmental) homogeneity among developed countries [and even developing countries are adopting some developed country institutions]

#### Implications

- If a firm has "global scanning" facilities such that it can costlessly obtain and translate information about other markets then PCH would play very little role in its evolution
- If a firm innovates to produce standardised products for global markets (e.g., aircraft), it takes on major risks and hence may want to keep innovation activities close to their home country, consistent with the PCH hypothesis
- If a firm focuses on its home market and leaves "analysis of foreign markets" to its subsidiaries then some of the implications of PCH will still apply but "the phase of the product cycle in which the parent is responsible for serving the foreign market will be foreshortened"

## Product cycle hypothesis Relevance – an example



Product life cycle theory predicts that after expanding into new, gr owing markets, as a product matures, companies will seek out low-cost production locations based on lower wages. Ultimately, as the product becomes a commodity, it is imported to the country in which it was originally produced. In the case of biomanufacturing, as technology has improved, regulation has loosened, and companies have become more comfortable making biologics, they have indeed moved production to lower cost locations, even if the product is not quite a commodity. However in this case, it is lower tax rates, not labor costs, that are driving the cost advantages, and they are found not only in "the South" or regions and countries in developing countries, but also in the "North" in a few European countries. In fact, offering a lower tax rate has been part of a concerted effort by a few countries and/or regions in the world to build up world-class biomanufacturing operations. This "middle station" between production in the innovator country such as the US, and production in the low cost country such as China or India, has emerged because of some of the unique attributes of the biomanufacturing industry. While a drug is under patent and no biosimilars exists, a company has on average 12 years of monopoly profits for its drug. Given the desire to be closer to major markets, and the relative lack of qualified, lower-cost manufacturing options in Asia that will provide solid IP protection, companies preferred to locate their facilities within the Triad. Knowing this, a number of countries and regions have differentiated themselves within the Triad by using tax breaks to attract biomanufacturing investments.

Reylonds, E.B. (2010). Institutions, public policy and the product life cycle: The globalization of biomanufacturing and implications for Massachusetts, Ph.D. dissertation submitted to the Massachusetts Institute of Technology. Downloadable from http://web.mit.edu/ipc/publications/pdf/IPC-Reynolds-dissertation.pdf, pp. 87-88.

Product cycle hypothesis – partial evidence

Table 3: Probit and Truncated Regression Models of Innovation and Export Propensity in UK and German Manufacturing Firms

	UK			Germany		-
Dependent Variable	Export Indicator	Export Propensity	•	Export Indicator	Export	_
	0/1	%		0/1	Propensity %	
Part A						
Constant	-0.452	-49.316**		-0.511**	-44.199**	-
	(-0.253)	(-3.182)		(-3.809)	(-3.332)	
Part of Multi-plant Group	0.030	5.236**		0.066	3.566*	
	(1.140)	(2.962)		(1.088)	(1.641)	
Graduate Employees	0.007**	0.174**		-0.003**	-0.051	
	(3.557)	(2.943)		(-2.922)	(-0.720)	
R&D Department in Plant	-0.793**	36.222*		0.893**	-11.012	
-	(-2.002)	(1.753)		(2.428)	(-1.087)	
R&D in Plant	0.157	9.317**		0.136**	0.691	
	(0.527)	(3.736)		(3.264)	(0.387)	
Plant Employment (x10 <sup>3</sup> )	0.297**	1.182		0.921**	1.813	
• •	(2.381)	(0.393)		(3.813)	(0.471)	
Plant Employment (Squared)	-0.019**	-0.067		-0.162**	-0.211	
	(-2.062)	(-0.266)		(-3.616)	(-0.263)	
Product Innovation	0.134**	0.307		0.146**	2.119	
	(4.394)	(0.144)		(4.658)	(1.235)	

Roper, S. and Love, J.H. (2002). Innovation and product performance: Evidence from UK and German manufacturing plants, *Research Policy*, 31(7): 1087-1102.

#### Uppsala model Construct

#### Empirical background

• ".... Swedish firms often develop their international operations in small steps, rather than making large foreign production investments at single points in time. Typically, firms start exporting to a country via an agent, later establish a sales subsidiary, and, eventually, in some cases, begin production in the host country."

