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Foreword

This Festschrift is presented in honour of Professor Jorma Larimo on the occasion of his 60th birthday on 27th September, 2014. It consists of 12 contributions by over 20 scholars from Finland, as well as Australia, Austria, Germany, Italy, Sweden, Slovakia, and United Kingdom showing the global outreach of Professor Larimo's research and academic contacts. He has been a dedicated researcher, lecturer and academic administrator, and over the years contributed immensely to international business subject area. During the process of editing this Festschrift, we also realized the respect he receives from academic colleagues from a various specializations and this collection of articles is a well deserving tribute to him.

This Festschrift contains chapters addressing a diverse range of topics, yet linked with Professor Larimo's areas of interest in one way or another. Foreign direct investment (FDI) by multinational enterprises (MNEs), and its performance analysis at both subsidiary and head quarter levels have been an interest area of Professor Larimo. Hence, the paper by Professor Stefan Schmid (ESCP Europe, Berlin, Germany) and Katharina Hefter (ESCP Europe, Berlin, Germany) is a good starting point for this book, as it develops a typology for subsidiary performance evaluation, and is expected to receive applause by Professor Larimo because of his key interest in this area.

The papers by Dr. Arnold Schuh (Vienna University of Economics and Business Administration) and Professor Sonia Ferencikoa are focussed on Central and Eastern Europe, a geographical area that saw enormous changes in transition to market economy, and has been one of the focus area in Jorma's research. Moreover, the paper by Professor Tuija Mainela (University of Oulu, Finland) and Professor Asta Salmi (Aalto University School of Business, Finland) addresses the transition markets of CEE from a relatively novel perspective of social network embeddedness. Due to Professor Larimo's close association to CEE region depicted by frequent academic visits and published papers, these papers are an important corner stone of this book.

The paper by Dr. Douglas Dow (Melbourne University, Australia) critically reviews the concept of "distance" in IB research. Professor Larimo has written many distance (psychic, cultural and institutional) focussed papers, and also collaborated with Dr. Dow in this concern. Hence, this paper is a well-deserved addition to the Festschrift.

The paper by Professor Rebecca Piekkari (Aalto University School of Business, Finland) and Professor Ingmar Björkman (Aalto University School of Business,

Finland) overviews Professor Larimo's contribution to process research in IB based on analysis of one of his most cited academic work. This paper is a well written tribute to Professor Larimo, where his academic, administrative and personal contributions are reviewed.

The paper by Professor Amjad Hadjikhani (Uppsala University, Sweden), Professor Pervez Ghauri (King's College London, UK) and Dr. Agnieszka Chidlow (Manchester Metropolitan University, UK) addresses the critical role that European Union plays in internationalization of the firms. Professor Larimo has been involved in research projects where country and super-national level institutional factors have been analysed in relation to internationalization activities of firms; this paper certainly adds value to the Festschrift.

One of the key contribution of Professor Larimo relate to organizing Vaasa IB Conference on regular basis, where international entrepreneurship and SME internationalization are one the key themes. The papers by Professor Antonella Zucchella (University of Pavia, Italy) and Dr. Stefano Denicolai (University of Pavia, Italy), as well as Professor Niina Nummela (University of Turku, Finland) and Dr. Eriikka Paavilainen-Mäntymäki (University of Turku, Finland) offer interesting insights to this important area of research. Moreover, the paper by Professor Peter Gabrielsson and Professor Mika Gabrielsson's book chapter address SME internationalization from a very interesting perspective of born global firms and stages in their growth and survival.

The paper by Professor Adam Smale (University of Vaasa, Finland), Professor Ingmar Björkman (Aalto University School of Business) and Professor Vesa Suutari (University of Vaasa, Finland) analyse Finland's contribution to international human resource management field. This is an area, where Professor Larimo has not been directly involved in research. However, as mentioned by the authors in paper also, he played a key role in development of this research area, in capacity of organizing doctoral courses in his capacity as director of Finnish Graduate School of International Business (FIGSIB), and chief organizer of Vaasa IB conference.

Last but not the least; the paper by the department colleagues of Professor Larimo including Dr. Ari Huuhka, Professor Martti Laaksonen, and Professor Pirjo Laaksonen analyses the new systematic forms in retailing and digital business. Professor Larimo has also been interested in retail internationalisation and has research projects in this area; this paper certainly offers him ideas that can be linked with internationalisation research also.

Finally, we would like to offer our special note of thanks to Professor Jorma Larimo. Jorma! You have been an exemplary doctoral supervisor, fellow researcher, and mentor for us. With this Festschrift, we want to celebrate your 60th birthday and thank you because what we are doing today is closely linked with your influence and mentorship. You have not only played key role development IB doctoral studies in Finland, but also offered potential researchers (both local and international) a chance to learn from you and then continue the academic journey. We wish you all the best for future and hope that we can continue to benefit from you in coming many years.

Ahmad Arslan and Minnie Kontkanen,

2nd June, 2014,

Vaasa, Finland.

Jorma Larimo 60 Vuotta

Jorma Antero Larimo syntyi Vaasassa 27.9.1954. Ylioppilaaksi valmistumisen jälkeen hän suuntasi askeleensa kotikaupunkinsa kauppakorkeakouluun, josta valmistui kauppatieteiden maisteriksi 1979. Akateemisen uran valinta johti kauppatieteiden lisensiaatin tutkintoon 1987 ja kauppatieteiden tohtorin tutkintoon 1993. Tällä matkalla Vaasan kauppakorkeakoulu muuttui ensin Vaasan korkeakouluksi ja myöhemmin Vaasan yliopistoksi. Jorma onkin ehtinyt kokea akateemisen ympäristön voimakkaan muutoksen ja osallistua sen sisällön kehittämiseen nykyiseksi liiketoiminta-orientoituneeksi yliopistoksi.

Akateeminen ura assistentista lehtoriksi (nimitys 1985) ja lehtorista professoriksi (nimitys 2001) on ollut menestyksekkään suora. Sitä ovat vahvistaneet dosentuurit Aalto yliopistossa ja Turun yliopistossa sekä kansainvälisen markkinoinnin osa-aikainen professuuri Tarton yliopistossa. Hallinnollisen vastuun kantaminen on tullut Jormalle tutuksi niin markkinoinnin laitoksen johtajana (2004-2009), kauppatieteellisen tiedekunnan varadekaanina (2010-) kuin tiedekunnan tohtoriorjelman johtajanakin (2011-).

Mikä leimaa Jorma Larimoa akateemisena henkilönä? Useita määreitä voisi liittää häneen, mutta tässä tärkeimmät: intohimo tutkimukseen, asiantuntemus kansainvälisen liiketoiminnan alalla sekä kehittämisorientaatio kansainvälisen markkinoinnin tutkimuksen ja tohtorikoulutuksen kentässä.

Jorman asiantuntemukseen on luotettu niin kansallisella kuin kansainväliselläkin tasolla. Tästä ovat osoituksena erilaiset tieteelliset asiantuntijatehtävät, johtoryhmien jäsenyydet sekä vastuulliset tehtävät kansainvälisten konferenssien organisoimisessa. Lisäksi luottamus hänen tieteelliseen asiantuntijuuteensa on johtanut jäsenyyksiin kansainvälisen liiketoiminnan johtavien tieteellisten julkaisujen toimikunnissa (*International Business Review*, *Journal of East-West Business*, *Management of International Review* ja *Journal of Euromarketing*). Hän on arvioijana lähes kahdessakymmenessä alansa keskeisessä akateemisessa kansainvälisessä lehdessä. Samoin hän on toiminut väitöskirjojen arvioijana ja opponenttina useissa kotimaisissa ja ulkomaisissa yliopistoissa.

Aktiivinen toiminta tieteellisissä organisaatioissa on Jormalle luonteenomaista. Hänen osallistumisensa Suomen edustajana EIBAn (*European International Business Academy*) johtoryhmään 2000-2010, pitkäaikainen johtajuus FIGSIBissä (*Finnish Graduate School of International Business*) sekä johtoryhmän jäsenyys Katajassa (*Co-operation Association of Finnish Universities*) ovat hyviä esimerkkejä pyrkimyksestä vaikuttaa tieteellisissä verkostoissa. Konkreettinen esimerkki verkottumisen voimasta ja sen kautta luodusta onnistuneesta toimintamallista on

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hänen perustamansa ja organisoimansa kansainvälinen tieteellinen konferenssi ”*Vaasa Conference in International Business*”, joka on järjestetty Vaasassa hänen johdolla kaksitoista kertaa.

Jorman väitöskirjan aihe oli aikoinaan ”*Foreign direct investment behaviour and performance. An analysis of Finnish direct manufacturing investments in OECD countries*”. Tämä suorien investointien ja kansainvälisten operaatioiden teema on osoittautunut tärkeäksi ja hedelmälliseksi myös hänen omissa jatkotutkimuksissaan sekä hänen ohjaamissaan väitöskirjoissa. Tuloksena on syntynyt mm. toistakymmentä väitöskirjaa. Väitöskirjat ovat osittain syntyneet Jorman johtamissa tutkimusprojekteissa, joita ovat rahoittaneet mm. Suomen Akatemia.

Kaiken edellä mainitun karriäärin taustalla on luonnollisesti aiemmin mainittu intohimo tutkimukseen. Jorman oma tutkimustoiminta on laajaa, monipuolista ja tasokkaiisiin akateemisiin julkaisuihin yltänyttä (esimerkkeinä *Journal of International Business Studies*, *International Business Review*, *International Studies of Management and Organization*, *Journal of East European Management Studies*, *Management International Review*, *Journal of Global Marketing*, *Journal of Transnational Management*, *Journal of American Academy of Business*, *Journal of Euromarketing*, *Journal of East-West Business*, *Journal of International Marketing*, *Journal of Business Research* and *Journal of World Business*). Kaiken kaikkiaan hänen julkaisuluettelonsa sisältää pitkälle yli 200 merkintää.

Onko hän ehtinyt lainkaan opettaa? Toki. Hänen ohjauksessaan on syntynyt yli 200 pro gradu –tutkielmaa. Omiin tutkimusteemoihin pohjautuvien luentojen lisäksi Jorma on vinyt vuosittain opiskelijat idänkauppaan tutustumisen merkeissä ekskursiolle Pietariin. Nämä opintomatkat pitävät Jorman itsensäkin ajan tasalla varhaisesta kiinnostuksen kohteestaan. Muistelen hänen opiskeluaikojensa ensimmäisen seminaarityön aiheen jo liittyneen itään suuntautuvan vapaakauppajärjestelyjen teemoihin.

Mitä jäi sanomatta? Paljonkin. Muun muassa se, että Jorma on keräilijäluonne. Kohteena ovat olleet merkittävässä määrin niin postimerkit kuin musiikkitalenteet. Joku voisi lisätä myös tieteellisen ”arkistoinninkin” tämän taipumuksen piiriin. Tennis ja lentopallo ovat muodostaneet vastavoiman työlle talvisin ja mökkeily kesäisin. Ja koti Marjatan kanssa on tarjonnut toisen tärkeän kiinnostuksen kohteen Palosaarella.

Martti Laaksonen

Stundarsissa 2.6.2014

Jorma Larimo, 60 Years

Jorma Antero Larimo was born in Vaasa 27.9.1954. Graduated from high school, he headed to his home town Vaasa School of Economics from which he completed a Master's degree (Econ.) in 1979. Choice of an academic career led to a Licentiate degree (Econ.) in 1987 and Doctoral degree (Econ.) in 1993. During this journey from Masters of Science to Doctor of Science the Vaasa School of Economics changed to University of Vaasa. Jorma has had a chance to experience the dynamic change of the academic environment of the business school and participate in the development of its content for the current business-oriented university.

Academic career from Assistant to Lecturer of International Marketing (appointment 1985), and from Lecturer to the Associate Professor of International Business Operations (appointment 1987) and to the full Professor in International Marketing (appointment 2001) has been successful and a direct path. It has been confirmed by the positions as a docent at Aalto University and University of Turku, as well as international marketing part-time professorship at the University of Tartu. Administrative responsibilities Jorma has taken care of by acting as the head of the department of marketing (2004-2009), as a Vice Dean at the faculty of Business Studies (2010-) and as a director of the Doctoral Programme at the faculty of Business Studies (2011-).

What characterize Jorma Larimo as an academic person? A number of attributes could be attached to him, but here's the key: a passion for research, expertise in the field of international business, as well as an orientation toward continues development in the areas of research in international marketing and in doctoral education.

Jorma's expertise have been trusted both at the national and international level. This is evident by the various academic expert positions, board memberships, as well as responsible tasks in the organization of international conferences. In addition, confidence in his scientific expertise has led to memberships of editorial boards in leading scientific publications in international business (*International Business Review*, *Journal of East-West Business*, *Management of International Review* and *Journal of Euromarketing*). He acts as a referee in almost 20 academic journals relevant in his field. He has also served both as a pre-reviewer and an opponent of Doctoral thesis in several universities in Finland and abroad.

Active participation in the scientific organizations is a typical attribute of Jorma. His participation as representative of Finland in the board of EIBA (*European International Business Academy*) 2000-2010, his role as a long term director of

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FIGSIB (*Finnish Graduate School of International Business*) and board membership in Kataja (*Co-operation Association of Finnish Universities*) are good examples of the aim to affect through academic networks. A concrete example of the power of networking is the international academic conference "*Vaasa Conference in International Business*", he founded and organized. It has been arranged in Vaasa under his leadership, twelve times.

The topic of Jorma's doctoral thesis was "*Foreign direct investment behaviour and performance. An analysis of Finnish direct manufacturing investments in OECD countries*". This theme of direct investments and international operations has proven to be an important and fruitful in his further studies, and in the doctoral theses he has supervised. Jorma has been able to successfully supervise over ten doctoral theses, where some have been financed by prestigious organizations like Academy of Finland.

In the background of all of the above in his career is naturally the previously mentioned passion for research. Jorma's own area of research activities is wide and varied and his research has been published in high-class academic journals (e.g. *Journal of International Business Studies, International Business Review, International Studies of Management and Organization, Journal of East European Management Studies, Management International Review, Journal of Global Marketing, Journal of Transnational Management, Journal of American Academy of Business, Journal of Euromarketing, Journal of East-West Business, Journal of International Marketing, Journal of Business Research and Journal of World Business*). All in all, his list of publications includes far more than 200 entries.

Has he had time to teach at all? Sure. Under his supervision more than 200 Master's thesis has been completed. In addition to the courses based on his own research themes, Jorma has each year organized the students an excursion to St. Petersburg to get to know the Eastern trade. These excursions keeps also Jorma's own knowledge up to date with his interest in the early days of his academic career. I remember that the first topic of the seminar work in the beginning of his studies was related with the free-trade arrangements in Eastern markets.

What was left unsaid? A lot. Among other things, the fact that Jorma is a collector of nature. Focus has been to a significant extent on stamps and music records. One could also add a scientific "filing" to this tendency. In his free time tennis and volleyball have offered a nice balance to work during winter and spending time at the cottage during summer. And the home in Palosaari with Marjatta has provided another important anchor.

Martti Laaksonen,

2nd June, 2014,

Stundars, Finland.

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1. EVALUATING THE PERFORMANCE OF FOREIGN SUBSIDIARIES: AN EXTENSION OF GUPTA/GOVINDARAJAN'S ROLE TYPOLOGY

Stefan Schmid (ESCP Europe, Berlin, Germany)

Katharina Hefter (ESCP Europe, Berlin, Germany)

Introduction

In his research career, Jorma Larimo has shown great interest in foreign direct investment (FDI) and he has contributed enormously to the stock of knowledge in this research area (Larimo 1993; Larimo 1995; Kallunki, Larimo & Pynnönen 2001; Larimo 2003). FDI undertaken by multinational corporations (MNCs) typically occurs in the form of foreign subsidiaries. Although other market entry modes, such as joint ventures or minority stakes, can lead to FDI as well, greenfield investments, brownfield investments and acquisitions are by far the most important source for FDI (see on greenfield investments and acquisitions, for instance, Arslan & Larimo 2011).¹

In many industries, most MNCs' foreign subsidiaries are not identical in terms of their tasks and activities. Instead, foreign subsidiaries have specific characteristics and take on different roles (Bartlett & Ghoshal 1986, Bartlett & Ghoshal 1989). During the last three decades, international business (IB) literature has produced many conceptual and empirical contributions on subsidiary roles. Scholars such as White & Poynter (1984), D'Cruz (1986), Young, Hood & Dunlop (1988), Ferdows (1989, 1997), Jarillo & Martínez (1990), Gupta & Govindarajan (1991, 1994), Pearce (1991), Birkinshaw & Morrison (1995), Taggart (1997a, 1997b), Forsgren & Pedersen (1998), Randøy & Li (1998), Benito, Narula & Grøgaard (2003), or Hogenbirk & Van Kranenburg (2006), have developed typologies which describe the roles of foreign subsidiaries. The existence of a high number of typologies is a strong sign that IB scholars have departed from viewing all subsidiaries just as identical agents of headquarters. Several literature reviews on subsidiary roles have been produced (Schmid, Bäurle & Kutschker 1998; Schmid

¹ It must be noted that Jorma Larimo's research is not at all restricted to FDI. His publications also cover other market entry forms, such as export (e.g. Larimo 2007a) or joint ventures (e.g. Larimo & Rumpunen 2007; Larimo 2007b).

& Kutschker 2003; Enright & Subramanian 2007), and one of these reviews was presented during one of the famous Vaasa Conferences in International Business (Schmid 2004), which Jorma Larimo has developed into a widely known and highly valued “institution” in the European academic landscape, appreciated by senior scholars and young faculty alike.

In the research stream on subsidiary role typologies, Gupta and Govindarajan’s typology has reached an exceptionally prominent status (Harzing & Noorderhaven 2006; Morschett & Schramm-Klein 2011). It captures knowledge flows which have gained increasing importance in (international) business and management literature (e.g. Nonaka & Takeuchi 1995; Zander & Kogut 1995; Anderson & Holm 2002; Schlegelmilch & Chini 2003; Chini 2004; Mahnke & Pedersen 2004; Adenfelt & Lagerström 2006; Williams 2007; Noorderhaven & Harzing 2009). Knowledge is often interpreted as one of the most important resources of a firm. In MNCs, knowledge can not only be created by headquarters, but also by subsidiaries (Schmid & Schurig 2003; Björkman, Barner-Rasmussen & Li 2004; Ambos, Ambos & Schlegelmilch 2006; Colakoglu, Yamao & Lepak 2014). For enhancing and securing their competitiveness, MNCs and their various sub-units need to absorb knowledge and transfer it internally (Bendt 2000; Harzing & Noorderhaven 2006; Minbaeva et al. 2014; Song 2014).

Gupta and Govindarajan (1991, 1994) were among the earliest IB researchers to focus on knowledge and to recognize that foreign subsidiaries can be important for using, establishing and developing the MNC knowledge base. Gupta and Govindarajan introduce the dimensions “knowledge inflow” and “knowledge outflow” to identify subsidiary roles and to define “Integrated Players”, “Global Innovators”, “Local Innovators” and “Implementors”. The resulting role typology is presented in Figure 1. It becomes evident that, already more than twenty years ago, Gupta and Govindarajan made us aware of the variation in subsidiary roles with respect to knowledge: foreign subsidiaries are not only receiving knowledge from headquarters (and other units of the MNC), but may also provide headquarters (and other units of the MNC) with their own knowledge, partially resulting from their initiatives (Rabbiosi 2011; McGuinness, Demirbag & Bandara 2013; Schmid, Dzedek & Lehrer 2014) and from their successful evolution over time (Birkinshaw & Hood 1998; Paterson & Brock 2002).

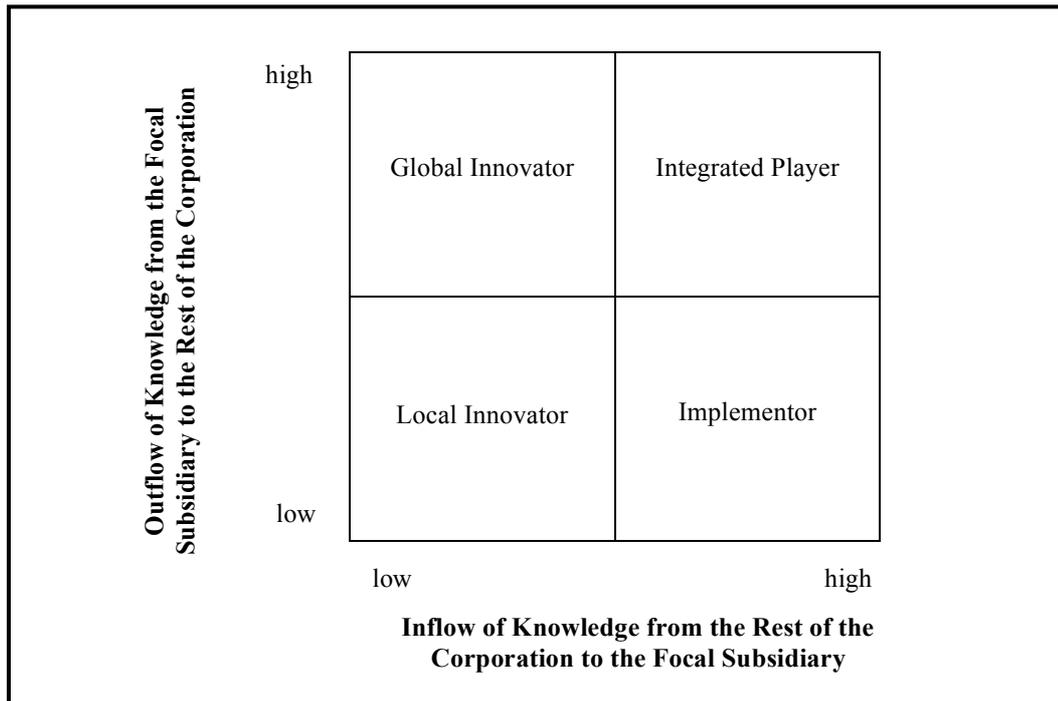


Figure 1. The Gupta and Govindarajan role typology

Source: Gupta & Govindarajan (1991: 774).

Differentiating subsidiary roles is not an end in itself. We assume that each subsidiary should be evaluated according to its role. The specific objectives, goals and strategies of each foreign subsidiary require appropriate performance measures (Kaplan 1984: 100; Otley 1999; Andersson, Björkman & Forsgren 2005: 525). IB literature has already claimed that subsidiaries ought to be coordinated and controlled according to their specific role (Govindarajan & Fisher 1990: 279-281; Harzing 1999: 308-309; Andersson, Björkman & Furu 2002: 119, 131). By this, a subsidiary can better leverage its resources and capabilities, thereby enhancing its own performance and that of the MNC as a whole (Macharzina 1993: 31; Nohria & Ghoshal 1994: 499). However, with some exceptions (e.g. Bartlett & Ghoshal 1986: 92-94, Bartlett & Ghoshal 1989: 236-238, 240-241; Martínez & Jarillo 1991: 441), only limited suggestions concerning the appropriate coordination and control mechanisms for specific subsidiaries have been made. While Gupta and Govindarajan (1991, 1994) related their typology to coordination and control, their recommendations do not cover the potential link between subsidiary roles and performance evaluation.

Why is performance evaluation important (see also Schmid & Kretschmer 2010: 219-220)? Headquarters need to know how existing subsidiaries perform, for example, when taking strategic decisions on international expansion (Chung,

Gibbons & Schoch 2002: 112). Likewise, the management at headquarters has to consider subsidiary performance before implementing strategies, for example before aligning strategy with structures or systems (Egelhoff 1982: 445-446; Wolf & Egelhoff 2001: 122-127; Young, Hood & Firm 2002: 8, 19). Performance evaluation is essential for revealing a true picture of subsidiaries' activities: best practices can be deduced when evaluation is positive, and early warnings can be a result of negative evaluations (Choi & Czechowicz 1983: 15; Rolander, Zander & Hedlund 1989: 1015). Furthermore, performance evaluation is necessary for motivating subsidiaries, and in particular subsidiary managers (Abdallah 1984: 3; Bergmann 1996: 56).

The present contribution aims at elaborating propositions on how to evaluate subsidiaries according to their role (see also Kretschmer 2009; Schmid & Kretschmer 2010). In order to reach this objective, performance evaluation in MNCs is conceptualized in three dimensions – the relevance, the content and the process of performance evaluation (section 0). We then link our concept of performance evaluation to Gupta and Govindarajan's role typology by developing predictions on performance evaluation for Integrated Players, Global Innovators, Local Innovators and Implementors (section 0). Finally, we draw conclusions and come up with avenues for future research (section 0).

The Concept of Performance Evaluation in MNCs

The Relevance of Performance Evaluation within the Control Mix

Most MNCs do not rely on a single coordination and control mechanism. Rather, they use a mix of several mechanisms for coordinating and controlling subsidiaries (Edström & Galbraith 1977: 260; Child 1984: 158; Kutschker & Schmid 2011: 1033-1060). Based on Ouchi, Maguire, Baliga and Jaeger, we can differentiate between two possible objects of control (Ouchi & Maguire 1975; Baliga & Jaeger 1984): output and behaviour. When output control is used, the focus of control lies on the ends and not on the activities undertaken to achieve them. Some authors, such as Mintzberg (1979: 149), refer to output control as performance control because performance is reached when objectives are achieved. Behaviour control (Ouchi 1977: 97; Baliga & Jaeger 1984: 26), by contrast, would require defining the way in which performance is to be reached. In addition to output and behaviour, a third control object exists: input (Jaeger & Baliga 1985: 118; Snell 1992: 297; Hamilton III & Kashlak 1999: 172). In the case of input control, a third way is effective. This control object refers to organizational members as input (Jaeger & Baliga 1985: 118) and is based on either explicit or implicit standards implying a fit between the individual and the organization (Jaeger & Baliga

1985: 118; Snell 1992: 297-298). Potential employees are monitored and evaluated before they enter an organization.²

Within the control mix of any MNC, performance evaluation can be rather relevant or rather irrelevant compared to other control mechanisms. The efficient use of performance evaluation as a control mechanism depends on specific requirements of output control. Ouchi specifies conditions for the application of each control object (Ouchi 1977: 97-98; Eisenhardt 1985: 135-136)³: output control is effective when output measures are available. For behaviour control, knowledge of the transformation processes or of the cause-and-effect-relationships is vital (Ouchi & Maguire 1975: 564; Govindarajan & Fisher 1990: 261; Snell 1992: 295). If one of the requirements – the availability of output measures or the process knowledge – is satisfied, either output or behaviour control can be applied. When neither condition can be fulfilled, within the overall control mix, input control is the best option (Ouchi 1977: 97).

If the conditions for output control are met, performance evaluation is expected to have a high relevance within the control mix. If behaviour control or input control is most appropriate, performance evaluation only plays a complementary role within the control mix.

The Content of Performance Evaluation

The control object – performance – requires further detailing. What is understood by performance can differ substantially (McGuire, Schneeweis & Hill 1986: 128; Meyer & Gupta 1994: 317-324). Despite the heterogeneity of performance measures, the distinction between quantitative and qualitative performance measures is often used and widely accepted (Blau & Scott 1963: 178; Grüning 2002: 142; Pun & White 2005: 51).⁴ Most quantitative measures are considered to be objective, while qualitative measures imply a certain degree of subjectivity.

Quantitative measures can be based on financial or non-financial data (Fisher 1992: 32; Simons 2000: 60). Financial measures are frequently categorized into

² Input is restrictively interpreted as human resource input. Additionally, one can think of input in terms of raw material, preliminary products, components or services (Simons 2000: 62).

³ Ouchi adapts Thompson's (1967: 85-97) four assessment situations which are determined by two dimensions: the standards of desirability (crystallized or ambiguous) and the beliefs about cause and effect knowledge (complete or incomplete). In addition to these two dimensions, cost and the desired level of innovation could also be considered when deciding which object to control (Simons 2000: 64-66).

⁴ The distinction between qualitative and quantitative measures is not always clear-cut: qualitative concepts are operationalized and turned into "quantifiable" measures. Employee satisfaction, for example, is a qualitative criterion which can be measured with an index based on answers to survey questions.

two groups (Ittner & Larcker 1998: 209-210; Gladen 2003: 39-50): on the one hand traditional, accounting-based measures, such as profit and return on investment, and on the other hand value-based measures, like economic value added (EVA) or cash flow return on investment (CFROI). Non-financial performance measures are often grouped into two categories – internally determined measures (such as productivity) or externally determined measures (such as market share) (for instance Keegan, Eiler & Jones 1989: 48; Neely et al. 2000: 1122-1123). Qualitative criteria used for performance evaluation can again be classified into either internal qualitative criteria (such as employee satisfaction) or external qualitative criteria (such as customer loyalty) (Gregory 1993: 281-287).

In summary, the content of performance evaluation is characterized by distinguishing between different performance measures which are grouped into quantitative and qualitative, financial and non-financial as well as internal and external indicators.

The Process of Performance Evaluation

Baliga and Jaeger (1984) not only differentiate various control objects; they also use another dimension in their control concept: the type of control. They distinguish between bureaucratic (formalized) and cultural types of control. Their concept of cultural control covers control by socialization and personal control (Baliga & Jaeger 1984: 26). Since socialization and personal control are distinct (Mascarenhas 1984: 95; Gupta & Govindarajan 1994: 447), we separate them and build two categories. In the present paper, the term cultural control is restricted to control by socialization. Baliga and Jaeger (1984: 28) use the terms “bureaucratic” and “formalized” interchangeably. The latter is adapted for this study and referred to as “formal” type of control. As a result, we differentiate three control types – formal, personal and cultural.

Although being ideal types, the control types are considered “a useful tool for the conceptualization of organizational processes” (Baliga & Jaeger 1984: 26). Control consists of three steps (Egelhoff 1984: 74): monitoring, evaluation and feedback. Therefore, output control is further subdivided into performance monitoring, performance evaluation and performance feedback. As evaluation is one important step of the control process, the three types of control can also characterize the process of performance evaluation: hence, we distinguish formal, personal and cultural performance evaluation of foreign subsidiaries.

Formal performance evaluation is based on codified rules, regulations and procedures (Baliga & Jaeger 1984: 26-27). In more general terms, the degree of forma-

lization within an organization can be defined as “the extent to which procedures, rules, instructions, and communication are written down” (Child 1972: 164, Child 1973: 3). Examples of formal performance evaluation are written performance reports and/or performance management systems, such as the Balanced Scorecard and the “Tableau de Bord” (Gleich 2001: 46; Pun & White 2005: 54). The second type of performance evaluation is personal evaluation. For instance, headquarters’ representatives phone or visit subsidiaries (Jaeger 1983: 95). Meetings, such as management audits and feedback sessions, take place at headquarters or at subsidiary level or via phone or video conferences. Besides formal and personal evaluation, a third type of performance evaluation can be distinguished: cultural performance evaluation.⁵ Cultural performance evaluation does not rely on codified rules or personal interaction, but on shared values and standards within a corporation (Ouchi 1980: 137; Baliga & Jaeger 1984: 26-28; Welch & Welch 2006: 25). Workshops, trainings, superordinates as role models and adequate individual or group rewards may foster such a shared performance culture (Chatman & Cha, 2003: 27-28). In (international) business literature, the term “normative integration” is often used to refer to the cultural dimension of coordination and control (Ghoshal & Bartlett 1988: 365; Ghoshal & Nohria 1989: 326; Kutschker & Schmid 2011: 1051). In management practice, formal, personal and cultural evaluation types do not exist in their pure forms. In reality, different performance evaluation processes are simultaneously found in MNCs with one type dominating (Child 1984: 158). Our concept of performance is summarized in Figure 1. It reflects our understanding of performance evaluation (see also Kretschmer 2009: 17-25 and Schmid & Kretschmer 2010: 224-229).

⁵ As cultural control is a non-cybernetic form of control (Egelhoff 1988: 156), cultural control cannot be subdivided into monitoring, evaluating and feedback. For consistency reasons, the term “cultural evaluation” is used and refers to cultural control in general.

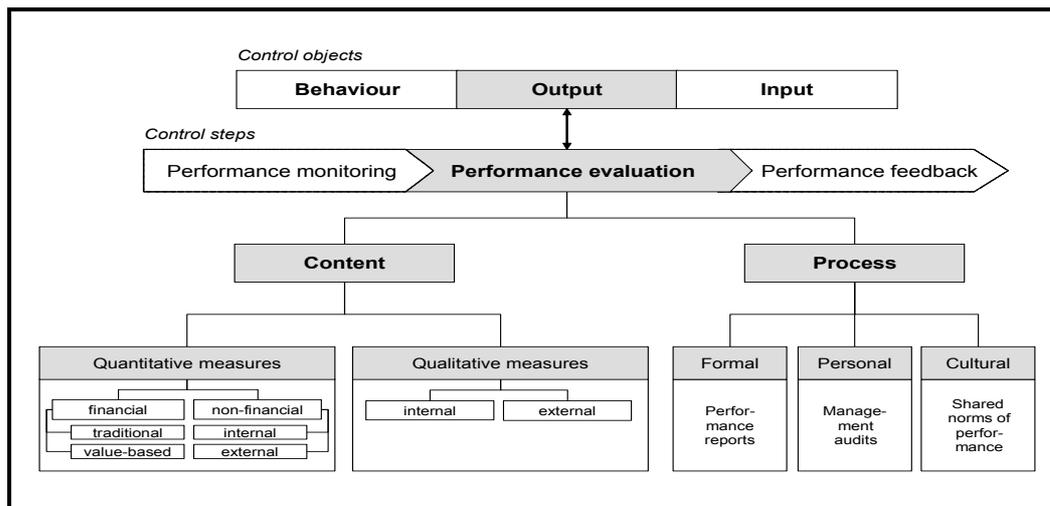


Figure 2. The concept of performance evaluation

Source: based on Kretschmer (2009: 24) and Schmid & Kretschmer (2010: 221).

Subsidiary Performance Evaluation According To Gupta And Govindarajan's Strategic Roles

Performance Evaluation According to the Level of Knowledge Flows

Gupta and Govindarajan (1991, 1994) use inflows and outflows of globally relevant knowledge as classifying dimensions for their role typology. These flows cover codified or explicit as well as tacit knowledge (see Nonaka & Takeuchi 1995: 8-11 and Cantwell & Mudambi 2004: 42 on the distinction of the two types of knowledge). Knowledge flows can either be internal (for instance, capabilities), or external (for instance, covering market data) (Gupta & Govindarajan 1991: 773).

In order to fulfil their roles as Integrated Players, Global Innovators, Local Innovators and Implementors, subsidiaries have to be evaluated differently. In other words, the subsidiary role influences performance evaluation in terms of the categories of our performance evaluation concept, i.e. relevance, content and process. This leads to the overall framework of this paper which is presented in Figure 3.

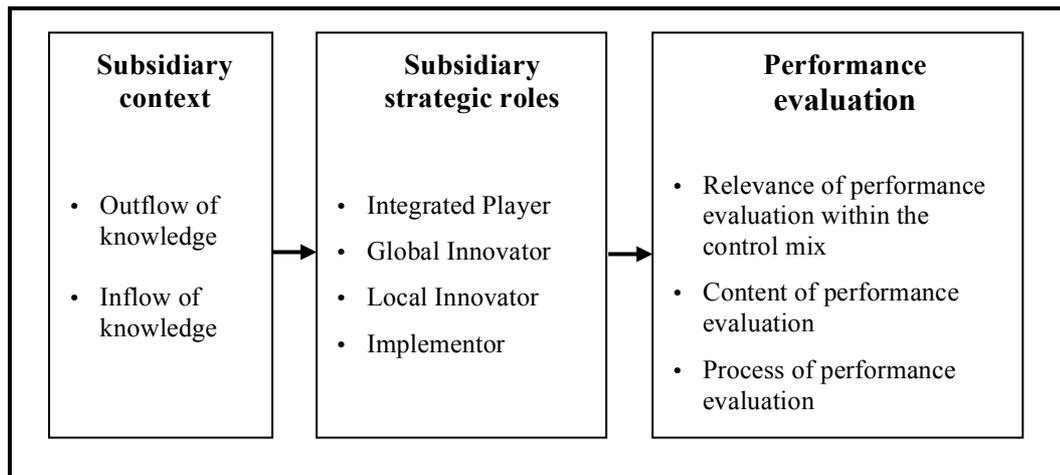


Figure 3. The conceptual framework

Before providing detailed propositions on the performance evaluation of each subsidiary type, the impact of the magnitude of knowledge inflows and outflows on performance evaluation will be analysed (Kretschmer 2009: 80-84).

Concerning the *relevance* of performance evaluation, we can predict differences depending on the level of knowledge inflow. When the inflow of knowledge is low, the subsidiary acts autonomously and based on its own competences. When, on the other hand, the inflow of knowledge is high, the subsidiary depends on the knowledge from headquarters and other subsidiaries. In this case, the output does not really reflect the activities undertaken by the subsidiary (O'Donnell 2000: 531). Thus, a lower degree of outcome measurability can be expected when knowledge inflow is high (Chung, Gibbons & Schoch 2000: 650). As long as headquarters are the knowledge provider, headquarters' representatives understand the processes involved when transforming inputs into outputs at subsidiary level. We can assume that the relevant cause-and-effect-relationships are known at corporate level. This leads to the frequent use of behaviour control (Ouchi & Maguire 1975: 564; Ouchi 1977: 97-98). When other units of the MNC provide knowledge, only input control remains feasible for headquarters. Thus, with an increase in knowledge inflows, a lower relevance of output control and performance evaluation compared to other control objects is expected.

1. The *content* of performance evaluation can also be affected by the magnitude of knowledge inflows. When knowledge inflows are low, subsidiaries' financial outputs can be evaluated separately and show the actual state of performance. Therefore, a frequent use of financial measures is predicted. However, when knowledge inflows are high, subsidiaries are not fulfilling their tasks

and activities independently. Part of their financial performance does not stem from the subsidiaries themselves, but from other units of the MNC. For this reason, financial measures often do not mirror the true performance of the subsidiary. Parts of the knowledge inflows are not reflected in the income statement or in the balance sheet (Gladen 2003: 158-160). Thus, more quantitative non-financial and qualitative internal indicators are expected to be used by headquarters to evaluate subsidiary performance.

2. The magnitude of knowledge inflows also has an impact on the *process* of performance evaluation. In the case of low knowledge inflows, a formal process is expected. The inflow of knowledge and socialization are positively correlated (Gupta & Govindarajan 1994: 453; Chung, Gibbons & Schoch 2000: 657). This finding on coordination and control can also be applied to performance evaluation. The inflow of knowledge might foster cultural integration, or, to put it differently: the knowledge flow can additionally incorporate certain values which are transferred simultaneously. This is expected to be frequent when headquarters are the knowledge provider. The success of the knowledge transfer often even depends on a common cultural understanding (Sørensen 2002: 76; Welch & Welch 2006: 15). In summary, it is predicted that a high magnitude of knowledge inflow is positively linked to shared norms of performance and a cultural process of performance evaluation.

Having discussed the influence of the level of knowledge inflow on performance evaluation, the second dimension of Gupta and Govindarajan's role typology – the outflow of knowledge – will be addressed in the following.

3. How does the level of knowledge outflow affect the control object and therefore the *relevance* of performance evaluation within the control mix? In the case of low knowledge outflows, subsidiary output is measurable. But when there are high knowledge outflows, determining subsidiary output by itself is too restrictive. Knowledge transfers from the subsidiary to headquarters or to other subsidiaries indirectly affect the output of the receiving units. Therefore, in many situations, the contribution of the subsidiary that acts as knowledge provider is more difficult to assess and measure (Bendt 2000: 217; Chung, Gibbons & Schoch 2000: 650). Output measurability is, therefore, low. When headquarters are the knowledge recipient, knowledge of the transformation process is low at headquarters. This leads to a preference for input control (Snell 1992: 295). If other units are receiving the knowledge, headquarters might be aware of the transformation processes causing a preference for behaviour control. Overall, input and/or behaviour control are predicted to be used to a higher degree. Thus, we propose that the relevance of output control and

performance evaluation within the control mix decreases when knowledge outflow increases.

4. The outflow of knowledge can also affect the *content* of performance evaluation. The subsidiary managers' willingness to provide knowledge to other MNC units is expected to augment when headquarters attach importance to the respective knowledge transfer in terms of specific performance evaluation measures (O'Donnell 2000: 533; Björkman, Barner-Rasmussen & Li 2004: 446). Where knowledge outflows are low, subsidiaries' financial measures reveal a true and measurable picture of performance, and the use of financial measures is most likely. When, in the opposite case, knowledge outflows are high, subsidiaries additionally provide their competences to other units of the corporation. Despite their importance for the MNC, these knowledge outflows usually do not appear on the income statement. Financial measures cannot reveal a true picture of the performance of the knowledge provider, nor would external financial measures reflect the performance because the MNC unit transfers its knowledge internally. Consequently, we propose that, in the case of high knowledge outflows, internal non-financial indicators and internal qualitative indicators gain importance.⁶

5. The *process* of performance evaluation can also be influenced by the outflow of knowledge from the focal subsidiary to other units of the MNC. When the outflow of knowledge is low, communication between the focal subsidiary and other units of the MNC is negligible. The opposite is the case when knowledge outflows are high (Gupta & Govindarajan 1991: 778). Then communication is not only necessary between the knowledge providing unit and the knowledge receiving unit, but also between headquarters and the knowledge provider. For strategic decision-making and evaluation purposes, headquarters need to know the competences of the subsidiaries. The relevant information can partly be provided formally to headquarters, although personal interaction is expected to a larger extent. It has been shown that integration via task forces, permanent committees and liaison positions has a positive impact on the outflow of knowledge (Gupta & Govindarajan 2000: 486-488). The more time headquarters' representatives spend in management meetings, feedback sessions and similar gatherings with subsidiary managers, the better

⁶ The knowledge provider could be evaluated in terms of financial and external non-financial performance of the knowledge receiving units. Nevertheless, this alternative is not pursued for two reasons: first, there is a certain time lag before the knowledge is really incorporated. Second, the contribution of the knowledge provider is difficult to assess separately.

they can fully assess the potential knowledge transfer of the subsidiaries (Andersson, Björkman & Furu 2002: 120). For this reason, we propose that the use of formal performance evaluation diminishes when the magnitude of knowledge outflows increases. At the same time, the use of personal performance evaluation is expected to increase.

Table 1 summarizes our tentative predictions on the impact of knowledge inflows and knowledge outflows on the performance evaluation of subsidiaries. In this table, the extreme values on each dimension are presented although, in reality, more subsidiary types will be found, often holding in-between positions (Doty & Glick 1994: 246). Based on these predictions, in the next sections of this paper, we will develop propositions on the relevance, the content and the process of performance evaluation for Integrated Players, Global Innovators, Local Innovators and Implementors (see Kretschmer 2009: 84-89).

Table 1. Gupta and Govindarajan's role typology dimensions and performance evaluation

Role Typology Dimensions		Predictions for Performance Evaluation		
		Relevance within the Control Mix	Content	Process
Knowledge Inflow	low	high	financial measures only	rather formal
	high	low to medium	more quantitative non-financial internal and qualitative internal indicators	rather cultural
Knowledge Outflow	low	high	financial measures only	rather formal
	high	low to medium	financial, quantitative non-financial internal and qualitative internal indicators	rather personal

Performance Evaluation of Integrated Players

A high level of knowledge inflows and knowledge outflows characterizes the Integrated Player. Its lateral interdependence is higher than the lateral interdependence of the other three subsidiary types (Gupta & Govindarajan 1994: 447).

1. The **relevance** of performance evaluation within the control mix: when knowledge outflows are high, output measurability is restricted. The same effect is expected resulting from high knowledge inflows (Chung, Gibbons & Schoch

2000: 650). Therefore, the importance of output control is reduced (Snell 1992: 296-297). As long as headquarters are the knowledge provider, the transformation processes are known at corporate level. This fosters the relevance of behaviour control (Ouchi & Maguire 1975: 564; Ouchi 1977: 97). When the inflow of knowledge is received from other units of the corporation, only input control remains feasible. However, for publication purposes and internal accounting reasons, (mainly financial) output has to be assessed as well (Kammer 2005: 178-180). This is why a certain level of output control is most likely in place. Thus, for Integrated Players, in addition to output control, behaviour control and input control are predicted to be effective. This leads to the first proposition:

Proposition 1: The relevance of performance evaluation within the control mix is expected to be medium for Integrated Players.

2. The **content** of performance evaluation: subsidiary managers can be motivated to transfer relevant knowledge when headquarters attach importance to such a practice and when they rely on specific performance measures (Björkman, Barner-Rasmussen & Li 2004: 446, 450). As knowledge outflows are directed towards headquarters and other subsidiaries, an internal focus is predicted for the content of performance evaluation of Integrated Players. We believe that the high intensity of knowledge transfer fosters the use of qualitative indicators because many knowledge flows are difficult to measure quantitatively (Gladen 2003: 158-160). However, to enhance the objectivity, qualitative dimensions are likely to be supplemented with quantitative measures. In summary, we propose:

Proposition 2: For evaluating Integrated Players, quantitative non-financial internal and qualitative internal indicators are expected to be used.

3. The **process** of performance evaluation: the high inflow of knowledge is accompanied by a transfer of shared norms of performance. This common understanding is also necessary for a successful outflow of knowledge.⁷ Hence the process of performance evaluation is expected to have a cultural com-

⁷ Reagans and McEvily find a positive relationship between strong ties of individuals and the transfer of knowledge between them (Reagans & McEvily 2003: 259). This relationship is also applied at the organizational level (Sørensen 2002: 76) supporting the link between knowledge outflows and shared norms of performance.

ponent.⁸ This is supported by Harzing and Noorderhaven (2006: 209) who find that Integrated Players show the highest level of control by socialization. Additionally, headquarters' representatives are interested in the knowledge stock available at the subsidiary level and try to assess it in meetings and similar personal interaction (Andersson, Björkman & Furu 2002: 120). In return, integration through personal contacts, joint teams and liaison positions even enhances the outflow of knowledge from the subsidiary (Gupta & Govindarajan 2000: 486-488; Björkman, Barner-Rasmussen & Li 2004: 451). Consequently, a high outflow of knowledge is expected to trigger personal interactions.

When combining both arguments, we arrive at the following proposition:

Proposition 3: For Integrated Players a personal and cultural performance evaluation process is expected.

Performance Evaluation of Global Innovators

The Global Innovator is characterized by a high outflow of knowledge and a low inflow of knowledge. This subsidiary type provides its competences to other units of the MNC (Gupta & Govindarajan 1994: 445, 447).

1. The **relevance** of performance evaluation within the control mix: as knowledge inflow is limited, headquarters often do not have complete knowledge of the transformation of inputs into outputs at subsidiary level. This limits the relevance of behaviour control (Ouchi & Maguire 1975: 564). Still, the output of Global Innovators is only partly measurable because the knowledge outflows are difficult to assess. As output measurability is low and the knowledge of cause-and-effect-relationships is limited, only input control is feasible (Ouchi 1977: 98; Snell 1992: 297-298). Thereby headquarters try to make sure to have the right managers at subsidiary level. Consequently, the following proposition is derived:

Proposition 4: The relevance of performance evaluation within the control mix is expected to be medium for Global Innovators.

⁸ High knowledge inflows and outflows signal a high degree of interdependence which is argued to be positively related to socialization, too (Ghoshal & Nohria 1987: 8; Chung, Gibbons & Schoch 2000: 650-651).

2. The **content** of performance evaluation: the low magnitude of knowledge inflows means that activities and output can clearly be attributed to the Global Innovator itself. At the same time, by focusing on internal performance measures, headquarters can motivate subsidiary managers to transfer the relevant knowledge to other units (Björkman, Barner-Rasmussen & Li 2004: 446). This makes an internal perspective in performance evaluation highly relevant. The following proposition can be deduced:

Proposition 5: For evaluating Global Innovators, financial measures and quantitative non-financial internal as well as qualitative internal indicators are expected to be used.

3. The **process** of performance evaluation: while low formalization is predicted for the process of performance evaluation in the case of Integrated Players, the process is expected to be more formal for Global Innovators. The limited inflow of knowledge towards the Global Innovator corresponds to restricted socialization (Chung, Gibbons & Schoch 2000: 657). For this reason, no cultural performance evaluation process is expected. However, the high level of knowledge outflows is likely to attract headquarters' representatives who become aware of the potential knowledge transfer (Andersson, Björkman & Furu 2002: 120). This leads to a more personal process of performance evaluation. In summary, we propose:

Proposition 6: For Global Innovators a formal and personal performance evaluation process is expected.