#### Proposition

 ".... the time order of such establishments seems to be related to the psychic distance between home and the import/host countries. .... The psychic distance is defined as the <u>sum of factors preventing the flow of information from and to the</u> <u>market</u>. Examples are differences in language, education, business practices, culture, and industrial development."

#### Evidence base

Case studies

# Uppsala model Preliminary observations

- Why could internationalisation be incremental?
  - New business contexts expose firms to both new opportunities and problems, but firms generally do not have ready solutions for the problems and have to develop or discover solutions on a case-by-case basis.
  - The process of problem solving in new contexts may be intermediated by uncertainty and (generally lack of) access to information. (Note that uncertainty and lack of information are not one and the same thing.)

Table I
Establishment Patterns for the Investigated Firms.

	Pattern	Sales subsidiary			Production subsidiary	
Firm	n a ↓ ↓ s s	n ↓ p	a ↓ p	s ↓ p		
Sandvik		2	18	0	2	13
Atlas Copco		3	14	0	3	9
Facit		0	14	0	2	3
Volvo		2	10	0	2	3
	* 555	7	56	0	9	28

<sup>&</sup>quot;n" denotes no regular export activity

<sup>&</sup>quot;a" denotes selling via agent

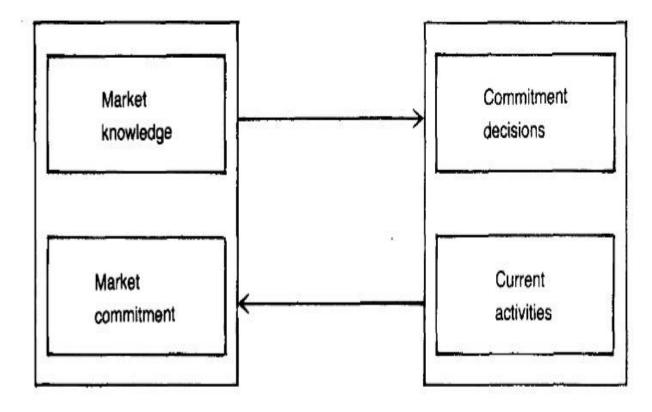
<sup>&</sup>quot;s" denotes sales subsidiary

<sup>&</sup>quot;p" denotes production subsidiary an arrow denotes change from one state to another

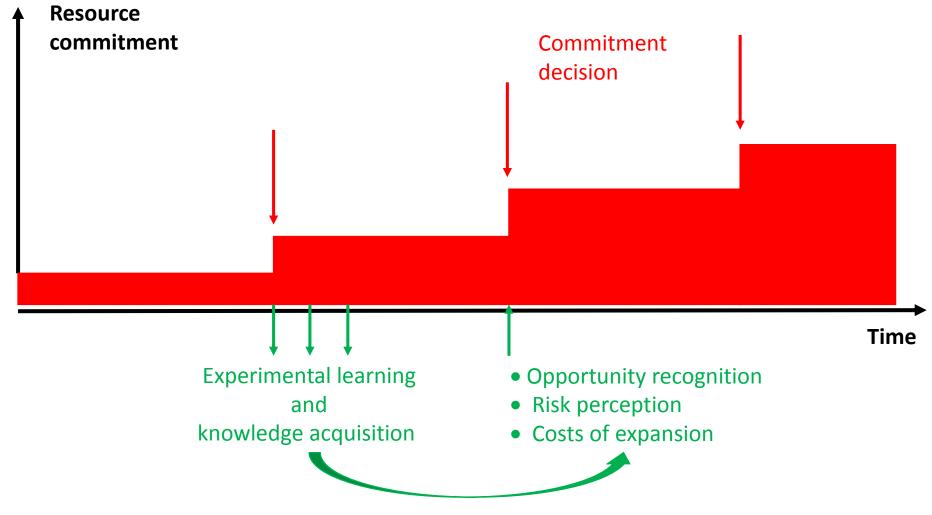
# Uppsala model Paradigm

- Market knowledge
  - Objective knowledge vs. Experimental knowledge
  - Key determinant of market commitment
- Commitment decisions
  - Relates to the extent of the "specificity" of a firm's assets to a given context
- Current activities
  - Generates experimental knowledge
- Market commitment
  - Depends significantly on market knowledge

Figure 1. The Basic Mechanism of Internationalization—State and Change Aspects.