Performance Evaluation of Local Innovators

The Local Innovator is characterized by a low knowledge outflow and a low knowledge inflow. Subsidiaries of this type are largely autonomous (Gupta & Govindarajan 1991: 775): they create the relevant knowledge themselves and apply it locally.

1. The **relevance** of performance evaluation within the control mix: headquarters have no knowledge of transformation processes in Local Innovators. Therefore, behaviour control cannot be recommended (Ouchi 1977: 97). At the same time, their output is measurable. Consequently, a high relevance of output control and performance evaluation within the control mix compared to other control mechanisms is expected. As a result, innovations at the local level are

encouraged because the Local Innovator is not restricted by tight behaviour control (Simons 2000: 65-66). Tseng, Yu & Seetoo (2002: 224-225) support this prediction because they find more output control for subsidiaries with a comparably low knowledge transaction intensity within the MNC. This leads to the following proposition:

Proposition 7: The relevance of performance evaluation within the control mix is expected to be high for Local Innovators.

2. The **content** of performance evaluation: Local Innovators are not connected to other subsidiaries or headquarters in terms of knowledge transfers. They do not contribute internally by providing knowledge to headquarters or other subsidiaries. Hence, headquarters are expected to concentrate on financial measures and equate performance of Local Innovators with financial performance as it is frequently done (see, for instance, Schmidt-Sudhoff 1967: 140; Glaum 1996: 138-139; Otley 1999: 3-4). The following is predicted:

Proposition 8: For evaluating Local Innovators, mainly financial measures are expected to be used.

3. The **process** of performance evaluation: we can assume that headquarters do not show much interest in the subsidiary-specific competences of Local Innovators since these are not relevant (or seem to be not relevant) for other units of the MNC. Based on this assumption, the use of personal performance evaluation is unlikely. The limited knowledge transfer from and to Local Innovators also restricts the simultaneous transfer of culture. Additionally, a common understanding between Local Innovators and other units of the MNC is not as necessary because knowledge transfer is limited. Harzing and Noorderhaven (2006: 209) find support for this low level of cultural control in the case of Local Innovators. To sum up, personal and cultural processes of performance evaluation are expected to be less frequent in the case of Local Innovators. This leads to the following proposition:

Proposition 9: For Local Innovators a formal performance evaluation process is expected.

Performance Evaluation of Implementors

The Implementor role is characterized by a high inflow of knowledge and a low outflow of knowledge. As for the Global Innovator, the lateral interdependence of the Implementor is at a medium level (Gupta & Govindarajan 1991: 776-777, Gupta & Govindarajan 1994: 447).

1. The **relevance** of performance evaluation within the control mix: as knowledge outflows are limited, the measurability of the output of Implementors should be high. This supports the relevance of output control for Implementors. Still, the high knowledge inflows make it difficult to attribute the output to subsidiary action (Chung, Gibbons & Schoch 2000: 650). This raises ambiguity of output measures and restricts the use of output control (Ouchi 1977: 97). When headquarters are the knowledge provider, they are usually aware of all transformation processes at corporate level. This adds to the importance of behaviour control. In the case of other subsidiaries transferring knowledge, the knowledge of the transformation processes is limited at headquarters. This restricts the relevance of behaviour control (Ouchi & Maguire 1975: 564; Snell 1992: 294-296). When summarizing the reasoning, the following proposition is derived:

Proposition 10: The relevance of performance evaluation within the control mix is expected to be medium for Implementors.

2. The **content** of performance evaluation: as the Implementor does not engage in knowledge transfers to other units, its performance can be quantitatively measured. Still, it might be difficult for headquarters to assess the real performance of the subsidiary because the Implementor heavily depends on knowledge inflows from other units. Financial measures only provide a partial view of the Implementor's performance since not all knowledge inflows are accounted for (Gladen 2003: 158-160). Therefore, we propose:

Proposition 11: For evaluating Implementors, financial, quantitative non-financial internal measures as well as qualitative internal indicators are expected to be used.

3. The **process** of performance evaluation: the high level of knowledge inflows is expected to transfer common performance standards. Implementors are even found to have the highest level of socialization compared to the other three subsidiary roles (Gupta & Govindarajan 1994: 453). The lack of knowledge

outflows restricts the relevance of personal interaction from the headquarters' point of view (Andersson, Björkman & Furu 2002: 120). Additionally, the activities performed by Implementors are not new to headquarters' representatives. The following proposition is deduced:

Proposition 12: For Implementors a formal and cultural performance evaluation process is expected.

The predictions on the impact of the subsidiary roles on performance evaluation are summarized in Figure 4.

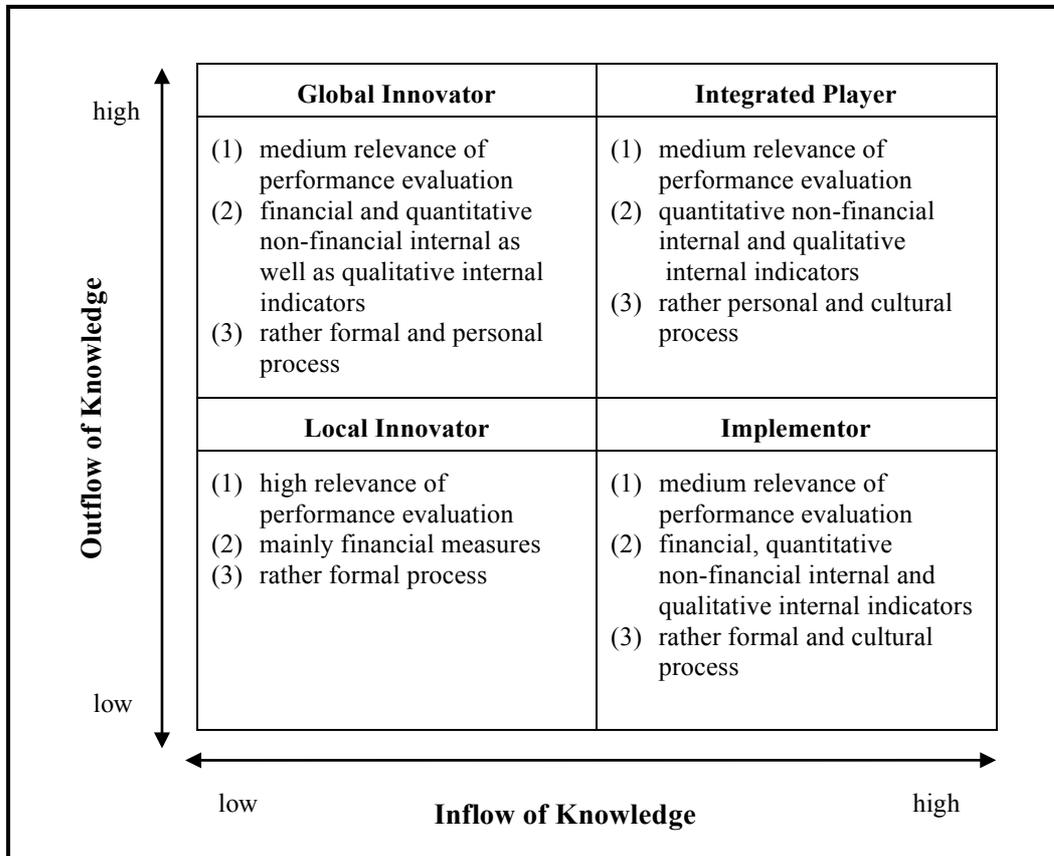


Figure 4. Predictions on role-specific performance evaluation of Integrated Players, Global Innovators, Local Innovators and Implementors

Conclusions And Avenues For Future Research

In this paper, we have developed a framework for the role-specific performance evaluation of foreign subsidiaries. Thereby we have examined the influence of subsidiary roles on performance evaluation within the MNC. For each subsidiary role, we have derived how relevant performance evaluation is within the control mix, and we have discussed the content and the process of performance evaluation. Furthermore, we have argued that it is not only important to differentiate subsidiaries according to their role; it is also essential to have an appropriate approach for performance evaluation so as to enhance the specific performance of each subsidiary and the organizational performance of the entire MNC. Our paper can contribute to existing literature in several ways. First, we offer an integrative concept of performance evaluation which is rooted in the literature on coordination and control of subsidiaries. Second, we extend Gupta and Govindarajan's role typology by arguing how relevance, content and process of performance evaluation are role-specific. Third, we adapt the concept of differentiated fit to role-specific performance evaluation, and bridge the existing gap between IB literature and literature on management control (Otley, Broadbent & Berry 1995: 41).

It is important to note several limitations of our contribution which lead to avenues for future research. While being more detailed than many existing concepts, our performance evaluation concept is still not complete. For example, within the content of performance evaluation, the main focus was put on the types of performance indicators, but not on the imposed level. Similar to Morschett & Schramm-Klein (2011: 10-13) who linked Gupta & Govindarajan's subsidiary types to the level of coordination we could have investigated the level of performance evaluation. The performance evaluation concept may be further refined by including the choice of currency, inflation, transfer pricing and accounting standards (Plasschaert 1996; Amshoff 2003: 347-348; Berens & Hoffjan 2003: 214-229; Chan & Lo 2004; Ho & Lau 2006; Hoffjan & Weber 2007: 10).

In the present paper, we concentrated on Gupta and Govindarajan's role typology. However, the Gupta and Govindarajan typology itself can be subject to criticism, for instance in terms of the number of dimensions chosen, the types of subsidiaries suggested and the broad and fuzzy use of the terms "knowledge" and "knowledge transfer" (Schmid, Bäurle & Kutschker 1998: 64-68, 95-97; Alavi & Leidner 2001; Kretschmer 2009: 107-111). Moreover, in addition to knowledge transfers, many other strategic context factors can determine subsidiary roles. Future research could, for instance, analyse the impact of the level of competence (Bartlett & Ghoshal 1986), the market, product and value added scope (White &

Poynter 1984; Birkinshaw & Morrison 1995; Tavares & Pearce 1999; Delany 2000) or the degree of localization and integration (Jarillo & Martínez 1990; Taggart 1996, 1997a) on the relevance, content and process of performance evaluation. It should also be noted that the activity spectrum of a subsidiary (which has some links to White & Poynter's value added scope) may have a high influence on the type of knowledge which is transferred. For instance, R&D units differ from sales units abroad, and so do full-fledged subsidiaries which cover the entire range of value chain activities. We should be aware that different value chain activities (of a specific subsidiary) may even be controlled and coordinated in different ways (e.g. Schmid et al. 2011; Grosche 2012) and hence also be subject to different ways of performance evaluation.

It is self-evident that, in business reality, performance evaluation is not only a question of the subsidiary role (nor that it should be only a question of the subsidiary role). Numerous factors at the MNC level (such as MNC orientation and MNC strategy), at headquarters level (such as headquarters' top-management and leadership), at subsidiary level (such as subsidiary size), and at the environmental level (such as environmental complexity) have to be taken into account when deciding on performance evaluation (see also Schmid & Kretschmer 2010). With respect to Jorma Larimo's academic writings, one factor would deserve more attention in future research – distance (Hennart & Larimo 1998; Dow & Larimo 2009; Dow & Larimo 2011). It can be expected that cultural, geographic, administrative and economic distance between headquarters and subsidiaries also influence performance evaluation (and hence, the relevance, content and process of performance evaluation). The few studies having already used “distance” as a variable (Hamilton, Taylor and Kashlak 1996; Hamilton & Kashlak 1999; Harzing 1999; O'Clock and Devine 2003) provide first evidence that “distance matters” for performance evaluation.

In this conceptual paper we have established propositions. These propositions should be confronted with empirical reality. Qualitative work can provide in-depth insights into performance evaluation and role differentiation within MNCs and help to understand the processes involved (Otley 1980: 425; Hartley 1994: 212; Otley & Berry 1998: 105-106, Kretschmer 2009: 93-95). Within the boundaries of cases, our predictions can be illustrated, supported or rejected and consequently refined (Ghauri & Grønhaug 2010: 109-113; Ghauri, 2004: 121). Furthermore, based on a qualitative assessment, a large-scale empirical test of our propositions could be a promising endeavour (Wright 2004: 63-64).

The need for a fit between strategy and management control as well as performance evaluation has been claimed in IB and management control literature for

years (Govindarajan 1988; Neely, Gregory & Platts 1995: 83; Slater, Olsen & Reddy 1997: 37; Otley 1999: 367; Welge & Holtbrügge 1999: 570-571; Chung, Gibbons & Schoch 2002: 110; Hoque 2004; Andersson, Björkman & Forsgren 2005: 525, Doms & van Oijen 2008). Some efforts have been made to link corporate and business unit strategy to management control systems (see Langfield-Smith 1997; Kald, Nilsson & Rapp 2000 for overviews and Govindarajan & Gupta 1985; Gupta 1987; Bruggeman & van der Stede 1993; John, Young & Miller 1999; Hoque 2004 for examples). However, subsidiaries' strategic roles have been considered by neither one of the two research streams so far. Both fields – IB and management control – will benefit from further research on subsidiary roles. The achievements of the research area remain partially limited as long as we are not able to link them better and more to managerial issues, such as the role-specific performance evaluation of foreign subsidiaries.

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2. Central And Eastern Europe After The Boom – New Business Realities For Western Multinational Companies Operating In The Region

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Introduction

The fall of the Iron Curtain in 1989 marked the end of the economic exclusion of a large part of Europe and the beginning of a radical transformation process in Central and Eastern Europe (CEE), namely the transition from a centrally-planned to a market-based economy. Never before such a large number of economies has embarked on this journey to a democratic and capitalistic system at the same time. The macro-economic growth model for CEE was based on a few basic ideas (Becker et al. 2010: 25-27; EBRD 2010: 69-71): The goal was to achieve a rapid political and economic integration into the EU via offering access to the Single European Market, providing EU funds for the reforming states to upgrade their infrastructure and liberalizing internal economic and foreign trade relations. The opening of these countries to foreign direct investors, so the thought, will bring the necessary capital, technology and know-how to restructure and modernize domestic businesses and industries. At the same time companies in CEE will get access to the high-income countries in Western Europe. A stepwise integration into transnational production networks through close cooperation and joint ventures with Western multinational companies (what later often ended in the takeover of the CEE partner) will further support the new orientation towards the West. Taken together these measures will generate for the reform states a higher growth rate than for their West European counterparts and so fuel the economic catching-up process of these economies.

The opening of CEE was like a “bonanza” for Western companies. In front of their doorstep a potential market of more than 300 million inhabitants emerged. This region was a “tabula rasa” on their strategy maps, a region that has been isolated from modern Western production and logistics systems, marketing and consumption cultures for more than four decades due to the fact that trading between East and West was limited and direct investments of foreign companies either forbidden or only allowed under severe restrictions before 1989. Product markets

were underdeveloped or even non-existing (e.g., financial services) and consumers were craving for Western brands and life-style (Lewis 2005: 90-118). Unsurprisingly, after the fall of the Iron Curtain Western companies flooded the markets of the region and began building a presence there. The new entrants were overwhelmingly welcomed by governments and businesses. Western multinational companies (MNC) were seen as ideal partners that would inject capital, bring modern technologies and management practices, teach local companies how to compete in a market-based system and offer them access to foreign Western markets. Via the establishment of special economic zones, long-term tax-holidays and subsidies for newly created jobs national governments courted foreign investors.

During the privatization of large enterprises foreigners bought firms in the telecom, banking, retailing and consumer goods sector. In the automotive industry and electronics industry greenfield investments were preferred. The investments of VW, KIA, Toyota, Tesco, Metro, REWE, Bosch, Samsung and other global giants have shaped the economic landscape, particularly in Central Europe. Seven out of the ten largest manufacturers in Central Europe and overall 281 out of the top-500 companies in Central Europe are controlled by non-CEE firms (Deloitte 2013: 16 and 28). The Western parent companies integrated their CEE subsidiaries into European and global value chains what allowed them to produce components or assemble final products for the whole corporate group. These industrial activities generate a production value going far beyond the sales potential that the local market could offer. For instance, within a decade Slovakia became the “Detroit East” of the automotive industry because of the highest automotive production value per capita in the world (Schuh 2009: 55). In general, Central and Southeastern European countries show FDI stock to GDP ratios of more than 50% what is significantly higher than the European average (wiiw database 2013). After two decades of major reforms many countries in Central Europe have already completed the transformation to a well-functioning market economy (i.e. Czech Republic) or are close to it, while the economies of Southeastern and Eastern Europe are still lagging behind (EBRD 2012: 9). In their collective behavior these foreign investors and exporters became major change agents which extended global market standards in production, retailing, marketing and sales to these countries and in this process reproduced their Western home market structures there (Schuh 2007: 287). In particular, the boom years from 2002 to 2008 with average growth rate of well above 5% in CEE reinforced the perception among executives of Western firms that the reforming economies of CEE will soon have caught-up with Western Europe and major differences in market structures and consumer behavior in Europe will soon become a thing of the past.

Then in 2009, the global financial and economic crisis (“Great Recession”) ended this six-year-long boom period. Although the CEE countries were not the cause of this economic downturn, economies such as the Baltic states (GDP decline of 14-18% in 2009) and Ukraine (-15%) were among the worst hit by the crisis (Schuh 2009: 56). The Great Recession did not only shatter the financial markets, banks and the real economy in the countries of the region but also the growth image of CEE. It ended the notion that CEE will continue to grow faster than the West European economies for the next couple of years and even outperform other emerging markets of the world. Suddenly, foreign MNCs were faced with collapsing markets, shrinking disposable household income, business customers and partners on the verge of bankruptcy and no sign of a quick recovery – a situation they were not prepared for. The growth model for CEE was heavily dependent on consumption which averaged 80% of GDP between 2005 and 2008 (Labaye et al. 2013: 5). Consumers relied on credit to finance their consumption what sent the stock of loans up by 26% annually while domestic savings only grew by 13%. Although the situation improved a little in 2011 (before it worsened again), the economic outlook and the sentiment of foreign investors have remained defensive. This is also reflected in the OeKB-CEE Business Climate Index which is based on quarterly interviews of 400 foreign direct investors (OeKB 2014: 1).

The CEE Business Climate Index has never reached the value of 100 in 2007 again and, after an all-time low of 72 in the second quarter of 2009, has been lingering between 80 and 85 since the fourth quarter in 2011. It is obvious that when faced with such a huge economic downturn, companies stop geographic expansion and put the brakes on investments what is mirrored in declining foreign direct investment inflows into CEE countries by 35-85% from their 2007-08 peaks in 2011 (Niessner 2013: 6). Even when the economic outlook should be improving for 2014-16 with an forecasted average GDP growth rate of 2-3% for Central and Southeastern Europe this figure is about half the one before 2008 (wiiw 2014: 18). Given such drastic changes in business environment it is clear that management has to review its strategy for CEE.

In this conceptual paper I discuss the effects of the economic downturn on the strategic orientation of Western MNCs active in CEE. First, I assess the underlying business model for CEE that guided Western MNCs in the past two decades and ask the question if it is still valid in this new business environment. Second, I present strategic and organizational responses of foreign multinationals to this massive crisis.

The business model for Central and Eastern Europe – Before and after 2009

The business model of Western MNCs that guided the “going east” of foreign MNCs can be described in a simplified form by the following criteria: motives, risk perception and strategy focus. The main motivation to enter CEE was the huge market potential of 20 countries with 330 million (underserved) inhabitants and the expected higher market growth rates that consumption and product ownership levels would generate (Manea & Pearce 2004: 53; Wes & Lankes 2001: 120-123; Larimo & Huuhka 2007: 65-66). Efficiency motives such as lower labor costs, lower taxes and generous subsidies by local governments as well as the access to commodities and cheap energy played a role too, especially in traditional and medium-technology industries such as automobiles, durable consumer goods, machinery, building materials or paper. However, when analyzing investment patterns a differentiation by industry, company size and country-of-origin of the foreign direct investor is advisable. In Table 1 major patterns of investment strategies of foreign MNCs in CEE are summarized and industries where these patterns are common given as examples.

Table 1: Investment strategies of foreign direct investors in CEE

Investment pattern	Examples
“Extended workbench“	Automotive, electrical industry, clothing, metalworking
“Extension of regional/ global coverage”	Globally operating MNCs, consumer goods and its suppliers (packaging, marketing services)
“Regional expansion into neighboring countries”	Medium-sized companies in trade, construction, services/tourism; Greek & Turkish firms in Southeastern Europe
“Active industry consolidation within the region”	Banks, insurances, mineral oil, telecom, retailing
“Springboard to EU for Asian MNCs”	Cars, consumer durables
”Russian firms going West“	Energy, telecom, commodities, banks
“Arabic, Turkish & Chinese investments in Central and Southeastern Europe”	Agriculture, cars, construction, R&D centers

While the advantages of an engagement in transitional markets are quite obvious the risks of doing business are harder to assess in an objective way. The higher risks of doing business in an emerging market results from the incomplete institutional framework and the underdeveloped rule of law. Foreign entrants face not only a lack of information about local competitors, potential customers and final users but also unclear regulations, inexperienced bureaucrats and corruption. However, the intention of Central and Southeastern European countries to join the European Union soon and their efforts to smooth the way into EU membership

made foreign multinationals believe that the risk of doing business in CEE was lower than what they would typically attribute to a transition economy (Schuh 2012a: 190). They assumed the “EU umbrella” will mitigate the risk as the countries adhere to the political, legal and economic principles set by the EU.

From a strategy perspective, a fast entry to enjoy first-mover advantages and a quick aggressive expansion in the region were the ingredients for success (Larimo, Marinov & Marinova, 2006: 381; Schuh 2000: 138). The expansion into CEE was seen as a kind of “copy & paste” process. The early successes of Austrian and German firms in their first expansion wave into the neighboring countries in Central Europe were then later replicated in their expansion to Southeastern Europe and Eastern Europe (Ninan & Puck 2010: 251). The weaker competition in the CEE markets, the superior quality, customer service and excellent reputation as well as a broader resource base were major reasons for the dominance of Western MNCs in CEE markets (Larimo, Nieminen & Springer: 2002: 107; Fahy et al. 2000: 72-74). A high degree of standardization with only limited adaptations to local market conditions is also characteristic for the approach of Western MNCs in CEE (Schuh 2000: 139). In order to better control local activities in the local markets foreign MNCs preferred high commitment operation modes such as (sales) subsidiaries, joint ventures or acquisitions (Nieminen, Larimo & Springer, 2002: 107). In general, this outlined business model offered foreign MNCs the chance to yield a higher return on investment than in their (Western) home markets – at least until 2008.

This leads us to the question how this business model was affected by the Great Recession. Interestingly, most of the parameters were not negatively affected (Schuh 2012a: 191-192). The market potential, the main motivation to go to CEE, is still there. Underdeveloped markets in terms of consumption rates and product ownership and deficiencies in infrastructure have not disappeared. Tapping these potentials in the different product categories is just postponed. There are even positive effects of the crisis (at least from a corporate perspective). Skilled labor workforce and the favorable resource situation were not eliminated by the crisis. The signs of overheated economies such as real estate bubbles and salaries and prices for supplies growing faster than normal inflation have gone and falling factor prices have created an attractive cost base for businesses again. In countries where the local currency depreciated against the euro or dollar this cost advantage was even enhanced. What really changed in the aftermath of the crisis is the risk perception of investors. Investment projects in CEE are now seen more realistically than in the boom time before 2008. Today, higher risk premia are charged reflecting a more realistic assessment of country and business risks and higher costs of bank loans in general. The predominant approach among foreign MNCs today

can be described as defensive and selective (Ernst & Young 2012: 18). They are not interested in expanding into new CEE markets now, their focus is still on the optimization of existing operations. Downward adjustments of costs and capacity may be painful and reducing profitability but they are preparing the companies for the next upswing.

A surge in demand in Western markets will help those export-oriented economies enormously and should bring CEE operations back to reasonable returns again. While most of the foreign MNCs might see this crisis and its repercussions as an interruption of the catching-up process, for some industries it comes close to a game changer – for instance for the banking industry which learned that financing domestic growth via huge capital imports and loans denominated in hard currency is not a sustainable business. This positive outcome of the assessment of the CEE business model does not mean that no review of strategy, structure and organizational model is necessary. On the contrary, a more detailed analysis on the different levels of regional strategy is the starting point for possible strategic redirections and corrective measures.

Strategy review for CEE

The CEE strategy is a regional strategy that is an integral part of the overall strategic plan of the MNC. In large MNCs regional strategy is developed and controlled by regional management. The regional management that is either part of the geographic structure in global headquarters or located directly in the region acts as an intermediary between subsidiaries and corporate top-management. In discussions with corporate staff and subsidiary management the regional strategy is developed and finally approved by corporate headquarters. A severe economic downturn such as the Great Recession is an external shock that can threaten the profitability and liquidity of the businesses in the region and sometimes even their existence. Therefore, besides quick corrective measures on an operative level a comprehensive analysis and discussion of the current strategy is needed. The strategy review should address the five decision areas that define a regional strategy (Schuh 2012a: 192-193):

- Role of the region: What is the role of CEE within the global strategy? Is CEE seen as source of growth or rather as production location and supply source?
- Participation in CEE markets: Which are major markets and which are peripheral ones? Where is a return to profitability not possible in the next years? Where should the MNC pull out or reduce its commitment?

- Activity location: Which elements of the value chain should be located in the region?
- Product and marketing strategies: What are the right product and marketing strategies for CEE markets? Do they have to be changed to be more appropriate for the more price-sensitive markets?
- Organizational model: What is the appropriate organization model for CEE now?

I acknowledge that it is difficult to generalize on the strategic moves of companies. Differences stemming from the industry background, business model, regional presence, market positions and business performance in country markets determine the exposure to such declines in demand and the impact on profitability. The following chapters give a brief overview of the strategic moves of regional players in CEE based on interviews with executives, published statements of companies, industry and company reports and surveys.

One of the most obvious results of this recession is the loss of the growth region status of CEE. All the planning for the emerging markets of Europe was based on a growth rate of two or more percentage points above the “old” EU’s growth rate. These high growth times will not come back that quickly as banks are driving down their lending, households are still busy with paying back their loans, unemployment remains still high, and the economic outlook is not showing extraordinary improvements. Current political crises in the region (“annexation of Crimea”; deteriorating economic and political relations between Russia and Ukraine) have already impaired business and investment climate in both countries and will very likely result in declining inward FDI and lower GDP growth rates in both countries. Foreign investments of MNCs will be, if not postponed, redirected to countries with a safer business environment and better growth outlook. Even the economically better off Central European countries might suffer from this political crisis in Eastern Europe when generalizations along the historic “Eastern bloc” dimension take effect among investors. Other emerging economies in Asia and Latin America may benefit from this political turmoil in the region although Western MNCs are facing different sort of troubles in nearly all emerging markets today (The Economist, March 8, 2014: 54-56).

The recessionary environment has highlighted the weaknesses in the business environment (e.g., excessive bureaucracy, prevalent corruption, weak court systems). Local governments desperately looking for new income sources to reduce their budget deficits have turned from an investor-friendly attitude to a more confrontational style. Increasing discrimination against foreign firms in favor of domestic ones and the introduction of new “crisis taxes” specifically targeting for-

foreign multinationals have tarnished the investment climate. In this stagnating market context management becomes now aware of the extra costs and risks of doing business in the region (EBRD 2010: 83-86). As a consequence, we can observe a more differentiated approach by MNCs toward the economies of the region as it is also mirrored in recent direct investment inflows and perceptions of executives (Ernst & Young 2012: 18).

The crisis has definitely ended the perception of CEE as a homogeneous bloc (“Eastern bloc”) which is primarily shaped by its communist past. Foreign investors see the increasing divergence in the economic development between sub-regions (Central Europe vs. Southeastern Europe) and even countries. The managers who have gone through the recession understand now better the close interdependencies between economic system and institutional framework. Soft factors such as the rule of law, corruption, and political consensus gain in importance in country attractiveness assessments. While in the past the orientation was mainly on growth potential and outmaneuvering competitors, foreign MNCs are interested now more on the profit margin that is left after deducting unexpected higher costs of doing business and depreciation of assets.

Another element of the strategy review is to rethink the presence in CEE. In the boom time a quick entry and broad presence in most of the CEE countries were seen as success factors. Being first to the market, snapping up local competitors during the privatization process and outmaneuvering competitors became a strategic imperative. In fast moving consumer goods and financial retail services the acquisition spree in the 1990s and early 2000s left many companies with a patchwork of operations that finally often did not form a coherent CEE strategy. The crisis brought out the strengths and weaknesses of each country operation and forced management to review and optimize their portfolio of regional activities. A continuing weak market position, unsatisfactory profitability and a deteriorating overall business climate in a country have put those local operations under close scrutiny. It does not come as a surprise, that foreign MNCs are rethinking their presence in particular markets when market volumes and sales decline, local units suffer losses and the business outlook remains unfavorable. In the last years, we have seen numerous examples of portfolio rationalization: ABInBev, one of the world’s largest brewery groups, sold its breweries in nine CEE countries to a private equity firm but kept the very profitable operations in Russia and Ukraine in 2009; the French retailer Carrefour stopped its expansion plan to become third largest retailer in Russia and exited Russia in 2010; Erste Bank from Austria and Commerzbank from Germany withdrew in 2012 from Ukraine. While there may be various reasons for the withdrawal from a CEE country the fact itself indicates the relative weak position of CEE in the strategic priorities of many MNCs.

This should not convey the impression that foreign direct investors have been leaving CEE in droves. The majority of direct investors has stayed in the region. In many cases you will not see a full retreat but a substantial reduction of the commitment to a country market by closing branches and cutting down the number of products and services actively offered. For instance, the leading bank in CEE, UniCredit Bank Austria, has merged its offices in the three Baltic states as well as in Czech Republic and Slovakia. Now they run the business in the Baltics from Riga and the Slovak business from Prague and turn the former national subsidiaries into branch offices. This is a major change of mind that has happened in the last two years and indicates the pressure that companies face in these countries. It is not a must for a MNC anymore – even a regional player with a broad presence and strong market position in the region – to be present everywhere in CEE. Raiffeisenbank International, one of the top-3 banks in the region, is discussing the withdrawal from two markets, Hungary and Ukraine. Similar discussions are taking place at a leading home improvement retailer Baumax in CEE which considers exiting Turkey and Romania. It is quite surprising that regional players discuss withdrawals from strategically quite attractive countries in 2013 and now in early 2014, quite some time after the crisis year 2009. This points at deeper problems that declining and stagnating markets have caused to companies that have bet on a continuing growth story, expanded their operations and ended up overinvested in some of the markets. Unfortunately, the excessive capacity expansion has nearly led some MNCs to bankruptcy. Kika/Leiner, the leading Austrian furniture retailer with a broad presence in CEE, ran into profitability problems because of its loss-making Southeastern operations and had to sell out to South-African Steinhoff Group in 2013 which is nicely complementing its presence in Europe by this acquisition.

Strong established players in the region may even take advantage of the ongoing industry restructuring. Due to their insider knowledge of the market and business environment and superior financial strength they exploit the weaknesses of smaller local and international competitors to improve their market share. In 2010 PepsiCo bought a majority stake in the Russian consumer goods manufacturer Wimm-Bill-Dann what turned the company into one of the leading industry players. France headquartered Groupe Danone merged its Russian (and CIS) dairy unit with the Russian Unimilk to become the region's largest dairy company in 2010. In these two cases the intention to get a stronger foothold in Russia and win a broader consumer base in the largest market of CEE can be obvious. But also Russian corporate giants take the opportunity to expand their business internationally by buying assets from troubled Western competitors. In 2012 Russian

Sberbank acquired the CEE-Holding of Austrian Volksbanken with 300 branch offices in eight Central and Southeastern European countries and turned the former head office into its European headquarters.

Regarding activity location in CEE the new EU member states were among the most favored target countries for product relocations in the German manufacturing industry in the early 2000s (Kinkel et al. 2009: 19). According to the “CEE-Barometer 2011” the CEE countries have further gained in attractiveness as a production location from 2009 to 2011 (Horvath & Partners 2011: 6-8). These results are in line with the findings of the latest Ernst & Young’s investors’ poll which confirm CEE’s attractiveness as a location for manufacturing (Ernst & Young 2013: 6). What is often overlooked from a foreign perspective is that Central European countries have undergone a massive “re-industrialization” (mainly driven by foreign investors) and that this sound industrial growth model has been paying off so far (Niessner 2013: 3-4). Foreign MNCs use CEE locations as an export platform to serve Western European and CEE markets. The well-developed industrial sector, particularly in Czech Republic, Slovakia, Slovenia and Hungary, which accounts for 30% of gross domestic product (compared to 19% in the Euro-zone), has been an economic success story and is still attracting investments in industries such as cars and automotive components, household appliances, machinery, consumer electronics and paper. Romania and Serbia are trying to repeat this industrial growth model as the production of the low-price car Logan manufactured by Dacia-Renault and the joint venture of the Serbian government with Italian car maker Fiat to build the Fiat 500L in Kragujevac illustrate. The geographic closeness to West European markets and the availability of a skilled workforce at lower costs than in the “old” EU have been driving the expansion of production capacity in CEE often at the expense of their West European sister companies.

In the last years business services have gained in importance among inward FDI. In order to become more cost-efficient West European MNCs have begun to outsource IT and business process services to CEE (Fifekova & Hardy 2010: 10-14). From Gdansk to Bucharest business service providers are mushrooming. Their activities range from back-office tasks such as accounting and order processing, to front-office activities such website management and customer service. This also applies to higher-value IT services such as infrastructure support and custom software development. The main reasons why CEE countries are thriving in this sector are the availability of a well-educated workforce, good infrastructure, recognition of intellectual property rights, location in the same time zone and a perfect cultural fit with West European cultures (Fifekova & Hardy 2010: 15-18).

The recession stopped the notion among Western executives that CEE will quickly adopt Western consumption behavior. Reduced salaries, increased unemployment and the dramatic indebtedness of many households markedly shrank the disposable incomes of consumers. Tight household budgets make them switch to cheaper alternatives such as promotional offers, private labels, local/regional products and self-grown produce. While consumer staples had been less affected, purchases of consumer durables and non-necessities declined dramatically. The Great Recession has led to a “forced rationalization” of consumer behavior in CEE. The spending spree of large parts of the population in the pre-2008 times has turned out to be more of a surface phenomenon strongly driven by consumer loans instead of a substantial harmonization in behavior. The formerly pyramid-shaped market structure has shifted even into a more bottom heavy pyramid. Upper-price segments, the domain of Western brands, have been losing volume to the lower price segments, the “bottom of the pyramid”. CEE households are looking increasingly for “good value for money” offerings. Discounters, private labels, strong local and regional producers and Asian low-price competitors benefit from this more price-sensitive consumer behavior. Western firms are not well prepared for this swing in demand. Their natural habitats are the top- and upper mid-tiers of the market where they position their well-known international brands with their comparative advantages in quality, performance, innovativeness and image (Schuh 2007: 280). Nonetheless, Western MNCs cannot assume anymore that the current market situation is a short-term phenomenon and the best response is to wait for demand to come back to pre-crisis heights. 56% of the consumers, or 57 million people, in Eastern Europe are low-income consumers with less than \$10,000 income per year. In Russia and Ukraine, 70% of the population falls in this category (Pfeifer, Massen & Bombka 2007: 51).

So it is obvious that CEE marketing managers face a dilemma. They would like to promote their newest high-performance products and build their brand image in this way. But the crisis has turned consumers into “smart shoppers” who are looking for the best deal. This search for “good value for money” products is retarding the convergence to Western market structures. Local and regional competitors are the winners of this development as the “good value for money” positioning, namely offering products of a comparable quality at a lower price, is very common among these competitors (Schuh 2014). Therefore, Western marketers have to consider affordability in their CEE marketing strategies too. There are Western companies in the fast moving consumer goods sector such as Groupe Danone and Henkel CEE that have already successfully launched products to low-price segments. “Danone Gratka” in Poland and “Casa Buna” in Romania are examples of affordability strategies in the yoghurt and dairy sector. Henkel CEE covers the low price segment in detergents with “Rex”, a so-called economy brand that is

distributed throughout the region. In multi-tier brand strategies the global brands are complemented by acquired or newly invented local or regional brands which target lower income segments and center on the affordability argument (Schuh 2007: 280). For large MNCs the launch of affordable brands in CEE markets is more than an intellectual exercise, particularly because they are otherwise marginalized in those markets. Another strong argument is the fact that you find increasingly similar polarized market structures with growing low-price segments in crisis-hit Western Europe too what expands the potential market for affordability initiatives.

As far as the newly emerging organizational model for CEE is concerned we still have to wait until the strategy reviews are completed. The tendency towards decentralization that could be seen in the early 2000s has been reversed in the crisis: the pendulum swung immediately back toward centralization. In the Great Recession when sales took a significant dip and profitability was threatened headquarters wanted to have more control over investments, costs, liquidity and key accounts. The situation may have improved in the meantime, but in many categories demand has not reached pre-crisis levels yet. Unsurprisingly, efficiency considerations are still dominating the management agenda. The management of MNCs in CEE seems to be predominantly occupied with itself, to set its house in order. This strong orientation towards internal affairs is underlined by a 2012 survey of CEE headquarters of foreign multinationals located in Austria. The two most important forces shaping organizational decision for CEE activities today are the pressure to reduce costs and the trend towards centralization in the corporate group (Schuh 2012b: 17). The study also shows that CEE headquarters will continue to play a constructive role in regional management. But it is obvious that the regional management level as an intermediary between global headquarters and subsidiaries is coming under pressure in this context. Its costs of 1-3% of sales have to be justified. So we can observe the trend to leaner regional headquarters and regroupings into larger regional units.

Actively the regional management can add most value by supporting subsidiary management in improving its performance, developing a regional strategy, spreading best practices within the regional group and giving the region a voice at global headquarters (Schuh 2012b: 16). Latter aspect is a strong argument in the CEE context. One major challenge for MNCs in CEE has always been the question how to manage so many small markets ranging from the Baltic states to the successor states of Yugoslavia. The establishment of CEE headquarters offers a solution to this management challenge but can't argue away the deeper problem of the strategic response to the cultural, economic and political fragmentation that companies encounter in the region. The subcritical sizes of operations in South-

eastern Europe in the aftermath of the crisis has led to clustering neighboring markets with similar characteristics and introducing shared service centers for back-office activities. The “lead country model” is whereby a larger and more developed neighboring subsidiary provides strategic guidance, shared services and managerial assistance to a smaller unit not only reduces costs but supports best practice transfer too. Given the divergent market developments between the more advanced markets in Central Europe and the emerging markets in South-eastern and Eastern Europe, MNCs have to postpone the introduction of highly standardized strategies and structures. Having organizational units in place that cluster geographically close subsidiaries at similar stages of market development seems to be a good way to develop local business and at the same time to keep costs in check. Given the variety in market situations and business environments the organization design for CEE has to match this need for differentiation and flexibility to be effective. The CEE organization in the making will finally resemble a regional network with dispersed roles (e.g., shared service center, center of functional/product excellence) among its national units that is orchestrated by regional or global headquarters.

Conclusions

Western MNCs are facing a new business reality in CEE. Gone are the times of high growth rates and fast expansion of the pre-2009 era. Now they have to decide on the appropriate set-up, namely their market participation and activity configuration in the region, and optimization of the regional network. Most of the MNCs active in CEE are still in the mid of this review and re-orientation process as news about market withdrawals, layoffs, closings of branch offices and relocations of activities show. Interestingly, the business model for CEE that guided the expansion of foreign MNCs into CEE is still intact. There are areas, such as the attractiveness of CEE as a production location, that look even better than before the crisis. However, MNCs are paying now more attention to country and business risks before they make an investment what indicates that the initial euphoria has given way to a more realistic assessment of opportunities and risks. A differentiated approach to the region is also part of this new realism. This new attitude includes that MNCs are willing to withdraw from loss-making operations and markets with a bleak economic outlook. Countries with unfriendly business environments are shunned. Investments are made in a more cautious and selective way as the lower inward FDI flows into the region show. Other large emerging economies outside of Europe are increasingly preferred. These benchmark economies are regarded as more dynamic, less fragmented and with a larger market potential. This comparative disadvantage is reflected in strategic reorientations of

the MNCs towards Asia, Turkey, Middle East and Latin America. Only political turbulences, deteriorating economic parameters and falling growth rates in those other emerging markets (e.g., Turkey, North Africa, Brazil, India) are currently hindering an even widening gap in managerial attention and investments. The strong industrial base, the close integration into European and global value chains, expected further improvements of the business environment and still undeserved markets right on the doorstep of West European MNCs are further on compelling arguments speaking in favor of CEE. And many of the CEE economies have done their homework in the last years and reduced current account and budget deficits, stabilized their economies and have continued with reforms of their infrastructure and regulatory environment. Western MNCs played an outstanding role in the transformation process in the last 25 years and will be pivotal actors in the new growth initiatives in the countries of this region too. Hopefully, these reforms and redirections on the institutional, macro- and microeconomic level will lead to the development of a regional economic space that is not only appreciated for high growth rates but also for its good business climate, well-functioning infrastructure, high-quality inputs and innovativeness.

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3. From The Transformation To A Market Economy: The Two Decades Management Story Of East-West Joint Ventures In Slovakia⁹

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Introduction: FDI and East-West joint ventures as a factor of change and emancipation of the transitional economies

In order for the transitional economies of Central and Eastern Europe (CEE) to be successful, it was essential that large, previously state-owned socialist companies learned to operate under newly-created market conditions. This ability to change depended on various internal and external factors. One key factor was also foreign direct investment in indigenous companies and their gradual transformation through the transfer of capital, technology, and know-how in various areas, as well as from better access to foreign markets. These elements, together with importation of new managerial ideas and practices, were critical to the process of enterprise change and restructuring in transition economies. Local firms had to drive growth and change in these economies, but foreign investment could also make a highly valuable contribution.

Conventional wisdom held that foreign direct investment (FDI) would be an important force for change, reconstruction, and growth in the exhausted Central and Eastern European economies (UNCTAD, 1995: 104). The strongest proponents of the role of FDI in CEE (see Dunning 1993: 20) argued that multinational enterprises supplied many of the necessary ingredients for economic growth, the reshaping of attitudes toward work and wealth creation, the redesigning of the business and legal framework, etc. Paliwoda (1997: 27) also underlined that the

⁹ The research for this paper was conducted under VEGA 1/0461/12 Manažérske kompetencie v zahraničných a domácich firmách v SR ako zdroj zvyšovania ich konkurenčnej výhody v ére globalizujúcej sa ekonomiky, ved. S. Ferenciková

Central and Eastern European nations are seeking to regenerate their economies quickly, which is a task in which FDI plays a pivotal role.

There are many articles about the role of FDI in transitional economies. While it may be accurate to assert that the highest levels of restructuring are to be found in enterprises with FDI, the precise nature of restructuring and change in these companies at the firm level, as well as their impact on other local companies and their functional environment, has not been described and analyzed in a systematic fashion. Case studies of enterprises with FDI are common: these usually describe the changes, conflicts and results after the entry of a foreign investor into the previously state-owned company (see for example Fogel, 1995, Nilsson, 1996).

Some authors point out that foreign investors should be more aware of the unique conditions in CEE, particularly of the obstacles to organizational change, which include such internal factors as unfavorable employee or managerial attitudes and incompetence, and external barriers, such as the legal environment and structures for corporate governance (Petrice 1995:14). On the other hand, several authors, especially from CEE, have a different perspective: they try to evaluate the positive and negative impacts of FDI on indigenous companies, and they do not pay attention to local obstacles (Balazova & Valent, 1995, Outrata et al., 1996).

While many specialists emphasize the important and dynamic role of FDI in CEE economic transition, several empirical studies point to the fact that the experience of FDI in the relatively short period of transition was uneven. Some studies focused on the implications of FDI for the former East Germany (for example, see Grabher, 1997), Hungary (see Sadler, Swain, 1994) or Slovakia (see Ferencikova & Smith, 1997). A study of the Vienna-based WIIW research institute by G.Hunya (see Hunya, 1996) shows a dramatic dichotomy between multinationals and local companies in Hungary, which was the biggest recipient of FDI among CEE countries at that time. Hunya concludes that companies with foreign involvement may well be the only dynamic part of the Hungarian economy: they have clear strategies, invest more, restructure more rapidly, and have modern technology, management, and Western market access. The issue is whether these advantages benefit local companies and the Hungarian economy as a whole, as well as the question of how to spread these positive features throughout the whole economy. Many companies with FDI are modern islands of export-oriented processing and assembly, often with high unemployment and abandoned capacities in traditional industries.

In the next decade of research, some other authors do not have any doubts about the convergence of the business environment of Central and Eastern Europe and the industrialized West. For example, J. Larimo states (see Larimo et al., 2002:

369) that the competition will be growing in Central and Eastern Europe and the market lead of the Western companies in the region is going to be reduced. However, he also underlines that the entry and the presence of Western companies have positive impact on marketing systems in Central and Eastern Europe. J. Larimo has also published a pioneering study related to the measurement of the joint venture performance in Central and Eastern Europe (see Larimo, 2010). After the years of the exhilaration about the success of the FDI-investors in CEE he suggests the sophisticated approach how to analyze the IJV performance and factors affecting it in Central and Eastern Europe based on the study of 140 IJVs established by Finnish firms in CEE countries during 1990 – 2005. According to him, the main influential factors were general investment and IJV experience, economic growth in the target country and age of the unit/IJV.

Situation framework, aim and methodology: East-West joint ventures in Slovakia

The aim of this paper is to examine the motivations of the partners, the results of the joint ventures and the impact of foreign investors on local companies and their environment through a discussion of the experience and results of the East-West joint ventures in Slovakia during two decades of the existence of Slovakia as market economy. The basic questions addressed by this research are as follows: What are the motivations of the partners in the joint ventures? What are the results of the joint ventures i.e. were the expectations of the partners met? How important is FDI as driver of change in local companies and their environment i.e. how strong is the influence of foreign investors on various areas of activity of these companies and on their operational environment such as the national economy? In which areas is the impact of FDI strongest and where is weaker than expected? What are the major differences between East-West joint ventures in the first decade of transformation of the Slovak economy and the second decade?

In the first decade we also discuss the impact of FDI and joint ventures on:

(1) change in the local company (joint venture): technology and knowledge transfer, market access, the transfer of management and marketing know-how, implementation of human resource management, changes in the production profile as well as in the volume and quality of production, and changes in overall productivity,

(2) change in the local parent company (impact of foreign investor on local partner): learning process, the increase of cooperation or competition, impact on labor force,

(3) change in the local environment (economy) in which the joint venture operates: impact on employment and labor force, diffusion of managerial ideas, impact on the local suppliers, the increase of competition, marketing issues (better supply and services on the domestic market), and export performance.

Manufacturing has been chosen for the study of the first decade because most FDI in Slovakia at the beginning of transformation process has been located in the manufacturing sector. The possibility of change resulting from FDI is therefore likely to be significant in this sector and higher than in the sector of finance or trade (the second and third biggest receivers of the FDI). It is also underlined by the fact that the FDI into manufacturing sector have higher effect on the local economy than the FDI in the services (through creation of the supplier networks, technology transfer etc.). Case study method due to the very low number of functioning JV has been chosen for the study of the first decade of the transformation of the Slovak economy (1993 – 2003). The first part of this paper is a result of the examination of a number of foreign direct investment cases in Slovakia since 1993. The research is based on interviews with expatriate and local enterprise managers, the official statistical data and other government information, and review of information available in international and Slovak economic press.

As for the next decade study (1994 – 2004) the research was aimed broader: at planning, managing and performance outcomes of international joint ventures (IJV) with the participation of Slovak companies. The information has been gained by questionnaire survey. In this decade the number of the IJV was much bigger than in the first one, and this fact has enabled us to change the method used for our research.

The questionnaire itself was divided into three sections: background information and structural characteristics of the international joint ventures; international joint venture relationship characteristics; and ownership changes and performance-related issues.

The companies were asked to fill in the questionnaire only if they met these conditions:

- the company is a partner in an international joint venture established and conducting business in Slovakia,
- the company established in Slovakia is a partner in international joint venture established and conducting business in country other than Slovakia.

The questionnaire survey was not feasible in 1990s, as there were only a few international joint ventures in Slovakia and the case study method was thus more appropriate. Nowadays, the situation is slightly different, even though state institutions pay no special attention to existing IJVs and it is still quite difficult to gain information about this type of companies.

There is no central or partial evidence of international joint ventures in Slovakia. In fact, the only way how to find out whether the company is a joint venture is to type the name of particular firm in Obchodný register (register of companies) and check the information made public – names and countries of origin of the associates (in the case of limited liability company – spoločnosť s ručením obmedzeným) or, if stated, the shareholders (in the case of the joint stock company – akciová spoločnosť).