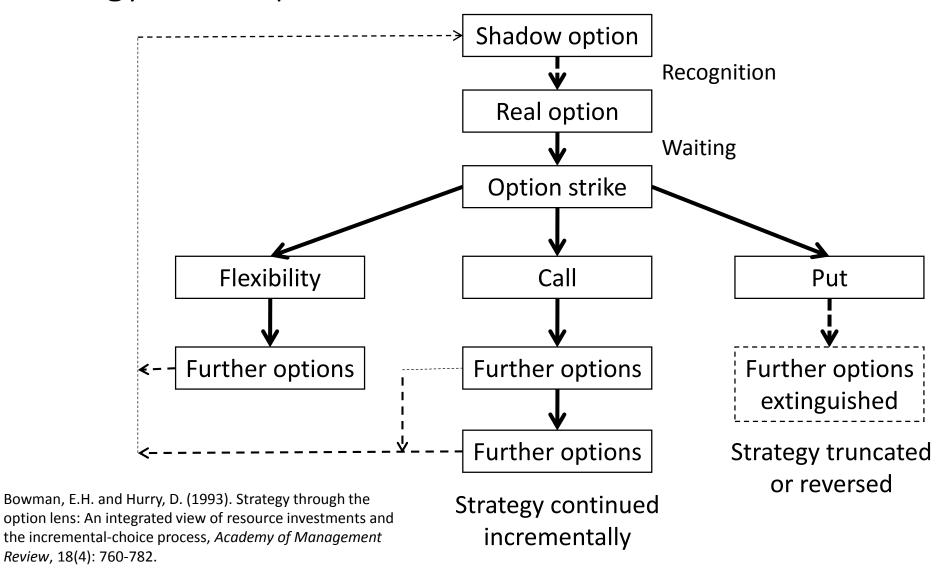


# Uppsala model Stages of internationalisation – visual



Source: Peng and Meyer (Figure 11.2)

## Digression Strategy as an option chain



## Uppsala model Updated – I

- "Knowledge does not accrue only from the firm's own activities, but also from the activities of its [network] partners, and since those partners also have other relationship partners with whom their activities are coordinated, the focal firm is indirectly engaged in a knowledge creation process that extends far beyond its own horizon. .... [W]e [therefore] add to our model the concept of relationship-specific knowledge ...."
- One also has to take into issues such as trust that "persuades people to share information, promotes the building of joint expectations, and is especially important in situations of uncertainty"
- "We do not believe that the correlation between the order in which a company enters foreign markets and psychic distance has weakened. .... [T]he relationship between market entry order and psychic distance operates at the level of the decision-maker, not that of the firm. .... [Also] the concept of liability of outsidership does not necessarily refer to countries. It is a firm-level concept that may relate to a network within a country, or to a wider region"

## Uppsala model Updated – II

- Opportunities constitute a subset of "knowledge" and are more important that other aspects of knowledge
- Relationships are characterised by the a combination of both knowledge as well as commitment and trust
- Learning is based not only on experimentation but also on the tacit knowledge of network partners
- A commitment to the relationship based on trust and commitment cements a firm's position within the network