The names of potential joint ventures with Slovak participation or joint venture partners were searched for in the newspapers, magazines and on the Internet. These entities were then contacted by phone, with the aim to gain phone number or e-mail address of the employee authorized to provide information on the cooperation with the foreign partner. Subsequently, he/she was sent an e-mail with the questionnaire attached. If there was no response in a month, the company or the given employee was contacted again by phone and the e-mail was re-sent. Some of the companies included in the research were asked to participate based on the previous knowledge of the authors about their equity structure.

44 filled in questionnaires have been collected and included in the research. They represent all the sizes of the companies (micro, small, medium, large) and all sectors of economy (agriculture, manufacturing, services), as well as the companies with the participation of state or municipalities.

Research results and discussions

A. The first decade of the East-West joint ventures in Slovakia

The first decade of the transformation of the Slovak economy and the East-West joint ventures created in this time period

In the first decade of the transformation of the Slovak economy (1993 – 2003) the joint venture structure as a form of entry into the Slovak market was the most

typical for manufacturing: in 1995 in Slovakia 90 % of FDI in manufacturing was placed in joint ventures, with only 10% in wholly-owned subsidiaries. (Ferencikova, 1997a:9). Manufacturing had only a small amount of greenfield investment or investment in wholly-owned companies because foreign companies sought out production facilities with existing equipment, skill levels, market knowledge, etc. At the same time, manufacturing requires a much higher volume of investment than, for example, distribution or tourism and in this sense it is riskier. Therefore foreign companies prefer to share capital costs and entrepreneurial risk in manufacturing by establishing joint ventures and using existing capacities, at least at the first stages of their activity, when they are still testing the environment and market. Many investors saw CEE as a prime site for access to new markets after 1989. Therefore they tried to ensure this access by building upon the local knowledge of existing domestic firms. Furthermore, in many cases, they were required by the host government to enter into joint ventures with state-owned firms.

The motivations of the foreign companies for the creation of the joint ventures were following: entry of the new markets, monopoly position of the partner, participation in the privatization, entering the networks, sharing the risks, sharing the costs, learning i.e. getting knowledge in doing business in transitional economies, obtaining low-costs suppliers for the global networks. The motivations of the local partners were almost the same, but of the “mirror-type”: learning i.e. the knowledge how to do business in market economies, getting capital, access to the distribution networks, access to the technological, organizational, marketing and management know-how, sharing profit.

Our small sample for the study of the East-West joint ventures in first decade of transformation consists of six East-West joint ventures created in the beginning of the 90's in Slovakia: BAZ-Volkswagen, Tatramat-Whirlpool, Palma-Henkel, Alcatel SEL Tesla, Hoechst-Biotika, BC Torsion - with the parent companies PSB and Dirickx. (See Ferencikova, 2001). All selected joint ventures in the sample manufacture sophisticated products belonging to either engineering, electrotechnics, or the light chemicals sector. These sectors are considered to be very important for restructuring Slovak industry, in which heavy industries (metallurgy, heavy engineering, chemical raw materials) traditionally play an important role. The choice of joint ventures includes some small- and medium-sized companies as well as the biggest firm in this category. The chosen companies were all originally joint ventures with the majority of parent companies from developed economies, by 1998 a half of them were subsequently bought out by the foreign MNC. The sample includes six companies with volume of FDI: one of them is a company with the largest volume of FDI placed in Slovak manufacturing (the

category of investor with an investment over SKK 1 billion), four companies attracted FDI ranging from SKK 100 million to SKK 1 billion, and the smallest company belongs to the group between SKK 10 million and SKK 100 million. The group also represents a variety of national sources of FDI (American, Austrian, French, and German capital) and geographic diversity within Slovakia (the Slovak capital, Western, Central and Eastern Slovakia).

As for the situation in the middle of the first decade (1998) the first one -- a car producer Volkswagen Bratislava, originally a Slovak-German joint venture BAZ – Volkswagen - was the biggest foreign investor in the industrial sector in Slovakia. This company is located in the Slovak capital Bratislava. As for the volume of FDI, the next four companies belonged to the category with the foreign contribution between SKK 100 million and SKK 1 billion. Whirlpool Poprad, originally a Slovak-American joint venture Whirlpool-Tatramat, produced washing machines in a small East Slovakian town called Poprad. The next company - Alcatel SEL THL - was located in the even smaller town Liptovsky Hradok in Central Slovakia. This German-French-Slovak joint venture produced telecommunication systems. Detergents and other chemicals were being manufactured in Henkel, an Austrian company (originally a Slovak-Austrian joint venture Palma-Henkel) with the plant in West Slovakian town Nove Mesto nad Vahom. Hoechst-Biotika - a Slovak-German joint venture is a pharmaceuticals producer with the headquarters in a Central Slovakian town Martin. BC Torsion - a French-Slovak joint venture - is the smallest examined joint venture established in a very small West Slovakian town Brezova pod Bradlom. Its production program involved various types of fences and wires.

Our attempt was to create a small, but as far as possible representative sample of manufacturing companies of various sizes, locations, origins and contributions of parent companies in order to determine common FDI-effects on them and their environments. To lesser extent, the choice was also driven by the willingness of managers of these companies to cooperate in this project i.e. the data were mostly collected through interviews with managers and from the internal materials of companies. A lot of useful information was also obtained by monitoring the economic press and the statistical surveys.

As mentioned, the chosen cases were all originally joint ventures, although some of them were subsequently bought out by foreign investors – three of them by 1998, the rest by the end of the first decade of transformation (2003). None of the joint ventures we studied in the first period has survived as a joint venture: all of them ended up as wholly-owned subsidiaries of the Western parent companies. This trend we call the incremental take-over of ownership of joint ventures: in all

the instances the Western partners have steadily increased their equity share in joint ventures. There are a number of reasons for this: (1) the global strategy of the MNC – Western parent company, (2) conflicts between the Slovak parent and foreign investors over joint venture strategy, profit share and over the control of key services such as energy (joint ventures are usually situated in the former plants of Slovak parent companies), (3) the inability or unwillingness of the Slovak parent to match investment funds required to maintain existing shares of ownership, and (4) financial problems in the Slovak parent company requiring the sale of its shares in the joint venture (see Ferencikova & Smith, 1997: 8) and finally (5) a complete bankruptcy of the Slovak parent company in the transformation process.

Foreign partners as agents of change in the first decade of transformation: paradoxes and perspectives

The companies studied range from the largest of its type -- Volkswagen -- to small and medium-sized firms. They also vary according to production programs, national origin and contributions of investors, investor strategies, etc. Nevertheless, some indicators of change are consistently present -- or absent -- in all these companies. As suggested in the introduction to this paper, these indicators can be followed in the internal as well as in the external environment of these companies.

(1) Change in acquired subsidiaries

All the companies studied were successful. Some foreign investments transformed and saved parts of domestic, Slovak companies (Volkswagen-BAZ, AL-CATEL SEL-Tesla, partially DIRICKX-PSB). Some foreign companies invested in local monopoly producers (Whirlpool-Tatramat, Henkel-Palma, Hoechst-Biotika), modernized them, and secured an excellent position on the domestic market. The cases of companies we studied show that FDI has **a significant change** on the host companies.

Generally, the West partner impact was concentrated in following areas:

* *Change in product line towards high-quality products.* Foreign investors launch new products, either totally (in the case of cars at Volkswagen and new telecommunication systems at ALCATEL SEL), or partially (at Whirlpool, Henkel, Hoechst, and Dirickx, beginning with modifications to local products and later

introducing new products and models). All of the above companies produced high-quality products, most of them with international quality certificates.

* *Technology improvement.* In every case, the foreign joint venture partner either transferred technology or provided another means for acquiring technology. The technology in two cases was the most advanced in its field. In the cases we studied, no foreign investor contributed obsolete technology, which is often predicted when firms from advanced economies invest in transitional economies.

* *Higher quality of labor force.* Although there was already a skilled labor force in every domestic company before the joint venture was created, all foreign investors invested in additional training on work practices, foreign language, or new technology. Local workers mastered new working processes rapidly and well. The contribution of foreign investors to the increase in the quality of local management is also considerable: the need of expatriates is extremely low (ranging from zero to three) in all the companies studied, with the exception of Volkswagen. By 1998, there were ten German managers working in Volkswagen Bratislava, a company with more than 2,600 employees. Later, with the growth of the company the number of expatriates grew as well.

* *Implementation of management know-how* (e.g., new accounting and finance system, simplified and more effective organizational structure). Every foreign investor brought changes to the organizational structures, which were previously designed for the needs of a command economy. Implementation of modern human resource management (new forms of evaluation, motivation and practices) is also typical for all these companies.

* *Implementation of modern marketing practices.* The transfer of marketing know-how has led to an increase of competitiveness for companies with FDI. The application of market research, and advanced methods in marketing high-quality products resulted in improved customer satisfaction. FDI improved the market position of the firms domestically and internationalized their value chain through two means: they bought supplies under better conditions by joining the foreign investor supply network, and they were able to increase their exports.

* *Foreign market know-how.* Although some international transactions were arranged by the foreign partner, most joint ventures learned how to operate in foreign markets and successfully sell their goods abroad (all studied companies were export-oriented).

* *Increase of productivity.* Productivity is the most comprehensive indicator of change in every FDI-invested company in Slovakia. It reflects a better organiza-

tion of labor and management, a higher-quality of labor force, its motivation, new technology, but also a more intensive production.

(2) Change in the local parent company

All of the domestic parent companies in the sample were state-owned at the time of the establishment of the joint venture. Managers in the domestic parent expected the above-mentioned positive effects to spread eventually from the joint venture to the parent, but these expectations were rarely met.

All the joint ventures in the sample were established at the beginning of the 1990's. Since that time, all the parent companies have gone through privatization. Some faced serious financial problems (Tatramat, Tesla) and even bankruptcy (PSB, BAZ). On the other hand, the Slovak parent companies Palma-Tumys and Biotika have gone successfully through the process of transformation and restructuring. These two companies are mostly oriented towards the domestic market, are in businesses with steady demand (food products, medicines) and are consumer products companies. As a result of their domestic orientation, they did not need to look for new markets after the collapse of COMECON, and their strong consumer orientation allowed them to avoid the ill effects of relying on a collapsing industrial sector. Part of their success is also the result of investment placed before 1989: under the socialist-planned system, while some companies were under-invested, others obtained a huge portion of investment if their production program corresponded to "socialist development programs". These firms also enjoyed natural low costs protection against foreign competition, good management and intelligent restructuring, and also higher impact of foreign investor in their joint venture.

Generally, the cases of companies we studied show that Western partner and FDI has only **a limited impact on the local parent companies**. The extent of the change in the Slovak parent can be the result of several factors:

* *"Unintentional learning"* - spreading of managerial attitudes, ethics, new corporate cultures, and work practices. This effect is undeniable, but indirect and hard to measure. Three companies in the sample are located on the same site as their Slovak parent companies (for example, the Slovak parent might contribute buildings from the former large production facility to the joint venture) which should theoretically make this kind of change very easy. This type of transfer is facilitated by labor force movements. Because of the higher or high salaries and wages in the FDI-invested companies, however, the movement of labor force from the joint venture to the original parent company is low. Moreover, some of the practices in

the joint venture are simply not applicable to other local companies (e.g., KAI-ZEN system at Volkswagen).

* *Intentional learning from the activity of its own joint venture.* Palma-Tumys literally copied the marketing methods of Henkel-Palma, which helped it to keep its share of the domestic market under the increasing pressure of foreign competitors. The influence of the foreign partner in this company is visible also in other areas, including decision making process, investment policy, human resource management. Biotika is another example of learning, but this impact is not seen in the other four Slovak parent companies.

* *Becoming supplier of its own joint venture.* When the parent company becomes a supplier to its joint venture, their linkage is direct, through the quality requirements of the joint venture, but also indirect, through adapting to the "modus vivendi" of the FDI company (e.g., timing of supplies, entrepreneurial ethics, correct attitude towards business relations). We have noticed two such cases in the pool: the first one was TESLA, which is not significant with regard to the volume of supplies. The other case was PSB, which manufactured technology equipment for BC Torsion and provided some subcontractor operation for it.

* *Becoming supplier of the corporate network of foreign parent company.* Again, we have noticed two such cases: the first one is TESLA, which is subcontractor to the German concern Alcatel, the other case is Tatramat - the parent company of the previous Whirlpool-Tatramat joint venture. It has established a joint venture with an Italian company to supply Whirlpool-Europe network with components.

* *Becoming direct competitor of its own joint venture.* No company enters any joint venture with this immediate target, but we found such an example in the pool (BC Torsion). Although competitive pressure can lead to dynamic efficiency gains in the future, currently it damages any cooperation between companies involved.

* *Receiving dividends or cash for shares after the buy-out by foreign partner.* It may help in solving immediate problems in cash-starved Slovak companies, but there is no evidence to show that it can cause significant long-term change.

None of these impacts is common among all the companies in the sample, with the exception of "unintentional learning". The impact of the Western partner on the local parent company is different in each case. However, this study still suggests certain conclusions. The cases of companies we studied show that FDI has, paradoxically, a limited impact on the local parent, even though all of them entered joint ventures with the explicit intention of improving the performance of

the parent firm. In our opinion, there are three main reasons for this. The first one is objective and lies mostly in an inheritance from the previous system: most factories have obsolete technologies and limited means for their renewal, i.e. they are not able to cooperate and keep pace with foreign companies, especially with the MNC (e.g., to enter their supplier networks with quality products or simply to learn from them). The next two are: (1) a very complicated process of privatization and transformation of local companies resulting in changes in ownership structures and management, and (2) high and unfulfilled expectations from the partnership and the ensuing jealousy and rivalry of local managers. If the combination of all these factors is present in the Slovak parent company, the FDI has no impact on it. If at least one is missing, the change is possible. Paradoxically, we find that the potential for change in the local parent depends to a much greater extent more on the attitudes of its management than on the presence of foreign partner.

Nevertheless, with the end of a privatization process and clearer ownership structures, we expected a more rational approach among local managers towards the creation of strategic alliances with foreign investors. We supposed that they will create resource- and learning-oriented alliances, and that they will prefer to cooperate with more comparable, medium-sized companies. In such cases, from the point of view of Slovak companies, the danger of take-over is not as high as with a large MNC, and at the same time, the chances that the foreign partnership will result in changes in the parent are much higher. In the next part of our study we address these questions more profoundly.

(3) Change in the local environment and economy

In comparison to the transfer of change to the parent companies, **the transfer of change into local environment is more significant**. The changes brought by foreign partners and their FDI in the Slovak economy are as follows:

** Influence on local suppliers (model of behavior).* In some cases the companies with FDI were mainly supplied from the global network of their foreign parent companies (Volkswagen, Alcatel SEL THL). In other cases (Whirlpool, Henkel) the volume of local suppliers has grown, meaning that local companies have successfully adapted to the quality requirements and entrepreneurial and cooperative principles of their partners. This learning process is significant, but it is limited by the number of companies involved in the suppliers' network.

* *Influence on labor force and employment.* In spite of the decline in employment in some joint ventures at the beginning of their operations, the companies with FDI are important employers (Volkswagen has ranked among the biggest Slovak employers after couple of years) who make significant investments in human capital. In all the companies we studied, the wages were higher (sometimes as much as two times) than the local or national average, which has created a dual labor market. Skill and knowledge transfer was low because of the slow movement of managers and workers from companies with FDI. The highest labor turnover is reported in Volkswagen, but only in the workers category.

* *Increase of competition.* This change is limited because the socialist idea of the division of production was based on monopolies: each factory had a different production program. This system remained intact in many ways: foreign investors often enter monopoly productions (Henkel, Whirlpool, Biotika) and have not directly increased domestic competition. However, since these companies import the goods from their global supplier network (e.g., Henkel cosmetics and various chemicals, Whirlpool with home appliances), there was increased competition for their domestic suppliers. The only company having a positive influence on competition is BC Torsion - and they compete with the joint venture's Slovak parent.

* *Development of entrepreneurial sector.* This effect is only possible if the local managers employed in FDI companies create their own companies on the basis of their experience. Only one such case was reported in the companies in the pool - some managers left BC Torsion and established their own company that import (but does not produce) the same products.

* *Influence on the domestic market.* All the companies with FDI in the sample manufacture and placed high-quality products on the Slovak market.

* *Export growth.* The quality of products, together with the use of distribution networks of foreign parent companies, has also led to higher exports on foreign markets. Export growth is often considered to be the proof of increased competitiveness and successful transition to market-oriented companies. Volkswagen has become one of the biggest Slovak exporters.

What was the situation at the end of the first decade of the existence of the East-West joint ventures and FDI inflows to Slovakia? As was seen from the ranking of the biggest Slovak companies, FDI-invested companies play relatively important role in Slovakia in quantitative terms. However, in contradiction to the situation in developed countries, most of them, including the companies in our pool, did not contribute to the development of the entrepreneurial sector and to the growth of competition in Slovakia. The reason of this paradox can be found

in the former monopolistic and artificially created industry structure and the ensuing high capital barriers to entry. The next paradox was the big influence of foreign investors on the quality of the labor force and its limited movement from FDI-invested companies to the domestic sector. The reason could be found in the existence of a dual labor market (high salaries in FDI-invested companies) and the limited possibility for relocating (shortage of flats, slow development of home mortgages). The influence on local suppliers was also still limited, mostly because of the fact that the local companies were not yet able to meet quality and quantity requirements among large MNCs. In order to adjust (and sometimes to survive), local companies were pressed to cooperate with foreign partners in the next decade to a larger extent (such as Tatramat with an Italian company, or Tesla with an Israeli company). This fact, together with the general necessity to seek resources, means and tools of transformation, led to the increase of FDI inflow to Slovakia and to the change of joint ventures patterns in the second decade of transformation in Slovakia (2004 – 2014).

Current situation

As for the companies from our case studies, all of them still exist, even though some original foreign partners withdrew their investment. In 1999, the Volkswagen-BAZ joint venture became Volkswagen's fully-owned affiliate. Nowadays, it is one of the biggest Slovak exporters and the biggest carmaker in Slovakia. Moreover, it is one of the most state-of-the-art production plants of Volkswagen in the world, exclusively producing SUVs as Volkswagen Touareg or Audi Q7. It was even considered as the potential site of production for the future Bentley SUV. Whirlpool-Tatramat became a fully owned subsidiary of the American partner in 1996. In 2012, the company celebrated the 20th anniversary of its entry to the Slovak market. During this time, it manufactured more than 20 mil. washing machines and is also the leader of this segment in Slovakia in terms of the units sold. Moreover, Whirlpool built a new warehouse in the west of the country serving not only Slovakia, but also the Czech Republic, Hungary and Poland. Tesla Liptovský Hrádok withdrew from the joint venture in 1999 as it became an affiliate of Alcatel. After the merger with Lucent in 2006, the company has been renamed to Alcatel-Lucent. As of today, it employs more than 70 people in the research and development centre in Bratislava. The research is focused on packet core solutions for 2G, 3G and LTE networks. The Hoechst-Biotika company ceased to exist in 2010, when it was renamed as HBM Pharma. However, the founding partners were no longer present in the company at that time: Hoechst withdrew in 2000 and Biotika in 2004. Nowadays, HBM Pharma is

a partner for contract manufacturing of pharmaceutical products as injectables or bulk tablets. Henkel-Palma was renamed to Henkel Slovensko in 1997, as it became a wholly owned subsidiary. In 2003, Henkel sold its production plant in Nové Mesto nad Váhom to Kematen cosmetics GmbH. Nevertheless, new Shared Service Center was opened in 2007. It provides financial services for whole Europe, USA, Canada, Middle East and Africa. BC Torsion is formally still a joint venture between DIRICKX and Mr. Tibor Lazarovič. However, DIRICKX owns 99,9 % of shares while Mr. Lazarovič is a CEO of BC Torsion.

B. The second decade of the East-West joint ventures in Slovakia

The development of Slovak economy in 2004-2014 and joint ventures with participation of Slovak entities in this time period

As for the next decade of Slovak economy development, new joint ventures continued to appear, but also some of the existing ones were dissolved or became affiliates of one of the partners. The period was marked by several milestones, which could have had an impact on joint ventures:

(1) Accession of Slovakia into the European Union

Slovakia became a member of the European Union on May 1st, 2004, alongside with other former socialist countries, such as the remaining members of the Visegrad Group (V4): the Czech Republic, Hungary and Poland. The EU membership represents an opportunity of easier establishment of international joint ventures for Slovak enterprises, given the existence of single market and the free flow of capital. The adoption of the euro currency in 2009 might facilitate the joint venture formation even more. According to Alhorr, Boal and Cowden (2012), the changes associated with economic integration on national level have positive impact on alliance formation. By the means of alliances, the companies from smaller economies (as Slovakia) can make use of the growth potential in the form of the single market, lowering their dependence on the domestic one. On the other hand, given that single market and single euro currency lower the risks of foreign expansion, they might also lower the need for equity arrangements.

(2) Export-driven economic growth

Slovakia experienced a period of continuous economic growth in the years 2000-2007, which was ended by the world financial and economic crisis in 2008. However, it returned to growth as early as in 2010. The openness of Slovak economy in terms of share of the foreign trade on GDP is the fourth highest in the European Union, reaching 186 % in 2012. This suggests that it is highly dependent on exports. However, the biggest exporting companies are mainly the foreign affiliates, with local enterprises (especially the small and medium-sized) lagging behind in terms of exports' value: in 2012, the number of exporting SMEs reached 27 474, which stands for 97,1 % of all Slovak exporters. However, the value of SMEs' exports was 17,486 bil. €, which represents only 27,8 % of the overall value of Slovak exports. Increase of SMEs' share of overall exports' value is one of the goals of Slovakia's pro-export strategy for the period of 2014 – 2020. One of the solutions of this problem might be the creation of SMEs' partnerships (and notably joint ventures) with foreign companies in order to facilitate the foreign expansion of Slovak companies.

(3) The adoption of the euro currency

Slovakia adopted the common currency in 2009, in the time of the economic crisis. However, the negative expectations concerning rising inflation were not fulfilled, partly due to the crisis itself: the inflation dropped from 4,6 % in 2008 to 1,6 % in 2009 and even more to only 1 % in 2010. The euro currency decreased the exchange rate risks for Slovak exporters, as the eurozone countries represent a significant share of Slovak exports (more than 43 % in 2013).

(4) State institutions and their support for the international joint venture creation

Given the rather small domestic market, many Slovak companies aim to expand abroad. However, SMEs in particular often have to cope with the scarcity of resources, both tangible (finance, technology) and intangible (foreign market knowledge, managerial know-how). In order to succeed on the foreign markets, they have to substitute the missing resources with others, e.g. unique product serving the niche market, patented technology or highly qualified and skilled human resources. All of them could serve as the sources of their competitive advantage. Based on this advantage, the companies could attract potential partners for joint venture, willing to provide the resources in need. Taking into account their lack of foreign market knowledge, only limited access to the distribution

channels abroad and possible negative country-of-origin effect, the partnership with the foreign investor might be the best solution to overcome these obstacles of foreign expansion. To achieve this goal, it is important to provide the companies with the opportunities to meet the prospective partners. The state institutions might be the right intermediaries facilitating the creation of such partnerships, for example Slovak Investment and Trade Development Agency (SARIO) is an institution which provides support for foreign companies willing to invest in Slovakia, but also for Slovak enterprises which aim to expand abroad.

Joint ventures with participation of Slovak companies in 2004-2014

There can be found several types of joint ventures with Slovak participation. One type of joint ventures are the partnerships of the state and foreign investors, particularly in the privatized former monopolies such as Slovak Telekom (telecommunications provider), Slovenský plynárenský priemysel (gas provider) or Slovenské elektrárne (electricity provider). All of these privatizations occurred during the government of prime minister Mikuláš Dzurinda, shortly before accession of Slovakia to the European Union. Slovenské telekomunikácie, the predecessor of Slovak Telekom, was privatized in 2000, the other companies were both privatized in 2002. However, we can observe the development in terms of changing foreign investors (in Slovenský plynárenský priemysel) or the attempt of state to finish the privatization (the ongoing case of Slovak Telekom).

There can be also found companies formally fulfilling the conditions of joint venture definition, but in fact, they are more similar to the affiliates of foreign investors, established by their other affiliates from different countries – for example, this is the case of IBM International Services Centre in Bratislava. Thus, we can assume that these firms do not possess the attributes of joint ventures such as cooperation of the partners, sharing of resources or learning.

There are also some cases of foreign partners which withdrew from the joint venture after the termination of investment incentives from the state. After the withdrawal from Slovakia, they set up new facilities in other countries, e.g., in Poland. We can assume that their main motive of entering the joint venture was the efficiency-seeking, aimed at lowering their costs. The relatively cheap Slovak labour force, combined with the various forms of incentives increased the attractiveness of Slovakia as the target country for their investment. Nevertheless, once the incentives expired, these companies chose to move their production to countries with more favourable conditions.

As for the joint ventures of Slovak companies abroad, to gain information about them is even more difficult than the Slovakia-based ones. They often stay only in the planning phase, as the companies use to announce their intent to media, but do not proceed in establishment of the joint venture. Some of the joint ventures that were realized in 1990s are already terminated, as is the case of electronics manufacturer OVP Orava and its venture in Russia. Some other are still existing and successful, for example the joint venture of Slovak company Matador in Russia, Matador Omskšina.

Concerning the international joint ventures in Slovakia which became affiliates of one partner, it is often not possible to gain information about them, as there are no longer any employees who worked in the company during the joint venture existence.

As already mentioned our research was aimed at planning, managing and performance outcomes of international joint ventures with the participation of Slovak companies. 44 filled in questionnaires have been collected and included in the research. They represent all the sizes of the companies (micro, small, medium, large) and all sectors of economy (agriculture, manufacturing, services), as well as the companies with the participation of state or municipalities.

Research results

Size of the international joint ventures

The research sample consists of 17 (38,64 %) large (250 and more employees) , 7 (15,91 %) medium-sized (50-249 employees), 10 (22,73 %) small (10-49 employees) and 8 (18,18 %) micro-companies (less than 10 employees). Two companies stated their number of employees only in the interval of 10-99, we can therefore assume they are either small or medium-sized firms. This division is based on the European Commission definition of the small and medium-sized enterprises (European Commission, 2003)

Line of international joint ventures' business

16 (36,36 %) companies are active in the field of industrial products, 4 (9,09 %) in the field of consumer products, 3 (6,82 %) firms in the both of them. The line of business of the remaining companies can be labeled as „other“ – meaning mostly various types of services, but also agriculture or technology development. This changing structure is the result of various developments, notably the changing structure of Slovak economy itself, emergence of new industries nonexistent

in 1990s (e.g., mobile and Internet technologies) and liberalization of conditions for foreign investors, related to the accession of Slovakia to the European Union.

Motives for international joint venture creation

The companies were asked about the importance of various motives for the joint venture creation. The importance was ranked as follows: 1 – not important at all, 2 – minor importance, 3 – some importance, 4 – rather strong importance, 5 – very important.

Gaining access to the low-cost resources (e.g., raw materials, labour force)

This motive is not important at all for 17 (38,64 %) companies and very important for only two (4,55 %) firms. It has minor importance for 5 (11,36 %) other respondents. 9 (20,45 %) joint venture partners claimed rather strong importance of this motive, while the remaining 11 (25 %) companies state that gaining access to the low-cost resources is important motive for the joint venture creation. The average response value is 2,41.

Gaining access to the distribution channels

5 (11,36 %) companies cite it as the very important reason for the partnership creation, on the other hand, it is not important at all for 6 (13,64 %) firms. 12 (27,27 %) companies stated the importance of access to the distribution channels as rather strong, while 7 (15,91 %) other consider it of minor importance. 14 (31,82 %) companies think it is important motive for the joint venture creation. The average response value is 3,07.

Establishment of a base to access other countries' markets

It is very important reason for joint venture creation for 10 (22,73 %) firms and a motive of rather strong importance for other 13 (29,55 %) companies. 7 (15,91 %) respondents state it as not important at all, while 8 (18,18 %) joint venture partners think this motive is only of minor importance. 6 (13,64 %) companies consider it an important reason for partnership creation. The average response value is 3,25.

Gaining access to new technologies

This motive is very important for 8 (18,18 %) respondents and of rather strong importance for other 10 (22,73 %) companies. 6 (13,64 %) firms cite it as not important at all, it is of minor importance for 3 (6,82 %) companies. Gaining ac-

cess to new technologies is important for 14 (31,82 %) joint venture partners. The average response value is 3,11.

Lower need of capital investment

3 (6,82 %) companies cite it as very important, 8 (18,18 %) firms as of rather strong importance. 7 (15,91 %) respondents think it is not important at all, another 6 (13,64 %) of them claim it is of minor importance. As many as 20 (45,45 %) companies state that lower need of capital investment is important motive for joint venture creation. The average response value is 2,86.

Need to overcome local government regulation barriers

18 (40,91 %) companies state it is not important at all, 10 (22,73 %) respondents think it is only of minor importance. This reason is very important for one firm and of rather strong importance for 5 (11,36 %) companies. It is important motive for partnership creation for 10 (22,73 %) respondents. The average response value is 2,11.

Learning from partner

It is very important reason for joint venture establishment for 4 (9,09 %) companies and of rather strong importance for other 14 (31,82 %) firms. 5 (11,36 %) respondents think it is not important at all, 10 (22,73 %) partners state it is only of minor importance. This motive is important for 11 (25 %) companies. The average response value is 3,05.

The results of the research suggest that the most important motives for partners in international joint ventures with Slovak participation are establishment of a base to access other countries' markets, gaining access to new technologies and gaining access to the distribution channels of the partner. Learning from partner is only the fourth most important reason to enter the joint venture.

The importance of base to access other countries and access to partner's distribution channels might point out that Slovak companies are willing to expand abroad and they seek the foreign partners in order to facilitate the foreign market entry. However, the relatively less important motive of lower capital investment need might imply that Slovak firms are rather looking for intangible (technology know-how, foreign market knowledge) than financial resources.

The lower importance of learning from partner suggests that priorities of Slovak companies have slightly changed compared to the situation in 1990s, when learn-

ing was among the main goals of Slovak firms entering the joint venture. It might be explained by the experience in business and entrepreneurship amassed during the years after 1989, by the development of Slovak economy and business environment, but also by the skilled labour force (mainly IT specialists) and the effect of modern information and communication technologies, which facilitate the knowledge gaining of (e.g., about foreign markets).

The least important reasons to enter the joint venture with foreign partner are the access to the low-cost resources and the need to overcome regulation barriers of local government. The lower need of low-cost resources might be explained by the fact that Slovak companies themselves dispose of resources relatively cheaper than those of the investor, notably the labour force. Another reason might be the lower resource-intensity of the business activities (e.g., in the sector of services).

Only minor importance of overcoming government regulation barriers might be interpreted by the structure of joint venture partners: majority of them comes from the EU member states and all the joint ventures included in the research are established in EU countries as well. Given the existence of single market and the free flow of capital, the situation is considerably different than in 1990s, when establishment of a joint venture was a precondition of Slovak market entry.

Importance of various performance criteria

The respondents were asked about the importance of various measures used to assess the international joint venture performance. Their importance was ranked as follows: 1 – not important at all, 2 – quite not important, 3 – neutral, 4 – quite important, 5 – very important.

Level of sales

This measure is the most important for the respondents, as 31 (70,45 %) labeled it as very important and 12 (27,27 %) as quite important. Only one company stated that level of sales is important as a performance measure. The average response value is 4,68.

Sales growth

It is very important performance indicator for 27 (61,36 %) companies, quite important for another 15 (34,09 %) respondents and 2 (3,41 %) firms cite it as an important criterion. The average response value is 4,57.

The research sample for the remaining criteria consists of 43 companies, as one respondent did not fill in the questions regarding the following performance measures.

Market share

This indicator is very important for 12 (27,91 %) respondents and quite important for 16 (37,21 %) joint venture partners. 8 (18,60 %) firms consider it as important, 4 (9,30 %) companies as quite not important and 3 (6,98 %) respondents think it is not important at all. The average response value is 3,7.

Profitability

This measure is very important for 26 (60,47 %) respondents and quite important for another 14 (32,56 %) of them. 3 (6,98 %) companies stated profitability is not important at all as the performance criterion, one joint venture partner thinks it is quite not important and one firm consider it to be an important performance measure. The average response value is 4,47.

Return on assets

17 (39,53 %) companies cite it as very important, 18 (41,86 %) firms think it is quite important performance indicator, another 6 (13,95 %) respondents consider it to be important measure, one respondent labeled it as quite not important and the last joint venture partner think it is not important at all. The average response value is 4,14.

Efficiency of distribution

10 (23,26 %) firms think it is very important performance criterion, 19 (44,19 %) consider it to be quite important, 9 (20,93 %) state it as an important measure, 2 (4,65 %) respondents hold the view efficiency of distribution is quite not important and the remaining 3 (6,98 %) companies think it is not important at all. The average response value is 3,73.

Efficiency of marketing

Only 8 (18,60 %) respondents consider it to be very important performance measure, it is quite important for another 17 (39,53 %) of them. 12 (27,91 %) companies cite it as important indicator, 3 (6,98 %) firms think it is quite not important and the last 3 (6,98 %) hold the view it is not important at all. The average response value is 3,56.

Manufacturing/quality control

21 (48,84 %) companies state that it is very important performance indicator, 16 (37,21 %) firms label it as quite important and 4 (9,30 %) as important. One respondent thinks it is quite not important measure, it is not important at all for one joint venture partner. The average response value is 4,28.

Cost control

Cost control is very important for 27 (62,79 %) companies, quite important for 14 (32,56 %) firms and important for 2 (4,65 %) respondents. The average response value is 4,58.

Accomplishment of goals set for the international joint venture

22 (51,16 %) companies think it is very important performance measure, 19 (44,19 %) cite it as quite important and 2 (4,65 %) respondents hold the view that accomplishment of goals is important criterion. The average response value is 4,47.

Overall performance compared to competitors

This indicator is very important for 18 (41,86 %) companies, quite important for another 15 (34,88 %) respondents. Performance of the joint venture compared to competitors is important for 8 (18,60 %) firms, one respondent cite it as quite not important and one as not important at all. The average response value is 4,12.

According to the answers from respondents, the most important performance criteria are the level of sales, the cost control, the sales growth, profitability, accomplishment of goals set for the IJV and manufacturing/quality control. On the contrary, the least important measures are efficiency of marketing, market share and efficiency of distribution. The results show that besides the financial criteria, also non-financial indicators as accomplishment of IJV goals and manufacturing/quality control are quite important for the partners.

Satisfaction with the performance of international joint ventures

Based on previous results showing the importance of respective performance criteria for partners in international joint ventures, we assess the satisfaction of respondents with joint venture performance measured by the six most important criteria. The research sample consists of 42 companies, as 2 firms did not answer

the questions concerning satisfaction with joint venture performance. The satisfaction was ranked as follows: 1 – very dissatisfied, 2 – dissatisfied, 3 – neutral, 4 – satisfied, 5 – very satisfied.

Level of sales

6 (14,29 %) companies state they are very satisfied with the level of sales, 21 (50 %) firms are satisfied with this performance criterion, opinion of 12 (28,57 %) joint venture partners is neutral. The remaining 3 (7,14 %) companies are dissatisfied with the level of sales. The average response value is 3,71.

Sales growth

4 (9,52 %) respondents are very satisfied with the sales growth, 22 (52,38 %) companies are satisfied with the level of this measure and 7 (16,67 %) firms are dissatisfied. Opinion of 9 (21,43 %) companies is neutral. The average response value is 3,12.

Profitability

Only 2 (4,76 %) firms are very satisfied with their profitability, another 19 (45,24 %) companies are satisfied and 5 (11,90 %) respondents are dissatisfied. 16 (38,10 %) firms hold the neutral view. The average response value is 3,43.

Manufacturing/quality control

As many as 10 (23,81 %) companies are very satisfied with this the level of this indicator, another 20 (47,62 %) respondents are very satisfied. Only one company is very dissatisfied with manufacturing and quality control. Opinion of 11 (26,19 %) companies is neutral. The average response value is 3,9.

Cost control

6 (14,29 %) respondents are very satisfied with the cost control in their joint venture, 27 (64,29 %) firms are satisfied and 6 (14,29 %) hold the neutral view. 3 (7,14 %) companies are dissatisfied with the performance of joint venture based on the cost control. The average response value is 3,86.

Accomplishment of goals set for the international joint venture

8 (19,05 %) companies are very satisfied with the level of this measure, 17 (40,48 %) are satisfied and 3 (7,14 %) firms are dissatisfied. Opinion of 14 (33,33 %) joint venture partners is neutral. The average response value is 3,71.

Results show that the companies are the most satisfied with the manufacturing/quality control, followed by the cost control. On the other hand, the respondents were relatively less satisfied with the sales growth of IJVs and their profitability. However, on the average, the firms are closer to the satisfaction with the performance results than the opposite.

Satisfaction with the overall performance of joint venture

The respondents were also asked about their satisfaction with the overall performance of joint venture. Even though only 8 (19,05 %) companies are very satisfied with the overall performance, as many as 23 (54,76 %) firms are satisfied and only 2 (4,76 %) are dissatisfied. 9 (21,43 %) companies hold the neutral view. The average response value is 3,88. 42 companies expressed their opinion on overall joint venture performance.

Satisfaction with current business and management strategy of international joint venture

The companies also had to state whether they are very satisfied with the current business and management strategy of the international joint venture. 10 (22,73 %) companies strongly agree with this opinion, 23 (52,27 %) firms partly agree and only one joint venture partner partly disagree. 10 (22,73 %) companies hold the neutral view. All 44 companies expressed their opinion about this issue.

Continuity and future performance of international joint venture

When asked if the companies plan to continue their participation in the international joint venture in the long-term horizon, 24 (54,55 %) companies strongly agreed, 12 (27,27 %) partly agreed and only 2 (4,55 %) strongly disagreed. 6 (13,64 %) respondents held the neutral view.

The respondents also expressed their opinion whether the joint venture will maintain/gain high profitability in the long-term horizon. 12 (27,27 %) companies strongly agreed with this statement, 15 (34,09 %) firms agreed and 2 (4,55 %) strongly disagreed. Opinion of 15 (34,09 %) companies is neutral.

In general, we can conclude that the majority of the joint venture partners are satisfied with overall IJV performance, even though the situation is slightly different when we take into account some of the respective performance measures (e.g., sales growth or profitability). The majority of the respondents is also content with the current business and management strategy of IJV, at least to some extent. As many as 36 companies (81,82 %) at least partly agree that they plan to continue their participation in IJV in the long-term horizon, which suggests their commitment to cooperation with the foreign partner. Nevertheless, when asked about future profitability of the IJV, only 27 (61,36 %) firms at least partly agreed that the joint venture will be highly profitable in the long-term horizon. This is in line with the slightly lower average satisfaction with the current profitability of IJVs.

Conclusions

The industrial structure of international joint ventures in 1990s was determined by the situation in the Slovak economy and the structure of state-owned companies available for privatization. Therefore, the IJVs were almost all created in the manufacturing sector. However, the gradual opening of economy for foreign investment and, after all, the development of the economy itself resulted in far more various structure of IJVs in the first decade of 21st century. The first major trend is the rising number of IJVs in services. Their establishment is motivated mainly by the vision of Slovak market entry in the field of telecommunications, finance, tourism, etc. The second trend is the emancipation of Slovak entrepreneurs willing to cooperate with foreign partners in order to become more competitive in the home market or even to enter foreign markets. This development was encouraged by the period of rapid export-oriented economic growth of Slovak economy. Nevertheless, many Slovak companies started to look for partnership opportunities abroad as well, resulting in the foreign direct investment of Slovak companies in the form of international joint venture.

The expectations of Slovak companies were mostly unmet in 1990s. They entered the partnerships with the aim to learn from the partner, to enter its distribution channels in the foreign markets and to transfer the knowledge, technology and know-how of the foreign investors. From the beginning, the intentions of foreign companies were completely different - often aimed at full acquisition of the Slovak firms, with little to no willingness to share the most valuable assets with them. Even if the Slovak company itself had not ceased to exist, it usually with-

drew from the joint venture, which eventually became a fully-owned subsidiary of the foreign company.

The motives of Slovak companies for creation of international joint ventures with foreign partners have changed since the first wave of joint ventures' establishment in 1990s. Given the elimination of government regulation barriers, foreign investors no longer have to create a partnership with local company in order to enter the Slovak market. Slovak companies also have greater opportunities to search for suitable partners if they aim to create international joint venture both home and abroad. Based on the importance of a base to access other countries and access to distribution channels as motives of joint venture creation, Slovak companies seem to be interested in their foreign expansion. The motive of gaining access to new technologies is still important, however, the significance of learning from partner in general is slightly lower. This might indicate that Slovak companies have gradually gained the needed knowledge themselves or that they can access or create this knowledge by other means than the partnership with foreign company. The relatively lower importance of capital investment motive might suggest that the Slovak companies have higher need for intangible (technology know-how, foreign market knowledge) than financial resources or that they can gain finance by other means with more favourable conditions than from the foreign investor.

In general, the companies are quite satisfied with the overall joint ventures' performance, even though the situation might be different in some respect, when we consider the respective performance criteria. Nevertheless, the majority of respondents plan to participate in the joint ventures also in the long-term horizon.

The current situation in international joint ventures with Slovak participation is different in many respects as it was in the 1990s: the motivations for participation have slightly changed, as did the structure of partnerships in terms of the economy sectors. The Slovak companies seem to be more content with the cooperation and the performance of the joint ventures, as they are also willing to continue the partnerships with foreign investors. This might be partly the result of the development of the economy and business environment, but also that of the companies themselves, as they could amass the knowledge, contacts and experience needed to successfully manage the partnerships during more than two decades since Slovakia experienced the shift to the market economy.

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4. Social Networks Embedding Business In Transitional Contexts

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Prologue

Jorma Larimo has been one of the key scholars in Finland focusing on Central and Eastern Europe and transitional markets. This is indicated both by his own research (e.g. Larimo, Nieminen & Springer 2002; Arslan & Larimo 2013) and his supervision of research (Mainela 2002; Arslan 2011). Furthermore, he has been actively involved in the international research community contributing to it with context-specific knowledge (e.g. Hennart & Larimo 1998; Larimo, Marinov & Marinova 2006; Segaro, Larimo & Jones 2013), as well as by organizing and participating in conferences (e.g. as the organizer of *Vaasa Conferences in International Business*, and as a regular participant in *Vienna Conferences on Marketing Strategies in CEE*). It is in this area especially that we have become to collaborate with him; consequently we here focus on questions related to contextuality and transition.

Introduction

Uncertainties and ambiguities arising from dissimilar contexts differentiate international business (IB) from domestic business (e.g. Johanson & Vahlne 1977). Various national, institutional, cultural, and socio-political contexts influence business strategies and operations, and they are therefore of interest to both managers and IB scholars (e.g. Hennart & Larimo 1998; Michailova 2011). From this viewpoint, the setting in which these contextual borders are crossed is a key variable and influencing factor in international business. The crossing of borders is concretized in the establishment of business relationships between various actors (Johanson & Mattsson 1987). Relationships with customers and suppliers, as well as with governmental organizations, municipal officials, or even competitors are vital to business (Hadjikhani & Ghauri, 2001). This way firms become embedded in network contexts. We rely here on the view that embeddedness is primarily a question of the roles that individuals and inter-personal relationships play in eco-

conomic exchange (see Araujo et al. 1998; Nahapiet & Ghoshal 1998). Consequently, there is a reason to analyse how social networks are used to organize (international) business.

Networks have been suggested to have varying importance and characteristics in different national and cultural contexts (e.g. Jansson, Johanson & Ramström 2007). Transitional contexts, such as Eastern European and Asian markets, have been featured as contexts in which inter-personal relationships play a particularly strong role, and networks tend to have a social character (Salmi & Bäckman 1999; Törnroos & Nieminen 1999; Sidorova & Michailova 2010). Relationship-building and the roles played by inter-personal relationships are likely to appear particularly transparent in these contexts. In the present paper, we claim that social networks are a specific structure for organizing business, which develops over time similarly to any formal organization. Thus, it is important not to downplay the role of social networks by taking them merely as a means to enter new markets or to facilitate business, but to see them as the fundamental form of organizing business.

We propose that there is a need for better conceptualization of social networks in international business. Indeed, social networks as *a form of organizing business* has, in our view, been largely neglected by IB scholars, and inter-personal relationships have been given a secondary role in supplementing business (relationships). Analysis of inter-personal relationships that are so intertwined with business relationships in a transitional context (Bäckman & Salmi 1998; Hutchings & Michailova 2004; Ledeneva 2009; Michailova & Worm 2003) gives a fruitful basis for understanding that business by its very nature is organized as a network.

We build this conceptual paper on research that discusses the role that networks and inter-personal relationships play in business in transitional contexts, and we ask the following question: “How are businesses organized as social networks in transitional markets?” We illustrate the key constructs of social networks as organising structures through examples from our own and other research in the transition markets of Russia, the Baltic States, and Poland. As a result, the findings of the present study are contingent on the specific (transitional) context but can also aid to understand the social network-based organizing in other contexts in which the networking and the roles of inter-personal relationships appear more hidden. Still, in the end, all business relationships are webs of interactive relationships between individuals (Håkansson & Snehota 1989).

Our aim in this paper is to discuss social networks as a structure that organizes business within transitional contexts. We suggest that in future IB studies Granovetter’s (1985) notion of business being embedded in social networks needs

more conceptualization and attention. The paper is structured as follows. We start by discussing the role of networks in transitional markets, and next, we investigate the concept of embeddedness with an emphasis on social embeddedness (that is, embeddedness of business in inter-personal relationships). Our discussion section focuses on the implications of social embeddedness of business for international business research. To conclude the paper, we link our conceptualization of social embeddedness to the IB key concept of distance.

Networks In Transitional Markets

Transitional markets have provided an interesting context for business managers and scholars alike. The fundamental institutional changes have directed attention to network building and human behaviour under very turbulent conditions. In the 1990s, the opening of the markets as a result of the transition in the former socialist countries of Central and Eastern Europe made them an interesting expansion area for Western firms (Nieminen, Larimo & Springer 2002). Yet, the often dramatic transition process also created turbulent circumstances where the rules of behaviour were vague and changing. Managers needed to act in a complex, intercultural setting in economically and politically unstable markets.

In transition, in addition to the economic and political changes, new institutions are created to govern the behaviour of people (Sjöstrand 1992; North 1997). These institutions do not consist of only a set of legally defined rights and obligations but are mental constructs developed through human interactions and exchanges (Sjöstrand 1992). The unfolding of extensive economic reform depends on the behavioural models at the level of individuals involved in companies (Salmi 1995: 211). The change of the behavioural patterns is likely to be the slowest of the various change processes that take place (Mattsson 1999). It evolves through interaction of all the connected actors, and the resulting institutions form the new, informal rules of the game (Salmi 1995: 20).

Transition changed the trade from being controlled by the central planning authorities into being conducted within the business relationships that were based on voluntary cooperation. For local firms this meant the freedom to pursue their own strategies, i.e. establish, develop and disrupt relationships in order to achieve an appropriate network position (Salmi 1995: 110). Foreign firms were confronted by the need to actively seek for business partners in an environment scarce of reliable information about local firms (Salmi & Bäckman 1999). The overall turbulence and the structure and functioning of the markets created a particularly

strong need for relationship building among various actors (Törnroos & Nieminen 1999; Johanson & Johanson 1999).

Countries have for long been seen to differ in terms of the relative importance they place on firm vs. person-based relationships in business (Johanson & Vahlne 1994: 92). Importance of personal relationships seems to be a feature of the Eastern European and Asian business cultures, in particular (Salk & Brannen 2000; Björkman & Kock 1995). Salmi (1995: 193–194) noted the crucial importance of personal relationships in economic activities in the former Soviet Union. Informal relations based on ‘blat’ and personal favours have characterized the Soviet and Russian economies (Ledeneva 2009; Michailova & Worm 2003). Törnroos and Nieminen (1999: 293) saw the networks as a prerequisite for doing business in Eastern Europe and as more personal in character than what is typical in Western countries. In Poland, the “*zalatwik networks*”, consisting of personal contacts with individuals who are able to provide some services, were seen as significant parts of Polish lifestyle (Hamilton & Roszkowski 1991). Therefore, in Poland the best way to achieve support in business matters was by personal interaction (Mainela 2002). Sidorova and Michailova (2010: 45) also recently noted that in Russia (and China) “networks are distinctly different from those in the West in that they are much more personal”.