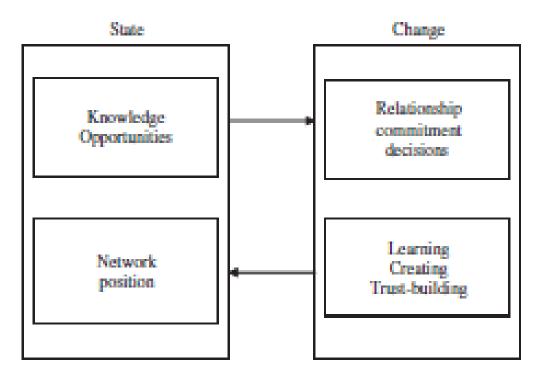
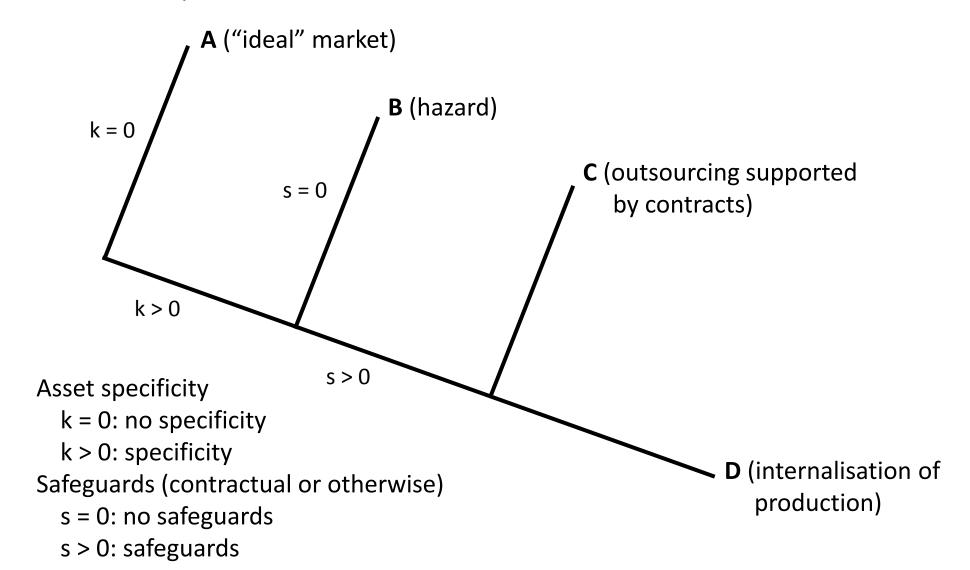


Figure 2 The business network internationalization process model (the 2009 version).

#### OLI model Structure

- A firm has **0**wnership-advantages
  - These advantages (e.g., proprietary technology, management knowhow, business model, brand, logistics) are transferrable across countries
  - They enable the firm to overcome liability of foreignness
- There are Locational-advantages associated with the local context (e.g., natural resources, skilled labour, market size and trade barriers, agglomeration, institutional quality)
  - The locational advantages allow the firm to create value that it could not have created in its home country
- The activities across the home and local locations are best organised Internally within the firm, rather than through arm's length market transactions
  - The rationale for organising production activities internally stems from the logic of transactions cost

# Digression Organisation of production within a firm



## OLI model Internalisation advantages – examples

#### FDI vs exporting

- Aluminium smelting firm in Europe and bauxite mine in Latin America
- Hold up problem because the aluminium smelting firms are required to have <u>specific features</u> to use the Latin American bauxite

#### FDI vs licensing

- Licensing involves dissemination risk, i.e., the risk that there would be unauthorised dissemination of the proprietary technology of the licensor
- The cost of transferring tacit knowledge may be prohibitively high
- The cost of monitoring quality and standards may be prohibitively high

#### FDI vs outsourcing

- Hold up problem because the offshore firm may have to make investment in contract-specific assets
- There is once again dissemination risk
- The cost of monitoring quality and standards may be prohibitively high

## OLI model Some criticisms and response – I

- The model identifies so many explanatory variables that its predictive power is zero
  - "[E]ach and every OLI variable identified by the eclectic theory is well grounded in economic or organisational theory"
  - "[T]he purpose of the eclectic paradigm is not to offer a full explanation of all kinds of
    international production but rather to point out a methodology and to a generic set of
    variables which contain the ingredients necessary for any satisfactory explanation of
    particular types of foreign value-added activity"
- The O, L and I variables are not independent of each other, e,g., when a firm plans to add to its O-advantages through R&D, it may have to reconsider the locations of its R&D sites
  - "Accepting .... the logic behind this criticism, I nevertheless believe there is something to be said for separating those reasons for MNE activity which are primarily due to the unique resources and capabilities possessed or accessed by firms of a particular ownership .... From those to do with the location-bound resources and markets of the countries in which they operate"

## OLI model Some criticisms and response – II

- OLI is a static paradigm with insufficient role for strategy
  - "At a given moment of time, the extent and pattern of MNE activity represents a point on a set of trajectories forward (or, for that matter, away from) their internationalisation path. The trajectory itself is set by the continuous and iterative interaction between the OLI configuration over successive time periods and the strategy of the firms in response to these configurations that, in turn, will influence the OLI paradigm in a subsequent moment in time"
  - "Later scholars have more explicitly introduced a time- and strategy-related dimension into their analysis. .... [R]einterpreting Knickerbocker's analysis in terms of OLI paradigm, we may say that firms are prompted to go overseas, in part at least, because they consider their O advantages are (or could become) threatened, if they do not follow their competitors' lead or because their advantages would be less without their presence. In other other words, the strategy followed by firms in response to a given OLI configuration in time  $t_0$  is governed by their desire to protect or influence that configuration in  $t_1$ "