The inclination to rely on personal relationships in transitional markets can also be seen to have its roots in the relationships between the planning authorities and the managers of the firms in the command economy (Johanson 2000). Although the relationships were generally one-sided and anonymous, the managers had some room to manoeuvre. If the manager had good relationships with people at governmental or authority level s/he could maybe negotiate for preferential treatment when the achievement of planned production goals was for some reason at risk. Relying on interpersonal trust could also be the only option when the institutions of the planned economy did not protect the interests of individual parties in business exchange (Mattsson 1999: 136).

In positioning their companies in the East European transition markets the Western managers were noted to intentionally make use of both their own and corporate contacts (Seyed-Mohamed et al. 1996: 82). The customer-supplier relationships in Russia relied as a whole on personal acquaintance and direct personal contacts, and the relationships with banks and authorities were also maintained through the person-centred network system (Salmi & Bäckman 1999). Knowing someone inside, or having relations to another actor, was crucial to all business dealings. Instead of relying only on the top managers, the relationships with the whole organization were used (Salmi 1995: 112) to ultimately find the actual de-

cision maker who may not have been the most obvious person (Salmi & Bäckman 1999: 156). Overall, inter-personal relationships formed the network capital that was the basis for setting up new business as well as operating the firm (Salmi & Bäckman 1999; Mainela 2007).

Recent research on transition markets maintains the importance of inter-personal relationships in business (Puffer & McCarthy 2011). Mattsson and Salmi (2013) conclude that it is critical to acknowledge the personal interactions and social networks as the basis for developing business exchanges for both increased cooperation and competition between firms in the Russian transformation. We shall proceed to discuss embeddedness and social networks as a business-organizing structure in the following section.

International Business Embedded In Social Networks

Interest in contextualizing business and economic activities has led scholars to investigate the concept of embeddedness in different fields: in business market studies (Halinen & Törnroos 1998) and more generally in management and organization studies (Dacin, Ventresca & Beal 1999). In the field of IB, embeddedness has mainly been analysed in the context of MNCs, where internal and external organizational networks have been studied (Andersson et al. 2002; Forsgren, Holm & Johanson 2007). However, the original conceptualizations of the embeddedness of economic activity in social structures have received little attention within IB studies. In this paper, we focus on social embeddedness.

We have above illustrated how social networks embed businesses in transitional contexts, in particular. More generally embeddedness has been seen as the concept that assists the understanding of businesses by avoiding the atomization of actors (Anderson 1997) and by providing explanation of change and development in business networks (Halinen & Törnroos 1998). We approach embeddedness through the view that social networks are a fundamental structure organizing business, as all economic action is embedded in concrete personal relationships between individuals (Granovetter 1985: 490). Therefore, the core of business interaction is the social exchange process in which individuals become committed to interaction in the relationship (Håkansson & Snehota 1989; 1995: 10). When individuals in the business relationships take actions to change the preferability positions of the companies and seek for social companionship, they create social organizations (Melin 1989). The social organization often embeds the business in informal, but highly influential, social structures.

In our conceptualization, social embeddedness has two primary dimensions: first, individuals as the actors of the business relationships and second, as a particular social community to which the individuals belong. These two dimensions to a great extent determine how business becomes organized. As it is the individuals who act in the relationships, their individual-level motivations, perceptions, cognitions and sense-making processes are the bases for the action taken in international business (Baker et al. 2005; Zahra et al. 2005). For example, Mainela & Puhakka (2009) stress the cognitive activities of individuals in interpreting the multicultural setting to develop business opportunities in international joint venture operations in the Polish markets. They show how the individuals' interpretation of the situation relates to personal initiatives over time, which in turn influences organizing business.

The existence of the social community explicates that all people belong to wider social structures. Therefore history, culture, value system, and the social circumstances inevitably intertwine with business activities and have a great influence on what is seen as acceptable and desirable in a particular situation and how individuals act on that basis (Zander 2004; Baker et al. 2005). The social community view gives rise to the question of membership in a particular social system. For example, Salmi and Bäckman (1999) illustrated how individuals are divided into inner and outer circles of inter-personal business networks in Russia which then determines the nature of their interaction. Hutchings and Michailova (2006), in turn, illustrate the differences of in-group and out-group knowledge sharing in Russia and China. The membership or position on a certain layer of the social system thus influences what a person is able to actualize in the social network.

The studies of subsidiary embeddedness have also indicated how the integration of subsidiaries into the MNC internal network varies and some units are more embedded in their local networks whereas others are more embedded in the internal MNC network (e.g. Andersson et al. 2002; Forsgren, Holm & Johansson, 2007). This seems related to the personal characteristics and preferences of the managers who are responsible for the subsidiary (see Marschan et al. 1996). Their actions define what kinds of relationships are established and with whom, although the dependence of the firms on the resources linked to their exchange relationships can be seen as the basis for business relationship development and gives the relationships specific roles.

In conclusion, as social networks embed business, organizing international business is to a great extent subjective and context dependent (see Baker et al. 2005). Individuals' motivations, subjective preferences and perceptions are important determinants of international business behaviour. Furthermore, individuals active

in business relationships become by necessity, but to varying extents, absorbed by the social community that contextualizes the international business behaviour in a wider social system. Furthermore, as individuals have different capabilities to appreciate and utilize the multi-cultural social contexts that are created in international business (see Muzychenko 2006; Williams & Lee 2009), in certain situations there is great variation in how business becomes organized. We therefore see it crucial to direct attention from formal organizations and organizing behaviours into informal organizations and acting within the social structures in international business.

Discussion: Implications Of Social Network Organizing For Ib Research

As we see it, social networks are always the core of and setting for business activities, but it is in certain contexts and situations where their significance becomes visible and acknowledged, and therefore, more easily accessible for investigation. The transitional context is one of these fruitful ‘test cases’ for more analysis on what the social embeddedness of business actually means and what are the implications of it for both research and practice.

Social networks (and social capital) in the business context have been widely studied. What remains problematic is that this analysis primarily relies on rather simple classifications and straightforward categorizations of social relations; as exemplified by, for example, the dichotomy of weak and strong ties (Granovetter, 1973). Social Network Analysis (SNA) is extensive, but the basis for studies is whether a relationship (contact or contract) exists or not. Such an analysis neglects intermediate forms of relating (e.g. acquaintance vs. friend), as well as different phases of relationships (as exemplified in e.g. initial contacting, intensive interaction or dormant relationships). As Dacin et al. (1999: 327) note: “a focus on embeddedness motivates attention to issues beyond the simple presence of ties”. We see that social bonding is a matter of degree and of different phases, thus taking place in a continuum and a specific spatial and time context, rather than being a dichotomous variable.

Social networks per se lack content, but they may facilitate exchange between firms, depending on the interests, motives and values of the individuals (Dacin et al. 1999: 327). Therefore, there is a need for more detailed analysis of the contents of social networks. Within the business network studies, initial efforts have been made to open up the various functions of social relationships in a business relationship. Turnbull (1979) identifies six different roles for personal contacts.

Four of the roles are task-related and serve organizational objectives: the information exchange role, the assessment role, the role of negotiation and adaptation, and the crisis insurance role. The remaining two roles are non-task related and exist for private social reasons: the social role and ego enhancement. Halinen and Salmi (2001) propose that personal relations may carry different roles in the different phases of business relationships; thus they may support or hinder business and also, play a different role in initiation, crisis or ending phases of business relationships. Mainela (2007) developed a typology of four types of inter-personal relationships that are related to different possibilities of action but can also be seen as layers of relationships that are activated for different purposes. These conceptualizations are helpful in indicating the versatility and complexity of social networks and networking in business. However, we need further work to analyse social bonds in a more nuanced way, and thus conceptualizing the inter-personal relationships and social communities as bases for business interaction and special logics for organizing business operations.

Our argumentation has several practical implications for IB research. Recently, Michailova et al. (2014) have noted the key role that relationships (and their ending in particular) between researchers and their respondents may have on the theoretical development of management studies. Our analysis follows this path. Furthermore, we suggest that more attention needs to be paid to the informal, rather than formal, activities in business. We call for more analysis of individual interaction and networking (rather than organizational structures), of the motives, values, and incentives of the interacting individuals, as well as of the features of the social communities involved in international business.

All these requirements pose several challenges to our research topics and methods. We need to

- address rich empirical contexts (by e.g. qualitative and case studies, but also by developing methods for quantitative analysis)
- gain and develop confidence and trust among the respondents to ensure that hidden and informal – even negative – experiences and actions in business are shared with researchers
- design and conduct research in settings that allow for dyadic and network analysis, in order to reach understanding of the inter-personal interaction between individuals, and
- develop means for better understanding the social communities in which business takes place.

Conclusions

As social networks carry such an important role and are an acknowledged phenomenon of transitional contexts, it is in this context that the peculiarities of organizing business around networks are particularly visible and enhance a broader understanding of organizing through social networks. While our study has implications for business in general, we see that the field of IB in particular can benefit from such an approach.

International business is all about contextuality: different contexts pose different challenges and opportunities for business behaviour. Individuals' interpretations of the context and their interests in and abilities to become involved in different social communities pave the way for crossing borders and thus, for international business. If individuals succeed in establishing relationships with various business partners, their firms have a chance of entering and building positions in the (new) business networks.

It is crucial for business relationships that actors (individuals and firms) manage to bridge the distances that exist between them. There is an early definition by Johanson and Vahlne (1977: 24) of psychic distance as "the sum of factors preventing the flow of information to and from the market. Examples are differences in language, education, business practices, culture, and industrial development". This definition already points to the role that individuals play in business interaction. Later on, Johanson and Vahlne (2003: 89) have specified psychic distance to relate to organizations and individuals (rather than nations), and they discuss experiential learning in relationships as well as commitment by actors, which are needed in particular to cover the relationship-specific psychic distance. The role of individuals is further emphasized in a recent study by Dow and Larimo (2009), who base their views on an extensive literature review, and suggest to measure perceived psychic distance at the individual level. They note that conceptualizations and measurements of distance have been too narrow so far and that further, individual-level perceptions are important since managers make business decisions based on their conceptions of their context. In general, we see that managerial perceptions and sense-making has been gaining increasing attention by IB scholars – our study is one fitting into this stream of development.

As noted in our discussion of the implications for the future IB research, our approach calls for new ways of making the hidden and informal (but omnipresent) interpersonal activities visible and legitimate targets for analysis. This is not an easy task, but in our view, worth pursuing further.

Epilogue

In this paper, we have used the transitionary markets to indicate how fundamentally social networks embed business. These contexts provide ample evidence of the intertwined nature of social and business networks, and of the inseparable formal and informal roles of people in business. In the research community too, successful academic work is embedded in social structures and well-functioning personal networks. We have always found cooperation with Professor Jorma

Larimo as enjoyable and rewarding, and it has been our pleasure over the years to cooperate in the scholarly work with such a hard-working and friendly academic.

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5. Transformation Of The Banking Sector In Slovakia¹⁰

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Introduction

Transformation from the former socialist planned economic system towards the market one has started in the former socialist (communist) bloc in 1989, right after the wave of the revolutions in the region. The phenomenon of transformation has attracted the attention from the research and academic circles: first, in the 90' it was rather limited, however in the last decades it has become the topic of growing numbers of national, regional and international academic forums. The pioneering research conference on transition, transformation and management and marketing strategies in transitional countries had been organized for 20 years in Vienna by Reiner Springer, Wirtschaftsuniversitaet Wien and Petr Chadraba, De Paul University Chigaco. These two athors together with several renowned and prominent international researchers as Jorma Larimo, University of Vaasa, Arnold Schuh and Gerhard Fink, Wirtschaftsuniversitaet Wien have led the foundations of the research of the management, marketing, foreign-investment and finance related topics of transformation. Currently, Professor Jorma Larimo is the most distinguished international researcher paying attention to the different features of transformation, including the activity of foreign investors (Finnish, Scandinavian etc.) in the region of Central and Eastern Europe (for example Larimo 2002, 2007, 2010).

We have decided to continue in the footprints of Professor Larimo and his colleagues by the analysis of the transformation of the banking system in Slovakia. As mentioned, Slovakia as an independent state has been the result of the peaceful division of former Czechoslovakia and has started its existence in 1993. (However, the economic transition in the country had started after the Velvet revolution in

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1989 with Slovakia being the part of Czechoslovakia). Since that time during the two decades Slovakia needed to build the basis of an independent state with all the institutions plus undergo transformation.

Banking systems can play a pivotal role for growth and catching-up in all transitional economies and only after some more or less costly measures of banking sector transformation have been carried through, can the actual market-oriented economic expansion start. As the other segments of the financial sector in all post-communist countries have remained so far rather underdeveloped, the role of banks as the dominant form of financial intermediation is even larger .

Slovakia started the transformation process as a part of the former Czechoslovakia. The two-tier banking system had been created and commercial banks had emerged as a result of a financial reform in 1990. After the split of the former Czechoslovakia, starting from January 1993, the independent banking system in Slovakia was formed. The National Bank of Slovakia (NBS) was established and first commercial banks were granted licenses (in 1993 altogether 23 commercial banks).

The banking sector in Slovakia was formed on the basis of a strategy to develop a relatively small, but economically effective net of commercial banks that gradually, would be able to provide all services and products required by the clients (Komínková and Múčková, 1996). Prevaingly, commercial banks in Slovakia have been established as universal banks, performing all basic banking activities.

Starting The Independent Monetary Policy In Slovakia

New central bank – NBS - started to perform basic functions of monetary policy. Its main function was to ensure the stability of the Slovak currency (SKK). To meet this task, traditional central bank measures were applied: issuance of banknotes and coins, money supply management, coordination of payments and settlement operations between commercial banks, supervision of banking activities and prudential performance of the banking system. The NBS performed these tasks basically independently from the Government. However, within legally permitted limits, it supported Government economic policy. The NBS also represented Slovakia in international financial institutions.

During the first years the NBS had to learn and adjust the basic know-how of the central banking policy within a market economy. Its relative disadvantage was that know-how acquired under Czechoslovakia (officially CSFR – Czech and Slovak Federative Republic) after the revolution in 1989 and the qualified per-

sonnel was mainly concentrated in the Czech Republic. However, the NBS managed to cope with these problems and gradually became one of the basic pillars of the financial system stability in Slovakia.

Monetary policy measures applied during the early 1990s were rather unconventional in comparison with developed market economies. The minimum reserve requirement was relatively high (9%), and credit limits were used. Discount rates of the NBS were also high (12% in 1993, 8,8% in 1996 – the latter being used also as an interest paid to citizens from the so called privatization bonds under “the second wave of the privatization”).

The exchange rate policy of the NBS was operating in a fixed exchange rate regime, the rate being defined towards a currency basket. After the split of the former Czechoslovakia and due to overall worsening of the macroeconomic situation, the Slovak crown was devalued by 10% in July 1993. Simultaneously the fluctuation band of the SKK was defined as +/- 1,5%. In order to avoid foreign exchange outflows, the purchase of foreign exchange by the population was regulated to SKK 9.000 in 1994 and gradually increased during next years. After a favorable development of the main monetary indicators, in 1995 a significant liberalization of the current account (of the balance of payments) regulation occurred.

In the monetary policy, the strategy of NBS was to decrease the importance of direct instruments (mainly credit limits) and to increase the role of indirect instruments (preferably open market operations). Implementation of this strategy increased the maneuverability of commercial banks and their lending activity. However, new demands on banking supervision – mainly in connection with the high share of “bad loans” and high dependency of banks on “strategic clients” – came to the forefront. The share of non-performing loans in the total volume of crown loans increased from 21,8% in 1993 to almost 40% in 1996 (Komínková and Múčková, 1996, p.25). Measures regarding capital adequacy of banks, limiting large credit exposure to individual clients, liquidity regulation, etc. were applied.

In this period, a deposit protection scheme (for deposits of physical persons) was also introduced. A Deposit Protection Fund was established. All banks in Slovakia accepting deposits from physical persons are obliged to contribute to this fund. Regulations regarding the deposit protection scheme, of course, have been changing over time.

However, in the second half of the 1990s it became clear that a more radical restructuring of the banking sector is necessary, including new forms of privatiza-

tion. NBS played an important role in planning and performing the pre-privatization measures (Tkáčová 2001).

Commercial Banking Sector In Slovakia During 1990s

From a quantitative point of view, the dynamics of the commercial banking sector was significant. The number of commercial banks increased continuously (although 3 banks were deprived license in 1996, new banks emerged), the number of employees, the volume and scope of operations increased as well. Before the start of the radical restructuring, leading to a dramatic increase in the foreign banks participation at the turn of millennium, the structure of the commercial banks sector was as follows (data for 1997):

Banks- residents in Slovakia (without or with some foreign capital participation)

25

Branches of foreign banks

4

Together

29 banks

+ representative offices of foreign banks

10

Out of 25 institutions registered in Slovakia, 21 banks were granted a universal banking license, 4 were specialized for specific activities (building savings banks, a guarantee bank and a consolidation bank). The equity capital of commercial banks was 13,8 bil. SKK in 1993 and grew to 30,6 bil. SKK in 1997. The foreign investors participation grew from 27% of the total volume of equity in 1993 to 52,2% in 1997. (Komínková and Múčková 1997, p.14, see also Appendix I).

Privatization of banks started under the former CSFR and 3 large state-owned banking institutions were included in the voucher privatization. New banks were established as private companies. After this first round of privatization, about 40% of Slovak banks' equity remained under the control of the state (mainly The Fund of National Property) and 60% was held by private owners.

However, there were significant problems in the Slovak banking sector (mainly concentrated in the 3 largest banks) that can be summarized as follows:

- Insufficient capital adequacy;

- Lack of long-term financial resources;
- High share of “bad loans”
- High share of state ownership, often connected with loans to connected parties and corruption.

Lack of long-term resources is connected with the structure of deposits (low share of long-term deposits) and its comparison with the loan term structure. The propensity for long-term savings was relatively low in Slovakia which was caused by internal and external socio-economic factors.

The most serious problem of Slovak commercial banking in the 1990s was an unfavorable loan portfolio, with a high share of bad loans. These bad loans were especially high in the three largest state-owned banks (VÚB, Slovenská sporiteľňa, Investičná a rozvojová banka). A portion of these bad loans was inherited from the centrally planned economy. However, new factors connected with the transformation process in the whole economy and some political decisions contributed to the increasing loan portfolio problem.

The first factor was the need to rapidly create a banking sector conforming to the needs of a transforming economy. The undersized banking sector was not able to handle the financing needs of many new business units. The second factor could be a lack of personnel with the necessary skills and experience to evaluate the riskiness of business projects and perform the prudent bank procedures. The business environment was unstable; prices, exchange rates, reliability of customers and suppliers were changing frequently.

Another reason could be that it was very easy to enter the banking sector. It was possible to establish a bank with relatively little basic capital. The ability of the bank's shareholders to secure the long-term success of the organization was not sufficiently examined.

In the very risky and uncertain situation of the early 1990s, guarantees on loans were very important. However, in reality their role was sometimes only formal. In many cases collateral was not marketable at all; guarantee contracts had many shortcomings. Moreover, the existing legal environment and court procedures created conditions favorable for debtors and detrimental for creditors (Kominkova and Múčková., 1997).

An even more important reason for increasing share of “bad loans” was the situation in the non-financial companies sector: insolvency of many companies just formally privatized during the voucher privatization, secondary inter-company indebtedness, and the general “debt-forgiveness” of enterprises (Kominkova and

Múčková, 1996). The profitability of many companies was lower than the interest paid on loans.

Due to the reasons mentioned a radical restructuring of the Slovak banking sector was inevitable. The restructuring process needed in the late 1990s should be aimed not only at the recovery of loan portfolio, but more generally at creating conditions for improving financial stability and forming commercial banks as prudent institutions, able to implement up-to date banking know-how and solve the crucial problem of the insufficiency of long-term financial sources. To summarize: the final aim of the banking sector restructuring should be to establish a sound, effective, competitive and creditworthy banking system.

However, the restructuring implemented in the late 1990s was not complex enough and not based on a long-term vision. The first step in the pre-privatization restructuring was aimed at solving problems in the two large state-owned banks: VUB and Slovenská Sporiteľňa and later on in Investičná a rozvojová banka (IRB). Two basic issues were to be solved:

1. Improving capital adequacy in the mentioned banks to achieve the standard 8%;
2. Reducing the level of “classified claims” (which was higher than 1/3 of the total volume of loans).

Two measures to achieve these objectives were used:

- The basic capital of the aforementioned banks was increased. The government used almost 25B SKK to increase the basic capital of the mentioned banks.
- A significant proportion of bad loans (classified claims) was shifted to other state controlled institutions, mainly to a consolidation bank. During the years 1999-2000 the 113,117B SKK of bad loans and guarantees were shifted from the three aforementioned banks to the Slovak Consolidation bank (Tkáčová, 2001).

Due to these measures the credit portfolio of the largest Slovak banks was significantly improved, their capital adequacy increased and the banks were prepared for the next round of privatization. As a basic form of this privatization an acquisition by foreign investors went underway. In 2001 Slovenská Sporiteľňa was acquired by the Austrian Erste Bank. The new owner of the Všeobecná úverová banka became an Italian group Intesa Bci (Tkáčová, 2001). The name of the bank and a majority of the local management remained. In 2002 the largest Hungarian bank OTP Bank Rt. acquired 98,94% of the shares of the former IRB. These acquisi-

tions led to a radical increase in the foreign capital share in the Slovak banking sector. The share of the foreign capital in the total equity of the Slovak banking sector increased from 31,6% in 1999 to more than 92% in 2003 (Preisinger.2004). These changes which occurred “at the turn of millennium” actually began a new era in the Slovak banking sector.

Although the restructuring measures during the late 1990s, and especially the subsequent dramatic entry of foreign capital, significantly improved the “health” and competitiveness of the Slovak banking sector, one comment on the restructuring process is required. An important aspect of the restructuring process in the banking sector is the relation “bank-client (debtor)”. The final success of the whole process depends also on restructuring the enterprise sector, making it more efficient and competitive. The restructuring of banking sector in the 1990s was oriented just on the “bank side” of the process. At that time large, either state-owned or just formally privatized companies prevailed in Slovak economy. The problem of their insolvency was not solved and even after further changes in the ownership structure, it didn’t disappear. However, the improvement of the quality of loan portfolios and the restructuring of banks, created conditions for the employment of financial resources in a new, effective way, which can be important for economic development in general, but also can significantly improve the cooperation between banks and their clients.

The restructuring process in the banking sector led to improvement in all primary banking indicators. The total assets of the banking sector increased, and credit risk was lower and didn’t endanger the capital stability of the sector. Conditions for the long-term sustainable growth of the sector were established. (Preisinger, 2004)

The Impact Of Foreign Investors And Eu Membership On The Slovak Banking Sector

Two basic factors influenced the structure and behavior of Slovakia’s banking sector during the last decade:

- The dominant position of foreign investors in the banking sector
- Slovakia’s membership in the European Union

Both factors are actually interrelated.

We can say that Slovakia's banking sector has been from the turn of millennium dominated by foreign banks. This can be made clear from all basic indicators: the share of foreign owned banks in the total number of banks in Slovakia, the share of foreign capital in the total banking sector equity, etc. Starting from 2002 the share of foreign capital in the total equity of the banking sector in Slovakia has always been above 90% - although fluctuating a little. Before euro currency adoption in 2008 it was more than 100%. In 2012 the total amount of equity of commercial banks in Slovakia was €2,701,4M. Out of this just €153.9M was the capital of banks without foreign ownership. The rest was the capital of foreign banks that are residents in Slovakia or of the branches of foreign banks doing business in Slovakia. (NBS, 2012). For more details see Appendix I.

From 16 banks registered in Slovakia (residents) in 2012 just two small banks were domestically owned, all other were foreign controlled. Additionally, there were 13 branches of foreign banks doing banking business in Slovakia. The list of banks and their owners can be found in Appendix II. Probably, the dominant position of foreign banks in Slovakia is the most evident in comparison with other CEEs (Merő, K. and Endrész Valentinyi, 2003).

The positive effects of foreign banks on the modernization of the banking business, improving credit policy, introducing new products and services and generally improving the international competitiveness of the banking sector are well-known from all post-communist countries. Amendments to the Banking Act, which came into force in 2002, moved the legal framework of Slovak banking closer to EU standards; among the key improvements were the introduction of consolidated supervision to forestall any schemes to spin off riskier activities to affiliated nonbanks subject to less oversight. Accounting rules have been upgraded substantially.

Some important problems remain: much like banks in other countries that experienced the economic shock of bank restructuring and that are moving toward hard budget constraints in the sector, Slovak credit institutions reacted by becoming (very) cautious lenders. Given the banking sector's lead in reforms, the enforcement of hard budget constraints has not yet fully spread to the real sector. Non-performing loans, while having declined considerably, have remained relatively high (about 8% of total loans at end-September 2004). So, banks adjusted their intermediation role and reshuffled their portfolio toward lower-risk investments, e.g. government securities and NBS securities.

The fact that the commercial banking sector in Slovakia has actually been controlled by foreign capital brought many benefits to Slovakia's financial sector by improving the stability of this sector and has also benefitted whole economy. For-

foreign investors introduced new banking products and services (e.g. asset management schemes), new types of loans and especially new know-how and ethics which contributed to increasing the quality of personnel and improvements in bank-client relations.

Foreign banks usually benefit from the advantages of having access to more advanced information technology and better expertise in the field than their domestic counterparts. However, while speaking about domestic counterparts in Slovakia, these competitors are actually foreign banks as well (maybe foreign banks from other countries, with different background and experience). Purely Slovak counterparts don't actually exist. The same is true regarding the spill-over of modern banking methods and skills in the sector. Due to intensive competition between banks such a spillover exists, but between foreign controlled banks themselves. For the domestic business sector such a spillover can happen just when former employees of banks move to domestic non-banking institutions where they bring and use the learnt and practically verified up-to-date knowledge and skills.

Sometimes in literature, a so called cream-skimming effect of foreign banks is mentioned as a disadvantage for domestic banks. In Slovakia, there were cases when foreign banks tried to acquire the most cost-efficient local institutions. However, the size of the bank's market, its image, etc. was also important. There are differences in cost-efficiency and profitability of individual commercial banks, (some of them are due to inherited factors), but most of them stem from the differences in strategies applied, management systems of particular banks and probably also the financial situation of the parent institution or the whole international banking group. However, these differences exist within the foreign controlled banking system itself.

Another disadvantage of the foreign banks dominance for host countries, often mentioned in the literature, is that foreign owners have not a sufficient idea of how the domestic economies work, they do not understand the peculiarities of the local legal system, psychology of clients, etc. This problem can be solved by keeping the staff of acquired local banks (which was important mainly during the first years) or sometimes hiring people from local industry or other local institutions. On the other hand, foreign banks may be less vulnerable to political pressures and less inclined to lend funds to connected parties, which in the past often led to bad loans.

In theoretical literature we find various motives for foreign banks to go to CE countries (Mynian 2012; Bonin-Wachtel 2005; Lanine-Vennet 2005). Among factors supporting foreign banks entry into CEE countries we can mention: the

previous development of the financial system (and especially the banking sector), the legal system and financial and political stability in a country, differentials in the rate of economic growth between the home and host country, and the distance between the bank group headquarters and host country. Similar factors also influence the form of foreign banks entry – although these forms also depend highly on a particular bank's global strategy.

For Slovakia, the mentioned motivating factors which were relevant are: Slovakia inherited a relatively developed banking system from the former Czechoslovakia, political conditions were favorable - government supported this form of privatization, geographical position of the county was favorable and although the level of non-financial corporations FDI in Slovakia was lower at that time than in other V-4 countries, the foreign banks expected a significant increase in FDI (in manufacturing, services, etc.) in the future. Their entry into the Slovak financial sector was also a way to prepare for these changes. In general we can say that the development of the banking sector during the first decade of the 21st century (with the dominant position of foreign banks) formed one of the comparative advantages of the country considered in FDI decisions by nonfinancial companies.

On May 1st, 2004 the EU experienced the largest enlargement since its creation. Slovakia entered the European Union as one of the 10 new member states. It had to adjust to the legislation of the EU, including the norms regulating the financial sector. Slovakia's financial system strategy should be formed in harmonization with the EU financial system development. For banks in Slovakia such an orientation was quite natural because most foreign owners of banks in the SR were from EU countries.

The financial system of the EU is often described in the literature as a bank-based system, owing to the prominent role traditionally played by banks in the major economies in the EU (Allen – Bartiloro- Kowalewski, 2006). In the years 1995–2004 the banking sector of the EU grew rapidly reflecting the financial deepening and integration of the EU financial system. In the same period the average growth of banks' assets outpaced GDP growth. The ratio of banks' assets as a percentage of GDP was in the EU15 more than 400%. In the new member states the role of financial intermediation was significantly lower and the ratio of bank's assets as a percentage of GDP was under 100%. However, in Slovakia this ratio was relatively higher and in 2004 it was 88%. Slovakia actually used to be (and still is) a country with bank dominated financial system. In 2005 the banking sector accounted for 84% of the total assets of the financial sector (NBS 2005).

The development of the banking sector in Slovakia during the years 2005-2007 (after EU entry) was positive. EU membership was one of the factors that created

a favorable environment for successful development of the Slovak financial sector. Internal factors were also important. Strong economic growth and an improving financial situation in certain economic sectors resulted in a greater volume of client loans. The positive trends were apparent in the increase in lending in almost all sectors. The growth was influenced above all by household lending. There was also a significant rise in the volume of lending to the corporate sector and non-banking financial companies. Although funds from foreign banks continued to increase, it was important for the stability of the system that the majority of banks had funds from domestic clients which were sufficient to finance the growth of loans at their disposal (NBS 2005,2006,2007). The profitability of banks grew, mainly in large banks.

During the years mentioned, Slovakia (and its financial institutions) were preparing for the introduction of the euro-currency. Different Slovak authorities and different financial institutions (mainly the central bank) were involved in this process. During the period analyzed, in cooperation with the European Commission, European Parliament and the European Central Bank published several reports on the practical preparation for the enlargement of the euro-area. In the eighth report (2008) the European Commission concluded that Slovakia's preparation was well advanced and the introduction of the euro could be smooth. The National Bank of Slovakia started to distribute euro coins and banknotes to commercial banks in September 2008. In order to address consumers' fears of price increases around the changeover, Slovakia implemented a whole set of measures (double prices immediately before and after the change (Ethical code of businesses declaring that prices will not be increased just due to a currency change etc).

The majority of the Slovak population accepted euro positively and for banks it was very advantageous that before the currency reform a massive increase in bank deposits occurred (people invested their money in bank accounts to minimize technical problems with the currency change). Paradoxically enough, at the time when western banks were facing serious liquidity problems, liquidity of Slovak banks was higher than before.

The Impact Of The Single European Currency Adoption On The Banking Sector In Slovakia

From January 1, 2009 adapting the euro currency in Slovakia became a reality. Slovakia was the first V-4 country that joined the Euro-area. The process of transition to the single European currency was smooth and actually without problems. Positive evaluation of the euro adoption prevailed, mainly in the business sector

(foreign investors regard the common currency as an important comparative advantage of Slovakia as a location for investment), and positive evaluations prevailed also in political institutions and among the population. During the first months of the global financial crisis the common currency helped to soften the impact of the crisis and supported financial stability. The euro as a stronger and more stable currency could protect our economy against financial risks. However, it is difficult to separate the impact of the euro's introduction from the impact of the start of the global financial crisis. Both processes occurred almost simultaneously.

From the point of view of the banking sector, the transition to a new currency is a more complex process. On the one hand, the central bank (NBS) played the leading role in the preparation process and mastered this task successfully. Commercial banks were involved in the preparation process as well and some measures were rather costly. On the other hand, from a deeper analysis of the causes of the crisis, some lessons for the financial system in general and banking sector as the key component of the financial system in Slovakia especially, can be learnt.

For Slovakia, as a country with high bank-real sector interdependency, developments in the real economy are of crucial importance for the future of the banking sector. Some of these tendencies are more general, relevant also for countries that are not euro area members. Some of them are more connected with euro introduction.

Due to some measures in the preparation process that were costly and due to a decline in revenues from exchange operations, profitability of commercial banks in 2009 declined by more than 50%. In this decline, of course, the development in the real economy and insolvency of many clients, is also reflected. Banks had to create higher reserves to cover losses from defaulted loans.

Membership in the euro area also radically changed the monetary policy. The Basic tasks of the monetary policy were transferred to the European Central Bank (ECB). Up to the end of 2008 there was a separate interbank market in Slovakia (rather well functioning) with the basic rate BRIBOR. After the euro area entry this market ceased to exist and Slovak banks have to raise short-term interbank loans at the European interbank market with EURIBOR as the basic rate. This rate is derived from the basic interest rate on refinancing operations which is set by the ECB. For EURIBOR lower volatility is more typical than for the former BRIBOR which can lead to a lower credit risk.

As a negative impact of the euro adoption in the context of the global financial crisis, a decline in the banks' profitability can be mentioned as well as lower in-

terest revenues from the inter-bank operations. Revenues of Slovak banks from exchange operations declined in 2009 (in comparison with the previous year) by 77% (Kiseľáková 2010).

The Impact Of The Global Financial Crisis On The Banking Sector In Slovakia

The world-wide financial crisis that broke out at the outset of the second half of 2007 was causing major global turbulences during the whole of 2008 and became so severe at the turn of the year that it began to threaten the very existence of the global financial system. Compared to other developed countries, the impact of this phase of the financial crisis on the Slovak banking sector was relatively low. One of the reasons to this relatively moderate impact on the Slovak banking sector was that the Slovak banking sector was predominantly linked with the domestic economy and the share of banks' activities related to foreign countries was negligible. Slovak banks minimized their exposure against many innovative instruments of the present-day world of finance that have proven to be the main cause of the crisis spread (NBS 2008).

However, the next year, when the global financial crisis also led to a global recession, with a heavy impact on Slovakia, the situation was different. As mentioned above, the banking sector in Slovakia was (and still is) intensively linked with the domestic real economy. A recession in the Slovak economy was a serious problem for the banking sector. Slovakia is a highly opened economy and the decline in demand from Germany and surrounding countries led to a deterioration of the economic situation in Slovakia as well. Economic growth fell by 4,9%, exports shrunk by 15.9%. The unemployment rate grew and risk that mortgage loans will not be paid on time increased.

To cover potential credit losses, several banks during the year 2009 increased their own funds. This measure led to a higher capital adequacy, but on the other hand, dividends were not paid or were lower. The behavior of banks became more conservative and this was particularly true in the asset-side operations. Lending activities of banks focused mainly on loans with high repayment probability. In the area of corporate financing, banks concentrated on less risky sectors and enterprises. Another important factor in the restriction of corporate lending was the decline in demand from enterprises, due to the declining number of investment opportunities. On the other hand, banks invested more in a relatively safer assets ,e.g. government bonds. Loans to households were also regarded as less risky than corporate lending and these loans grew in 2009.

During the crisis, differences in effectiveness of individual banks became more apparent than in the past. These differences could be seen, for example, in the quality of loan portfolios or the differences in the financial condition of large vs. small banks. Although most banks recorded a drop of interest income from the corporate sector, large banks maintained their interest income from the household sector. Overall, the banking sector profits in 2009 included sizeable differences between individual banks. Differences in financial condition were typical not only for subsidiaries or branches of foreign banks in Slovakia, but also for foreign parent companies of the bank, where a financial injection from the (home country) government was needed.

The financial situation of a bank also depended on the type of real economy sector with which the bank had been intensively connected. Credit risk grew mainly in export-oriented sectors and in the transportation sector. Over the course of the year, banks' exposure to the property market emerged as a significant risk because due to a drop in demand and prices it was difficult for property developers to repay loans.

The situation in the household sector worsened as well, but the effect of the crisis was more moderate. Especially loans to lower income groups represented for banks' high credit risk, predominantly concentrated in consumer loans and current account overdrafts, where the default ratio was relatively high (NBS 2009).

In 2010, some positive trends in the financial market developments and economic growth in Slovakia and abroad appeared and these trends had a significant impact on the situation in the Slovakia's banking sector. The global economy recorded a recovery boosted by monetary and fiscal policies, and international trade grew, but significant differences between countries remained. Emerging countries of Asia and Latin America became the drivers of global economic growth.

For Slovakia, 2010 was a positive year. Economic growth recovered (GDP growth was 4.4%), manufacturing grew by 13.3%, mainly due to the rapid growth in the production of automobiles, electronics and machinery. For the Slovak financial sector this year was also relatively positive. Most sectors of the financial system recorded increased profitability.

Banks provided more funding for the real economy, mainly through housing loans. Banks in Slovakia strengthened their financial position. The profitability of the banking sector as a whole doubled in comparison with the previous year (NBS 2010). The profitability growth was driven mainly by increasing income from retail operations. Revenues from investment in debt securities also increased, largely due to the increase in their volume. Banks also increased the volume of

their own funds to cover unexpected losses. In general, risk management systems improved significantly in the majority of banks. Although it seemed that the worst of the crisis was over, businesses, including banks, regarded the recovery as a fragile one and were very cautious. The amount of corporate financing provided by the domestic banking sector remained relatively flat in 2010 and only to a small degree reflected the economic recovery. However, there were substantial differences between companies regarding their borrowing potential. The largest rise in borrowing was seen in those sectors where the crisis-induced impairment of loans was less pronounced. The amount of lending to the sectors harder hit by the crisis continued to decline.

Over the past two years, domestic financial institutions have seen their share of total corporate lending decline, and at the same time the financing of corporations from abroad increased (which can be reflected also in increasing the intra-company lending).

For the stability of the banking sector it is important that the amount of households' financial assets deposited in banks continues to exceed the amount of loans that banks extend to households. Banks tried to support a shift towards deposits with longer-term maturity by means of interest rates changes or by introducing new financial products, connecting traditional deposit operations with financial investment (NBS,2010).

One can say that during the crisis a special modification of the banks' strategy has been developed, with some features common to all banks (and most countries) and some bank specific and country specific features. The basic objective of this strategy modification has been to take into account the new dynamics of the financial world development and global economy development as a whole, to cope with increasing uncertainty in their environment and to improve (or sustain) their global competitiveness under present conditions. Common features, applied by all banks, include mainly:

- Cost reduction measures.
- Improving risk management methods and involving them in the core of the strategy.
- Keeping the position of a “global player” and adjusting organizational and regional structure to changing environment (Of course, last feature is typical for multinational banks. However, in Slovakia, this type of foreign parent companies prevails).

Headquarters of different banks active in Slovakia, can choose different orientations to achieve the synergic effect within the whole bank group. There can be differences in relations to host country governments, in a degree of supporting a positive macroeconomic and social development in host countries, in the orientation on different types of clients, etc. There can be also differences in the degree to which “cross-financing” within the bank group is regarded as acceptable.

Recently, an interesting paper has been published by three Czech and Slovak authors (Taušer--Sroka--Žamborský 2013). The paper analyses the behavior of foreign controlled banks under conditions of the financial crisis in two countries – Czech Republic and Slovakia. The behavior of subsidiaries of four multinational banking groups (Raiffeisen Bank International, Erste Group, Volksbank International and UniCredit) in both countries is examined. The question to be answered is whether the multinational banks pursue a coherent strategy for the whole region, to cope with the risks connected with the crisis, or focus on finding local solutions. The authors come to the conclusion that all banks followed the strategic directives of their parent companies. For Slovakia this means:

- Tatra Banka (belonging to the Raiffeisen group) implemented a prudent, non-expansionary risk strategy, focused on stabilization, even at the cost of a moderate decrease in some profitability indicators;
- Slovenská sporiteľňa (Erste Group) focused on SMEs within corporate banking and regarded retail as important as well. Its aim was to maintain and strengthen good customer relations;
- Volksbank Slovakia emphasized relations with small business, but was careful in granting loans to newly established companies;
- UniCredit Bank Slovakia attempted to achieve stability by focusing on anti-cyclic industries.

However, even if the same basic strategy of the banks within a group was applied, the financial indicators were different for subsidiaries in different countries. Local conditions probably significantly influenced the results. Another specific factor is the financial position of the parent company. If there are serious problems at the headquarter level, the parent company can decide to sell the subsidiary (to other foreign investor). The case study supporting this analysis started exactly in this way.

Some tendencies that appeared in the banking sector during the crisis are relevant also today – due to still remaining uncertainties in the macroeconomic and international environment.

Recent Situation

The economic environment of the banking sector remained uncertain also during the last two years. Although financial markets calmed, they did so mainly in response to measures taken by the ECB, rather than due to expectations of an improvement in the macroeconomic situation. Risks associated with euro area periphery economies were acute mainly in 2011, but, on the other hand, economic growth was weak due to low competitiveness.

Slovakia's rate of growth declined. A positive phenomenon can be that Slovak government bond prices completed their recovery from the turbulent autumn of 2011, thus providing a boost to the domestic financial sector. The drivers of the growth of the Slovak financial sector were not only financial markets, but mainly favorable developments in the household sector, as households increased both their borrowing and their investments in the financial sector. Increase in lending to the households sector was most marked in housing loans, which account for the majority of the household loan portfolio, but consumer credit also rose. On the other hand, a different situation was observed in the corporate sector. As a result of weakening demand for loans and tight credit standards, the outstanding amount of corporate loans initially recorded lower growth and then, began to decrease. The pace of their decline in the second half of the year 2012 was similar to the levels seen at the end of 2009 (NBS 2012).

The aggregate net profit of the banking sector in 2012, according to data reported by banks, declined by almost one-third year-over-year. This can be largely explained, on the one hand, by the imposition of an extraordinary banking levy and, on the other hand, by an increase in credit risk costs in the loan and guarantee portfolio. Bank profits were further squeezed by the continuing decline in interest rate margins.

The banking sector's capital adequacy ratio (CAR) increased in 2012 to its highest level since 2005. It is 16,2% at present (NBS 2013). This was largely because a significant share of the sector's 2011 profit was retained, and also due to a direct increase in own funds. The Slovak banking sector reported adequate self-sufficiency in terms of solvency, especially in comparison with banking sectors of

other countries. It is positive that most banks ensured sufficient provisions for non-performing loans despite an increase in the amount of such loans.

The banking sector continues to have an ample liquidity cushion and is adequately self-sufficient in regard to funding. Consequently, the sector is lessening its exposure to the possibility of an increase in external funding costs resulting from a renewed escalation of Europe's sovereign debt crisis.

This is a positive tendency from the point-of-view of the financial sector stability. The financial sector stability of Slovakia was rather positively evaluated by international ratings. According to the recent Financial Development Report (WEF, 2012) Slovakia is in 23rd place (out of 62 evaluated countries) based on the financial stability criterion and based on the banking system stability criterion in 17th place. High ratings were also given for retail access to loans (19th place) and Central bank transparency (5th place).

As the banking sector in Slovakia is significantly dominated by foreign banks and the space for national banks supervision (still in competency of the NBS) is rather limited, the project of *The European Banking Union* is very important for Slovakia. Actually this project is important for all Central and East European countries, where banks headquartered in Western Europe play a central role. All three elements of the full banking union - common supervision, resolution and safety net with backstops –are required for its effectiveness. Banks generally support the banking union project and argue for it to be as comprehensive as possible. However, there are differences in views of different countries regarding the allocation of tasks between local (national) supervisors and the ECB and some procedural rules.

As for Slovakia, the interplay between ECB and local authority in the area of macro-prudential policy is important. Local bodies better understand the real economy and sometimes are able to more effectively assess the risk. For Slovakia as well, it is important that the approval of intra-group (within the bank group) financial support should be in the competence of national supervisors. As the governor of the NBS pointed out (Makúch 2013) “European Stabilization Mechanism has been established primarily to provide support to Member states and not banks, the contribution key should be re-designed so that the contributions by Member States are linked to the risks embodied in their financial systems.... It also has to be ensured that in the setting-up of a European Resolution Scheme, the use of any European funds do not raise issues of moral hazard and/or unjustified mutualisation of losses stemming from the past.”

Conclusion

During the last two decades banking sector in Slovakia transformed from a rigid, inefficient system into a modern, flexible network of banks (although still with a dominant position of a few large banks), able to practically apply up-to-date banking techniques and skills and provide up-to date services to their clients. The banking sector has always been the dominant part of the financial intermediaries system in Slovakia and this role of commercial banks is true also today.

The key role in the modernization of the sector and improving its competitiveness has been played by foreign investors. Some foreign owned banks existed in Slovakia even at the beginning of the transformation process. However, the most intensive entry of foreign banks into Slovakia's banking sector occurred at the turn of millennium when the largest, state controlled banks were acquired by foreign investors. We can say that Slovakia's banking sector is actually foreign capital controlled. The share of foreign capital in the total equity of commercial banks is 94.4% (as for July 2013). The activities of domestic banks are limited to some special fields (guarantees to SMEs, Exim bank).

Foreign capital dominance and Slovakia's EU membership are interrelated. Foreign owners of banks in Slovakia are interested in EU membership (and euro-area membership) of the country and, on the other hand, integration into the European Union provides impulses for further growth of banks and globalization of their activities. However, the single European currency adoption in Slovakia had also some negative implications for banks. There were additional costs connected with the currency change and revenues from exchange operations of banks declined. This was negatively reflected in the banks' profitability.

Almost simultaneously with the euro adoption in Slovakia, the global financial crisis started. The immediate impact of the crisis on Slovakia's banking sector was not so profound as in other countries. The basic reason is that banks in Slovakia are financed mainly from domestic resources (deposits of local clients) is that, their liquidity in 2008 was high and their dependence on international financial markets transactions was relatively low. However, the recession in Slovakia (culminating in 2009) had a significant impact on the banking sector. The high openness of Slovakia's economy makes the country very vulnerable to downturns in Western Europe. The banking sector in Slovakia has had very close links with domestic enterprises. This was a disadvantage for banks during the downturn in Slovakia's economy. The profits of banks in 2009 declined by more than 50%. In their lending activities banks began to behave more conservatively. They paid more attention to the actual repayment of loans, new loans were concentrated on less risky sectors and organizations, and financing conditions were tightened. In

crisis years, the differences between banks (regarding the riskiness of their credit portfolios and loan default ratio) became more apparent. This was reflected in the level of losses or profits.

Despite some recovery in the real economy during the next years, basic features of the “conservative approach” in lending strategy are relevant also today. Future development of the banking sector will depend primarily on the real economy development in Slovakia and Europe in general. Most banks in Slovakia have a relatively high loss-absorption capacity due to their high capital ratio and solvency. This can be the basis for the banking sector stability.

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Appendix I.**Share of foreign capital in total equity of commercial banks in Slovakia
(1993-2008 in SKK mil.)**

Year	1993	1994	1995	1996	1997	1998	1999	2000	2001
Total equity of commercial banks	13411	14707	24546	29336	30898,4	34426,9	52837	53998	53154
Share of foreign capital (%)	27	34	44,6	52,4	52,2	53,6	31,6	34	71

Year	2002	2003	2004	2005	2006	2007	2008	
Total equity of commercial banks	41316	43287	44278	44364,6	44416,4	48708	50501,2	
Share of foreign capital (%)	92	94,3	92,6	92,5	92,6	94,5	100,3	

Years 2009-2012 (after euro adoption) in € mil.

Year	2009	2010	2011	2012
Total equity of commercial banks	2074,3	2024,5	2477,0	2701,4
Share of foreign capital (%)	90,8	90,6	92,4	94,3

Source: NBS, Development of the banking sector, for corresponding years

Home countries of the most important foreign investors (as for December 2012)

Country	Share in total banking sector foreign investment
Austria	26,6 %
Czech Republic	20,7%
Luxemburg	18%
Cyprus	13%
Belgium	11,6%
Hungary	3,4%

Source: NBS, 2012

Appendix II.

LIST OF BANKS IN SLOVAKIA (as of July 2013)

Central banks

National bank of Slovakia
Eximbanka SR

Commercial banks (residents in SR) and their ownership

Československá obchodná banka (subsidiary of KBC Group, NV)
ČSOB stavebná sporiteľňa
OTP banka Slovensko (member of OTP Bank, Hungary)
Poštová banka
Prima banka (member of Penta Group)
Privatbanka (member of Penta)
Prvá stavebná sporiteľňa
Raiffeisen Bank
Slovenská sporiteľňa (member of Erste Bank group)
Slovenská záručná a rozvojová banka (state owned)
Tatra banka (member of Raiffeisen Group)
UniCredit Bank (member of UniCredit)
Sberbank Slovensko (member of Sberbank)
Všeobecná úverová banka (member of Intesa Sanpaolo)
Wüstenrot stavebná sporiteľňa

Branch offices of foreign banks

Banco Banit Mais, SA
BKS Bank, AG
Calyon (member of Calyon Credit Agricole)
Citibank Europe, plc. (member of Citigroup)
Commerzbank AG
Fio Banka
ING Bank N.V. (member of ING Group)
J&T Banka (member of J&T Group)
Komerční banka Bratislava
mBank (owned by BRE Bank, member of Commerzbank, AG)
Oberbank AG
Royal Bank of Scotland
ZUNO (member of Raiffeisen Zentralbank)

6. Distance In International Business Research: Are We Really Making Any Progress?

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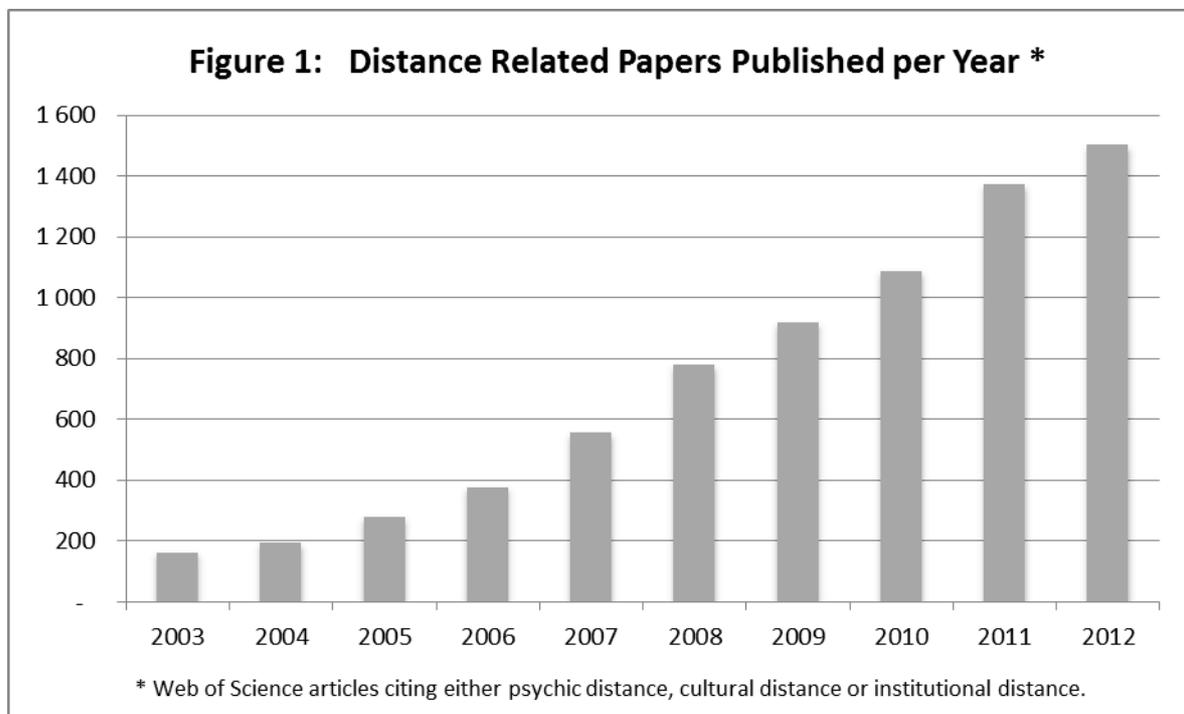
Introduction

Within the realm of international business research (IB) the importance of the distance construct has been echoed by numerous commentators over the past two decades. For example, Cho and Padmanabhan (2005: 309) conclude that "almost . . . no international business study can be complete unless there is an explicit variable controlling for cultural distance". Similarly, Zaheer, Schomaker, and Nachum (2012: 19) claim that "essentially, international management is [the] management of distance". They argue that distance is the defining characteristic that distinguishes IB from the discipline-aligned forms of research. Measuring the pervasiveness and popularity of the construct in another ways, the incidence of various forms of distance being included in international business research has more than doubling in the Journal of International Business Studies (JIBS) between 2005 and 2010 (Em, 2011). Looking slightly more broadly, in the Web of Science database, more than 1,500 peer-reviewed articles published in 2012 cited some form of distance (Figure 1). Indeed, the two most highly cited articles in the history of JIBS are both inextricably related to the concept of distance. The most cited JIBS article - Johanson and Vahlne (1977) - is renowned for resurrecting, defining and popularizing the concept of psychic distance; and the second most cited JIBS article - Kogut and Singh (1988) - is famous for the creation of the now ubiquitous 'national cultural distance index'. As a result, the pervasiveness of the distance concept is hard to dispute; however, just because a concept is pervasive does not mean it is necessarily without controversy, and it is no guarantee that we are making progress in the way we deal with it.

In parallel to the legions of authors who have embraced and incorporated some aspect of distance into their research, an equally vigorous, though numerically smaller legion of authors have lamented about how their colleagues have conceptualized, measured and incorporated the more abstract forms of distance into their research (Harzing, 2003, Shenkar, 2001, Tung & Verbeke, 2010, Zaheer, *et al.*, 2012). This chapter joins that stream of literature in terms of being a critique of how the measurement of distance has been practiced, but with a subtly difference twist. First of all, rather than just repeat criticisms already eloquently explained

by others, this chapter focuses on what subsequent progress has been made in each area of criticism, and what the implications are for future research.

In addition, this chapter is intended to highlight one specific issue. Many commentators (e.g. Evans & Mavondo, 2002, Sousa & Bradley, 2006) claim that the superior approach to measuring the more abstract forms of distance is in terms of individual-level perceptions, rather than in terms of exogenous national-level metrics. However given the difficulties inherent in measuring *a priori* perceptions of key decision makers, it is critical that we have theoretical frameworks to explain what drives these perceptions, and are able to understand when, how and why they diverge from the more widely available national-level factors. Without such an understanding, our ability to appropriately model and incorporate the distance construct into our research will be severely hampered.



In the remainder of this chapter, the history of the distance construct as it has been used in IB research is briefly summarized. Then each of the major criticisms of the literature, as drawn from the major commentators, are addressed in turn with particular focus on what progress has been made in correcting the situation, and what are the implications for future research. The final criticism raised brings us to an extended, and as yet unresolved, debate within the field - the use of exogenous national-level measures of distance versus individual-level measures of perceptions of distance. Here we focus on a particular implication of this debate:

how and why these two approaches may yield different results, and what the implications are for future research.

A Brief History of the Distance Construct in IB Research

Arguably the earliest application of the distance construct in IB research was as a surrogate measure of transportation costs in bilateral trade flow studies. In conjunction with the size of the respective markets, usually measured in terms of GDP, geographic distance formed the cornerstone of the now famous gravity equation (see Anderson, 1979 for a more detailed explanation of these models). Anderson (1979: 106) describes it as "probably the most successful empirical trade device of the last twenty-five years". However, even in the earliest years of this literature, Beckerman (1956) and Linnemann (1966) were suggesting that in addition to transportation costs, cross-national differences may be influencing trade flows; and used distance as a metaphor for the magnitude of these differences. Indeed, Beckerman (1956) is generally credited with coining the term 'psychic distance' to describe this effect.

Unfortunately, despite the early recognition of these factors, the more abstract forms of distance did not gain significant attention in the IB literature until Johanson and Vahlne (1977) included Beckerman's psychic distance as one of the key constructs in their internationalization process model. They argued that psychic distance, arising from differences in language, education and industrial development, creates uncertainty about foreign markets; which in turn may influence a firm's choice of markets, and its degree of commitment to those markets. However, despite the importance and emphasis that Johanson and Vahlne (1977) gave to the construct, the incorporation of more abstract forms of distance did not really gain prominence in the empirical international business literature until Kogut and Singh (1988) created their now ubiquitous 'national culture distance' scale by collapsing four of Hofstede (1980) cultural dimensions into a formative index. It is from that point onwards that the inclusion of cultural and/or psychic distance in research agendas began to grow rapidly. In particular, over the past decade the number of Web of Science articles citing cultural, psychic or institutional distance has grown 25% per year. Moreover, during this period, the Kogut and Singh index quickly became the dominant instrument for measuring abstract forms of distance – be it cultural, psychic or instrumental distance (e.g. Harzing, 2003, Yiu & Makimo, 2002, Zhao, Luo, & Suh, 2004).

In the mid 2000's, in response to mounting criticism of the Kogut and Singh index (e.g. Shenkar, 2001), a number of alternative distance scales began to emerge – most notably the GLOBE effort (House, Hanges, Dorfman, & Gupta, 2004) to create a revised set of cultural dimensions, and several efforts to broaden the range of distance dimensions beyond just culture (Berry, Guillen, & Zhou, 2010, Brewer, 2007, Dow & Karunaratna, 2006). A third stream of researchers (e.g. Brouthers, 2002, Dow, 2000, Evans & Mavondo, 2002, Håkanson & Ambos, 2010, Luo, Shenkar, & Nyaw, 2001, Sousa & Bradley, 2005) also began to explore more direct approaches of surveying people's perceptions of distance. However, despite the merits of all these efforts, to date the Kogut and Singh index has continued to dominate the field in terms of usage (Em, 2011).

In terms of the business issues to which the distance construct has been applied, it covers an extremely broad range, varying from predicting export market selection (Ellis, 2008), trade flows (Dow & Karunaratna, 2006), FDI flows (Davidson, 1980), entry mode choice (Hennart & Larimo, 1998), establishment mode choice (Brouthers & Brouthers, 2000), adaptation in foreign markets (Dow, 2001), and performance in foreign markets (Evans & Mavondo, 2002) to the use of HRM practices in international settings (Boyacigiller, 1990). In light of the depth and breadth of the settings in which the distance construct has been applied, it is not surprising that commentators such as Zaheer, *et al.* (2012: 18) have referred to it as “the much-loved construct”. Nevertheless, as argued earlier, this extremely broad and deep application of the construct does not guarantee that it is without controversy.

The Criticisms of How Distance is Operationalized in IB Research

Subsequent to Johanson and Vahlne (1977) and Kogut and Singh (1988), one of the most significant turning points in the conceptualization and application of distance in IB research is the seminal article by Shenkar (2001) for which he won the JIBS decade award. In this article, Shenkar laid out eight main criticisms of the way in which distance research has typically been conducted; several of which have been subsequently echoed, endorsed and enhanced by other commentators (e.g. Harzing, 2003, Tung & Verbeke, 2010, Zaheer, *et al.*, 2012). For the remainder of this chapter these critiques, and particularly the seminal paper by Shenkar (2001) will form the basis of our review. For each of the major criticisms, the subsequent research and corrective action will be discussed, and implications for future research will be addressed.

Neglecting the Underlying Mechanisms

The first major criticism of the field is not one originally raised by Shenkar (2001), but rather by Zaheer, *et al.* (2012) in their tribute to Shenkar's earlier work. They argue (2012: 19) that one of the major problems underlying the entire field is that "most distance constructs have been used in a fairly superficial manner in research, without much attention paid to exactly what mechanisms are at play in the influence of distance, or to its underlying conceptualization". In essence, too often researchers rush to apply the concept of distance to their work and neglect to carefully consider the underlying theories of why distance matters in the first place.

The empirical literature that explicitly employs 'cultural distance' as an explanatory variable seems particularly prone to this weakness. The vast majority of this research simply cites previous empirical work that has used the same metric and is entirely silent on the underlying mechanisms. Most often the implicit assumption in these works is that cultural distance is a source of transaction costs as argued by Kogut and Singh (1988). This view is reinforced by Zhao, *et al.* (2004) and Tihanyi, Griffith, and Russell (2005) who in their meta-analyses categorize cultural distance as an indicator of 'internal uncertainty' within a transaction cost framework and use this literature as evidence of the importance of internal uncertainty.

Within the empirical literature that explicitly cites 'psychic distance' (e.g. Ellis, 2008) the situation is substantially simpler and more explicit, thanks to the early work of Uppsala researchers. Johanson and Wiedersheim-Paul (1975: 308) lay down a reasonably concise definition of psychic distance:

"The sum of factors preventing or disturbing the flow of information between firm and market. Examples of such factors are differences in language, culture, political systems, level of education, level of industrial development, etc."

This definition has been frequently criticised (e.g. Evans & Mavondo, 2002) for not emphasizing the perceptual nature of psychic distance, a curious omission given that even Beckerman's original 1956 paper emphasized the perceptions of individuals; however it does have one very strong positive aspect in that it clearly identifies the critical mechanism – factors which disturb the flow of information. For this segment of the literature the theoretical underpinnings tend to be more explicit, but unfortunately it has tended to be less than a quarter of the total literature.

The third and final theoretical perspective with respect to the role of abstract forms of distance in IB research is institutional theory. The concept of institutional distance was first suggested by Kostova (1999) and initially showed much promise in providing a new perspective on the debate (Xu & Shenkar, 2002). In particular, institutional theory predicts that a firm's desire to attain 'legitimacy' is a key mechanism driving various aspects of MNE behaviour such as market selection and entry mode. Unfortunately, the sad reality is that subsequent applications of institutional distance have tended to make identical predictions as the cultural distance and psychic distance perspectives, as well as frequently using the same indicators. As a result, to date, the results from an institutional distance perspective are essentially indistinguishable from those of the psychic distance and cultural distance perspectives.

In terms of implications for future research, the first step is to encourage researchers to take heed of the calls of Harzing (2003), Zaheer, *et al.* (2012) and others in being more explicit about what are the underlying mechanisms that the various forms of distance are intended to represent. Are they talking about difficulties in people communicating with and understanding one another, is it about the desire of people and organizations gaining legitimacy in the eyes of those around them, or is it something else? In essence before we even start measuring any forms of distance, we need to ask ourselves 'why are these differences important?' On top of that, more work needs to be done to help discriminate between these three perspectives (i.e. transaction costs, the need for legitimacy and barriers to information flows). Institutional distance in particular was initially embraced as a fresh new perspective, but unless it can attain some level of discriminant validity, and generate new predictions about firm behaviour, it will not advance our understanding of international business. This may require more creative research designs, and possibly more qualitative and/or experimental approaches.

The Assumption of Equivalence

Shenkar (2001) and others (e.g. Zaheer, *et al.*, 2012) have argued that a broader range of distance dimensions beyond just the classic Kogut and Singh index should be considered in most distance-related research. Tung and Verbeke (2010) characterise this as the '[non-] equivalence of cultural distance and psychic distance' in acknowledgement of the fact that even Johanson and Wiedersheim-Paul (1975) explicitly cited a much wider range of factors such as differences in language, education and industrial development as antecedents of psychic distance. As Tung and Verbeke (2010) argue, concept of distance is so much broader than

just the original four dimensions of culture popularized by Hofstede (1980), and yet the vast majority of researchers default to this narrow set of indicators, presumably for the sake of convenience and expediency. In many respects it is a sad comment on the state of our discipline. In a related criticism, Shenkar also argues that not all dimensions of distance, even within the original four Hofstede framework, are equally important. In effect, not only should we consider other new dimensions, but we should also turn a critical eye to the salience of the existing dimensions. Shenkar labels this as the 'assumption of equivalence'.

Both of these issues have subsequently been addressed by multiple researchers such as Dow and Karunaratna (2006), and Berry, *et al.* (2010) who have proven that indeed the Kogut and Singh index only seems to be capturing a small fraction of the total effect (also see Dow & Ferencikova, 2010, Dow & Larimo, 2009, Dow & Larimo, 2011). On top of that, they also find that the relative contributions of each dimension do differ dramatically and the relative proportions can vary depending on what criterion variable one is investigating. Furthermore, Larimo and Dow (2009) found that when tested separately, rather than as a combined index, only two of the four Hofstede dimensions are significant predictors of entry mode.

In terms of future research, to some extent the initial work on this issue has already been done. There may be other new dimensions out there, and researchers should keep an open mind to such innovations, but the major challenge is to ensure that the main stream of distance research continues to move away from excessive reliance on the Kogut and Singh index and embraces a broader set of dimensions. So far this perspective has been gradually gaining wider acceptance (e.g. Avloniti & Filippaios, 2014, Castellani, Jimenez, & Zanfei, 2013, Malhotra & Gaur, 2014, Martin & Drogendijk, 2014), but the trickle needs to be converted into a flood. The biggest constraint here is that many researchers simply want to 'control' for distance; and thus, they have a preference for a single formative index. On this particular issue, a pragmatic approach is probably optimal. While Shenkar and others are correct in cautioning us against the 'assumption of equivalence', once the merits of each individual dimension has been tested and endorsed, the use of a formative index is quite appropriate.

The Illusion of Stability

Similarly, Shenkar (2001) also highlighted the 'illusion of stability' – i.e. challenging the argument that culture is relatively stable over time and very slow to change. This is a particularly relevant criticism given that the dominant scale is more than 40 years old. In response to this criticism Taras, Steel, and Kirkman (2012) have used a meta-analytic approach in order to provide updated estimates for each of the original Hofstede (1980) dimensions. Their analysis does indicate some statistically significant movement across the decades; however, in contrast to the previous issue, there does not yet appear to be any evidence as to whether these more recent estimates significantly improve the predictive power of the index.

In some respects, the recent efforts by the GLOBE team (House, et al., 2004) could be interpreted as addressing both of the preceding issues. Their revised cultural dimensions are certainly more recent than Hofstede (1980), and quite intentionally cover more dimensions, although they still constrain themselves to aspects of culture. Unfortunately, subsequent analyses have shown that the GLOBE 'values' and 'practices' dimensions are frequently negatively correlated (Maseland & van Hoorn, 2008, Taras, Steel, & Kirkman, 2010), and this has created substantial controversy and uncertainty over their use. At this stage, the limited evidence available (Meschi & Riccio, 2008) does not provide any clear evidence as to whether the GLOBE scales provide superior predictive power relative to the original Hofstede-based scales.

Overall it is quite apparent that the prevailing sentiment of the commentators (e.g. Tung & Verbeke, 2010) is that these forms of distance do change substantially over time. However, Table 1 shows two very opportunistic comparisons that cast doubt on that assumption. In 1991, a PhD student at Uppsala surveyed Swedish managers for their perceptions of the psychic distance of a selection of foreign countries (Nordstrom & Vahlne, 1994). Roughly 15 years later, Håkanson and Ambos (2010) conducted a somewhat similar survey amongst Swedish teachers. Despite almost two decades and differences in both instrument design and sample population, the two scales are amazingly similar with a Pearson Correlation between them of $r = 0.952$. Indeed if they were placed in the same measurement model, most researchers would typically examine the Cronbach Alpha (0.966) and conclude that they are extremely reliable indicators of the same construct. A similar comparison spanning over a 10 year gap can be made with respect to Australia. In 1994, Australian Trade Commissioners were surveyed about their perceptions of the psychic distance from Australia of a selection of countries (Dow, 2000). Roughly 10 years later Håkanson and Ambos (2010) conducted their sur-

vey. Once again the two scales are remarkably similar ($r = 0.954$) and under most circumstances would be considered effectively identical.

This data presented in Table 1 is obviously opportunistic, and is in no way comprehensive enough to draw firm conclusions; however, it does signal that more work does need to be done in this area. Not only is the ‘illusion of stability’ unsubstantiated, but the limited evidence available does seem to indicate that Hofstede may have been correct about the stability of these metrics over time.

The Illusion of Symmetry

A fourth criticism raised by Shenkar (2001) and echoed by others (Tung & Verbeke, 2010, Zaheer, et al., 2012) is the ‘illusion of symmetry’. The argument here is that the direction of a difference may matter. For example while English and Japanese may be dramatically different languages, it may be much more difficult for an English speaking person to master Japanese than for a Japanese speaking person to master English. Adapting the ‘distance’ metaphor, while the distance between two cities is technically symmetric, it still matters whether they are at the same elevation. The journey uphill may be substantially more difficult than the journey downhill.

Table 1. Surveyed Perceptions of Psychic Distance (on a 0-100 Scale)

	Distance from Sweden			Distance from Australia	
	Nordstrom 1991	Håkanson & Ambos 2003-2008		Dow 1994	Håkanson & Ambos 2003-2008
Norway	0.5	9	NZ	17.2	
Denmark	3.3	13	UK	28.0	30
Finland	8.5		Singapore	28.5	
Great Britain	14.8	20	Fiji	32.0	
West Germany	17.7	22	Hong Kong	32.1	
Switzerland	20.7	26	USA	32.1	29
Austria	22.2	28	Canada	37.8	30
Netherlands	23.4	20	PNG	40.5	
USA	25.3	31	Malaysia	41.2	
Canada	27.1	34	S Africa	43.8	
Belgium	31.7	26	Philippines	48.3	
France	34.8	32	Indonesia	49.6	
Spain	38.2	34	Thailand	50.0	
Australia	39.2	46	Sweden	52.5	60
Italy	39.9	34	Germany	53.5	50
Portugal	47.5		Italy	53.6	48
Japan	59.5	74	Taiwan	55.6	
Turkey	71.6	58	France	55.8	49
Brazil	74.0	65	Japan	56.1	49
Mexico	74.2	63	India	56.2	59
Argentina	78.2	71	China	62.0	59
Chile	79.2		S Korea	62.6	63
			Saudi Arabia	72.7	
			Iran	78.8	
			Russia	81.5	81
	Pearson Correlation	0.952		Pearson Correlation	0.954
	Spearman' Rho	0.938		Spearman' Rho	0.794
	Cronbach Alpha	0.966		Cronbach Alpha	0.975

To date the empirical investigations into the issue of symmetry have almost exclusively been conducted by Håkanson and Ambos (2010), with interesting results. By surveying the bilateral perceptions of psychic distance across 25 different countries, Håkanson and Ambos (2010) were able to demonstrate that there are significant asymmetries in those perceptions, and in contrast to the aforementioned data on the temporal stability of the various distance measures, the asymmetries seem to represent a substantial portion of the total variance. For example,

within the Håkanson and Ambos (2010) dataset, if one regresses the distance from country A to country B on to the distance from B to A, only 48% of the variance is explained. It is tempting here attribute the remaining 52% of the variance to asymmetries but in reality it represents both the asymmetries and the measurement error. Nevertheless, it is reasonably strong evidence that the asymmetries may be substantial.

This presence of potential asymmetries represents an important new research agenda for the distance literature. While at an anecdotal level it is easy to acknowledge asymmetries, provided a consistent and broad based approach for quantifying them is much more difficult. If one is directly employing a measure of people's perceptions of distance, then any asymmetries are implicitly incorporated in the instrument; however, if one is employing exogenously measured differences, such as linguistic distance or religious distance (Dow & Karunaratna, 2006), then compensating for asymmetries is problematic. The potential solution here is for a new stream of research that investigates when, how and why asymmetries might arise. Håkanson and Ambos (2010) and Håkanson (2014) have begun this investigation; however, substantially more work needs to be done.

The Illusion of Homogeneity

The fifth, and for this chapter, the final criticism of how distance has been measured is the 'illusion of homogeneity' (Shenkar, 2001). At face value this criticism simply reflects the fact that no matter which dimension one chooses to investigate, most approaches to measuring distance in the IB literature neglect the fact that there are likely be within-country variations. However, this criticism almost inevitably leads into, and overlaps with a discussion of whether one should measure psychic distance in terms of the perceptions of the individual.

A number of commentators (e.g. Evans & Mavondo, 2002, Sousa & Bradley, 2006) have strenuously argued the need to measure distance as an individual-level perception. Indeed, they go so far as to redefined psychic distance as an individual-level perception. Conceptually this line of argument is particularly strong if one is applying the distance construct to explain choices made by managers. For example, distance has frequently been cited as a predictor of entry mode choice (Tihanyi, et al., 2005). The logic here is that decisions are not made by firms but rather by managers, or small subsets of managers. As a result, it is the perceptions of those managers that is most critical. Exogenous 'facts', such as the differences in language, religion or culture are only inputs into the formation of those perceptions. Thus, it is most appropriate to measure the perceptions of the key

decision maker, or the top-management-team involved in the decision. This perspective is empirically bolstered by the findings of Zhao, et al. (2004) that the entry mode – distance relationship is much stronger when distance is measured as a perception, rather than using exogenous national-level indicators.

The major limitation in terms of researchers heeding the call to measure distance at the level of the individual is a practical one. While the decision maker's perception of distance at the time he/she makes a major decision is arguably the most appropriate metric, given the infrequent and erratic nature of these decisions (at least in terms of when they are made), it is virtually impossible to capture the manager's a priori perceptions (Dow & Karunaratna, 2006). In addition to that, there are methodological concerns about measuring post hoc perceptions since the post-decision experiences are almost certainly going to influence the manager's perceptions. A second concern with the approach of directly measuring the decision maker's perceptions is that it may provide a more powerful predictor variable, but if one stops there we are left in the quandary of not knowing what factors are shaping those perceptions.

As a result, in terms of research agendas, the major issue here is understanding what factors are shaping individual-level perceptions of distance, and in particular what is causing them to deviate from the commonly used exogenous national-level indicators (e.g. Berry, et al., 2010, Dow & Karunaratna, 2006). To a large extent this issue is virtually unexplored to date. However we can propose three broad reasons why individual-level perceptions of distance may deviate from exogenously derived national-level indices: within country heterogeneity, the international experience of the individual, and biases in the formation of people's perceptions. We will briefly discuss each of these in turn.

Heterogeneity within each country: The first and most obvious explanation as to why an individual's perception of distance might deviate from exogenously derived national-level indices is the fact that there is substantial heterogeneity within many countries (Shenkar, 2001, Sivakumar & Nakata, 2001, Tung & Verbeke, 2010). As noted earlier, Shenkar (2001) labels this the 'assumption of spatial homogeneity,' although the issue had been acknowledged much earlier (e.g. Welch & Luostarinen, 1988). This might be manifest in terms of within-country variations in dimensions such as spoken language, religious affiliation, and the presence of minority ethnic groups. For example India and South Africa are highly multilingual countries; whereas Japan and Portugal are largely unilingual countries. Similarly Malaysia and Ukraine are highly diverse in terms of the religions practiced; whereas Yemen and Peru are relatively homogeneous in terms of religion. All three of these factors may be strongly linked to high levels of

immigration; and thus, countries with high levels of immigration may have greater within-country heterogeneity. This same issue has also been long acknowledged in the cross-cultural literature (e.g. Wallace, 1970).

Nevertheless, despite the fairly broad acknowledgement of this issue, empirical investigation into just how much intra-country heterogeneity causes individual perceptions to deviate from national averages (i.e. how much information is one sacrificing if you employ a national average) seems to be exceptionally rare. Moreover, the limited research in this area does not yet yield a consistent pattern of results. In one of the few studies addressing this issue, Au (2000) found that the intra-cultural variance (using the World Value Survey) can differ dramatically across countries and dimensions. However, Dow (2009) when examining the perceptions of psychic distance by Australian managers, found that individual-level factors (e.g. if the respondent spoke another language or practiced another religion different from the national norm) only explained one tenth the variance in perceptions as national-level factors (e.g. differences between countries in official national languages and religions). With similar, though slightly less extreme results, Smith and Schwartz (1997) found in their 13 country study that the respondent's home nation as a factor accounted for three times more variance in the Schwartz value survey than any within-country variable.

Notwithstanding the preceding results, we still find the advice of Tung and Verbeke (2010: 1267) – i.e. that national-level averages “should not be blindly adopted in micro-level studies” to be sound. The concern is that researchers need to be applying data at the appropriate level of analysis. This is not an issue of ‘perceptions’ deviating from ‘reality,’ but rather, that the ‘reality’ for any given manager may differ from the ‘reality’ of the national average, and that selection bias may magnify the frequency of such events. Note that we are not suggesting that one must necessarily measure each and every manager’s perception of psychic distance - that is not always possible on an *a priori* basis, but it may be possible to measure the educational, linguistic, religious, cultural and ethnic backgrounds of key decision-makers. Where possible this should be preferred over using national averages.

The International Experience of the Individual: The second potential explanation as to why an individual’s perception of psychic distance might deviate from exogenously derived national-level indices is the fact that knowledge is not a static concept (Shenkar, 2001, Tung & Verbeke, 2010). As managers operate in the international environment they gain tacit knowledge both about specific countries and about techniques for dealing with different cultures and environments. This increase in their stock of tacit knowledge will reduce their difficulties in

communicating with and understanding foreign markets. Thus, in turn, this experience should reduce their perceptions of the psychic distance of those markets. As with the preceding ‘heterogeneity’ argument, we are discussing here a very real and rational change in perceptions of psychic distance (as opposed to a behavioral bias). It is not an accident that this very argument is a cornerstone of the Uppsala internationalization process model (Johanson & Vahlne, 1977).

At the empirical level this issue has been implicitly reflected in the broad-based use of firm-level international experience as a control variable to complement cultural and/or psychic distance (Zhao, *et al.*, 2004); however, in most instances these studies have not directly modelled the mediating role that perceptions of psychic distance play in say the international experience – entry mode choice relationship. Sousa and Bradley (2006) completed one of the few empirical investigations into how international experience influences perceptions of psychic distance. In their 2006 article, they explored how the classic national cultural distance index (Kogut & Singh, 1988) predicts perceptions of psychic distance, and in the process confirmed that international experience plays a statistically significant role in reducing those perceptions of distance.

In a more indirect fashion, Håkanson and Ambos (2010) noted a similar effect when studying the antecedents of national perceptions of psychic distance across 25 countries. They found that for their data set, the size and GDP per capita of a target country is directly related to lower perceptions of distance. They attributed these effects to respondents being better informed about larger and higher income countries due to economies of scale and better developed infrastructures for the collection and dissemination of information. Hence, indirectly confirming that people’s perceptions of distance can and do change as they gain more information about the countries in question.

Biases in Perceptions: The third and final potential explanation as to why an individual’s perception of psychic distance might deviate from exogenously derived national-level indices is potential biases in the development of people’s perceptions and/or beliefs. This is the point where our arguments depart from the classic assumption of a rational decision maker and move into the realm of cognitive biases. It is here we need to draw heavily from the field of social cognition, which has a much deeper history in such issues.

At both the empirical and theoretical level, this topic has remained virtually unexplored in the international business literature. At the empirical level, the only study we are aware of is once again the work of Sousa and Bradley (2006). In addition to international experience, Sousa and Bradley found that the ‘conservation values’ (Schwartz, 1992) of the respondents have a tendency to magnify their

perceptions of psychic distance. While Sousa and Bradley were not explicitly citing social psychology theories, their work was implicitly building on similar issues; and thus, their study is the only empirical international business research that we are aware of, to explicitly investigate such biases.

Nevertheless, there is one qualitative international business paper, which has implicitly explored the issue of cognitive biases in the perception of distances. In 1996, O'Grady and Lane published an exploratory paper based on Canadian retailers entering the US market. In this paper they proposed there might be systematic biases causing the Canadian firms to underestimate how different the US market is from Canada. While O'Grady and Lane (1996) did not specifically cite any social cognition literature, their arguments have strong parallels with the concept of confirmation bias (Klayman, 1995). This thesis of the 'psychic distance paradox' has been subsequently expanded and explored by other researchers (Evans & Mavondo, 2002, Magnusson, Schuster, & Taras, 2013); however, to our knowledge no published paper to date has explored the perceptual bias underlying that thesis¹¹.

It is for these reasons that we argue that the international business literature can learn a great deal about the factors that shape perceptions of psychic distance by drawing on the existing and extensive social psychology literature. As noted above, the issue of confirmation bias may go a long way to explain the psychic distance paradox. If a person initially believes that a particular country is psychically distant, then they will tend to be more accepting of and place more emphasis of information that confirms that belief. Similarly, with countries that they believe are psychically proximate, they will tend to ignore and dismiss any information that is contrary to that belief. As a result people will eventually overestimate the distance of psychically-distant countries and underestimate the distance of proximate countries.

Another social psychology concept which may have relevance here is the concept of cognitive complexity (Bieri, 1955, Levy, Beechler, Taylor, & Boyacigiller, 2007). Psychic distance is undeniably a complex and multidimensional construct. However, when managers have a low level of international experience they may have a more simplistic view of psychic distance, and may use simple heuristics such as geographic distance. This in part may explain one of Håkanson and Ambos (2010) unusual results –where geographic distance is far and away the strong-

¹¹ One paper currently under review – Baack et al. (2011) – does explore this issue but is yet to be published.

est predictor of their estimates of psychic distance (their sample population was school teachers). In contrast, when they gain more international experience the managers may develop a more complex and nuance view of the construct. In keeping with Johanson and Vahlne (1977), we might conjecture that their perceptions of psychic distance would decline as they gain international experience; however it might also be the case that they gain a greater appreciation of the complexity and magnitude of the challenge. Eventually this should improve their ability to deal with this distance, but it may not necessarily cause them to rush into such situations more quickly.

At this stage the number of potential new research ideas that can be drawn from the social psychology literature seems quite substantial; however the major challenge is that researchers may have to begin embracing different research techniques – specifically experimental methods. Many, if not most of the social psychology concepts are sufficiently subtle that the classic IB approach of analysing large-scale surveys, or secondary-source panel data will not suffice. New techniques and approaches will have to be adopted.

Conclusion

As argued at the outset, distance has played a pervasive but contentious role in IB research. In many respects most of the major problems and concerns about how we collectively have employed distance in our research have been highlighted multiple times over the past decade – but have we made any progress since then? I would argue a tentative 'yes, but with a significant caveat - we still have a long way to go'. Some of the prescriptions and recommendations going forward are merely cautionary – such as paying more explicit attention at the theory development stage to the underlying mechanisms of why distance is important. The same applies to encouraging researchers not to just use the Kogut and Singh (1988) national cultural distance index 'because everyone else does'; but rather, to consider using other broader measures of distance that are freely available.

Nevertheless, two more substantial, but so far unfulfilled research agenda's, lie in confirming and exploring the stability and symmetry of the various dimensions of distance. These are issues that most commentators agree are important, and yet there is a dearth of research on them. The first step is in confirming the magnitude of the issue/problem – i.e. is it really as large a concern as initially feared or is the effect size trivial? This is an important first step. Following on from that - if it is sizable effect - then we need to explore what is driving the change over time and/or asymmetries?

However, across the broad spectrum of issues relating to the role of distance in IB research, I would have to rate the final issue as the most critical. To what extent do individual-level perceptions of distance deviate from the commonly used, exogenous national-level indicators of distance, and what is causing those differences? In essence, we need to have a better understanding of what is shaping those perceptions. This is particularly critical given the inherent difficulties in directly measuring a decision-maker's *a priori* perceptions. It is only on a rare occasion that we will have the luxury to directly measure them. Thus it is only by understanding the antecedents and moderators that we will be able to estimate what those perceptions might be, and compensate for those factors. However, this may force many of us to explore new territory in terms understanding the rich history of social psychology and learning the methodological techniques that go along with them.

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7. Process Research Is Back: A Tribute To Jorma Larimo's Contribution On Fdi Decision-Making

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Introduction

Recently, calls have been made to “put process back” into research on firm internationalization (Liesh, Nummela & Welch forthcoming, Welch & Paavilainen-Mäntymäki 2014). While firm internationalization has been conceptualized as a process since the 1970s (Johanson & Wiedersheim-Paul 1975, Johanson & Vahlne 1977, Luostarinen 1979), the way it has been studied has not always given justice to this conceptualization.

Jorma Larimo's early work represents an exception which we will analyze in this chapter. Larimo defended his doctoral thesis entitled “Foreign direct investment behavior and performance: An analysis of Finnish direct manufacturing investments in OECD countries” in 1993. In this study, he analyzed the routes to undertaking a foreign direct investment (FDI) decision and the performance of such an investment. His doctoral thesis was based on an impressive data collection effort, with the data set comprising a very significant part of all Finnish corporations that had carried out FDIs at the point of his study. He drew on behavioural rather than economic theory to explain FDI behavior and adopted a processual perspective to the internationalization of the firm. Larimo's doctoral thesis and some of his subsequent work built on the Finnish tradition in this area (Björkman 1989, Luostarinen 1979) as well as Aharoni's (1966) pioneering study on FDI decision-making processes in US firms. In his subsequent work, Larimo continued to have an interest in foreign direct investments and how these decisions are made.

An FDI represents a strategic decision for the company in question. The decision-making leading up to a commitment to carry out a foreign direct investment is a complex social process characterized by dynamic and unstructured elements. However, it is not self-evident that by “having selected a process phenomenon to study or posed a process-based research question, the final theoretical contribution will also be processual” (Paavilainen-Mäntymäki & Welch 2013: 245). In fact, recent reviews suggest the contrary (Welch & Paavilainen-Mäntymäki

2014): internationalization of the firm, including FDI processes, are frequently studied based on cross-sectional research designs. Contributions that pose process-based questions are few in number (Welch & Paavilainen-Mäntymäki 2014).

In this chapter, we draw attention to Jorma Larimo's processual contribution to the study of FDI decision-making which lies at the heart of the field of international business. We will describe and evaluate one his most influential articles (Larimo 1995) as an exemplary contribution to the FDI literature and international business research more generally. Further, we will also heed his instrumental role in integrating the community of senior and junior IB researchers in Finland and systematically internationalizing it during the past decades.

Jorma Larimo: The exemplary FDI process scholar

Jorma Larimo published the article entitled "The foreign direct investment decision process: Case studies of different types of decision process of Finnish Firms" in the *Journal of Business Research* in 1995. It has been widely cited in the field and represents a comparative case study which is particularly suitable as a research strategy for capturing multiple time points (Welch & Paavilainen-Mäntymäki 2014). In Larimo's later work the processual approach is less evident than in this piece from 1995 but it nicely complements his early research by addressing a range of issues related to FDIs by Finnish firms (see for example, Hennart & Larimo 1998).

In the focal paper, Larimo retrospectively traces the strategic decision-making processes leading up to the FDI decision in five Finnish manufacturing firms that operate in electronics, consumer goods, chemicals, vehicles and plastics. Larimo's case study is an excellent example of process research on internationalization because of the way he applies the processual approach from the initial research design, case selection, data collection and analysis to the discussion of the findings.

The design and aim of the study

An FDI decision-making process can be studied in many different ways ranging from a variance to a process approach (Welch & Paavilainen-Mäntymäki 2014). As such, an FDI decision represents a particular episode in the internationalization process of the firm and researchers may prefer not to investigate the entire process behind it. Instead, they may opt for a variable-oriented approach that would entail an analysis of internal and external stimuli mediated by managers'

perceptions of the firm's resources, strategy and environment, for example (Welch & Paavilainen-Mäntymäki 2013). Another research design would be to examine the antecedents and outcomes of an FDI decision but exclude the intervening process connecting them altogether. Alternatively, the focus could be on the outcome of the decision-making process rather than the process itself, by e.g. classifying the kind of FDI that firms undertake in terms of their form, type and motives driving the investment (see Table 1, Larimo 1995: 28-29).

Larimo chose a process approach and dived deep into the complex and messy world of FDI decisions. He uncovered the patterns of critical events that his informants related to him. Thus, these key turning points in the FDI decision-making process were identified 'from inside'; that is, they were examined from the perspective of the key decision-makers in the case companies rather than the researcher himself.

Larimo (1995: 25) posed the general research aim of his study as follows: "to highlight the FDI decision process in five foreign manufacturing investments made by Finnish firms". He was interested in understanding how the decision-making process evolved over time and studied it after its completion, i.e. retrospectively. The five investments processes varied in length. The starting point was the recognition of the need to make a decision to address a problem, crisis or an opportunity. The longest decision process took 5 years while the shortest only a couple of months. Larimo (1995) did not only cover the decision-making process leading up to the FDI but also the subsequent years in order to explain the financial outcomes of the investment decision.

In line with the work by Minzberg, Raisinghani, and Théorét (1976) on the general model of strategic decision processes Larimo (1995) divided the FDI decision process into three phases: identification, development, and selection to capture its unstructured nature. These three phases consisted of central and supporting decision-making routines at the workplace. The general model of strategic decision processes by Mintzberg et al. (1976) provided the theoretical framework for Larimo's (1995) study and guided his empirical work.

Case selection

The five cases were selected from a larger sample of 59 FDIs that Larimo (1986, 1987) had reviewed earlier. His aim was to ensure maximum variation among the case companies in terms of their background (firm size, extent and experience in international operations, especially in FDI), process data (process nature, routines and dynamic factors), and situational data (competition, motives for FDIs, envi-

ronment, role of organizations affecting the FDI; Larimo, 1995: 26). Interestingly, Larimo used the availability of process data as an explicit criterion in case selection.

Data collection

In line with case study tradition, Larimo (1995) drew on multiple data sources including personal interviews, annual reports, in-house magazines, and questionnaires. He interviewed the key managers who had personally been involved in the FDIs reviewed. In four of the five cases, this meant interviewing one person per company. Larimo complemented the retrospective interviews with written documents that represented a source of real-time, historical data. This was particularly important in the oldest cases where distortion and memory failures were possible.

Data analysis

The way Larimo analyzed his data and wrote up the findings is undoubtedly the major contribution of his 1995 article. Larimo was able to delineate the full historical background of the emerging decision-making processes in the five investments and placed time at the centre of his inquiry. The unit of analysis was the entire process rather than a single variable in the decision-making process and Larimo traced it back and forward in time. Each investment decision process was written up as a rich case narrative and graphically visualized in Figures 2-7. These figures vividly demonstrate the non-linear, dynamic nature of FDI decision-making processes which were characterized by interruptions, delays and discontinuities. In addition to the key internal players, Larimo also included external actors such as consultancies and advisors in his narratives. In this way, he avoided portraying the firms as unitary entities and accentuated the political aspects of this complex process. In this way, he provided the reader with a highly contextualized view of the FDI decision-making processes in the five Finnish firms.

However, a good process study goes beyond mere description of phases of events. Larimo (1995) identified the underlying mechanisms that connected the critical time points in the FDI decision-making processes and explained how and why these temporal patterns occurred. These were related to financing, technology and management related issues. Paavilainen-Mäntymäki and Welch (2013: 231) argue that “[w]hat differentiates a process [from longitudinal research] is not so much the timespan but rather the presence of a cause, an effect and the mechanism connecting the one to the other.”

In short, Larimo retains the process focus throughout the study. He has a process-related research aim, collects process data and analyzes the process in its entirety. Larimo situates the FDI decision process in its natural context of the firm's internationalization path. As Welch and Paavilainen-Mäntymäki (2014) point out, processes cannot be understood in isolation of context. Larimo also builds process theory by identifying generative mechanisms that explain why and how the processes unfolded the way they did in each case company. At the end of the article, he classifies the five FDI processes according to the extent to which they display elements of the decision-making steps and routines.

Assessment

Larimo's 1995 article has stood the test of time really well. It is a rigorous, thorough and highly insightful analysis of the 'backstage' of FDI decisions. Larimo gets very close to action which renders his study highly relevant for managerial practice. It is, of course, always possible to make suggestions to any study, even the most well-crafted one. A possibility in Larimo's study could have been to present verbatim quotes of the interviewees and let their voices be heard in the stories from the field. Since the publication of Larimo's article in the mid-1990s, however, important advances have been made in terms of how to present and write-up qualitative research which can be found in guidebooks (Piekkari & Welch 2011) and editorials (Bansal & Corley 2011).

Sometimes the researcher is able to study decision making processes in real time as events unfold. By participating in meetings and discussions about the focal FD the researcher can avoid post-rationalization and reconstructions of reality that are commonly associated with retrospective interviewing. Data can also be collected through personal diaries which may provide additional insights into the phenomenon at hand. Still today, almost 20 years later, Larimo's study serves as an excellent example of high-quality process research that many IB scholars would do well to emulate.

Jarmo Larimo: The "Godfather" of IB research in Finland

While Jorma Larimo has made important contributions through his research achievements, he has also had a significant impact as the "Godfather" of international business research in Finland which we would like to acknowledge in this chapter.

One part of Larimo's "Godfather" role is his long-term work within the Finnish Graduate School of International Business (FIGSIB). He was first a board member during 1996-1997. In 1997 Larimo succeeded Professor Reijo Luostarinen as the Director of FIGSIB. His role was not restricted to chairing the board meeting only; rather he personally carried out a large share of the administrative work that was an integral part of running FIGSIB. He also took a personal interest in following up the progress of the doctoral students who were funded by FIGSIB or just participated in some of the doctoral courses that FIGSIB offered. During 2005-2012 no less than 58 PhDs graduated within FIGSIB – and all of them are indebted to Jorma Larimo for his institutional work.

In 2013, Jorma Larimo organized the Vaasa IB conference for the 12th time. The conference also has a doctoral tutorial which has established itself as a "must" venue in Finland as well as abroad. The Vaasa IB conference has attracted a large number of well-established IB scholars to Finland, including Jean-François Hennart, Gabriel Benito, Douglas Dow, Marian Jones, Stefan Schmid, Ulf Andersson and Klaus Meyer. Many of them have served as key note speakers and discussants at the conference and the doctoral tutorial. Finally, Jorma also served as a long-standing representative for Finland in the European International Business Academy (EIBA).

Jorma, our best congratulations!

As authors of this chapter, and as your colleagues and friends, we would like to thank you for all your work and wish you all the best on your 60th birthday!

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8. The Internationalisation Of The Firm: Managing Political Environments In The European Union

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Introduction

Firms doing business in international markets confront with two fundamental sets of environments; business and political. While models on management in international business have paid much attention on the firms and their business environment, the interdependencies between firms and political actors and the political activities of firms has attracted less research (Hadjikhani, Lee and Ghauri 2008; Boddewyn and Brewer 1994; Boddewyn 1988; Ring et al., 1990). The studies that have paid attention on the management of political actors can range from the presumption that management is a function of response to political environment (Ghauri and Cateora 2010; Conner 1991; Ghadar 1982; Korbin 1980; Pointer 1985) and to design coping strategies (Ring et al. 1990 and Johnson 1982). The coping strategies view is often dealt with as management of risk (Miller 1992), country risk ratings (Cosset and Roy 1991), firm-state interdependencies and industrial (Ring et al., 1990) or corporate structure (Murtha 1991 and Lenway and Murtha 1994) by using ,e.g., institutional theory. Against this stream, there are studies which give deeper attention to the interplay between the business and political actors and present theoretical concepts for the political behavior of firms in their political markets (Hadjikhani, Elg and Ghauri 2012; Keilor et al. 1997; Brewer, T.L. and Klemm, R.J. 1993; Boddewyn and Brewer 1994; Ring et al. 1990). They make a distinction between the business and political markets and study international firms' political activities which claim to be a neglected area. Brewer and Brewer (1994) extend further and explain that political behavior is neither merely an alternative nor complement to economic behavior, but it constitutes an intrinsic part of international business as it interfere with the allocation of resources.

Following this track, this paper focuses on the firms' political environment and discusses the firms through behavioural theory (Cyert and March 1963). The purpose is to explain international enterprises' political actions in managing this environment. The management of political actors is explained by Boddewyn and Brewer (1994) and internationalisation of the firm (Johanson and Vahlne 1977 and Buckley and Ghauri 1993) and network theory (Johanson and Vahlne 1990 and 2009, Kooiman 1993 and Håkansson and Snehota 1995). The aim is to describe and discuss the political behavior of Swedish firms in relation to the European Union after integration of Sweden into the Union. In line with this view it can be interesting to study how different Swedish firms being in different phases of internationalisation, i.e. export and direct investment, behave when interacting with political actors in the European Union.

Inasmuch firms' business activities are interrelated with political activities, can knowledge in political behaviour enhance our understanding of firm's market behaviour (Ring 1990). In line with this, the paper attempts to study how firms behave in their political markets. In Europe, interest in these questions has increased during the last decade because of the development of the EU (Elg, Ghauri and Tarnovskaya 2008; Hooghe 1995). The study employs a comparative view and discusses similarities and differences in political activities between large international firms and emphasises on how these different firms manage their relationships with EU. The political activities do not necessarily aim to gain a direct financial support but can strive for aims like influence (Hadjikhani et al 2012; Alt and Chrystal 1983) which ultimately subsidises the business activities.

Within political science some researchers have studied this interplay from the point of view of the state. These studies are in the fields like development economics (Maddison 1991 and Esping-Andersen 1985) and regional economics (Hanf and Toonen 1985 and Nowtotny et al. 1989), concern of government and its impact on firms is the main topic in these studies. Some studies (Kooiman 1993 and Buckley and Ghauri 1993) explore it with network of interest groups for political and competitive decisions. Later studies, in governance (see e.g. Elg et al. 2013; Streeck 1992 and Fligstein 1996) explain the failure of political hierarchy and discuss that the internal dynamics and differentiated social system are factors making the centralised political control in the traditional juridical way more difficult. This also can be traced in business studies addressing national governments weak position (Buckley and Ghauri 2004; Vernon, 1977). Following that criticism, some studies present the view of interest groups (see e.g. Potters 1992; Yarbough and Yarbough 1987 and Boddewyn 1988) suggesting a dyadic view for analysis of relationships between political and business actors where MNEs are reported to pro-actively trying to shape their political environment.