Table 1. The contributions of Dunning and Vernon to international business theory and policy

	1950s		1990s
Key Issue	Dunning (1958)	Vernon (1966)	Globalization theory today
Unit of analysis	United States TNC in a host nation (country level)	United States TNC from a home base (Industry + country level)	Triad-based TNCs (United States, E.U., Japan) (firm Level)
Type of FDI	one-way Inward	one-way outward	two-way FDI
Basic theory	benefits and costs of FDI	home base firm innovation and timing of FDI	Internalisation/eclectic theories resource based view holistic approach
Public policy	assess foreign ownership and performance of TNCs; regulate FDI	understand reasons for home-host country production switches	liberalize both inward and outward FDI
Managerial Implications	hierarchical parent; branch plant	hierarchical home parent controls location and timing of subsidiary production	choice of home base or strategies plus the development of associated core competencies and dynamic organizational capabilities

Source: the author's compilation.

# Accounting for EMNEs Background



- [The] success [of the first wave MNEs from the developing world] was due as much to the difficulties encountered at home (such as market restrictions and export difficulties) as to the incentives driving internationalisation
- The emergence of the second wave MNEs is to be sought in pull factors that draw firms into global connections, rather than push factors that drove firms as standalone players in the first wave. .... [T]he rise of second-wave MNEs from emerging economies "is less driven by cost factors per se, but more by a search for markets and technological innovations to compete successfully in the global economy"
- Their sudden appearance cannot be explained by conventional multinational strategies .... Nor can their appearance be attributed to a new form of small firmlarge firm dependence, since many of the newcomers and latecomers are shaping the emergent form of a global market .... They are not simply occupying space vacated by incumbents, because in many cases they are creating new economic space by their own organisational and strategic innovation

# Accounting for EMNEs Examples

- Ispat (Mittal Steel)
  - Started as a small steel producer in Indonesia in 1976
  - First international foray in 1989, into the Caribbean
  - Competitive advantage based on <u>latecomer advantage</u> in utilization of mini mills and electric arc technology
  - Global network of interconnected mini mills developed through acquisition of state-owned steel mills and other steel mills that Ispat could run at a lower cost than their incumbent management

#### Acer

- Founded in Taiwan in 1976
- Started its internationalisation in the late 1980s through large acquisitions, and, chastened by the financial shock that followed readjusted its strategy to one of incremental growth in the periphery
- Its competitive advantage is based on innovative organisational forms that it developed as a latecomer, involving the use of a "fast food" business model, whereby local businesses locally assemble components manufactured and shipped out from Taiwan

# Accounting for EMNEs Distinctive characteristics

- Accelerated internationalisation
- Organisational innovation
  - Acer's "fast food" model that helps overcome subsidiary-headquarter conflicts (Is process innovation an O-advantage?)
- Strategic innovation
  - Internationalisation strategy designed to enhance access to resources and leverage strengths of other firms, rather than on leveraging their own strengths
  - "[G]lobal giants see themselves as having much to lose, and little to gain, by sharing their resources in partnerships and other contractual alliances. The newcomers and latecomers, by contrast, have everything to gain by tapping the resources of others, and internationalise explicitly with this goal"

# Accounting for EMNEs Linkage-leverage-learning

#### Linkage

- The focus of the (small/medium) EMNE is not leveraging its own advantages but to leverage advantages of other firms through linkage
- In order to mitigate the risks associated with outward ventures, the small/medium EMNEs will prefer partnerships and JVs over wholly owned subsidiaries

#### Leverage

- The EMNE's focus will be on the resources that are available externally and the accessibility of these resources
- This contrasts with the conventional narrative about *O*-advantages where the concern was about diffusion of proprietary knowledge or advantages