Internationalisation and Political Behavior

The conceptual ground of this paper points at the dyadic interplay of political and business actors (Hadjikhani and Ghauri 2001; Boddeweyn 1988) which is embedded in a network. Within this context, the political behavior at the firm-level has its basis on the theory of international business political behavior (Boddeywyn and Brewer 1994) and the model of internationalization process of firms (Johansson and Vahlne 1977; 1990 and 2009). This view is similar to the study of Keilor, et al. (1997) when they integrate the two theories to conceptualize the political behavior of the firm. Boddewyn and Brewer (1994) with the presumption of political behavior as a factor of production, present a model for study of business and political behavior which is composed of the three interactive conditions; business, political and strategic. For the first dimension, the interactive conditioning factors, the levels introduced in the model are nonmarket actors, firm and industry. The non-market environment interaction with the firm can be explained by the network model within which the dyadic interaction of political and business actors are embedded (Seyda et al 2012). The industrial network approach which has its origin in social network and behaviour theory is extensively explored in industrial marketing (Ford 1990 and Håkansson and Snehota 1995) and international business studies (Buckley and Ghauri 2004 and Forsgren et al. 1995) but exclude the non-business actors. This paper, following the trace of Brewer (1994) goes beyond this stream and explains that the foreign enterprises are dependent on the governments and that the governments are also dependent on the foreign enterprises as firms make investments and that affect groups like people and media which the governments are dependent on (Jacobson et al. 1993; Hadjikhani 1996). Political actors in seeking for legitimacy (Eliassen and Kooiman 1993) incorporate values from these groups into their decisions (Boddewyn 1988) and business firms for their exchange of resources are also dependent to the business actors in their networks.

The second dimension refers to the firm-level where firm characteristics are the most important factors (Barlett and Goshal, 1992; Salorio, 1992). In this view the differentiated political activities are reflected by the firms' degree of internationalization. The behaviour theory of internationalisation (Johansson and Vahlne 1977 and 1990) explains that the firm's management activity is a consequence of its knowledge and market commitment. The principal obstacle is discussed by commitment decision which is connected to the learning about the foreign market.

By increasing political knowledge the perceived uncertainty of the market investment declines and market commitment increases. Commitment can be explained by size of investment or links not only between focal actors but even oth-

ers in the network. Links include both the tangible and intangible investments that firms have committed itself to (Denekamp 1995 and Scott 1994; Becker 1961), the political or his connected actors, called by Andersson and Weitz (1992) as idiosyncratic investment or intangible commitments. As a result, the knowledge dimension contains the experiential knowledge of the firm (Blankenburg et al. 1997) and also the knowledge that the firm accumulates from others in the network (Johanson and Vahlne 2009). Business actors in their interaction with political actors need information about the values and activities of others like people and media in the network. The varieties in the degree of commitment and knowledge among the firms explain the differences in the managerial behaviour which can make the relationship of each firm with political actors unique (Lee 1991).

The ultimate objective of the firms' internationalization process is increasing commitment illustrated by export to direct investment and in political market explained by Brewer and Boddewyn (1994) by the factors of efficiency, market power and legitimacy. These three factors can gain a process dimensions by covering them in the factors of influence and adaptation (Miller 1992 and Makhija 1992). In the process of political behavior firms having less political knowledge and commitment apply the objective of adaptation related to the factor of efficiency as political coerciveness cannot be eliminated (Keillor et.al 1997). Influence is exerted through negotiations, lobbying and co-operation (in the third dimension of the Boddewyn and Brewer 1994) in which firms aim to gain support in terms of e.g. legitimacy or political power. By development of knowledge and commitment the process of change in the political behaviour proceeds from adaptation to influence. Firms with a low level of knowledge and commitment rely on the first mode of political activity which considers internal change to adapt business activities to the political rules. The next one implies to the act of changing counterpart's behaviour, namely, to overcome political rules which fit with the enterprise's business objectives. The final outcome of the management decision becomes an antecedent to the firms' commitment and knowledge and political activities of political actors (Elg et al 2012).

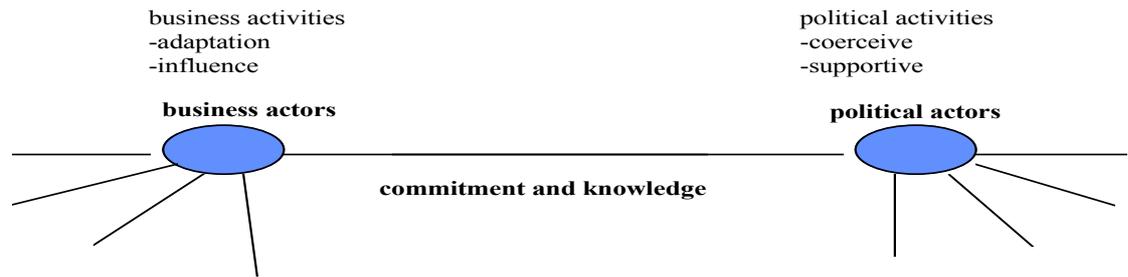


Figure 1: Interaction between Political and Business Actors.

Adapted from Ghauri and Hadjikhani 2001.

As illustrated in the Figure 1, on the other side of the dyadic interaction are the political actors who are connected to several other actors at multiple levels within conflicting interests (Hadjikhani et al 2012). The interaction of political actors with these actors and business actors makes them to undertake supportive or coerceive actions. Enterprises require rules and supportive measures distributed by governments and governments gain legitimacy as these enterprises satisfy people and other groups that they are responsible to. The interaction between the two requires adjunction of conflicting interest, but also arena for exploring options and sharing common values (Hult and Walcott 1990). As figure 1 illustrates, the alternative behavioural options for the political actors are coercive or supportive which can contain general or specific influence (Boddewyn and Brewer 1994, Korbin 1982 and Hadjikhani et al 2008).

Political Decision Process in the EU

European Union (EU) involves 27 European countries accepting EU's supremacy which suggest finding ways to incorporate rules to create Single European Market. Business related policies are of three broad types. First, policies designed to dismantle existing barriers to the free movements of goods, people and capital. Second, to harmonise and replace many national standards for example, for business activities. Third, to promote competition, removal of restrictive practices and prevention of abuses of dominant trading positions and also elimination of state subsidies distorting competition (Regulation 4064/89).

From the four principal institutions responsible for development and implementation of rules (the European Parliament, the Commission, the Council of Ministers and the Court of Justices) the first three concerns this study. The European Council brings together, at least twice a year, the head of governments. The Council of Ministers is the EU's principal legislative body and also is EU's decision making

body, and the Commission is the EU's institution which deals mostly with business related matters.

The political propositions are suggested by Commission and then are discussed in the European Parliament (EP) which finally are delivered to the Council of Ministers (CM) as the ultimate instance to accept or reject a proposal. The Commission has a monopoly position to take initiative and formulate political questions. It is because of this function that the Commission is the most important section in the EU to influence. The more influence an international firm has in this section for its proposal, the more likely that the final outcome of the political policy will be supportive for that company (Anderson and Weitz 1992). The organisation of Commission is divided into 36 different General Directorates (GD) and offices and each member of Commission has access to several GD or offices. When proposing a suggestion the Commission refers to the expert committees. Some of these committees are permanent but others are ad-hoc groups. It lies within the duty of the Commission to gain information from experts and private firms and engage them in the discussions. The Commission members have realised that involvement of these groups increases solidity in the proposal and also provides less execution problems (Bern 1994). The 518 members of the EP are also temporary and are elected by the people in the EU countries. The members of the EP are to discuss and consult with Commission before a decision is made. Their attitude depends on the members ideology and their final advice to the CM depends on the group constellation at each specific period. In most of the cases the Commission's proposals are accepted by the CM.

Method for Data Collection

Considering the nature of the objective of our study, in depth understanding of interaction between business and political actors, we decided to adopt case study method with in-depth interviews (Ghauri and Gronhaug 2005; Eisenhardt 1989). The subject of 'firms' relationships with political actors' is however a sensitive area as many firms are unwilling to disclose information to outsiders. Firms that are satisfied, aim to keep the relationship away from public opinion while those that are dissatisfied are afraid of negative publicity. Accordingly, the study started with a survey of more than hundred firms asking for their willingness to disclose information about their political networking. The positive responses were few and accordingly, the study only focused on those that were willing to be interviewed and provide information. The information in the cases is based on both primary and secondary data. Three MNEs agreed to be interviewed and provide us with some secondary information. The primary information was collected by inter-

views in which 11 Swedish managers in Brussels as well as 4 politicians in the Commission were interviewed. Beside these, other interviews were conducted with Swedish managers in Sweden and also with Swedish representatives in the EU. The secondary data is collected from brochures and information released by these firms for their political operations in the EU, as well as through published information provided by EU.

The three MNEs, SAS, ABB and Ericsson presented in this paper, have made large market investments in the European countries which started decades ago. The direct investments in more than 100 countries have also forced them to be active in their political environments. These firms organise their political activities in a completely different way.

Empirical Facts:

1. SAS

In 1992, when questions like deregulation became serious for the EU's politicians, SAS realised a need to come closer to the decision makers. The headquarter decided to make investment for political activities and among others opened a political unit in Brussels. Totally the firm engages twelve persons, two of them are located in Brussels six in Sweden and the rest in other European countries. The task of the unit in Sweden is to assist the unit in Brussels by, for example, providing information or negotiation with the Swedish politicians involved in EU's political decisions. The political questions that SAS is concerned cover areas such as; rules for flying time; consumer protection laws, taxes, competition law, pricing and environmental issues. Before the Swedish entry into the EU, SAS already had experience in political questions like deregulation because; a) the deregulation of the airline industry in 1987 in Sweden which had created a new competitive arena; b) the company is a corporation of air companies from Sweden, Norway and Denmark.

The main job of the unit in Brussels is to collect information and exercise influence on the rules before they are proposed to the Council of Ministers. To gain a support for the suggestions, the unit first of all works with committees from Commission and then parliament. The unit also discusses the proposals with Swedish and even Danish representatives in the EU. The manager explained that his duties are, among others, to engage in the formal and informal meetings and to follow the media and protocols. He divided the activities into internal (within SAS) and external ones.

More than 40% of their time is spent for formal meetings and 20% is devoted for informal activities like engagement in social arrangements (2-3 times a week). The remaining time is devoted to study protocols, media, competition and consumers. One fundamental area mentioned by the manager is to build and maintain the social relationships. For that, the manager explained, the contacts starts when there is a concrete question. This contact later becomes fertilised in social meetings which assists the co-operation. Knowledge about the politicians' social beliefs and ideas, he explained, increase the confidence when negotiating. Engagement in informal clubs or parties is recognised as important part of the political process. Establishment of contacts are easy, but the major task, manager explained, is to create confidence and maintain it.

The acceptance of a proposal for discussion in a committee is related to the matter of how a proposal includes EU's political values. If a political question is not actualised by the EU or media, the managers are to collect enough technical and market information which can convince the Commission that there is a need for a political decision in interest of the consumers. The case of 'ground handling' is a typical example. The aim of SAS was deregulation of the ground handling for flight slots. SAS aimed to have freedom, or at least being able to buy flight slots from different sellers. In London for example, the airlines could choose among 7-8 alternatives. SAS argument was based on economical effect of the deregulation. The decision could decrease the costs for the airline industry and subsequently reduce the price and increase the quality of the service to the passengers. The initiative was taken by SAS in 1992/1993, long before the issue was discussed in media or any political institution. SAS manager realised that competitors like Lufthansa and KLM had a similar view and accordingly they decided to act together. They built an ad-hoc group to put forward a suggestion to the DGVII and DGIV in the Commission. The committee involved in the question agreed and suggested the proposal to the Commission since the proposal was in line with the consumer welfare policy. The proposal was sent to the parliament but there the social democrats and some other business groups acted against. Social democrats because they were against deregulation in general, interest groups like flying slots sellers because such deregulation could give more freedom to the airlines. At this stage the proposal of the committee is handed over to the Council of Ministers.

2. ABB

The manager of the political unit in Brussels explained that relationship with political actors in EU is one of the most important area specially for the products like power generation. In 1993, ABB established a political unit engaging 15 peo-

ple. Beside these people, 5 other people in different European countries are engaged to deal with political matters. The main interest of the manager is to cover political question like; a) R&D and projects to develop new products, b) deregulation and harmonisation of the market; c) The White Paper - explaining the energy politic - for the year 2020; d) environmental questions like reduction of chloroxide in Central and Eastern Europe, echo-audit, standardisation specially ISO 2000, EMAS (environmental certificate) and even general social and economical questions like employment. The sections in the Commission dealing with these issues are among others, DGIII for industry; DGXI for environment; DGXII R&D; DGXVI for energy and DGXIV for public procurement.

In ABB's political unit, there are 9 persons whose main task is to collect market, technological and political information needed for proposals. The first important knowledge criteria mentioned by the manager is about the EU's bureaucratic function, i.e., the position of different people and the changes in their positions that occasionally happens. He follows the daily news and incidents since questions like chloroxide or dangers with nuclear energy and alternative energy sources are usually discussed in the media and people has shown great interest. They check the public opinion in the media to give strength to the proposals given to the Commission. Besides the influence that the unit aims to achieve to change the political rules, another primary goal is to gain financial funds distributed by the EU for different projects.

The manager stated that of the reasons for having a person responsible for political issues in Sweden is to keep alive the contacts with the Swedish politicians engaged in the EU. Since the power of the EU Parliament is increasing, ABB's political unit also is working for close relationships with parliament members from 7-8 EU countries which have mutual interest in questions like energy politic and environment. The task is to gain support not only in the Commission, but even in the EP and the CM. The effort is always accommodated with engagement in social meetings. According to the managers the social investment is necessary in both periods before and during negotiations. For R&D project for example, these contacts have both continuity and sporadic natures. It intensifies when there is or will be a project. These contacts, manager explained, sometimes take another shape as politicians are periodically replaced and contacts become delivered to new ones. They were to collect information about these politicians' political values.

ABB is a well reputed international firm and is one of the biggest companies in Europe. This facilitates social contacts and increases reliability in the proposals. At the time of interview, Percy Barnevick, the former Managing Director of

ABB, was the chairman of the Competitive Advisory Group in the EU. This naturally facilitated the negotiation of the ABB's proposals. The role of ABB for its high technology products and declaration of the social responsibility in terms of employment or environment and future vision, has strengthened the position of the ABB's political unit. When the political issue has a general nature and is for the benefits of several competitors, then ABB acts in branch organisation. In Euroelectrics all the competitors work together to propose general future plans for nuclear power energy. External organisations having general utility in the political issues are R&D organisations, universities and media that are used by the ABB's political unit to strengthen the argument.

The group in Brussels spends 50% of their time to collect information and also to inform groups and units related to the questions and 50% of the time is devoted for external meetings and discussions. According to the manager, the relationships with these organisations and social contacts with politicians are necessary, but it is the specific knowledge on market, industry and technology that are the basis to affect political decision. One major task of the managers in the unit is to identify and explain the socio-political benefits of the proposals. In the case of Success-story 95, for example, the technical solutions together with political and socio-economical applications of the proposal made that ABB succeeded to receive 1,5 billion (ECU) from EU funds. The manager explained that it was because of these and the position of ABB's managing director in EU's political organisation that the firm received such a fund.

3. Ericsson

At the end of 1990, by the increasing political role of the EU in telecommunication market, Ericsson decided to establish a unit in Brussels. The main task of the unit is to collect information and influence on strategic questions of; a) liberalisation of telecommunication (TELC) market which started at the end of 1980s; b) merging and acquisitions rules for TELC companies, and c) harmonisation of TELC product standards, for example, if a product is tested in Sweden, it has to be accepted in other EU countries. One person with experience on foreign political affairs became responsible and he co-operates with 10-20 market coordinators / experts in Sweden. To develop a proposal the manager involves those experts who have relevant technical and market knowledge. The manager's political task is; a) relationships with EU's political units, i.e. contact with politicians, treatment of political issues, and also supervision of the political decisions on TELC market in countries like USA; b) mobilise resources in Ericsson when a political proposal or decision is under treatment.

For each question the manager deals mainly with specific political section of the Commission. For telecommunication and treatment of the product and future telecommunication market with DGXIII; DGI for international branch, for industry in general with DGIII, for competition custom duties with DGIV and DGXXI. The political members of the committees lack detail knowledge on TELC market and technology, and are thus dependent on Ericsson and other companies in this field. Ericsson's technical knowledge in, for example, IPR, made the Commission to ask the company to co-operate and give technical suggestion.

The manager studies official journals, financial times and cover reports on IT. This duty takes more than 15% of the manager's time. Some duties have social nature, for example, engagement in formal social arrangements and meetings, specifically those which are arranged for people from TELC. But the manager explains that these contacts mainly activate when a political issue becomes under question, i.e., there is a problem of continuity in the contacts. The time spent for social and official meetings is 50% and for the phone calls is 10-15%. The crucial factor lies in his and colleagues' technical and his market knowledge when explaining problems and suggesting solutions. Accordingly, the manager is to gain information about the questions like; the needs of the customers, competition rules, custom duties and new political suggestions and decisions.

The name of Ericsson as a big International firm together with an established social contacts facilitates to initiate an issue. The concept of GSM which has more than 50% of the TELC market and the technical development of mobile phone which has now become more adapted to the consumers' need, are well known by the political members. These elements facilitate negotiations for questions like technical standards for sub-contractors and future development of products and market. Since the committees may also involve competitors, the more technical and market knowledge a company has to convince the committees' political members, the more influence they can have on the content of the proposal suggested by the committees to the Commission and the parliament.

When a decision stands in benefit of several companies, then they build an ad-hoc group and involve branch organisations in Brussels to give strength to the proposal. Competitors in the TELC market can, for example, co-operate temporarily for political questions like liberalisation and state subsidises. The case of ITA (Transatlantic Business Dialogue) for example, which was to eliminate the custom duties for IT-products between USA and EU, involved all the competitors in Europe to work together to influence on politicians for new custom rules. A committee with 30 people from different countries was established. The committee engaged political groups, branch organisations and experts from firms like

Ericsson and Nokia. The result presented by representatives from DGXIII and DGI to the parliament and council of ministers and finally led to the political decision between the USA and EU.

Discussion

As described in the cases, firms undertook different managerial behaviour. MNEs' committed political activities to gain specific political support. The reasons that the firms proceeded in a certain manner, as explained in the cases, was depended upon the firms' commitment and knowledge. However, the results will now be discussed in more detail under three different themes: a) the commitment and knowledge in terms of the political investment and experience, b) the variety in the behaviour of the firms' 'political product'; c) product generation activities of the firms.

Political Investment and Experience

As illustrated in Table 1, all the investigated firms recognised political activities as a critical part of their market interaction. The three MNEs had several years of experience in political matters. This commitment covered not only Brussels, but even other European countries. SAS and ABB, for example, had organised groups and people in several foreign countries to affect the politicians. The three cases illustrated how political units in their relationships with EU politicians mobilised internal and external resources to affect the political decision. The investment for a unit in Brussels and other countries were claimed to be necessary to come closer to the political actors.

Table 1: A summary for the Firms Political Behaviour.

	Three International firms
Major questions	The major issues varied from deregulation, liberalization and harmony in the rules
Organization for political action	There was a differences among these firms, SAS and ABB had more than 10 involved for political issues, Ericsson had 1 in Brussels and more than 10 in other countries
Place of Actions	For all three firms was mainly Brussels, Nordic countries
Forms of behaviour	They chose 2 different types of behaviour, Alone, and Ad-hoc with competitors
Major source in EU	All the three firms were concerned with the Committees in Commission and Parliament

One crucial factor in interaction with political actors was related to the firms' progress in the internationalisation process, i.e., which level of business internationalisation they have reached and their international market involvement. The three MNEs had made large direct investments in several foreign countries. The cases illustrate that, the more progress the firms had in their internationalisation of business activities, the more advanced was their political commitments (Hadjikhani et al 2012). Beside this, there was also a relationship between the firms' business and political commitments. The higher business commitment of three firms became as an idiosyncratic investment leading to, for example, reputation (Anderson and Weitz, 1992) which affected their political relationships. As the three cases show, a higher level of business commitment induced to the gain of a more idiosyncratic affects on the political interaction.

Heterogeneity in the Behaviour

Companies are generally seen in studies as homogeneous units constrained by the governments (Jansson et al., 1995). Our cases illustrate a completely different picture. The three MNEs had heterogeneous offensive influential strategies. Their activities were aimed at influencing decisions before they were decided upon. Cooperation, negotiation tactics were used to overcome results as suggested by Ghauri et al (2012). The discussion in the cases also reveals the fact of specificity in the management behaviour of the firms. Each of the three MNEs, had specific question and the task was to gain specific political support. The aspect of specificity is different than what is proclaimed by studies in risk (Miller 1992, Ting 1988 and Shubik 1983) or firm/state interdependency (Egelhoff 1988 and Porter 1986). These firms managed their relationships differently as suggested by Elg et al (2012). As illustrated in Table 2, they had for example, different types of political questions, different administrative commitment and they were connected to different groups of actors.

Table 2: Firms' behaviour in relationships with political units.

	Three international firms
Commitment	Concerning resources devoted to manage the political relationships; the firms had a high foreign political organisational and social commitment, idiosyncratic investment.
knowledge	The firms have a high knowledge on how the rules will affect the firms' business operation. For their earlier experience in dealing with similar issues they had high earlier political knowledge, high social and technical knowledge. Further they had a high knowledge on institutions and high knowledge on specific questions. They could see the heterogeneities in the political agendas and who are involved.
political actions	The firms knew that they have to manage the relationship otherwise, as they stated the costs of adaptation could be high. Therefore, their major task was to influence. Political interactions with Swedish and foreign political actors in Brussels and other countries, interaction with other technical and legal units, were the means to reach such an aim.

The major effort of the managers was to find out and understand the new rules and make change in organisation or bureaucratic procedures. As internationalisation process models (Johanson and Vahlne 1977, 1990 and 2009) have proposed, the resource and knowledge capacities created hinders to move from adaptation to influence. The MNEs made big commitments in several foreign countries to influence the political actors in Brussels. No matter if the rules had general or specific nature.

Political Product

Our study indicates to a crucial fact that the relationships were 'question' related. For each political suggestion, the political units needed information from experts and others in the society. The relationships activated for a particular political question and for new questions the political units in Brussels activated another relationship. A crucial issue that comes forth is the aspect of product generation. That is, generation and exchange of political ideas which could convince a number of political actors, -'selling an idea'. The fundamental task for the firms was to propose a technically and socially appropriate product to the committees. The more genuine was the idea in satisfying the EU's political units and their norms,

the more specific was the political support that they gained. The product also needed to satisfy social and economical groups connected to the political actors. Thus, they were to produce / generate an idea- and sell it to the EU's politicians and their connected groups.

The committees and Commission members had shortcomings in technical knowledge required to generate ideas which could reflect the needs of business and social groups. This made them dependent to the MNEs' and their specialists having such a competence. The matter of influence of these firms in the interaction with political actors was not only related to technological competency. The big enterprises, beside the organisational commitment in Brussels, also had created a group of technicians in Sweden, for example, ABB had more than 10 people assigned to give technical assistance.

The view of political product originally divides the entire market activity into two different but interwoven products (Ghauri et al 2012; Boddewyn 1988). One is the business product which is produced in interaction with business actors and the next is the political product which is produced in interaction with political actors. The outcome in the latter one can be influenced or adapted accordingly. The political outcome is attractive for MNEs for several reasons. It creates winners and losers (Hadjikhani et al 2012; Alt and Chrystal 1983), and can reduce the organisational or marketing costs. Lack of activities to provide unique product makes the political actors to be coercive.

Conclusions

The study gives some indications to argue that there is a mechanism of parallel existence of the two processes of business and political internationalisation. While the process of commitment in business internationalisation is explained by the level of involvement i.e., from export to direct investment (Johanson and Wiedersheim-Paul 1975), the process of commitment in political market is identified from adaptation to influence. Internationalization starts from local commitment to gain information to the stage of influence on foreign market's political environment. The study also pinpoints the firms' management activities which can apparently be divided into business and political markets. The political activities are an essential and distinguishable part which supplements the business activities particularly in the EU context. As the cases illustrate two markets are complementary and proceed side by side. As an outcome of ideocyncratic relationships, the commitments in both markets diffuse and affect the relationships in

each market. The higher the international business commitment, the bigger is the firm's legitimacy among people and political actors in the foreign markets and the more influence will the firm gain (see figure 3). The higher is the influence, the more privileged is the firm in its business activities. Followingly, while some studies confer to homogeneous (Miller 1992) or unidirectional impacts of the governments (Ghauri and Cateora 2010; Kogut 1991) and some others concern the economic model for dyadic view (Boddeyn 1988, Ring et al.1990, and Jacobson et al., 1993), this study provides a different dimension. Following the role of specificity in the network, the variety in the management behaviour is explained by the differences in the firms' commitment and knowledge in the network.

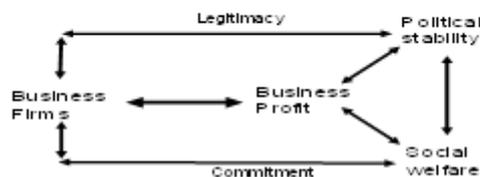


Figure 2: MNE gaining legitimacy

Contrary to studies such as, Boddeyn (1988) and Janson et al., (1995) the paper discusses influence on decisions before they are decided and not after. The act of influence, either by political actors' shortcomings or acquisition of the actors receptiveness, is explained to be connected to the aspect of the specificity in the business and political actors' relationships. The more political knowledge and commitment an enterprise has, the more influence it gains and the more specific support it can receive. On the other hand, the low level of political knowledge and commitment leads to low influence and enterprise will realise the relationship as coercive. Further, distinguishing political market from business market leads to another conclusion which concerns the aspect of political product. In gaining specific support from political actors the management function of the business actors is generation of product which can be sold to political actors. The uniqueness in this product can be explained by the management ability to incorporate the business resources with the needs of political actors and others in the political system (see figure 3).

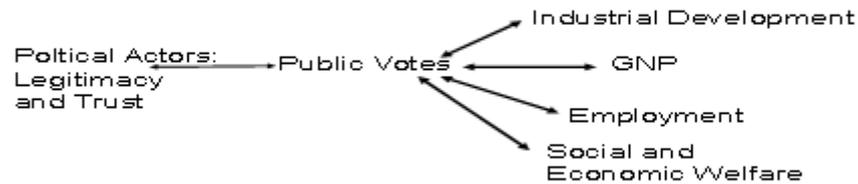


Figure 3: Political actors gaining legitimacy

Network defined for this study is a set of actors -enterprises, media, governments, specialists; public opinion- related to one another in various exchanges. The interaction of these elements is explained to have a loose network (Weick 1979; Orton and Weick 1990). Contrary to industrial network (Ford 1990; Axelsson and Easton 1992), the network in this study is contingent upon a situation in which position of political actors is not stable and the nature and values of the connected actors are changing. More than 30% of the managers' time was devoted to know political actors' positions, new comers and new ideas released in the media, political actors and even competitors' political activities. The incessant commitments on new, e.g., social relationships is one managerial devices that keep the relationships alive. In this respect another conclusion can be discussed for cases where a network is weak and the business and political actors are related to each other by 'gatekeepers' or intermediaries. In such a case, the relationship loses its mutuality and authority rules force for adaptive or coercive behaviour.

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9. International Entrepreneurship And Dynamic Capabilities: Theoretical And Empirical Issues

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Introduction: Emerging Issues In The International Entrepreneurship Studies

Studies on international entrepreneurship have grown impressively in the past decade, challenging the boundaries dividing different fields of research and raising new questions to researchers. This contribution is based on the premise that not every small firm or new venture engaged in some international activity is *per se* an International Entrepreneurial Organization (IEO), according to the concept proposed by Zucchella, Scabini (2007). An entrepreneurial organisation is defined by attributes such as proactiveness, innovativeness, risk taking. This concept also holds for the international entrepreneurial orientation of an organisation (Covin, 2013). As a consequence, an entrepreneurial organisation should not be defined simply by being newly born and/or small, but by organisational processes corresponding to the above mentioned entrepreneurial attitudes, which may also emerge in terms of the ability to reconfigure its capabilities dynamically. According to this premise, this paper aims at:

- identifying and modeling the capabilities that can define an entrepreneurial organisation;
- comparing domestic versus internationally-oriented firms. The goal is to analyse their entrepreneurial characteristics in a dynamic capabilities perspective;
- investigating if international ventures and – in particular - international new ventures show more pronounced entrepreneurial characteristics than the others. This would support the idea that going international is: on one hand a symptom of an organization's entrepreneurial attitude, and/or that going international fuels processes of innovation/reconfiguration, on the other.

The internationalization of the firm has been a widely explored field of research in the last decades. Until the 1970s the dominant issue in IB research was represented by the motivations for international expansion and the application of economic theory paradigms to this emerging field (Hennart and Larimo 1998; Kose *et al.* 2003; McDougall *et al.* 1994). The gradual spread of behavioural models enriched and complemented this perspective and provided a better understanding of the internationalization process. The advent of a resource-based view (RBV) in strategic management studies (Penrose, 1959; Wernerfelt, 1984; Barney, 1991; Peteraf, 1993) further enriched the analysis of internationalisation and of the international firm itself from the perspective of strategic and organizational resources and processes (Dhanaraj and Beamish, 2003). The RBV coupled with entrepreneurship approaches (Venkataraman, 1997; Dana and Wright, 2004; Etemad, 2004) proved very promising in interpreting the international expansion of small and infant firms. The behavioural models of firm internationalization fitted in this general theoretical framework and could be integrated in the overall strategic management of the firm.

In this framework, an important piece of literature is represented by the dynamic capabilities approach (Teece, Pisano and Shuen, 1997) – based on an RBV vision of the firm and its strategic management - which might prove useful in the perspective of international entrepreneurship. In the recent years, a number of studies explored the interplay between these two streams (e.g. Autio *et al.* 2011; Khalid and Larimo 2012b; Mort and Weerawardena 2006). These contributions highlight the relevance of this topic, inviting researchers to conduct more empirical work over the foundations and peculiarities of dynamic capabilities within international new ventures. This research falls within a dynamic capabilities framework and addresses international entrepreneurship issues based on these conceptual premises.

From the pioneering work of Schumpeter (1934) up until the recent surge of studies on entrepreneurship, one of the expressions of entrepreneurship has been identified in the decision *per se* of foreign market entry. Nowadays, a number of firms recognize that this decision is more a necessity than an option due to the saturation of domestic markets, the need to react to global competition, the need to reach an adequate market size in niche-oriented productions, the necessity to follow customers or suppliers moving abroad (Hennart and Larimo 1998; Zucchella *et al.* 2007). In addition, the phenomena of regional integration have made the foreign market concept less clear-cut than before. This entails that the frontier of entrepreneurship in IB is now more complex to define. The foundations of entrepreneurship - opportunity seeking, risk assumption, innovativeness and proactiveness - need a reinterpretation in the new global market framework on one side

(Oviatt and McDougall 2005), and a better definition in terms of managerial processes driving an effective international entrepreneurial orientation on the other side (Al-Aali and Teece 2014). Our contribution explores the dynamic ability/attitude of IEOs to renew their competences and organizational structure.

The paper is structured into two main parts: the first one provides a review of literature comparing different theoretical frameworks, from International Business (IB) to International Entrepreneurship (IE), exploring their connections with the Resource-Based View (RBV) and the Dynamic Capabilities (DC) approach. It also provides a simplified theoretical modeling of a dynamic capabilities framework as applicable to international ventures, in order to evaluate their entrepreneurial attitude. The second part reports the preliminary results of an exploratory survey on a sample of 209 small firms, 33 of which have international activities, typically exporting.

This contribution does not deal with the antecedents of international entrepreneurship, which would involve an analysis of the experiential and psychological traits of entrepreneurs, but instead focuses on the outcomes of international entrepreneurial behaviour in terms of development of dynamic capabilities at the firm's level of analysis. The purpose is to relate internationalization attitude and performance to the firm's ability to mobilize resources and to develop and reconfigure its capabilities and core-competences.

International Entrepreneurship And Dynamic Capabilities

The theories of multinational firms argue that some enterprises are international because of certain firm-specific capabilities and routines that they possess and accumulate (Kogut, 1984; Leonard-Barton, 1992 (Tan and Mahoney 2006). On the other hand, theories of international entrepreneurship argue that some firms become international because of entrepreneur-specific capabilities (Knight and Cavusgil, 1995; Bloodgood and et al., 1996). This paper argues that the latter view is not alternative but complementary to the former, since entrepreneur-specific capabilities influence the firm's strategic management and organizational architecture. This process generates a progressive consolidation of capabilities and organizational routines stemming from the resource mobilization and integration worked up by the entrepreneur since the new venture's start up. Firm's and entrepreneur's capabilities are thus different but closely related constructs, in the sense that they are reciprocally influencing dimensions, especially in the case of small firms. In small firms the founder/entrepreneur and his/her management team shape managerial processes from inception. This paper builds on the prem-

ise that not every small firm or new venture with some international activity is *per se* an international entrepreneurial organization, but that the latter is defined by processes of dynamic reconfiguration of capabilities, driving international orientation through continuous innovation.

The importance of entrepreneurs has been dealt with in many IB studies, and the findings reveal a positive relationship between the entrepreneurs' international attitude, orientation, experience, network and their firms' international development (Preece et al., 1998; Ibeh and Young, 2001; Westhead et al., 2001; Kuemmerle, 2002; Andersson, 2003; (Al-Aali and Teece 2014; Keupp and Gassmann 2009). In this perspective, the entrepreneur's as well as the intrapreneur's ability to learn and to develop an appropriate network is crucial to access complementary knowledge and to innovate (Khalid and Larimo 2012b). The ability to develop organizational routines supporting a dynamic, continually renewing international entrepreneurial orientation -at the organisational level- has a critical importance.

Shane and Venkataraman (2000, p. 27) define the study of entrepreneurship as the, "examination of how, by whom, and with what effects opportunities to create future goods and services are discovered, evaluated, and exploited". McDougall and Oviatt (2003, p.72) state: "International Entrepreneurship is the discovery, enactment, evaluation, and exploitation of opportunities - across national borders - to create future goods and services". Both definitions focus on opportunity discovery, evaluation and exploitation but leave the area of the managerial processes through which this takes place underexplored.

In the perspective of this paper, the entrepreneurial behaviour at the firm level is rooted in some managerial processes, which enable a firm not only to be entrepreneurial at one point in time (for example, at inception) but also to maintain this characteristic over the years.

These definitions of international entrepreneurship are consistent and can be fruitfully complemented with the dynamic capability framework (Teece, Shuen, Pisano, 1997) that emphasizes the ability of the firm to "anticipate the future", instead of passively following market signals or imitating the behaviour of leading firms. This framework postulates a proactive approach of the organisation, aimed at creating new unexploited/unexplored opportunities, while continuously renewing its core competences.

Larimo and Khalid (2012b) investigated the role played by dynamic capabilities and intangible assets for the survival and growth of international new ventures. Their findings show that the performance of these organizations is positively re-

lated to the ability to continuously renew a firm's assets and capabilities since inception. However, this study focuses on the 'resource' dimension and it doesn't consider the role of managerial processes underpinning the dynamic capabilities.

In another study, Larimo and Khalid (2012a) obtain similar outcomes by exploring the role of alliance and international collaborations, especially in terms of inter-firm learning. In particular, the Authors argue that the value from alliance knowledge may be created not only through exploitation and augmentation of the extant knowledge bases, but also through entrepreneurial orientation in accessing and integrating strategic resources owned by the interacting partners. Similarly, Mort and Weerawardena (2006) contributed to the IE research by investigating the impact of networking capabilities in international new ventures and argued that dynamic capabilities are crucial in this context. Autio et al (2011) developed a cognition-based model aimed at understanding origins and evolution of capabilities in new ventures. It extends the capability development and learning implications of internationalization to the fundamental character of organizing processes in start-ups.

Fladmoe-Lindquist (1996) studied the dynamic capabilities of international new ventures based on franchising-based business models. It offered further confirmation regarding the circumstance that international entrepreneurs require capabilities which are different from those needed in the domestic context. Most importantly, this study showed that these capabilities have to be dynamic: the development of the international franchising capability is not a one-time event and requires continuous learning. Further investigations comprising a more diversified sample in terms of business models are needed in order to generalize this evidence.

The survey of Filatotchev and Piesse (2009) provides intriguing insights regarding the role of path dependence in shaping the dynamic capabilities of entrepreneurial firms with international attitude. The Authors examine the interplay among R&D, exporting and growth of newly listed firms and found that R&D intensity is an important antecedent factor for the internationalization of sales. At the same time, the R&D activity is path dependent and depends upon the firm's portfolio of resources, especially the intangible ones. These outcomes are very important in the framework of this study, but once again the process dimension of dynamic capability remains under investigated.

This concise literature overview shows that - despite the growing attention to the topic - there is still much to say regarding the foundations and the role of dynamic capabilities in international entrepreneurial organizations. Recent contributions

confirm that this is emerging as one of the most debated topics (Al-Aali and Teece 2014; Casillas and Acedo 2013).

The contribution of Teece and Al-Aali (2014) expands the Oviatt-McDougall framework regarding sustainable international ventures by including the dynamic capability paradigm. In particular, it incorporates entrepreneurship and capabilities into MNE theory and applies them to foreign direct investments of new ventures. This model emphasizes that international entrepreneurs must be able to: sense an opportunity abroad, seize it by addressing the foreign market or by tapping new inter-firm networks and finally they should transform the organization as the foreign environment requires and allows. The Authors make a fundamental step forward but recognize that the understanding of these dynamics is at the beginning and that they have just initiated this process.

An increasing number of studies explore the relationship among international business and entrepreneurship (Jones *et al.* 2011; Keupp and Gassmann 2009; Onetti *et al.* 2012; Oviatt and McDougall 2005). The ability to internationalize successfully in foreign markets is a function of the internal capabilities of the firm (Autio *et al.*, 2000; McDougall *et al.*, 1994, Zahra *et al.*, 2000 Al-Aali and Teece 2014; Eriksson *et al.* 2014). Performing global firms show timely responsiveness, flexible organizations, high managerial capabilities to innovate and develop networks of resources and knowledge (Teece, 2000; Nooteboom, 2002).

The importance of internal capabilities is rooted in evolutionary economics (Winter, 2003). The ability to sustain innovation and create new knowledge leads to the development of capabilities, consisting of competences and organizational routines. Their knowledge base, capabilities, financial resources, equipment and other physical resources are the main drivers that older firms use to perform in foreign markets, whilst young firms lack them. New ventures rely mostly upon intangible knowledge-based capabilities in approaching foreign markets. Capability-based resources are particularly important to SMEs, because they are poor in tangible resources and deal with different environments in different countries around the world (Knight and Cavusgil, 2004).

Long-run performance depends not only on a firm's resources and capabilities *per se* but – most importantly - on the firm's ability to mobilize and combine external and internal resources dynamically, to pursue incremental as well as radical innovations, to reconfigure and transform capabilities continually in non-imitable configurations.

We argue that dynamic capabilities are at the core of not only sustainable competitiveness and performance, but also – in particular - of international expansion.

Being international implies the access to a wider potential market, but – most importantly - also a global space where to mobilize complementary resources for innovation and long-run performance. Teece, Pisano and Shuen (1997) defined dynamic capabilities “as the firm’s ability to integrate, build, and reconfigure internal and external competences to address rapidly changing environments” (ibid. p. 516). The firm’s competitive advantage is thus a highly dynamic one, and requires continual innovative reconfigurations as well as resource mobilization, that take into account path dependence and market positions (Leonard-Barton, 1992).

In this perspective, entrepreneurship and dynamic capabilities share the common issue of resource mobilization and combination as fundamental activities.

Firms compete for resource acquisition, integration and development before competing for final product/service markets (Penrose, 1959) and, according to Wernerfelt (1984: p. 171), “for the firm, resources and products are two sides of the same coin”. Firms build their resource positions by either acquiring different kinds and combinations of external resources, or developing firm-specific resources internally or partnering with other firms for joint development and sharing. In this perspective, the Resource-Dependence Theory (Pfeffer, Salancik, 1978) argues how crucial it is for the firm to be able to reach external resources by adopting network strategies. Indeed, each firm is dependent on some external scarce resource, thus the entrepreneur’s ability to create partnerships – by using both formal and informal inter-firm co-ordination systems – becomes an important managerial process, especially in the case of small firms with a poor stock of internal resources.

A number of International Entrepreneurship studies refers to *international new ventures* (INVs) and/or *born-globals* (Oviatt and McDougall, 1994; Madsen and Servais, 1997 Gabrielsson *et al.* 2008; Zucchella *et al.* 2007), which are viewed as typical expressions of International Entrepreneurship and sometimes as International entrepreneurship *tout court*. These firms are defined as business organizations that, from inception, seek to derive a significant competitive advantage from the use of resources and the sale of outputs in multiple countries. Being international/global from inception (or within the first three years of life) is the expression of international entrepreneurship, according to many studies. According to another perspective, international entrepreneurship is about the entrepreneur’s traits and attitudes, education, skills and experience, which seem to be important variables to explain how an entrepreneur interprets and shapes managerial processes to lead his/her firm. The objective (firm) and subjective (entrepreneur-intrapreneur) IE perspectives are closely inter-twined, since the entrepreneur’s

traits determine the new/small venture characteristics. The same holds true for the case of intrapreneurship in large corporations.

Oviatt and McDougall (1995) point out that having a global vision since the firm's inception is probably the most important characteristic associated with Born Global entrepreneurs. They argue that the creation of international ventures stems from the ability of the founders to see market opportunities in a cross-national context. Founders generally develop this ability in their earlier career. Prior international activities lead to building capabilities including language skills and the ability to access national networks of contacts that grant access to resources. McDougall et al. (1994) and Madsen and Servais (1997) all concluded that the entrepreneurs' background and experience have a major influence on the emergence of Born Globals. According to the above mentioned theories, a high level of absorptive capacity coupled with a good inter-firm network can facilitate the access to, and the interpretation of information and opportunities.

In this work, we propose to consider the issue of international entrepreneurship in a different perspective. We do not consider every international firm or every INV/born global firm as an expression of IE: we are going to try and identify the IEO driving processes, building on parameters of international resource mobilization and capabilities reconfiguration. This perspective is based on a RBV framework and borrows some cornerstones from the dynamic capabilities model.

Being international in a resource mobilization and capabilities reconfiguration (i.e. entrepreneurial) perspective involves regarding foreign markets as wider spaces (widening the opportunities arena) where to acquire and combine external resources and to find partners for joint resource development (Khalid and Larimo 2012a). In a knowledge management view, this wider potential combinations of ties is likely to generate novel combinations and improve the potential of cognitive distance optimization, thus fueling innovation and knowledge development (Denicolai *et al.* 2014). In this perspective, internationalization is no longer just a matter of exploiting the home base knowledge and competitive advantage (Kuemmerle, 2002), but more of exploring new knowledge and of dynamical capabilities reconfiguration (Autio *et al.* 2011).

Table 1 shows a collation of the different theoretical frameworks that can prove influential for international business and international entrepreneurship studies. Our contribution aims at highlighting the importance of the dynamic capabilities approach for a better understanding of entrepreneurial activities and their international growth. In applying the dynamic capabilities framework to IE, the analysis should focus on international entrepreneurial organisations. Table 1 also underlines that – according to this contribution – the different theoretical approaches

considered focus on a common core activity, i.e. resource mobilization. The above-mentioned entrepreneurial effort shaping an international venture is thus observable in this perspective.

International entrepreneurship is here expressed as an activity of international resource mobilization. The other side of the same coin is to express IE in terms of the wider global opportunities the entrepreneurial venture is scouting.

Table 1. Different theoretical frameworks compared

Theoretical frame	Resource-based	Dynamic capabilities	Entrepreneurship	International entrepreneurship	IE in a dynamic capabilities frame
Level of analysis	Organizations	Organizations	Entrepreneurs, intrapreneurs, startups	International entrepreneurs; Born global startups; Corporate entrepreneurship within MNEs	<i>International entrepreneurial organizations</i>
Unit of analysis	Resources	Processes Positions Paths	Individual; Entrepreneurial Team; startup;	Resources and attributes of entrepreneurs, intrapreneurs and BG firms	<i>Learning via partnerships with players and clusters which are geographically dispersed; Coordination of resources and capabilities at the global level; Transformation of capabilities over time, by taking into account country-specific factors</i>
Core activity	Resources mobilization and combination	Resources mobilization and reconfiguration-transformation	Opportunity discovery and evaluation. Exploitation through resource mobilization	Opportunity discovery and exploitation, integration and coordination at international scale	<i>Resource mobilization, reconfiguration and transformation at international scale; Opportunity creation and exploration at international scale</i>

Source: adapted from Zucchella, Scabini (2007)

Processes, Positions And Paths In International Ventures

In this paper we apply a dynamic capabilities approach to small and medium international firms. We do not refer only to International New Ventures or Born Global Firms, identified as new ventures showing an early and fast process of internationalization. We rather refer to any organization able to mobilize, to coordinate and to reconfigure resources and capabilities in order to perform internationally. Ability to address international changing environments rapidly and proactively, is seen as an entrepreneurial act. The assumption of this paper is that entrepreneurs, especially in SMEs, develop dynamic capabilities at the firm level to better perform internationally.

According to the above-mentioned literature analysis, one of core activities of International Entrepreneurial Organisations (IEOs) is resource mobilization by either external acquisition or internal development. The opportunities discovered/created through resource mobilisation are then exploited, but new opportunities also arise.

The superior ability to integrate and to reconfigure internal and external resources, both domestic and international, leads the firm to develop dynamic capabilities and core-competencies. The dynamic capability framework proposes three dimensions of analysis: positions, processes and strategic paths available (Teece, Shuen, Pisano, 1997). Our contribution focuses on managerial processes, meaning: inter-firm learning, coordination at the international scale, transformation of capabilities according to emerging opportunities and country-specific factors. It is consistent with the above-proposed literature review, which highlights the “overlap” between the entrepreneur’s and the firm’s dynamism, especially in terms of managerial processes. Moreover, the ability to reconfigure activities to changing environments is a significant issue in the International Entrepreneurship agenda.

In this entrepreneurial approach to the dynamic capabilities model, the role of entrepreneurs is of central importance (Al-Aali and Teece 2014) for the following reasons: (a) they can have special skills for the co-ordination and integration of internal and external activities at the global level, resources and technologies; (b) entrepreneurs/managers can also shape learning processes within the firm and through global ties; (c) they can have the ability to reconfigure the firm’s asset structure in terms of product portfolio and/or internal processes. These arguments are particularly consistent in the case of small firms and new ventures where decision-making is driven by one or a few persons, and the entrepreneur has a crucial role (Bloodgood et al., 1996; Westhead, et al., 2001). It is generally affirmed that in small firms entrepreneurs and managers often tend to coincide, but similar considerations may be valid also for corporate entrepreneurship and intrapreneurship.

Finally, dynamic capabilities allow the firm to perform internationally in terms of profitability and growth. Performance can change the previous stock of internal resources - and the need for external ones – thus giving rise to a new cycle.

This study focuses only on the process dimension of the dynamic capabilities, by remitting the analysis of the role played by the resource portfolio and path dependence to further studies. The goal is to highlight the nature of international activities as a 'process' in itself. Thus, we investigate the international behaviour as an idiosyncratic class of processes embracing three main forms: '*learning*', by exploiting interactions with players at the global level, '*coordination*' of resources and activities which span across diverse countries, '*reconfiguration*' of capabilities in order to cope with diversity and dynamism of production/suppliers (upstream) and customer needs (downstream) in the international arena.

Figure 1 illustrates the conceptual framework, which builds on international resource mobilization and drives long-term performance through managerial processes supporting entrepreneurial orientation.

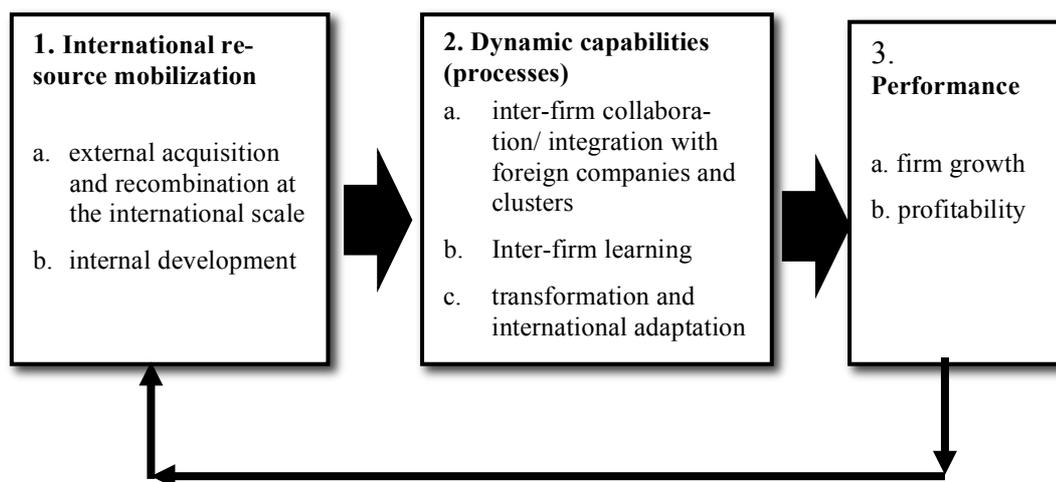


Fig. 1. From resource mobilization to dynamic capabilities: theoretical framework for IEOs

Source: Adapted from Zucchella, Scabini (2007)

An Exploratory Survey: Preliminary Results

This section shows the outcomes of an exploratory survey aimed at investigating the relationship among the key processes of dynamic capability and the international entrepreneurship orientation of SMEs. This empirical analysis is limited to univariate statistics and correlations. We think that - due to the complexity of the topic - an in depth exploration of these aspects is a fundamental premise for regression studies and other econometric analyses which we remit to further research.

The construct of “entrepreneurial organization” has been operationalized by the key variables identified in the previous section and summarized in the model portrayed in figure 2. International resource mobilization has been considered in terms of both external and internal acquisition. The former was split in intra and extra European acquisition. The decision to split the global marketplace into these two main areas depends on the phenomena of regional integration, which reduces trade barriers and transaction costs within macro-regional areas. In this perspective, extra-EU resource mobilization involves higher uncertainty and cognitive distance.

Internal Development refers to the attitude of investing in R&D and the eventual consequent patenting of innovation. We are aware that other forms of internal development exist, but we decided to test this specific one for its relevance to the perspective of the paper's assumptions and research questions, as well as for its conceptual importance in entrepreneurship and innovation studies. We expected international ventures to select resources all over the world to better perform in international markets, while developing more resources internally than just utilizing local ones, especially in terms of the resources and capabilities that are more oriented to produce innovations.

The sample consisted of 209 Italian SMEs, and is representative of the Italian population of small firms in terms of industries, size, age distribution and domestic/international orientation. Hence, the firms were mostly very small, belonging mainly to traditional (apparel, footwear, food and beverages) or specialized (mechanic parts and machinery, specialized chemistry) industries. They did not belong to local clusters/districts to avoid biases on international orientation deriving from access to local externalities and knowledge, and from pure imitative behaviour.

A questionnaire of 20 questions (one question for each variable) covering a wide number of issues (governance, strategy, products, organization, inter-firm relationships) was sent to 800 firms. The valid respondents were 209 (valid redemption rate: 26%). Only 33 firms, all belonging to the manufacturing industry, declared some international activity, namely exporting, sometimes coupled with importing. Both results are compatible with the characteristics of the sample, where micro-firms predominate and address their sales primarily to the local market. In this framework of micro and small firms,¹² exporting usually constitutes the prevailing form of internationalization. This confirms that exporting is the predominant international activity of small firms (Tesar and Moini, 1998; Westhead, Wright and Ucbasarab, 2001; Audretsch, 2002; Kundu and Katz, 2003 (O'Cass and Weerawardena 2009)).

The empirical survey aimed at highlighting the traits of the 33 international ventures, which developed an international orientation in a rather hostile environment, characterized by the absence of the shared facilities - service centres, export consortia, firm associations, logistic facilities, specialized public institutions, etc. - that traditionally sustain the foreign market expansion of small firms in local clusters and districts (Maccarini, Scabini, Zucchella, 2003). Moreover, in local economies lacking density and medium or large-sized players there are no opportunities of imitative behaviour (follow-the-leaders) in approaching foreign markets.

Hence, the empirical survey aimed at profiling the 33 small international players compared with the wider control group of the remaining 176. The 33 firms were then contacted for in-depth interviews lasting two hours each, in order to deepen the questionnaire issues and to profile them better. The interviewed persons were the entrepreneurs who usually coincided with top managers.

We did not automatically assume that these 33 small firms were examples of international entrepreneurship, according to this research premises. This gave us the opportunity to verify whether the entrepreneurial activities -in these small international ventures evaluated through the lenses of resource mobilization and dynamic capabilities - are actually more outstanding than in locally-oriented firms, and which of the many expressions of entrepreneurship appear to be more important in international firms. Among international firms special attention was devoted to the sub-group of firms which experienced internationalization in their first three

¹² According to EU definition, by micro or small firm we mean firms with less than 50 employees.

years of life (International New Ventures). Table 3 shows the profile of the overall sample we have analyzed and shows data regarding the International Resource Mobilization. The Column “All International Firms” refers to the firms in the sample that reported at least 5% of total sales as foreign, in order to exclude marginal and occasional exporters.

At a first glance, international firms are bigger and older than domestic ones. This evidence is consistent with the idea that international firms are more structured than domestic-oriented ones. In geographical terms, measured by intra and extra-EU export, international firms show a prevailing European orientation. Within international ventures, firms that internationalized within three years from inception are bigger than the overall sample and younger than the other international firms; in terms of export geographics, INVs are more extra-EU oriented. These characteristics can be considered as proxies of stronger entrepreneurial orientation, since international firms – and notably INVs – are more growth-oriented. Besides being more growth-oriented, INVs confront themselves with international markets from the beginning, thus exposing themselves to the risks and uncertainties associated with both the liability of newness and the liability of foreignness, and are more prone to engage in extra-EU operations. According to these findings, entrepreneurship seems to be a process, not just a status, and lies in organizational activities expressed in terms of resource mobilization and dynamic capabilities.

The variables referring to international resource mobilization are external acquisition and internal development. Comparing the two groups, international firms mobilize more external resources, in terms of international suppliers and business partnerships, than the control group (non-international firms). On one side, it is consistent with the idea that international ventures have a wider economic opportunity seeking activity than domestic ones – including the sourcing side of their business. On the other side, it may also mean that international sales enlarge the resource mobilization process of firms. The two aspects - firm push and market pull - are closely intertwined.

International firms also show a higher than average number of patents and more frequently invest in R&D than their locally-oriented counterparts. This also implies that internal resource mobilization is higher in international ventures and they are characterized by stronger innovativeness.

These considerations seem to confirm that international ventures are better at mobilizing resources than non-international ones. In particular, table 2 shows that this is more evident in international new ventures.

Table 2. Firms' profiling and International resource mobilization (univariate analysis)

	Control group (non international firms)		All international firms		International firms (>3)		International new ventures (<3) INV		
	Mean	Stand dev	Mean	Stand dev	Mean	Stand dev	Mean	Stand dev	
1) Size	4.30	7.35	26.55	31.45	24.20	35.38	30.15	31.34	
2) Age (years)	18.82	12.74	30.30	22.43	35.60	23.82	22.15	18.00	
3) Export intensity (%) [absolute value]	/	/	34.73	28.41	35.88	28.71	32.96	29.01	
4) Export precocity (months)	/	/	120.89 (10 years)	193.35	226 (≈19 years)	223.06	8	13.45	
5) Export scope [relative value]	% intra EU	/	74,43	24.27	77	26.33	69	21.45	
	% extra EU	/	25,57	5.69	23	11.04	31	21.50	
6) External acquisition	% intra EU	0.98	6.39	10.88	23.37	9.95	20.73	12.31	27.79
	% extra EU	0.06	0.77	2.61	7.70	1.85	4.70	3.77	10.99
7) Internal development	R&D (%) *	7.39	0.26	57.58	50.19	60.00	0.50	53.85	0.51
	patents (n°)	0	0	0.85	2.05	1.35	2.51	0.08	0.27

- size: number of employees;
- age: number of years from inception;
- export intensity: percentage of foreign sales to total sales;
- export precocity: number of months between inception and first export activity;
- export scope: ratio intra to extra-EU sales;
- external acquisition: geographical location of suppliers and business partnerships;
- internal development – R&D to sales;
- internal development – patents: number of patents for each firm in the past 10 years.

This stock of mobilized resources has to be combined and integrated to reach competitive advantages. The adopted theoretical framework refers to the dynamic capabilities pattern (box 2 of figure 1). The focus is on the process perspective, according to the theoretical analysis proposed in section 3. Networking, learning and reconfiguration are the three core processes considered by our framework.

We operationalized the *networking process* by adopting two variables:

- a) number of formal co-ordination agreements, such as consortia, joint ventures, etc.; this variable highlights the attitude of the entrepreneur to formal agreements for networking;
- b) size of alliance portfolio in terms of number of ties with other domestic or international firms;

The *learning process* was operationalized as follows:

- c) knowledge stock, in terms of frequency of training courses for employees and education degree of the latter;
- d) knowledge variety, in terms of variety of product portfolio and internal processes (operations, work organization).

Finally, we analysed the *reconfiguration/transformation* variable focusing on:

- e) degree of renewal of the product portfolio in the past 3 years;
- f) degree of renewal of organizational processes and routines in the past 3 years.

Each variable - from “a” to “f” - was measured by respondents using a Likert scale (1-4). Table 3 presents the link between these variables and export intensity. As mentioned above, in this explorative survey we limit the multivariate procedure to a correlation analysis. We adopted the 'Spearman' coefficient in order to manage different types of variables and - above all - to consider the categorical ones. This approach led to create four intervals for the percentage of exports (“Total”, “intra-Europe” and “extra-Europe”), which were originally quantitative continuous variables (range: 0-100). Though this conversion is less accurate, it allows to compare export intensity with the other variables in terms of a Likert scale. Table 3 also shows the Likelihood ratio chi-square as a control value for the Spearman correlation reliability.

Each variable is significantly correlated to the export performance of international firms, except for knowledge variety. An explanation is that these small international firms focus on a few products or only one. Results confirm that entrepreneurship as measured by dynamic capabilities is correlated to international orientation. The outcomes are more significant for export towards European countries than to extra EU. We could not collect sufficient data to deepen the correlation between export intensity of International New Ventures and dynamic capabilities. Table 4 and Figure 2 shows a focus on managerial processes and performance.

International New Ventures seem to possess stronger dynamic capabilities than other firms. Nevertheless, this evidence needs to be confirmed by more sophisticated statistics.

Tables 3 – 4 and Figure 2 show the outcomes on the performance of firms (box 3 of figure 1) in terms of profitability and growth. We adopted a subjective measure to operationalise the performance. The respondents were asked to evaluate their performance in terms of growth and profitability. The reason for this choice is the traditional difficulty of small and micro firms to provide detailed information about their economic and financial performance. On the other side, officially available economic indicators about small firms cannot be considered sufficiently reliable, since these firms do not submit complete financial statements, from which one could calculate the usual performance ratios and assume them as a proxy for firm success. In addition, subjective measures makes it possible to align the entrepreneurial effort with a self-evaluation of one's entrepreneurial effort results.

While empirical results confirm a significant correlation between growth and export intensity of international firms, mainly for intra-EU sales, profitability shows a significant correlation only for extra-EU sales (Table 3). This evidence suggests that dynamic capabilities support the international expansion only in the long run, whilst their role in the short term is uncertain. It is consistent with the mainstream literature (Helfat *et al.* 2007). Further investigations and regression analyses are needed to confirm this assumption.

Table 3. Dynamic capabilities and Performance (Spearman correlations)

		International firms (% of total export)		International firms (% intra EU)		International firms (% extra EU)	
		correlation	<i>chi-square</i> (<i>al-pha</i> =0.05)	correlation	<i>chi-square</i> (<i>al-pha</i> =0.05)	correlation	<i>chi-square</i> (<i>al-pha</i> =0.05)
		Inter-firm collaboration/ integration (networking)	<i>a. formal agreements</i>	0,2114	<0,0001	0,2222	0,0011
	<i>b. number of ties</i>	0,3772	<0,0001	0,3770	0,0002	0,3282	<0,0001
Artikkeli I. earning	<i>c. knowledge stock</i>	0,3489	<0,0001	0,3507	<0,0001	0,2783	0,0008
	<i>d. knowledge variety</i>	0,1433	0,0670 (rejected)	0,1466	0,1594 (rejected)	0,1011	0,8485 (rejected)
Artikkeli II. reconfiguration/ transformation	<i>e. products</i>	0,3062	0,0060	0,3095	0,0054	0,2563	0,0181
	<i>f. processes</i>	0,2063	0,0402	0,2118	0,0111	0,1624	0,0529 (rejected)
Artikkeli III. performance	<i>g. growth</i>	0,1220	0,0030	0,1273	0,0062	0,0851	0,0003
	<i>h. profitability</i>	- 0,0012	0,0008	0,0007	0,0464	0,0285	<0,0001

On the other hand, dynamic capabilities applied to International New Ventures affect both growth and profitability (Table 4 and Figure 2), but as mentioned earlier, these results need to be statistically verified through further analyses, such as a regression study, on a broader sample.

Table 4. Dynamic capabilities and performance (Likert scale: 1 to 4)

	Non international- al firms (NIF)	All international firms (AIF)	International firms >3 (IF)	International new ventures <3 (INV)	a) Variables used
Networking	2.53	2.73	2.85	2.65	<i>number of nodes</i>
Learning	2.27	2.97	2.85	3.15	<i>frequency of training courses and education</i>
reconfiguration	1.87	2.67	2.65	2.69	<i>innovation (process- product mean)</i>
profitability	2.24	2.27	2.25	2.31	<i>profitability in the past 3 years</i>
Growth	2.54	2.82	2.7	3	<i>growth in the past 3 years</i>

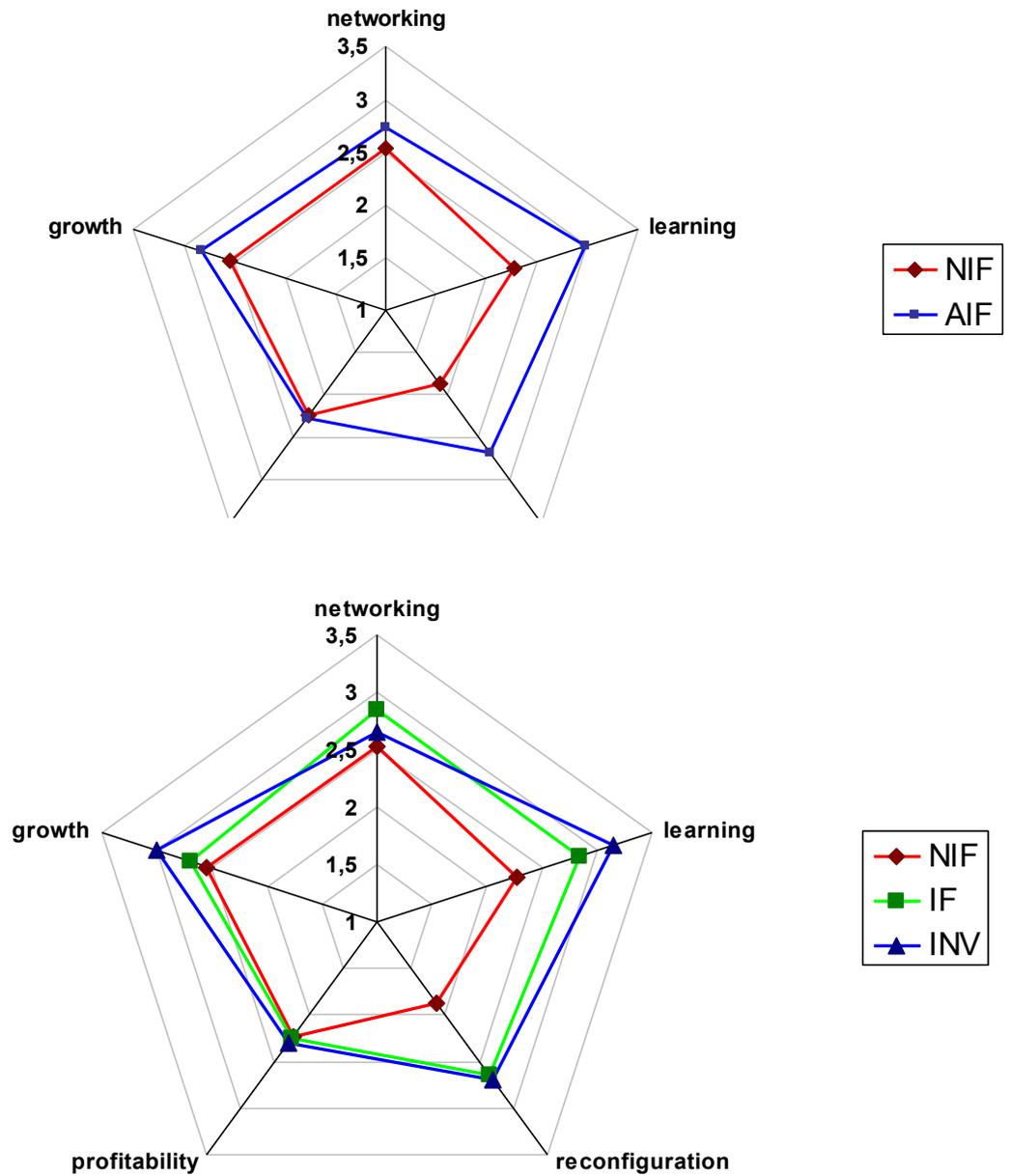


Figure 2. Radar graphs of dynamic capabilities and performance in the overall sample

Conclusions: Entrepreneurship Is A Process, Not A Status

International entrepreneurship is actually a challenging domain of studies for both theoretical and empirical surveys. Its boundaries with International Business are not always clear. Going international is not *per se* an act of entrepreneurship: this idea arose in a period of separated markets and high barriers to foreign market entry, while nowadays we observe phenomena of regional integration, market interdependence, and lower barriers to entry. The study of international entrepreneurship requires an appropriate theoretical framework, which has to be grounded on managerial processes qualifying entrepreneurship, such as resources mobilization and combination, and the development of dynamic capabilities. Entrepreneurship is a process, not just a status, and as such requires dynamic attributes. It requires that the original entrepreneurial effort to give birth to a new venture is maintained over the years, promoting proactiveness and innovativeness through capabilities reconfiguration.

The dynamic capabilities approach applied to International Ventures can capture the attitudes of IEOs to perform internationally. In particular, in this study, the learning, networking and propensity to innovate capabilities are correlated to the international performance of small firms. Our results confirm that in international firms the entrepreneurial orientation, as above measured, is higher than in locally-oriented ones. The former are better at mobilizing international resources as well as at dynamically reconfiguring capabilities to respond/anticipate changes in their environment.

Moreover, our findings support the idea that International New Ventures – reported in literature as an expression of International Entrepreneurship – associate performance (in terms of both growth and profitability) to dynamic capabilities more than other firms. In order to deepen these findings others statistical analyses are needed. Nevertheless, our empirical findings offer intriguing elements in order to design further investigations.

The main limit of this exploratory study lies in the characteristics of the sample: the nature and structure of small firms and the size of the sample – only 33 international firms over 209 were identified - do not allow us to sufficiently generalize our outcomes. Notwithstanding these limitations, we think that the theoretical model supporting our empirical survey can be applied to different types of firms, in terms of size and age. The managerial implications of our study are potentially important, because the model draws the attention of managers and entrepreneurs on critical processes for long-run performance. Pursuing an international orientation of the firm is, on one hand, grounded on such processes and, on the other hand, supports them by enlarging the firm's opportunities to mobilize and commit

resources, and improving its access to complementary knowledge and learning processes.

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10. International Entrepreneurship Research In Finland: Past, Present, And Future

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Emergence of international entrepreneurship as a research field

The origins of the international entrepreneurship (IE) research stream date back to the late 1980s or early 1990s, specifically to the articles by McDougall in 1989 and Oviatt and McDougall in 1994 (e.g., Autio 2005, Jones, Coviello & Tang 2011). These articles are considered to have laid the cornerstone of IE research by distinguishing international entrepreneurial firms from other types of firms and by bringing together the fields of entrepreneurship and international business to provide an explanatory theoretical foundation to the emerging phenomenon.

Researchers in the two fields developed interest in the same phenomenon but came from diverse backgrounds. In the 1990s, international business research acknowledged the acceleration of the SME internationalisation process (Hedlund & Kverneland 1984, Christensen 1991). Additionally, and partly parallel to this, entrepreneurship research went through an evolution of theory development. This resulted in the introduction of numerous partly overlapping concepts, such as born-global, born exporter, international new venture, global start-up, infant multinational, early, rapid, accelerated, born, and instant international (e.g., Lindqvist 1991, Rennie 1993, Oviatt & McDougall 1994, 1995, Knight & Cavusgil 1996, Quelch & Klein 1996, Madsen & Servais 1997, Majkgård & Sharma 1999, Coviello & McAuley 1999, Preece et al. 1999). These concepts created a need to revise and renew internationalisation theories as the growth of these companies clearly deviated from the traditional incremental theories from the 1970s and early 1980s (Wright & Ricks 1994, Liesch et al. 2002, Etemad & Wright 2003, McNaughton 2003, Kuivalainen et al. 2007). In entrepreneurship research the focus broadened to include successful family enterprises, networks and internet-based companies, and ethnic and gender-related entrepreneurship, including economic, regional, and national considerations as well as ethic, societal, and developmental entrepreneurship (e.g., Blackburn & Kovalainen 2009). Interestingly,

during the first years of IE research, interest lay mainly in small new ventures, but later the field expanded to international entrepreneurial behaviour in larger organisations (Jones et al. 2011).

During the 2000s, interest in IE increased, and its position as a separate field of research has institutionalised; dedicated journals have been published, the number of IE studies has been accumulating exponentially due to the ever broadening research scope, and international conferences – or IE tracks in larger conferences – have been introduced. However, IE has been criticised for still being a fragmented and inconsistent field of research in its infancy (Keupp & Gassmann 2009). This has prompted IE researchers to establish and legitimize their field by presenting definitions and concepts, delimiting the focus and aim of the field, and reviewing the progress of the field (e.g., McDougall & Oviatt 2000, Coviello & Jones 2004, Oviatt & McDougall 2005, Jones et al. 2011).

During the past decades, Finnish researchers have been important contributors in the field, but to our knowledge their role has never been systematically assessed. Therefore, the aim of this chapter is to describe the state of international entrepreneurship research in Finland. The study is based on publicly available data (literature reviews, websites, and citation databases, such as Google Scholar). The analysis of prior research on international entrepreneurship relies heavily on the work by Jones et al. (2011). That review was chosen as the starting point of our analysis for three reasons: (1) it is recent, (2) it is comprehensive as it covers 20 years of work and a substantial number of publications ranging from well-established journals to those that are emerging, and (3) the data collection process has been described in a highly systematic and transparent manner, thus enabling replication and verification of the process. The chosen review is also very clear on defining the field, which seems to be a common problem in earlier reviews (Keupp & Gassmann 2009). To define the field, the review combines two definitions: the first formal definition of the field (McDougall & Oviatt 2000) and a later revised definition (Oviatt & McDougall 2005). Thus, it focuses on studies that:

- combine ‘innovative, proactive and risk-seeking behavior that crosses national borders and is intended to create value in organisations’ (McDougall & Oviatt 2000: 903)
- focus on ‘the discovery, enactment, evaluation and exploitation of opportunities – across national borders – to create future goods and services’ (Oviatt & McDougall 2005: 540).

This approach has two notable benefits. First, it enables the inclusion of an important sub-branch of international entrepreneurship – comparative international entrepreneurship – which focuses on cross-national comparisons of domestic en-

trepreneurship (cf. Terjesen et al. 2013). Second, the definition does not contain any limitation on company size, which has been considered a problem by some scholars (Keupp & Gassmann 2009).

Contribution of Finnish researchers in international entrepreneurship research

Scale and scope of research

In their domain ontology and thematic analysis, Jones et al. (2011) examined international entrepreneurship research conducted between 1989 and 2009. They identified 323 journal articles in international entrepreneurship, of which 36 articles had at least one Finnish-based author (the authors are later referred to as ‘Finnish researchers’). These authors were either:

- Finnish researchers who have an affiliation with a Finnish university
- Finnish researchers who have an affiliation with an overseas university
- Non-Finnish researchers who have a tenured position at a Finnish university.

The share of the Finnish contribution in international entrepreneurship research (11% of the articles) can be considered substantial, not least because of the small size of the country and academic community. Multiple reasons for the notable role of Finnish researchers in the field exist. First, the country holds a long and well-established tradition of research in the internationalisation of the firm since the 1970s and the early works of Professor Reijo Luostarinen. Continuing on this path has been a natural progression for the Finnish academic community. Second, for the success of a small open economy such as Finland, internationalisation and in particular the emergence of international new ventures has always been decisive. Third, the strong role of knowledge-intensive industries in Finland created a favourable research environment for investigating early and rapid internationalisation.

In their thematic analysis, Jones et al. (2011) classified the IE journal articles into eight categories based on their primary theme. With the exception of studies in cross-cultural comparison, Finnish researchers had contributed to all of them. However, their contribution to studies on venture type (11 articles), internationalisation (9 articles), and networks and social capital (6 articles) is more noticeable than to the other categories. *Venture type research* is the oldest thematic area in IE literature and it focuses on the characteristics and survival of international new ventures or provides comparisons of venture type (Jones et al. 2011). Interestingly, one of the early articles of this stream, by Jolly et al. (1992), has a Finnish

author. The Finnish contributions are approximately one-fifth of this stream, and many of the studies originate from the former Helsinki School of Economics (today, Aalto School of Business). The second category – *internationalisation* – is more diverse, but the overarching theme is the patterns and processes in internationalisation or influences on it (Jones et al. 2011). This is the largest category in the review, but even here, Finnish researchers are involved in about one-tenth of the articles. The study with the most significant impact in this category is by Autio et al. (2000). It is noticeable that most of the Finnish contributions in this category are written by teams of researchers from multiple universities, particularly from Lappeenranta and Turku. *Networks and social capital* has also been a theme that has been of interest for Finnish researchers. This theme includes studies that focus either on networks and relationships, network processes, or social capital (Jones et al. 2011). Although this theme is considerably smaller than the two others mentioned, the contribution of Finnish researchers is noticeable – one-fourth of all studies are conducted by Finnish researchers. One of the most impactful studies in this category is the one by Yli-Renko et al. (2002).

Visibility and impact

Finnish authors have not only been active publishers in the field of international entrepreneurship but their work has also had an impact on later research in the area. In order to give an overview of the visibility and impact of Finnish scholars in the field of international entrepreneurship, we collected citations from Google Scholar. To find the studies that have had the most impact, we used the Jones et al. (2011) review as a starting point for our data collection. This was complemented by additional searches related to the works of well-known Finnish scholars in the field. Altogether, citation information was searched for 40 IE Finnish researchers. We found 16 journal articles by Finnish authors that had had a substantial impact on the field, i.e., they had received more than 100 citations in Google Scholar (Table 1).

Table 1. Examples of the most cited¹³ IE articles by Finnish authors (names of Finnish authors in bold)

Article (Finnish author(s) in bold)	Citation index*
Yli-Renko H., Autio E. & Sapienza, H.J. (2001) Social capital, knowledge acquisition, and knowledge exploitation in young technology-based firms. <i>Strategic Management Journal</i> , 22(6-7), 587–613.	1655
Autio E. , Sapienza, H.J. & Almeida, J.G. (2000) Effects of age at entry, knowledge intensity, and imitability on international growth. <i>Academy of Management Journal</i> , 43(5), 909–924.	1542
Sapienza, H.J., Autio E. , George, G. & Zahra, S.A. (2006) A capabilities perspective on the effects of early internationalization on firm survival and growth. <i>Academy of Management Review</i> , 31(4), 914–933.	529
Arenius P. & Minniti, M. (2005) Perceptual variables and nascent entrepreneurship. <i>Small Business Economics</i> , 24(3), 233–247.	497
Yli-Renko H., Autio E. & Tontti, V. (2002) Social capital, knowledge, and the international growth of technology-based new firms. <i>International Business Review</i> , 11(3), 279–304.	393
Jolly V.K., Alahuhta M. & Jeannot J-P. (1992) Challenging the incumbents: How high technology start-ups compete globally. <i>Strategic Change</i> , 1(2), 71–82.	348
Arenius P. & De Clercq, D. (2005) A network-based approach on opportunity recognition. <i>Small Business Economics</i> , 24(3), 249–265.	303
Holmlund M. & Kock S. (1998) Relationships and the internationalization of Finnish small and medium-sized companies. <i>International Small Business Journal</i> , 16(4), 46–63.	254
Zahra S.A., Korri J.S. & Yuc J.F. (2005) Cognition and international entrepreneurship: implications for research on international opportunity recognition and exploitation. <i>International Business Review</i> , 14(2), 129–146.	235
Jantunen A., Puumalainen K., Saarenketo S. & Kyläheiko K. (2005) Entrepreneurial orientation, dynamic capabilities and international performance. <i>Journal of International Entrepreneurship</i> , 3(3), 223–243.	222
Gabrielsson M. & Kirpalani V.H.M. (2004) Born globals: How to reach new business space rapidly. <i>International Business Review</i> , 13(5), 555–571.	211
Nummela N., Saarenketo S. & Puumalainen K. (2004) A global mindset—a prerequisite for successful internationalization? <i>Canadian Journal of Administrative Sciences</i> , 21(1), 51–64.	209
Korhonen H., Luostarinen R. & Welch L. (1996) Internationalization of SMEs: inward-outward patterns and government policy. <i>Management International Review</i> , 36(4), 315–329.	169
Gabrielsson M. , Kirpalani V.H., Dimitratos P., Solberg C.A. & Zucchella, A. (2008) Born globals: Propositions to help advance the theory. <i>International Business Review</i> , 17(4), 385–401.	167
Kuivalainen O., Sundqvist S. & Servais P. (2007) Firms' degree of born-globalness, international entrepreneurial orientation and export performance. <i>Journal of World Business</i> , 42(3), 253–267.	161
Saarenketo S., Puumalainen K., Kuivalainen O. & Kyläheiko K. (2004) Dynamic knowledge-related learning processes in internationalizing high-tech SMEs. <i>International Journal of Production Economics</i> , 89(3), 363–378.	115

From the viewpoint of the development of the field, it is extremely positive that the articles with the most impact have been written by several authors and that the authors represented different institutions in Finland. It should also be noted that a considerable number of recent journal articles have not yet reached the limit of 100 citations, but given the positive trend in the number of citations, they are expected to meet the criterion in the near future. This indicates that the Finnish IE community continues to have a significant impact in the field of international entrepreneurship.

¹³ Citations accessed through Google Scholar 28–29 April 2014.

Clusters of international entrepreneurship research in Finland

In the beginning of the new millennium, there was strong academic and political interest to develop business-related research to meet the requirements of the turbulent and changing international environment.¹⁴ As a result, the two major Finnish funding organisations, the Academy of Finland (AF) and the Finnish Funding Agency for Innovation (TEKES), launched a series of research programmes that focused on management competence both in domestic and in international settings. The first in the series of programmes was ‘The Finnish Companies and the Challenges of Globalisation Research Programme (LIIKE)’, which was launched by the Academy of Finland in 2000 and implemented from 2001 to 2004. The second phase of the programme (LIIKE2) was implemented from 2006 to 2009. Besides supporting research from different fields of management competence, both programmes also aimed to develop research environments and support collaboration and coordination of scattered research groups.

In parallel with the programmes of the Academy of Finland, TEKES had its own business-related programmes. While they emphasized the importance of close industry collaboration more than the AF programmes did, the research themes were partly overlapping. The LIITO programme (Innovative Business Competence and Management) funded research projects over the period of 2006–2011. The key themes were related to value creation in business/to customer, creation and management of business growth, and strategic management of business. Additionally, TEKES had more specific programmes for selected industries, such as SERVE (Pioneers of Service Business) and VerSO (Vertical Software Solutions).

Interestingly, all programmes also funded research projects that were related to international entrepreneurship (Table 2). Many of these projects were collaborative efforts between two or three universities, thus increasing collaboration among IE researchers who were affiliated with different institutions across the country.

¹⁴ The description of the research programmes and the list of projects are based on information collected from the websites of the funding organisations as well as three programme reports (Ihanamäki & Lehtimäki 2011, Jönsson et al. 2006, Liike 2014, Liike2 2014, Serve 2014, Tuominen et al. 2014).

Table 2. Examples of IE-related research projects with external funding

Name of the project	Responsible universities	Funding organisation/programme
Born Globals – International from inception	Aalto University, University of Vaasa	TEKES/LIITO
GLOBAL – The successful internationalisation of SMEs	Hanken, Åbo Akademi, University of Vaasa	Academy of Finland/LIIKE
Global Network Management	Lappeenranta University of Technology, Turku School of Economics	TEKES/LIITO
INVnet – International growth of SMEs	Hanken, Lappeenranta University of Technology, Turku School of Economics	Academy of Finland/LIIKE2
Steps in multicultural software business globalisation: Models, methods, and practices towards increasing competitiveness (STEP)	University of Jyväskylä	TEKES/VerSO
SwGrowthMan – International growth strategies of the Finnish software industry	Aalto University	TEKES/VerSO
Value chain management of internationalising software firms	Lappeenranta University of Technology, Turku School of Economics	TEKES/VerSO
Venture capital activities of Finnish Growth SMEs. A challenge for owner-managers and venture capitalists	Turku School of Economics	Academy of Finland/LIIKE

One reason for the formation of the IE research consortia is probably the lively network among researchers. An important and beneficial platform for this collaboration has been the biennial Vaasa International Business Conference, chaired by Professor Jorma Larimo, which has brought together all Finnish IB and IE researchers since 1991. Regular meetings with national and international colleagues have planted the first seeds of joint research projects.

Most of the research projects also involved doctoral students, which meant that a growing number of students received long-term funding for their studies. At the same time, the Finnish Graduate School in International Business (FIGSIB) offered full-time research funding for approximately six students annually. Both of these developments were the key reasons why the number of doctoral dissertations related to international entrepreneurship increased substantially during the last decade. In fact, more than 25 doctoral theses related to international entrepreneurship were defended in Finnish universities between 2004 and 2014 (Table 3).

Table 3. Examples of doctoral dissertations on international entrepreneurship in Finnish universities 2004–2014¹⁵

Doctoral student name	Topic of thesis	University	Publication year
Almarri Jasem	Social entrepreneurship in practice: the multifaceted nature of social entrepreneurship and the role of the state within an Islamic context	University of Oulu	2014
Taina Eriksson	Dynamic capability of value net management in technology-based international SMEs	Turku School of Economics	2013
Galkina Tamarra	Entrepreneurial networking: Intended and unintended processes	Hanken	2013
Kaartemo Valtteri	Network development process of international new ventures in internet-enabled markets: service ecosystems approach	Turku School of Economics	2013
Sepulveda Fabian	The development and performance of international new ventures: links between networks, entrepreneurial orientation, and firm performance	Aalto University	2013
Torkkeli Lasse	The influence of network competence on the internationalization of SMEs	Lappeenranta University of Technology	2013
Volchek Daria	Internationalization of small and medium-sized enterprises and impact of institutions on international entrepreneurship in emerging economies: the case of Russia	Lappeenranta University of Technology	2013
Hallbäck Johanna	International new ventures as a multifaceted phenomenon - Towards a contingency approach in international entrepreneurship	University of Vaasa	2012
Kohonen Tenho	Tiedonsiirto ja -luonti metallialan osatoimitajien kansainvälistymisessä: lähtökohtina sosiaalinen pääoma ja oppimiskulttuuri	Aalto University	2012
Segaro Ethiopia	Internationalization of family small and medium sized enterprises: Impact of ownership, governance and top management team	University of Vaasa	2012
Juho Anita	Accelerated internationalisation as a network-based international opportunity development process	University of Oulu	2011
Kontinen Tanja	Internationalization pathways of family SMEs	University of Jyväskylä	2011
Kuuluvainen Arto	Dynamic capabilities in the international growth of small and medium-sized firms	Turku School of Economics	2011
Sasi Viveca	Essays on resource scarcity, early rapid internationalization and born global firms	Aalto University	2011
Söderqvist Anette	Opportunity exploration and exploitation in International New Ventures: A study of relationships' involvement in early entrepreneurial and internationalisation events	Hanken	2011

¹⁵ The listing of the doctoral theses has been compiled based on the information available on the websites of the respective universities.

Vapola Terhi	Battleship strategy: exploring the management of global innovation constellations in high technology industries	Aalto University	2010
Heinonen Laura	On the pursuit of growth in technology-based companies. The role of public financing in the start-up process of Finnish drug development companies	Turku School of Economics	2009
Khalid Saba	Exploring firm level market knowledge competence and its implications for the speed and success of export expansion: A mixed methodology study from the software industry	University of Vaasa	2009
Paavilainen-Mäntymäki Eriikka	Unique paths. The process of international growth among selected Finnish SMEs	Turku School of Economics	2009
Turunen Helena	The internationalisation of location-bound service SMEs – Resources and networks in Finnish tourism companies	Turku School of Economics	2009
Hätönen Jussi	Managing the process of outsourcing - Examining the process of outsourcing product-development activities in software firms	Turku School of Economics	2008
Ojala Arto	Internationalization of software firms: Finnish small and medium-sized software firms in Japan	University of Jyväskylä	2008
Ruokonen Mika	Market orientation in rapidly internationalizing small companies — Evidence from the software industry	Lappeenranta University of Technology	2008
Renko Maija	Market orientation in markets for technology – Evidence from biotechnology ventures	Turku School of Economics	2006
Vahvaselkä Irma	Strategic behaviour and performance in internationalisation of SMEs	University of Vaasa	2006
Elo Maria	SME internationalisation from a network perspective : an empirical study on a Finnish-Greek business network	Åbo Akademi University	2005
Jantunen Ari	Dynamic capabilities and firm performance	Lappeenranta University of Technology	2005

As both the research projects and accepted doctoral dissertations demonstrate, research in international entrepreneurship is still quite fragmented in a number of Finnish universities. However, there are signs of change; a shift from the early Helsinki-centred research to a number of centres of excellence has occurred. The start from Helsinki was quite natural – Professors Reijo Luostarinen (Helsinki School of Economics) and Erkkö Autio (Helsinki University of Technology) both had strong research groups. However, during the last decade, prominent research groups in international entrepreneurship have emerged in Lappeenranta, Oulu, Turku, and Vaasa, and also the future of Jyväskylä and Kuopio looks quite promising. From the viewpoint of the development of the field, this change is welcome as it guarantees that Finland as a country will continue to have a stronger footprint in the field than its size would indicate.

Future of Finnish IE research

The aim of this chapter was to provide an overview of the state of international entrepreneurship research in Finland. We were very pleased to notice that Finnish IE scholars, coming from the disciplines of marketing, international business, management, and entrepreneurship, have been well represented in the field internationally and that their work has had a considerable impact on the development of the field. Indeed, our state-of-the-art review shows that there is a solid and comprehensive foundation for the future of Finnish IE research.

It seems that Finnish researchers have been following the newest developments of the field closely, or have been ahead of them, and they have been able to earmark certain themes in which their contribution has been particularly noticeable. The competitive advantage that Finnish researchers have been able to develop seems to be sustainable, as their role has become stronger since the early 1990s. Admittedly, Finnish IE researchers have benefited from the supportive research environment as well as public funding for their research efforts, particularly during the last decade. However, the future of IE research in Finland looks promising. Research groups have emerged in a number of institutions, and it can be argued that the Finnish IE community already has ‘critical mass’, which is required to make a contribution. Nevertheless, given the limited resources, this requires that the collaborative efforts continue into the future.

Recent reviews in the field of international business and entrepreneurship point out areas that would be worth investigating. We agree with Jones et al. (2011) that the main focus of future IE research should be in theory development, which would further strengthen the discipline. Interesting research topics may include both underdeveloped and more mature areas of research, but in the IE context, it is important that they capture both academic and stakeholder interest (cf. Blackburn & Kovalainen 2009). We suggest that Finnish IE researchers should consider how their strengths could be optimally combined in order to maximise the benefits of critical mass. For example, Finnish researchers have a strong research tradition in process research, and thus it would be possible to take advantage of this and study internationalisation as a process that combines learning, networking, internal politics, and capability development (cf. Welch & Paavilainen-Mäntymäki 2014). Additionally, Finnish researchers have acknowledged methodological competence on longitudinal context-sensitive research that combines diverse types of data and methods of analysis, something that is called for in IE research (Nummela, forthcoming).

All in all, numerous novel topics in the IE domain wait for scholars to grasp them. Finnish scholars have thus far demonstrated their skills and capabilities in ad-

addressing these topics, thereby rightly obtaining a clear and undisputable position in the international IE research arena. In our opinion, there is every reason to believe that the good work will continue into the future.

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11. Born Global Growth Stages, Survival And Future Study Avenues

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Background

It is extremely important to understand the optimal growth paths firms follow, so startups can rapidly develop to become large global multinational companies. Moreover, it is essential to understand what growth phases and strategies firms should apply along this development to succeed. It should also be noted that research has been limited with understanding these aspects (Gabrielsson & Gabrielsson 2013; Sapienza et al. 2006). Earlier research on the internationalization process of firms has found patterns of how companies proceed in stages towards higher foreign market involvement (Johansson & Vahlne 1977; Luostarinen 1979).

More recently a new type of firm that globalizes rapidly almost from inception has appeared called Born Global and it seems that earlier models are not applicable in explaining this phenomena (Oviatt & McDougall 1994). Born Globals deviate from the traditionally internationalizing firms by suffering from resource scarcity, newness to the market and smallness. These firms seem to be particularly common in small and open economies, in which globalization pressure is high but domestic markets offer limited expansion possibilities. In the management literature, a number of multistage models have been proposed that show predictable patterns in the growth of organizations (Kazanjian & Drazin 1989). We argue that by integrating the results of earlier studies of the life cycles of organizations with the internationalization process and with research on International New Ventures, a better understanding of the growth phases of International New Ventures may be achieved. In this chapter, we will describe the growth paths and phases of Born Globals based on the results of the project. We will also examine the critical decision points, potential survival crises and strategies during growth. Lastly, we will turn to examine which factors influence advancement along growth phases and survival. The article presents the findings of case study research and survey results reported earlier in Gabrielsson and Gabrielsson (2011). This consists of case examples produced by the Born Global growth stages and

survival TEKES project team as well some empirical support based on our survey results.

Main growth paths and phases of Born Globals

There are two main paths available for firms to expand to global markets. A company can choose a Born Global growth strategy; from inception it pursues the global market opportunities outside the home continent. Alternatively, it may rapidly enter nearby markets, but fail to expand to other continents and thus follow a Born International strategy. Also, another path called Born-again Globals is to internationalize rapidly only after a long domestic phase (Bell et al. 2003), but this was not the main focus of this project. In our Finnish survey, 56 percent of rapidly internationalizing firms had used the Born Global path while 44 percent the Born International path. In this research Born Globals were found to evolve through four phases during growth towards large firms: (1) introductory, (2) commercialization and foreign entries, (3) rapid growth and foreign expansion, and (4) rationalization and foreign maturity. (Gabrielsson and Gabrielsson 2009) See Figure 1.

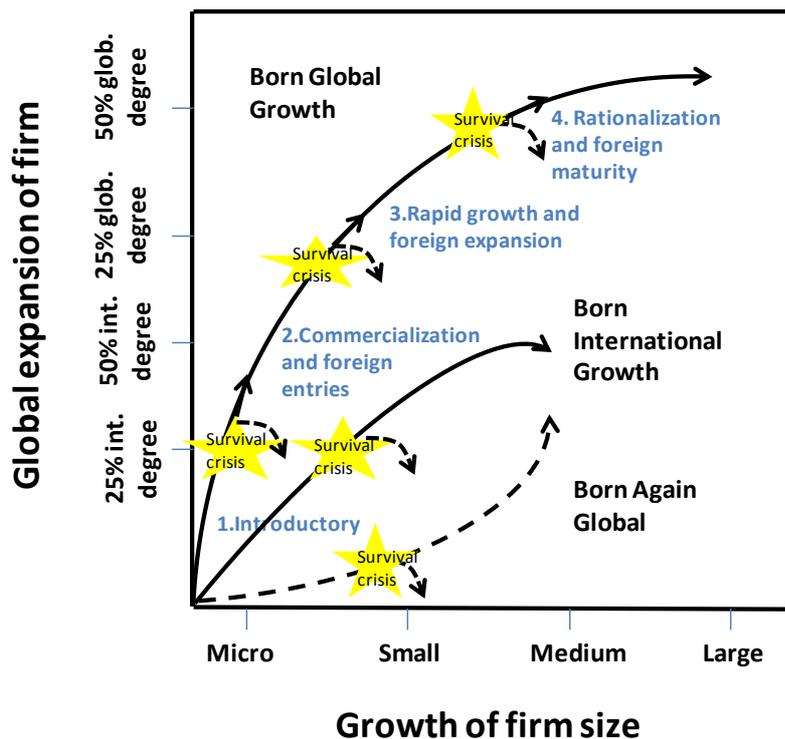


Figure 1. Main growth paths and phases of International New Ventures (adapted from Gabrielsson and Gabrielsson 2009)

In the first phase the primary focus is on developing a commercially acceptable product, securing adequate financing and developing the market. In the second phase the firm makes a number of successful foreign entries and sells products in large volumes. In the third phase, growth is rapid and the firm penetrates existing countries further and expands to new continents. The final fourth phase requires increasing alignment of operations and marketing to be able to reach global synergies. In our survey in Finland, we saw that firms are evenly distributed in these phases and also survival crisis may occur at any phase, but the amount of these seems to be greatest in first phase. Firm size and foreign expansion progressed along the phases. When reaching the fourth phase, firms had achieved sales in nearly 30 countries on average. See also Laukkanen (2011). See table 1.

Table 1. Growth phases of International New Ventures based on the Finnish survey

	1st Phase	2nd Phase	3rd Phase	4th Phase
Share of firms	27,2 %	30,2 %	16,8 %	25,7 %
Number of foreign countries with sales	9,61	9,34	10,21	27,87
Share of firms facing survival crisis	18,2 %	9,8 %	11,8 %	9,6 %

Comparison between Finnish and Swedish Born Global firms

For this article, we have selected cases from Finland and Sweden, which are among the most advanced Born Globals. These cases are selected so that they allow for comparison between countries. As can be seen, all the firms have advanced to phase three or four. Furthermore, they fulfill high internationalization (share of sales outside home country) and globalization (share of sales outside home continent) degrees early on. There were firms from each country that have reached a large size (Vacon, Roxtec) and firms that are close to large (Biohit, Odd Molly), and SME-sized ones (Tectia, Trade Extension). The basic characteristics of these firms can be found in Table 2.

Table 2. Selected Finnish and Swedish Cases

	Vacon Finland	Biohit Finland	Tectia Finland	Roxtec Sweden	Odd Molly Sweden	Trade Extensions Sweden
Foundation	1993	1988	1995	1990	2002	2000
Vision	Global from inception	Global from inception	Global demand surprise	Global from inception	Global from inception	Global from inception
Field of business	Frequency converters	Liquid handling & diagnostic test systems	Security software	Sealing solutions for cables	Fashion apparel	Management software
Size	Large	Close to large	SME	Large	Close to large	SME
Internationalization degree: 3rd year / Now	51% / 79%	90% / 97 %	56% / 96%	91% / 92%	48% / 75%	40% / 60%
Globalization degree: 6th year / Now	35% / 34%	25% / 45%	63% / 72%	36% / 41%	25% / 25%	40% / 60%
Growth phase	Phase 4	Phase 3/4	Phase 3	Phase 4	Phase 3/4	Phase 3

As can be seen in Figures 2 and 3, both Finnish and Swedish firms advance along the phases. During their advancement, they have had to make critical decisions in order to advance to the next phase. Also, many of the firms have run into a survival crisis, which they have had to solve to survive. Interestingly, in some cases they have had to use a retrenchment strategy of taking steps backwards by divesting business and foreign country markets (Tectia, Roxtec). After focusing their business, these firms have again been able to continue global growth.

Turning into the examination of the Finnish cases, it can be seen that all have progressed through the phases reaching either the third or fourth phase. It can be seen that Tectia, now in phase three, has selected the most aggressive strategy by focusing on global expansion rather than increasing the firm size (see also Hashimoto 2011). Biohit has followed similar path but has also been able to increase the firm size to close to large and is now entering the fourth phase (see also Stotzka 2010). Vacon has advanced on both dimensions in a more balanced way and has been able to reach a global status and large firm size, thus clearly placing it in the fourth phase (see also Grönroos 2010). For the examined Finnish firms innovation and networking has been critical for growth. Many firms reported that the most critical decisions for growth were related to patenting innovative products and closing licensing deals. Moreover, the Finnish firms had utilized their

networks in order to expand abroad and establish new foreign operations. (Gabrielsson and Gabrielsson 2013) Two of the Finnish firms had experienced survival crises but been able to overcome them. See Figure 2.