#### Learning

• The knowledge obtained through linkage can be leveraged efficiently only after learning, and this can be done through repeated acquisitions (e.g., Ispat) or creating mechanisms to ensure flow of knowledge from the partners to the EMNEs

Table 2 Why do MNEs out-compete their domestic rivals? OLI and LLL frameworks compared			
Criterion	OLI	LLL	
Resources utilized	Proprietary resources	Resources accessed through linkage with external firms	
Geographic scope	Locations established as part of vertically integrated whole	Locations tapped as part of international network	
Make or buy?	Bias towards operations internalized across national borders	Bias towards operations created through external linkage	
Learning	Not part of the OLI framework	Learning achieved through repetition of linkage and leverage	
Process of internationalization	Not part of the OLI framework: MNE's international reach assumed	Proceeds incrementally through linkage	
Organization	Not part of OLI framework; organization could be multinational or transnational	Global integration sought as latecomer advantage	
Driving paradigm	Transaction cost economics	Capturing of latecomer advantages	
Time frame	Comparative static observations, comparing one point in time with another	Cumulative development process	

# Accounting for EMNEs Rethinking competitive advantages

#### **Country-specific advantages**

- Natural resources (Brazil, Russia)
- Large home market and low cost labour (China)
- Ethnic social networks in other countries (China in SE Asia)
- Combination of high skilled labour and overseas networks (Israel)
- Idiosyncratic or historical factors (English education in India)
- Government relationships

#### Firm-specific advantages

- Products suited to emerging markets
- Production and operational excellence
- Privileged access to resources and markets (through government relationships)
- Adversity advantage (through innovation to mitigate institutional weaknesses
- Traditional intangible assets (e.g., biofuels in Brazil)

# Accounting for EMNEs Stages of evolution

	Stage 1:  Infant MNE	Stage 2: Adolescent MNE	Stage 3: Mature MNE
Importance of home- country CSAs	High	High to Medium, and falling	Medium to Low, and falling
Ratio of exports to overseas production	Exports exceed overseas production	Exports and overseas production in balance	Overseas production exceeds exports
Geographic footprint	Few countries in home region, unless EMNE is pursuing the low-cost partner strategy	Several countries, with emphasis on home region	Dozens of countries, in all major regions
Brand	Strong at home, unknown abroad	Strong at home, up- and-coming abroad	Strong global brand
Examples	Most EMNEs	Korean MNEs, such as LG or Hyundai	Western and Japanese MNEs, such as IBM, Siemens, Sony, or Toyota

Ramamurti, R. (2008). What have we learned about emerging-market MNEs? Insights from a multi-country research project, In: Ramamutri, R. and Singh, J. (Eds.) *Emerging Multinationals from Emerging Countries*, Cambridge, UK: Cambridge University Press, Chapter 13.; Table 13.3.

## Entry decision Choice of location

Strategic goals	Location-specific advantages	Examples
Natural resource seeking	Quality and cost of natural resources	Oil exploration in the Middle East, Russia and Venezuela
Market seeking	Strong market demand and customers willing to pay	Manufacturing and sale of good anywhere in the world
Efficiency seeking	Economies of scale, abundance of low-cost labour force and suppliers, transport and communication infrastructure	Manufacturing in Guandong, China; Logistics in Rotterdam, Vienna and Miami
Innovation seeking	Innovative individuals, firms and universities, industry agglomeration	Chinese acquisitions of technologies and brands in Germany; Bio-tech firms in Cambridge and Copenhagen; IT in Silicon Valley and Bangalore

Source: Peng and Meyer (Chapter 12); Table 12.1

# Entry decision Timing of entry – pros and cons of early entry

- First mover advantages
  - Early establishment of a strong brand enables the firm to pre-empt competitors
  - Early entry can also impose switching cost on customers that further pre-empt competitors
  - Early build up of sales volume can generate scale and "experience curve" economies
- First mover disadvantages arising from "pioneering costs" that result from the following:
  - The cost of learning that pioneers have to bear while late entrants can free ride on the experiences of the early entrants
  - The cost of creating customer awareness about overseas brands and products which once again late entrants may not have to bear to the same extent
  - The (potential) cost of regulatory changes that can render an early movers strategies ineffective

# Entry decision Options approach to decision about timing of entry

Minimal competition Retain option until weaker competitors exercise it; pre-No pre-emption risk and hence emption possible but dominant option held till expiration firm can corner most of the benefits of exercising option **Shared option Proprietary option** competition Early exercise of options to Rapid exercise of option for preclude loss of value on defensive or pre-emptive account of competition reasons Intense

# Entry decision Advantages and disadvantages of entry modes

Entry mode	Advantages	Disadvantages
Exporting	Ability to realise location and experience curve economies	High transportation cost Trade barriers Problems with local marketing agents
Turnkey contracts	Ability to earn returns from process technology skills in countries where FDI is restricted	Creating efficient competitors Lack of long term market presence
Licensing	Low development costs and risks	Lack of control over technology Inability to realise location and experience curve economies Inability to engage in global strategic coordination
Franchising	Low development costs and risks	Lack of control over quality Inability to engage in global strategic coordination
Joint ventures	Access to local partner's knowledge Sharing development costs and risks Politically acceptable	Lack of control over technology Inability to engage in global strategic coordination Inability to experience location and experience economies
Wholly owned subsidiaries	Protection of technology Ability to engage in global strategic coordination Ability to realise location and experience economies	High costs and risks

Source: Hill (Chapter 15); Table 15.1

# Source: Peng and Meyer (Chapter 12); Table 12.3

# Entry decision Advantages and disadvantages of equity entry modes

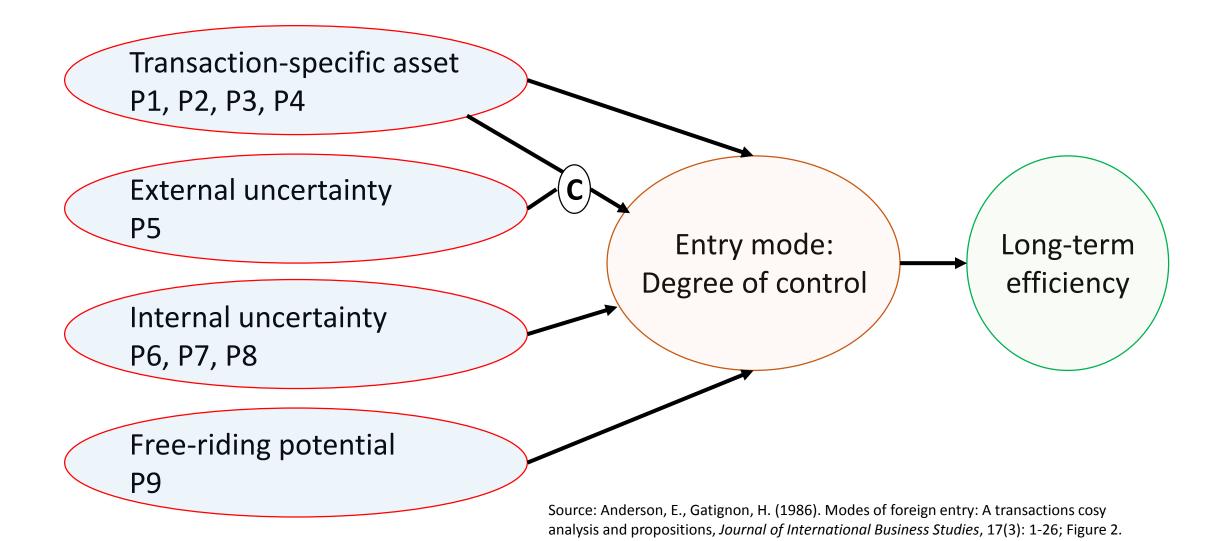
Entry mode	Advantages	Disadvantages	Risks
Greenfield	Designer operations to fit the parent Complete equity and operational control, hence better protection of know-how and ability to coordinate globally Option to scale operations to needs	Adds new capacity to industry Slow entry speed (relative to acquisitions)	No co-owner related risks No integration-failure risk High investment risk due to large capital commitment and long pay- back periods
Full acquisition	Complete equity and operational control, hence better protection of know-how and ability to coordinate globally Does not add new capacity Fast entry speed	Political sensitivity High up-front capital needs Post-acquisition integration challenges	High investment risk due to large up- front capital commitment Integration process related risks No co-owner related risks
Joint ventures	Sharing costs and risks (and profits) Access to partner's knowledge and assets Politically acceptable	Divergent goals and interests of partners Limited equity and operational control Difficult to coordinate globally	Limited investment risk due to lower capital commitment High risk of coordination failure
Partial acquisition	Access to operations that the previous owner is reluctant to give up Previous owner's continued commitment	Need to restructure and integrate, yet with limited control	Limited investment risk due to low capital commitment High risk of integration problems High risk of conflict with co-owner

# Entry decision Pros and cons of acquisitions

Туре	Purpose (example)	Risks
Conventional acquisition	Take over a company that has complementary resources and capabilities	Overpayment Post acquisition integration
Brownfield acquisition	Obtain specific asset controlled by another firm, but upgrade it to fit global operation	Very high capital investment Complex post-acquisition upgrading and integration
Multiple acquisitions	Build a strong market share in a previously highly fragmented market	Very high capital investment Integration of multiple local units, as well as integrating them with the global operation
Staged acquisitions	Take over a firm whose owners are unwilling to let go, or where their continuing commitment is important	Integration process with initially limited control Uncertainty over long-term ownership structure

Source: Peng and Meyer (Chapter 12); Table 12.5

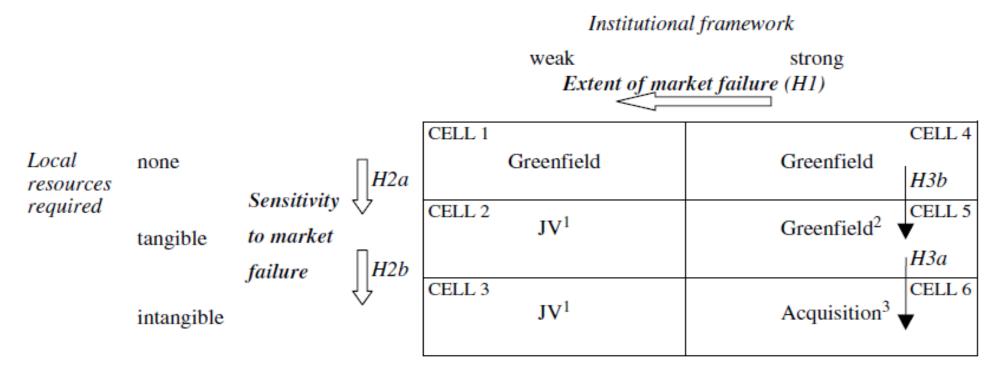
# Entry mode choice Transactions cost approach – I



## Entry mode choice Transactions cost approach – II

- P1: Modes of entry offering greater control are more efficient for highly proprietary products or processes
- **P2:** Entry modes offering higher degrees of control are more efficient for unstructured, poorly-understood products and processes
- P3: Entry modes offering higher degrees of control are more efficient for products customised to the user
- P4: The more mature the product class, the less control firms should demand of a foreign business entry
- **P5:** The greater the *combination* [**C**] of country risk and transaction-specificity of assets (P1-P4) the higher the appropriate degree of control
- **P6:** The entrant's degree of control of a foreign business entity should be positively related to the firm's cumulative international experience
- **P7:** When sociocultural distance is great, high-control levels are more efficiency only when there is a substantial advantage to doing business in the entrant's way
- P8: The larger the foreign business community in the host country, the lower the level of control
  an entrant should demand
- P9: Entry modes offering higher degrees of control are more efficient the higher the value of a brand name

## Entry mode choice Integrating TCE with resource based view



<sup>&</sup>lt;sup>1</sup> In rare cases acquisition may be feasible (e.g., acquiring subsidiary of another MNE).

Source: Meyer, K.E., Estrin, S., Bhaumik, S.K., Peng, M. (2009). Institutions, resources and entry strategies in emerging economies, *Strategic Management Journal*, 30(1): 61-80; Figure 1.

<sup>&</sup>lt;sup>2</sup> Except when asset specificity is high, when acquisition or JV may be appropriate.

<sup>&</sup>lt;sup>3</sup> Except when market failure is bilateral and takeover is infeasible (e.g., due to scale issues), when JV may be appropriate.

#### Entry decision Risk management perspective Model risk Information Risk ignorance Success/ Agency Stress test Failure Managers risk Risk Instruments transformation Internal vs. outsourcing Cost