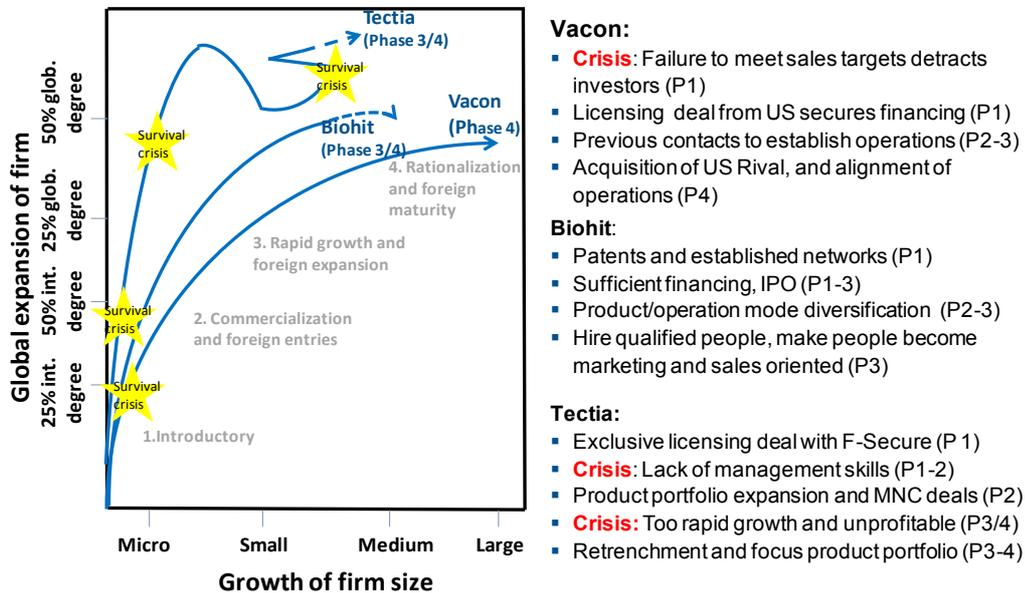
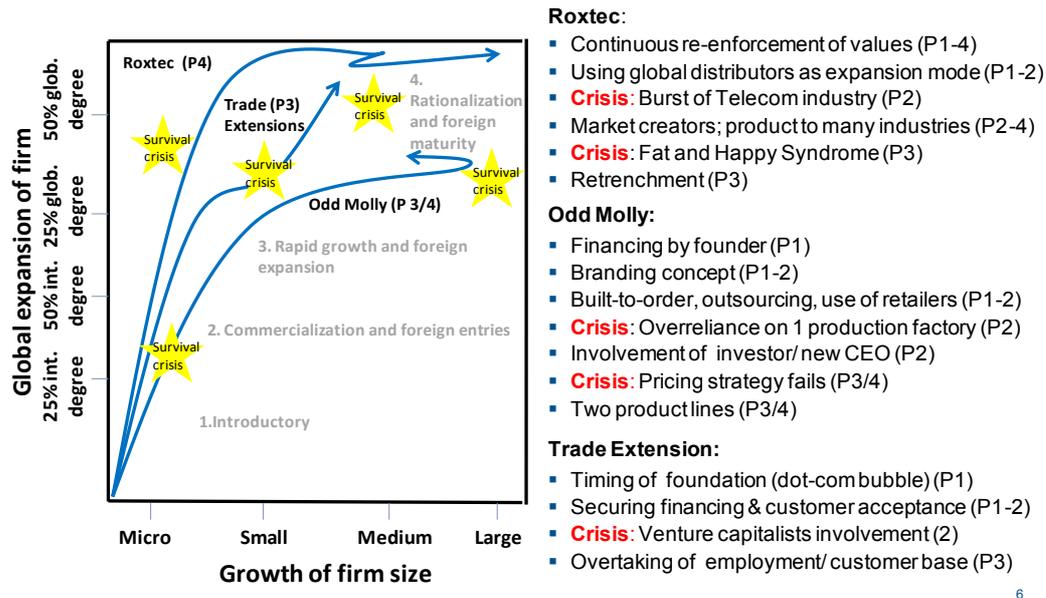


Figure 2. Growth paths, critical decision points and crisis: Finnish cases

When analyzing the Swedish cases closer, it can be seen that here the firms have also progressed through the phases to either the third or the fourth. Roxtec has selected the most aggressive global expansion, but has also been able to increase firm size and advance to the fourth phase. While the two other Swedish cases (Trade Extensions, Odd Molly) have selected a more balanced strategy, they are in phase three or approaching phase four. (See Ilvoranta, 2011). The Swedish case firms' critical decisions points included investments on branding and human resource management. Many Swedish firms emphasized the importance of firm values in achieving growth and an innovative branding concept. All Swedish cases had experienced survival crises. For example, Roxtec had run into a so called 'fat and happy syndrome' due to uncontrollable expansion and an increase of personnel without paying enough attention to effectiveness.



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Figure 3. Growth paths, critical decision points and crisis: Swedish cases

When comparing the Swedish firms to Finnish firms, the following principles appeared to be used more extensively by Swedish firms: (1) Simplicity is important. Many Swedish firms had flat organization and low bureaucracy creating an open and dynamic atmosphere, which increases growth speed and market responsiveness. (2) Soft management is essential. Many Swedish cases showed that competitive advantages are built upon company culture and values that empower employees to strive for growth. (3) Market creation is vital. Early identification of potential markets, creation of new customer needs and investments in branding increase growth.

Growth, operation, and product strategies

When analyzing the growth strategy, it was evident that organic growth was the most frequently used, although partnerships and acquisitions were used to a similar extent. In many cases, several growth strategies were used in parallel. (See also Öhman 2011) In particular, firms that used the Born Global path relied more heavily on partnerships and acquisitions than firms using the Born International path to grow rapidly to global markets.

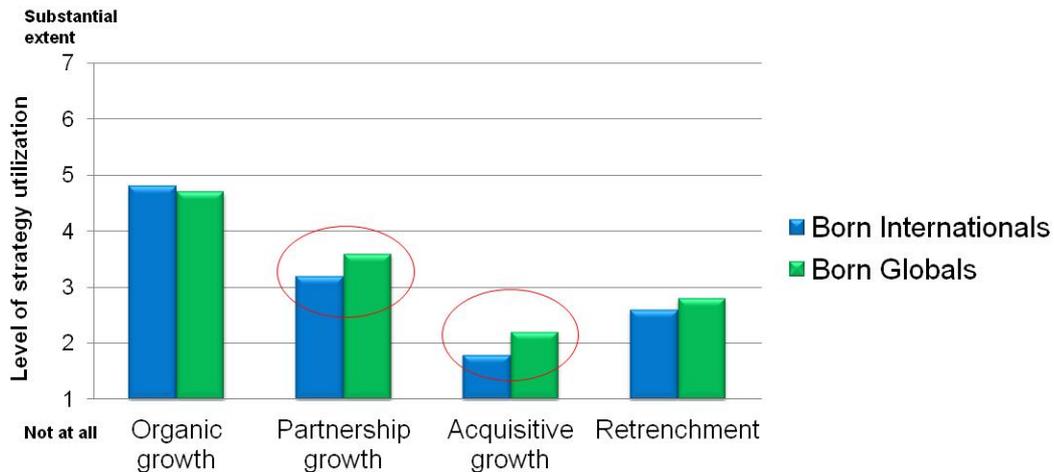


Figure 4. Growth strategy by selected path

An interesting finding was that Born Globals used export modes to a great extent and they were important in all phases. This is understandable given the firms' scarce resources and aggressive growth speed. It could be seen that a firm's own subsidiaries were increasingly established in the fourth phase of growth and the emphasis was on sales subsidiaries instead of foreign R&D and manufacturing units. A highly important finding was that from firm inception, MNCs were utilized as sales channels, and their use increased toward the latter phases. (see also Heikkinen 2011) See Figure 5.

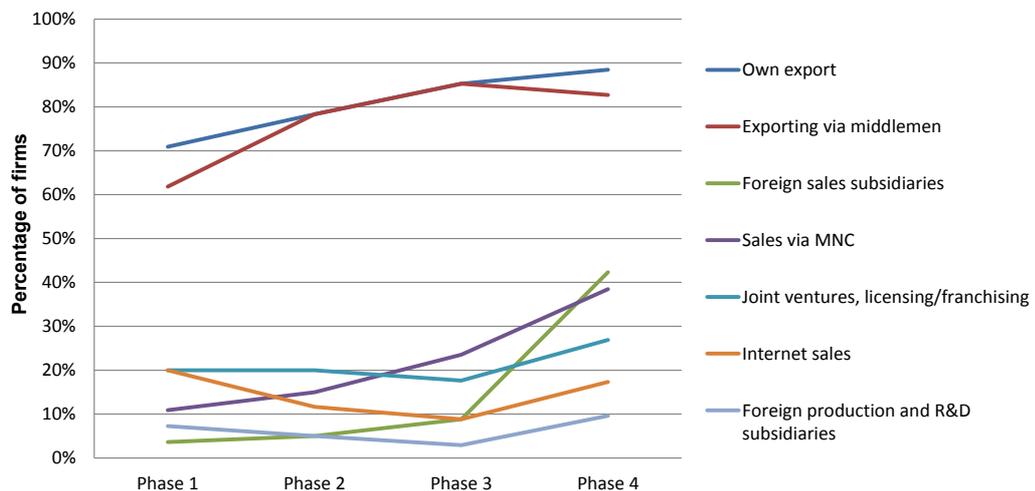


Figure 5. Operation modes and growth phases

When analyzing the product offering, it was evident that service characteristics are important for many Born Globals. This is understandable since Born Globals

need to bring to the market a complete solution. For this kind of unique global products or services there is no ready infrastructure, which forces Born Globals to be proactive in this respect. Moreover, an important finding was that Born Globals need to select a focused product offering in the early phase and then expand it as they advance through the phases. However, when expanding the offering it is important not to scatter the resources through unrelated product diversification.

Influencing factors on growth and survival

Research on the growth phases and survival of International New Ventures has identified several influencing factors: the globalization of the environment (Yip 1989), resources (Sapienza et al. 2006; Reuber & Fischer 1999) and the extent of substantive and dynamic capabilities (Zahra, Sapienza & Davidsson 2006), networking capability (Mort and Weerawardena 2006) and entrepreneurial orientation (Lumpkin & Dess 1996). In addition, government support may also be an important influencing factor. These factors may have different effects on firm growth and survival, as we examine next.

Based on regression analysis of the survey data from Finland we can see that the advancement through growth stages is positively driven by resources amount, networking capabilities, proactive entrepreneurial orientation and government support. The perceived survivability of the firm was influenced positively by resource amount and dynamic capabilities. Surprisingly, government support influenced negatively the perceived survivability of the firm. It can be therefore assumed that government's support is important for growing the firms, but if received in excessive amounts and without the firm's offering being competitive on the market place, it may just prolong the existence of firms that would not survive in the longer term anyway.

Conclusions and managerial recommendations

The understanding of the growth phases and survival of Born Globals and the influencing factors is important for both firm management and academic researchers. Hence, the article contributes to the new research stream interested in the survival and growth of International New Ventures (Sapienza et al. 2006; Mudambi & Zahra 2007) and earlier management literature discussing the stages of

growth of organizations (Kazanjian & Drazin 1989). We have shown that there are four critical phases in Born Global growth: (1) introductory, (2) commercialization and foreign entries, (3) rapid growth and foreign expansion, and (4) rationalization and foreign maturity.

There are a number of important managerial implications. First, growth happens in phases but in some cases, survival crises require the tough decision to retrench to regain growth speed. This was evidenced in both Finnish and Swedish empirical data. Second, critical decisions must be prioritized and solved to be able to advance to next phase, and firms may learn from more advanced organizations. Third, when advancing from the introductory to successive phases, the firm needs to invest in professional management. In many firms this was very important for successful growth. Fourth, for Finnish firms innovations and networking have been critical for growth, while Swedish firms place stronger emphasis on investments in intangible assets such as human resources and branding. It could be worthwhile for Finnish firms to investigate the Swedish firms' practices further. Fifth, low investment operation modes such as exporting and MNC channels are highly important. Although some sales subsidiaries were established in later phases, a lower number were production or R&D subsidiaries. The high share of export modes can be explained by the resource scarcity of Born Globals. It is highly important to use modes that can be implemented with little financing, but obviously as the firms grows, it becomes important to gain more control of the operation modes. Sixth, firms need to select a focused product offering to enter foreign markets, but may later expand their portfolio in a related way. Seventh, it was found that organic growth is the main growth method, but rapid global growth also calls for the use of partnerships and acquisitions.

In conclusion, growth and survival are facilitated by the existence of sufficient but not slack of resources. This was one of the main influencing factors on growth and survival. Thus, firms need to have the right amount of resources and avoid excessive amounts that may lead to unprofitable investments and loss of focus. Moreover, proactiveness and networking capabilities are crucial for advancing through growth phases while dynamic capabilities are critical for survival. Interestingly, it was found that government support advances growth, but survivability may be endangered especially in the long term.

Future study avenues

Future research would benefit from investigating the entrepreneurs' decision-making logic more as has been pointed out recently (Gabrielsson & Gabrielsson, 2013). The understanding of the decision-making logic may reveal how Born Globals are able to meet the huge challenge of global growth problems and survival crises despite their liabilities regarding newness, size, and foreignness. Effectuation logic, which emphasizes improvisation, exploitation of contingencies and market creation through alliances and partnerships, offers great hopes in this respect due to its potential to mitigate resource requirements. Moreover, an in-depth understanding of how the international entrepreneurial culture changes during globalization (Gabrielsson, Gabrielsson, and Dimitratos, forthcoming) may enhance our understanding of Born Global growth and survival.

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12. Finland's Contribution To The Field Of International Hrm

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Introduction

Since its origins some 40 years ago, the field of International Human Resource Management (HRM) has grown rapidly. Today, it is acknowledged as a distinct field within the international business (IB) community, and currently attracts a modest yet growing number of scholars from around the world. This short chapter illustrates what kind of role Finland, and scholars based in Finland, have played in the development of International HRM research. In many ways, this contribution shares similarities with Finland's disproportionate contribution to IB more generally, and would not have been possible without the intellectual input and support from the thriving Finnish IB community.

The Origins of International HRM in Finland

The field of International HRM (IHRM) has come a long way since the early work on top management attitudes and staffing decisions in multinational corporations (Perlmutter, 1969; Edström & Galbraith, 1977), and expatriation (Tung, 1981; Torbiörn, 1982). The field today is characterised by a broad range of subjects that has come to be defined as covering "all the issues related to managing the global workforce and its contribution to firm outcomes" (Björkman, Stahl & Morris, 2012: 1). Indeed, looking back over the IHRM body of work, it is possible to identify one over-arching question, which has been and remains: (i) "How are people managed in multinational corporations?", and (ii) "what are the outcomes?" (Björkman & Welch, 2014). The first part of the question refers to the work centred on explaining how and why MNCs manage people in the various units and affiliates differently. This includes the roles played by HR departments and other organisational actors in managing human resources globally. The second part of the question concerns outcomes: endeavouring to link HRM systems

and activities to organisational performance; and incorporating the effects of HRM across different groups of participants and levels of analysis, ranging from individual employees and their families, through to societies within which multinational corporations (MNCs) operate.

Based on a citation analysis of the articles published in the *International Journal of Human Resource Management*, the most dominant research themes between 2000 and 2009 were strategic HRM, expatriate management, international management development, comparative HRM, and global staffing (Lee et al., 2011). To varying extents over the past two decades, IHRM scholars in Finland have made contributions to all these themes, which also partly speaks to the breadth of Finland's contribution to IHRM research in addition to its size. However, the roots of IHRM research in Finland go back more than two decades.

Helsinki School of Economics can be considered the birthplace of IB research in Finland. Reijo Luostarinen not only did path-breaking research on the internationalization of the firm (Luostarinen, 1979), but also led the development of a significant IB research group. Probably the first ambitious study on International HRM was carried out within the FIBO research project led by Luostarinen, leading to a research publication on personnel issues in Finnish MNCs (Svärd & Luostarinen, 1982). It was not until in the 1990s that researchers at the Helsinki School of Economics returned to the field of IHRM. While the focus of Rebecca Marchan's doctoral thesis (Marchan-Piekkari, 1996) was not specifically on HRM issues, her early work certainly had a number of implications for personnel issues in MNCs and she gradually made important international contributions to research on language issues in MNCs (see below). Tuomo Peltonen's (1998) and Marja Tahvanainen's (1998) doctoral theses were arguably the first carried out at the Helsinki School of Economics that specifically dealt with IHRM.

At the Hanken School of Economics, the first international peer-reviewed publications on international people management issues emerged in the early 1990s (Björkman & Gertsen, 1993; Björkman & Schaap, 1995), and by the turn of the century several doctoral theses on a range of issues in or related to IHRM had either been defended or were in the making (Lohrum, 1996; Furu, 2000, Lindholm, 2000, Barner-Rasmussen, 2003, Peltokorpi, 2003). IHRM has remained an important topic area for doctoral students and scholars at Hanken up until today.

In Vaasa, IB traditions have existed for some time, whereas IHRM research started to emerge in the late 1990s as an extension of cross-cultural and comparative research (e.g. Suutari, 1996). There has been a gradual increase during 2000s due to the growth of the research group working in this area. In the early stages, research focused on expatriation but has later expanded to areas such as global ca-

reers, global leadership, and HRM practices in MNCs. The doctoral dissertations during this period have covered an even wider range of themes such as diversity management within MNCs, HRM in international M&A's, and e-HRM in MNCs (Antila, 2006; Sippola, 2007; Leponiemi, 2008; Heikkilä, 2013).

In addition, people management issues were increasingly being studied by doctoral students and researchers at other Finnish universities and business schools such as Turku School of Economics and University of Oulu. To be noted is also the gradual increase in the number of foreign PhD students researching IHRM in Finland.

International HRM and International Business

As described above, the main impetus behind developments in IHRM research in Finland was an active IB community and many of the main contributors to the IHRM field were and continue to be active members of the IB community more generally. The timing of the early developments in Finland can also be seen to follow on from a number of key milestones being achieved in IHRM in the late 1980's and early 1990's. These include, firstly, a rapid increase in the number of IHRM publications. The number of publications in top journals directly related to IB and IHRM grew from 59 between 1990–1996, to 129 between 1997–2003, to 186 between 2004–2010 (Björkman & Welch, 2011). Secondly, the first academic IHRM Conference was organised in the late 1980s (the 13th conference to be held in 2014) and was followed by many seminars and workshops dedicated to IHRM-related topics. Thirdly, the Cranfield Network on International Human Resource Management (Cranet), launched in 1989, was established to meet the need for ready access to data on best practice and comparative performance within Europe and later globally. This was to provide IHRM scholars, particularly in the area of comparative HRM, with a tremendous repository of internationally comparable data about HRM in different countries which could also be analysed against company and national data. And fourthly, the first dedicated IHRM journal – the *International Journal of Human Resource Management* – was established in 1991. Over time, IHRM research has earned an established place in mainstream IB journals such as the *Journal of International Business Studies*, *Journal of World Business*, and *International Business Review*. Together with the *IJHRM*, these journals have been the home of much of the influential work published on IHRM, including research produced in Finland (see Table 2).

As interest in IHRM and the number of doctoral students researching IHRM topics grew in different parts of Finland (Hanken, Helsinki, Vaasa, Turku, etc.), there

was a need to provide doctoral education in IHRM. An important development in doctoral education came when The Finnish Graduate School of International Business (FIGSIB) under the leadership of Jorma Larimo, as a part of the Finnish Doctoral Program for Business Studies (KATAJA), agreed to support and finance a module on 'International HRM Research' (to be organised for a sixth time in 2014). This module has been instrumental in bringing faculty and doctoral students together from around Finland and producing much-needed high-level doctoral education in IHRM. Many of the IHRM scholars listed in Table 1 and the co-authors in Table 2 have either taught or studied on this module, or both.

Finland's Scholarly Impact on International HRM

Since International HRM research began in Finland back in the early- to mid-1990's, Finland's most cited scholars have collectively produced over 400 publications and amassed over 12,000 citations (note: includes double-counting and self-citations). It is thus fair to say that Finland occupies a central position on the global IHRM research map. Table 1 presents a list of the scholars most active in International HRM research according to their number of citations (after removing non-IHRM publications), grouped according to the Finnish university in which they conducted the majority of their IHRM work.

Taking a closer look, it is clear to see that the epicentres of IHRM research have been at the Hanken School of Economics, at the University of Vaasa, and at the Helsinki School of Economics (now Aalto University School of Business).

Table 1. Finnish university affiliations of the most cited scholars¹ in the field of international HRM

	<i>No. citations</i> ²	<i>No. publications</i>
<i>Hanken School of Economics</i>		
Ingmar Björkman (1983-2011; Aalto 2012-)	3559	82
Eero Vaara	981	20
Kristiina Mäkelä (2006-2012; Aalto 2012-)	431	25
Wilhelm Barner-Rasmussen	398	30
Vesa Peltokorpi (-2003)	362	22
Riikka Sarala (-2008)	163	10
Jennie Sumelius	154	14
Mats Ehrnrooth	142	18
<i>University of Vaasa</i>		
Vesa Suutari	2117	58
Risto Sääntti (2009-)	367	5
Adam Smale	262	20
Tiina Jokinen	253	3
<i>Aalto University School of Business</i>		
Rebecca Piekkari / Marschan-Piekkari	1391	51
Janne Tienari	459	9
Marja Tahvanainen	249	10
Sinikka Vanhala	199	14
<i>University of Oulu</i>		
Tuomo Peltonen (2001-2009; TUT 2009-2013; Turku 2013-)	374	28
<i>Helsinki University of Technology</i>		
Satu Teerikangas (-2009)	245	21

¹ Scholars with Finnish nationality or a long-term affiliation to a university in Finland

² Based only on work published in the field of international HRM. To be noted is that the question of which articles are to be viewed as part of the field of IHRM is a non-trivial one — the decision on what to include was made by the first author applying the definition of IHRM presented in this paper. Data was retrieved between 14-17 March 2014 from Publish or Perish version 4.1 using Google Scholar as the data source.

At Hanken, the main thrust of the research has been on HRM practices in the multinational firm setting. This includes research on the explanations for patterns of HRM practices found in MNC subsidiaries, as well as research on the performance effects of those practices (see Table 2). Much of this research is rooted in research traditions found in the IB field and is conducted at the organisational level with a strong focus on China (based partly on Ingmar Björkman's long-standing personal interest in China) and Russia. Eero Vaara's research, on the other hand, has applied an existing focus on culture and identity issues in mergers and acquisitions to the MNC setting and to cultural and identity dilemmas specific to cross-border mergers and acquisitions. Due to the nature of doctoral supervision and the inclusion of doctoral students and post-docs in large-scale research projects on these topics financed by the Academy of Finland and the Finnish Funding Agency for Innovation ('Tekes'), these themes are also evident in the research carried out by a number of other IHRM researchers based at Hanken.

In Vaasa, the emphasis in IHRM research has been on international and mobile individuals – expatriates and global leaders. In no small part due to the excellent access to data on Finnish expatriates provided by the Finnish Association of Business School Graduates (SEFE), Vesa Suutari and colleagues at the University of Vaasa have been able to study the roles, careers, development, and well-being of Finnish assigned expatriates – and more recently self-initiated expatriates – quantitatively, qualitatively and longitudinally. Individual-level research has also covered other mobile and international employees such as international frequent flyers and short-term assignees. Research has also been gradually strengthening around core and emerging HRM practices and processes in MNCs such as talent and performance management, and electronic-HRM. At the moment the Vaasa IHRM group consists of around 10 researchers (including full-time doctoral students).

IHRM research at Aalto (Helsinki School of Economics) has had somewhat more diverse origins. Even though Rebecca Piekkari's research interest in language issues in MNCs dates back to the late 1990's, this topic within IHRM research, and IB more generally, has only recently started to attract a larger number of contributing scholars, some of which originate from Finland. As can be seen from Table 2, language issues in MNCs has come to represent a significant proportion of the IHRM research to come out of Finland and continues to be a sub-topic where Finnish scholars are making significant contributions to global academic discourse. These contributions are not fully understood without noting the parallel advancements in methodology. Whereas the vast majority of research conducted on HRM in MNCs has been based on more traditional quantitative, survey-based research, the study of language (and post-acquisition integration) has incorporated

a focus on high-quality qualitative research, driven by Rebecca Piekkari's pioneering work on qualitative methods in IB and Eero Vaara's application of critical and discursive approaches.

As mentioned above, the Cranet network has been collecting comparative HRM data across many countries since its establishment, and Sinikka Vanhala at Aalto has been the main person responsible for collecting the data for Finland for most of that time. This has allowed for several publications, mostly by Sinikka Vanhala and colleagues, comparing HRM in Finland with neighbouring countries, as well as for more focused contextual studies on the evolution of HRM in Finland.

Last but not least, Finland's IHRM scholars have also made a significant contribution to what might be referred to as the 'critical IHRM' school. Albeit in slightly different ways (and in different places), professors Peltonen, Vaara, Tienari and Piekkari have all contributed to this school. In essence, the critical perspective on IHRM has sought to challenge some of the dominant epistemological and ontological approaches characterising the mainstream, North American-influenced IHRM literature, and has been advanced through the use of more reflexive and interpretative schemes in combination with more non-traditional methodologies (e.g. grounded theory, ethnographic case studies, participant observation, and various text and talk analytical techniques).

Table 2. Most cited publications on International HRM by Finnish scholars, by subject

<i>No. citations</i> ³	<i>Publication</i>
<i>HRM in Multinational Corporations</i>	
663	Minbaeva, D., Pedersen, T., Björkman, I., Fey, C.F., & Park, H.J. (2003). MNC knowledge transfer, subsidiary absorptive capacity, and HRM. <i>Journal of International Business Studies</i> , 34(6), 586-599.
236	Björkman, I., & Kock, S. (1995). Social relationships and business networks: the case of western companies in China. <i>International Business Review</i> , 4(4), 519-535.
235	Fey, C.F., Björkman, I., & Pavlovskaya, A. (2000). The effect of human resource management practices on firm performance in Russia. <i>International Journal of Human Resource Management</i> , 11(1), 1-18.
198	Björkman, I., & Xiucheng, F. (2002). Human resource management and the performance of Western firms in China. <i>International Journal of Human Resource Management</i> , 13(6), 853-864.
196	Fey, C.F., & Björkman, I. (2001). The effect of human resource management practices on MNC subsidiary performance in Russia. <i>Journal of International Business Studies</i> , 59-75.
162	Björkman, I., & Lu, Y. (1999). The management of human resources in Chinese-Western joint ventures. <i>Journal of World Business</i> , 34(3), 306-324.
126	Björkman, I., Fey, C.F., & Park, H.J. (2007). Institutional theory and MNC subsidiary HRM practices: evidence from a three-country study. <i>Journal of International Business Studies</i> , 38(3), 430-446.
122	Park, H.J., Mitsuhashi, H., Fey, C.F., & Björkman, I. (2003). The effect of human resource management practices on Japanese MNC subsidiary performance: a partial mediating model. <i>The International Journal of Human Resource Management</i> , 14(8), 1391-1406.
<i>Language issues in Multinational Corporations</i>	
255	Marschan-Piekkari, R., Welch, D., & Welch, L. (1999). In the shadow: the impact of language on structure, power and communication in the multinational. <i>International Business Review</i> , 8(4), 421-440.
134	Marschan-Piekkari, R., Welch, D., & Welch, L. (1999). Adopting a common corporate language: IHRM implications. <i>International Journal of Human Resource Management</i> , 10(3), 377-390.
130	Vaara, E., Tienari, J., Piekkari, R., & Sääntti, R. (2005). Language and the circuits of power in a merging multinational corporation. <i>Journal of Management Studies</i> , 42(3), 595-623.
118	Charles, M., & Marschan-Piekkari, R. (2002). Language training for enhanced horizontal communication: A challenge for MNCs. <i>Business Communication Quarterly</i> , 65(2), 9-29.
<i>Expatriation & Global Leadership</i>	
205	Suutari, V., & Brewster, C. (2001). Making their own way: international experience through self-initiated foreign assignments. <i>Journal of World Business</i> , 35(4), 417-436.
185	Suutari, V., & Brewster, C. (2003). Repatriation: empirical evidence from a longitudinal study of careers and expectations among Finnish expatriates. <i>International Journal of Human Resource Management</i> , 14(7), 1132-1151.

123	Jokinen, T., Brewster, C., & Suutari, V. (2008). Career capital during international work experiences: contrasting self-initiated expatriate experiences and assigned expatriation. <i>The International Journal of Human Resource Management</i> , 19(6), 979-998.
118	Jokinen, T. (2005). Global leadership competencies: a review and discussion. <i>Journal of European Industrial Training</i> , 29(3), 199-216.

Table 2. Most cited publications on International HRM by Finnish scholars, by subject (cont.)

No. citations ³	Publication
<i>Cross-Cultural Management in International Mergers & Acquisitions</i>	
169	Björkman, I., Stahl, G.K., & Vaara, E. (2007). Cultural differences and capability transfer in cross-border acquisitions: The mediating roles of capability complementarity, absorptive capacity, and social integration. <i>Journal of International Business Studies</i> , 38(4), 658-672.
157	Teerikangas, S., & Very, P. (2006). The culture–performance relationship in M&A: From yes/no to how. <i>British Journal of Management</i> , 17(1), 31-48.
124	Vaara, E., Tienari, J., & Säntti, R. (2003). The international match: Metaphors as vehicles of social identity-building in cross-border mergers. <i>Human Relations</i> , 56(4), 419-451.

³ Data retrieved between 14-17 March 2014 from Publish or Perish version 4.1 (using Google Scholar as the data source).

The most cited publications on IHRM presented in Table 2 reveals that the main contributions have been in the areas of HRM practices in multinational firms, language issues, expatriation and global leadership, and cultural issues in international mergers and acquisitions. Re-emphasising the close links between research and scholars in IB and IHRM, the most cited IHRM publication where a Finnish scholar has been an author was the article by Minbaeva et al. (2003), which won the *Journal of International Business Studies Decade Award* in 2013. Another indicator of the growing recognition of Finnish IHRM research internationally, are the different international awards from conferences and journals, as well as several doctoral theses have been internationally awarded (e.g. Mäkelä, 2006, Smale, 2007, Sumelius, 2009). The teaching case on Lincoln Electric in China written by Björkman and Galunic (1999) has also received a best case award by the European Case Clearing House.

However, in addition to these most cited and awarded works, other notable publications include Finland's scholarly contributions to the educational literature on IHRM. For instance, the 'Handbook of Research on International Human Resource Management' (Stahl & Björkman, 2006; Stahl, Björkman & Morris,

2012), now in its second edition, collates contributions from leading international IHRM scholars of which several are Finnish scholars listed in this chapter. In addition to Björkman's co-authored textbook on IHRM 'The Global Challenge' (Evans, Pucik & Björkman, 2012), scholars in Finland have also contributed a number of chapters to the growing number of IHRM-focused textbooks and research handbooks (e.g. Sparrow, 2009; Harzing & Pinnington, 2011, Edwards & Rees, 2011; Hayton et al., 2011; Sanders, Cugin & Bainbridge, 2013; Collings, Wood & Caligiuri, 2014 forthcoming; Al Ariss, 2014 forthcoming).

Conclusion: Looking Forward

The field of IHRM research in Finland has come a long way since its inception. Today, the Finnish IHRM community is a sizeable, vibrant community that regularly publishes in leading academic journals like *Journal of Management Studies* (Mäkelä et al., 2012), *Journal of International Business Studies* (Mäkelä et al., 2013; Peltokorpi & Vaara, 2014) and *Human Resource Management* (Björkman et al., 2013; Sumelius et al., 2014). A new generation of young scholars have entered the field in recent years, and we believe that issues related to people management across borders will continue to be an important and fruitful research area in Finland for years to come.

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13. The Evolution Of New Systemic Forms In Retailing And Digital Business

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Introduction

Digitalization, the rise of the digital world, is one of the high-impact megatrends for the consumer goods and retail industry (Capgemini 2013). The analysts have drawn attention to the international retailers' increased use of variety of channels and customer touch points when entering new markets and building their physical and digital presence (e.g. Deloitte 2012). Currently international retailers have moved to seek the growth potential of the online operations especially in the emerging and developing markets including China, Brazil and Russia (e.g. A.T.Kearney 2012). International store based retailers are increasingly launching online operations to test the market potential, to learn about customers or just to make the brand known in the new markets (e.g. A.T.Kearney 2012). Store based retailers have been challenged by international e-retailers and online marketplace companies. The strategic importance of multichannel retailing has risen. According to Deloitte (2014: 38) the vast majority of the world's top 50 e-retailers, including Amazon, Apple, Wall-Mart and Tesco, are multichannel retailers.

There is a need for an updated view on the evolution of new systemic forms in retailing and digital business. These new forms include multichannel and omnichannel retailing, e-marketplaces, digital business platforms and ecosystems. Research on international retailers' entry and penetration strategies and operation modes has placed much emphasis on retailers' store based operations. Online sales, for instance, have traditionally been viewed as a form of exporting (e.g. Alexander & Doherty 2009; Delaney 2013). Research has thus far been fairly silent on many other forms of operations that are the essential elements in global retailers' multichannel strategies and in the creation of the firm's or brand's digital presence. Moreover, although research in the field of retail institutional change theories has evolved from uncomplicated theories into comprehensive combined theories (Laaksonen & Huuhka 1999), the research has not thus far addressed the dynamics brought about by the rise of digital economy.

This essay brings up the elemental issues on the evolution of new systemic forms in retailing and digital business. The primary aim is to give point of views and to lay ground for the future research. The essay has three objectives. The first objective is to point out and describe the emergence of multichannel and omnichannel retailing. The second objective is to offer a holistic, systemic view, to understand and conceptualize the complexities of digital marketing and digital business platforms. The third objective is to hypothesize the assimilative and accommodative processes in the dynamic interrelations between the key actors in the digital markets.

Outline of the emergence of multichannel and omnichannel retailing

In the simplest form multichannel retailers have been defined to be “those retailers that sell merchandise or services through more than one channel” (Levy & Weitz 2007). The early forms multichannel retailing originate from the mid-1990s parallel with the emergence of the internet retailing (e.g. Doherty & Ellis-Chadwick 2010; Reynolds 1997, 2002). The potentialities of internet were noticed not only by new pure play online retailers (web stores) but also by physical store based retailers and mail order companies. In the U.S., the mail order fashion retailers (e.g. Land’s End) were among the first companies that started to employ the internet as a new distribution channel to complement their catalogue sales. Historically catalogues have had a significant role in retailing and they can be regarded as the pre-internet era multichannel options. Interestingly, despite the early predictions that the internet would make the catalogue channel obsolete, international retailers (e.g. Otto, IKEA) have recently brought the catalogues into the digital age with augmented reality applications.

In the early days of e-retailing the potential benefits of online operations were not yet understood by store based retailers. The threat of channel conflict often prevailed. Online channel’s possible sales reducing (cannibalizing) effect on the physical store’s sales might have slowed down the early adoption of store based retailers’ multichannel practices. The array of channel options widened and the complexities in multichannel adoption further increased when the internet went mobile and social networks gained popularity. This change was supported by new communication technologies like Wi-Fi and 3G internet accesses, laptops and mobile phones’ web browsers. Although the mobile channel and social media channel can be conceptualized as distinct channels, they at the level of consumer usage are reciprocally interlinked. They have evolved to become highly integrated platforms belonging to wider ecosystems. This pattern of development has been facilitated by the advent of mobile shopping and location based applications (e.g.

Foursquare) and social networks (e.g. Windows Live, Facebook). The world's first social network website SixDegrees was introduced in 1997 (Sperry 2010); shortly other sites began to pop up in many cultures and to attract millions of users. Facebook, the today's most dominant social media platform, was established in 2004. Currently Facebook still has an important customer connecting role in many social media oriented omnichannel retailing operations.

Retail change is context dependent. The numerous factors and drivers, that make possible or impede certain patterns of retail development, e.g. the emergence of multichannel retailing, vary in degree in different retail environments. Factors like consumer acceptance together with the related changes in consumers' buying behavior, technological progress, competition, legislative and institutional factors have been attributed to be among the driving forces in particularly in the earlier development of business to consumer (B2C) e-commerce practices in the developed markets (Reynolds 2004: 126–132). If we take a look at the emergence of multichannel and omnichannel retailing, three waves of development can be identified.

The decade long first wave of development that started from around the mid-1990s was essentially retailer and technology driven. First mover retailers and IT companies initiated multichannel operations and pushed the still novel technologies to consumers who were not yet accustomed to them (e.g. Bagge 2007). The consumer acceptance remained low. Besides, in many cases retailers' operations in multiple channels lacked channel integration: store and online channels were often viewed and managed as distinct channels. Among the pioneering multichannel retailers in the specialty retailing sector in the U.S. was REI. This outdoor equipment and apparel retailer launched online operations in 1996 and began to use the online channel synergistically with its existing store and catalogue channels (Duffy 2004). In Europe, the British store based food and non-food retailer Tesco initiated online operations in the mid-1990s, and had since then become the world leader in e-grocery retailing (Koskinen 2013).

Presently developed markets with advanced technological infrastructures and high percentage of internet and smart phone usage are at the peak of the second wave (emphasizing multichannel integration) and in the transition towards the third wave of development (omnichannel retailing). The second wave of multichannel development is related to the many fundamental changes that have been brought about by the rise of digital economy during the last ten years. The key driver for the digital economy has been technological progress, especially the arrival of new customer-centric technologies that have democratized production and distribution of digital content and provided new means of connections between supply and

demand (see Anderson 2008). However, compared to the retailer and technology driven multichannel retailing development in the first wave, the second wave is essentially driven by consumers' increased acceptance of the new technology and their "desire to shop" whatever channel they want (Bagge 2007; see also Mercier et al. 2012).

The retail industry as a whole has not been innovative enough to act proactively. Retailing began to lack behind the aforementioned rapid changes. Since about 2008 retail industry analysts began frequently to point out multichannel integration as the top trends and priorities in global retailing (Deloitte 2008, 2009, 2010): the need for store based retailers to embrace the different channels more strategically in an integrated way (Bagge 2007; Morse 2011; RCE 2012). The required strategic changes have been harder for those retailers whose existing business models and value chain constellations have been fine tuned to maximize the internal efficiencies of the supply chain. Multichannel integration would require changes at the level of business model, and in particular the abandonment of the traditional view that the physical store is the final and the only customer touch point in the end of the supply chain.

The third wave of development, the emergence of omnichannel retailing, has required retailers to take more proactive approach to engage customers. It has been argued that in the digitalized world the new generation of technologically knowledge shoppers do not make distinctions between channels (Deloitte 2012; van Bruggen et al. 2010). Moreover, according to the contemporary view, every possible channel or customer touch point can be used as a marketing communication channel to connect customers with brands (e.g. van Bruggen et al. 2010; Edelman 2010). Due to the multiple customer touch points omnichannel retailing calls for higher degree of channel integration. Omnichannel retailing is not only more interactive but also more content and brand experience oriented than multichannel retailing. The digital content can originate from the company or it could have been co-created by the customers. The central issue in omnichannel retailing is to integrate physical and virtual customer touch points to make it possible for customers to experience the brand in a unified way all of them (e.g. Bellaiche et al. 2013; Rigby 2011).

Omnichannel retailing is not a mainstream practice in retailing. Thus far it has been most apparent among brand oriented fashion, luxury and apparel retailing sectors including online only retailers (e.g. Oasis) and store based retailers. Among the prime examples of the innovative companies in omnichannel retailing is the British high street fashion retailer Burberry. The company's recent move into luxury retailing has involved the strategic creation of the brand's presence

both in various digital platforms and especially in its flagship stores to engage and communicate with customers with the brand related content.

Systemic view on digital marketing and digital business platforms

Along with the emergence of multichannel and omnichannel retailing the nature of retailing and retail competition has changed in many ways. The boundaries between physical and virtual retail environments have become highly blurred in omnichannel retailing (e.g. Brynjolfsson et al. 2013). Retailing has evolved to encompass diverse forms. Besides, retailing has become more networked and dependant on selecting the right strategic partners. The implementation of digital strategies requires the retailers to co-operate and network with a range of new actors including for instance digital marketing service firms and customer relationship marketing and cloud computing firms.

Omnichannel retailing calls for the high amount of channel integration and strategic decisions concerning the intensity of the company's physical and digital presence within and across channels (physical and/or virtual) (e.g. van Bruggen et al. 2010). The higher the chosen intensity, the farther the company moves from the domain of retailing business into digital business. The implementation of the full scale omnichannel approach brings along the new kind of competitive environment. In digital business the competition takes place not only at the level of digital business models but also at the level wider technological ecosystems. The competition between business models calls for the novel use of digital content, engaging customer experiences and facilitating technological platforms (see e.g. Weill & Woerner 2013; Weber 2013). Beyond the competition between business models there is the competition between different facilitating technological platforms, which have evolved into comprehensive ecosystems.

Chaffey et al.'s (2009: 22-23) framework of the alternative digital business models and transaction alternatives between business and consumers can be adapted and used to exemplify and conceptualize the systemic characteristics of business-consumer interactions in the digital world (Table 1). The framework takes into account the five different forms of online presence (transactional sites, service-oriented relationship-building sites, brand building sites, portal or media sites, social networks or community sites). The framework also acknowledged the role of consumers and businesses as the users and as the providers of the digital content or services. The resulting four categories (C2C, C2B, B2C and B2B) exemplify the possible domains of digital business models.

Table 1. Domains of digital business models. (Adapted from Chaffey et al. 2009: 21).

		FROM: SUPPLIER OF CONTENT / SERVICE	
		CONSUMER	BUSINESS
TO: USER OF CONTENT / SERVICE	CONSUMER	C2C - e-marketplaces: eBay, Rakuten - peer to peer: Skype - blogs and communications - product recommendations - social networks	B2C - transactional: Amazon - relationship building: BP - brand-building: Unilevel - media owned: News Corp. - comparison intermediary: Kelkoo
	BUSINESS	C2B - price comparison sites: e.g. Priceline.com - consumer-feedback, communities or campaigns	B2B - different forms of extranets - transactional: Eurooffice - relationship building: BP - media owned: Emap - B2B marketplaces: EC21, Amazon supply.com, Google shopping for suppliers - social networks

The four domains of digital business models are dynamic and interlinked. In the C2C domain e-marketplace companies have (e.g. eBay) have together with social network providers (e.g. Facebook) given consumers multiple platforms to communicate and interact, to make consumer to consumer transactions and to create social content (see also Hagiu & Wright 2013). In the business to consumer domain companies like Amazon have evolved from transaction oriented companies into companies that expand their operations into the B2B and the C2C domains. The B2B domain has evolved to encompasses a variety of internet-based interorganizational systems like extranets (e.g. Angeles 2001), transactional sites and B2B marketplaces. Besides, social networks have become increasingly important communication channel in business to business sourcing and sales. In the C2B domain new channel intermediate companies (e.g. Priceline, TripAdvisor) have emerged to connect consumers and companies with consumer created content.

The evolution towards broad systemic forms can also be seen in the patterns of technological progress and convergence since the early days of e-retailing. Separate technological devices and applications have become connected. They have evolved from technology-oriented computer-mediated environments into customer-centric digital marketing platforms. These platforms enable the various transaction alternatives in the aforementioned four domains. According to the current view due to the dynamic interlinked character of these facilitating technological platforms they can be conceptualized as comprehensive ecosystems (Table 2).

Table 2. Digital business platforms and ecosystems.

FROM NARROW TECHNOLOGY-ORIENTED VIEW TO BROAD SYSTEMIC VIEW			
PLATFORMS		ECOSYSTEMS	
COMPUTER-MEDIATED ENVIRONMENTS	DIGITAL MARKETING PLATFORMS	SOCIAL MEDIA ECOSYSTEMS	DIGITAL BUSINESS PLATFORMS / ECOSYSTEMS
Conceptualization of computer mediated environments as the link between a "sponsor" (e.g. a seller) and "users" (e.g. customer) involving information technology, feedback (i.e. interactivity) and customization (Winer et al. 1997)	Typology of digital marketing platforms: (1) desktop, laptop and notebook platforms (including browsers, apps, email, feeds, video) (2) mobile phone and tablet platforms (including browsers and apps) (3) other hardware platforms (including gaming, indoor & outdoor kiosk-type apps, interactive signage); (4) social networks platforms / ecosystems. (Chaffey & Smith 2013)	Conceptualization of online social media, as an ecosystem of related elements involving both digital and traditional media (Hanna et al. 2011)	Competition between digital business platforms / ecosystems. The actors include digital marketing service firms, CRM and cloud computing firms. These ecosystems can include C2C, C2B, B2C and B2B domains. Customized e-business solutions, CRM dashboards, applications etc.

Summary

This essay has focused on outlining the development patterns related to the emergence of new systemic forms in retailing and digital business. These new forms include multichannel and omnichannel retailing, e-marketplaces, digital platforms and ecosystems. Digitalization is impacting and changing businesses at many levels. The dynamic drivers in the digital economy originate increasing from the systemic processes beyond the changes at the institutional level. The existing theories of retail institutional change cannot offer complete explanations. There is a need for new approaches to hypothesize the complex evolutionary processes.

The Piagetian systemic view on the processes of assimilation and accommodation (see e.g. Chermack & van der Merwe 2003) can be used to hypothesize the system dynamics of the interrelations between the different actors in the digital markets. An assimilative process is a process where an actor (e.g. retailer) uses new information to sustain its existing behavioral patterns and the underlying value structures. An accommodative process is a process where an actor uses new information to change its behavior and value structures. The hypothetical model with a behavioral emphasis is presented in Figure 1.

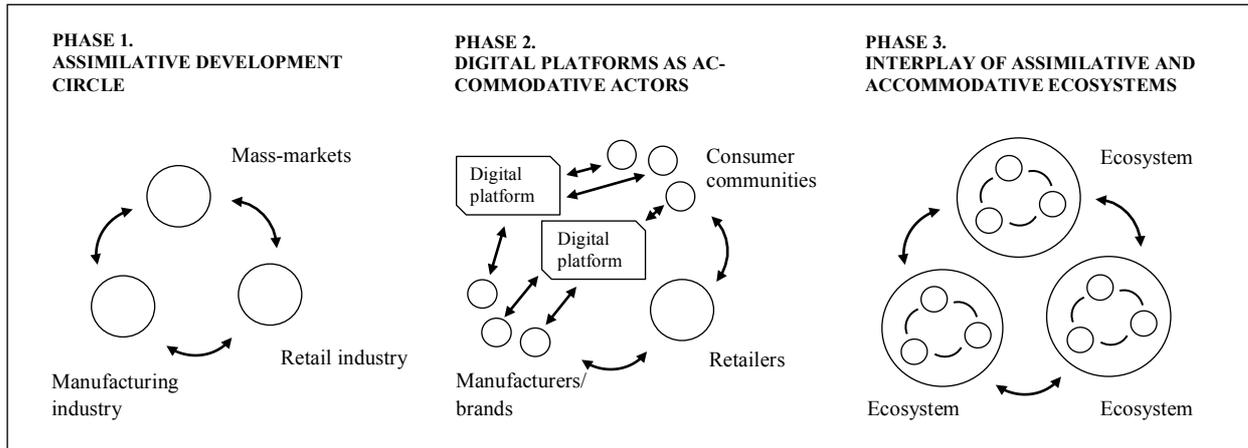


Figure 1. Hypothetical model.

In the first phase, the three key actors, retailers, manufacturers/brands, and consumers, are connected with reciprocal assimilative processes. Store based retailers are the main channel intermediaries between supply (manufacturers/brands) and demand (consumers in the mass-markets). Manufacturing industry seeks to fulfil the demand and pushes the merchandising into distribution channels. Retail industry strives for the economies of scale. Despite of the advent of e-retailing and the early developments in multichannel retailing practices, retailing is still dominated by store-based retailers. The assimilative development circle enforces the existing channel structures and value chain configurations (e.g. the retailers' maximization of supply chain efficiencies).

In the second phase, the technological progress has made customer-centric technologies available to consumers. Digital marketing and business platforms begin to emerge and have an increasingly influential role as accommodative actors. On the demand side the traditional mass-market has disappeared because consumption has become fragmented. The digital platforms enable consumers to connect with each other and with the brands. Consumers form brand and social communities that create and share customer generated digital content. On the supply side, the idea of open innovation (e.g. crowdsourcing, collective customer commitment) has brought about new possibilities for innovative companies to use lead users as the sources of innovation for new products and services. New systemic forms (e.g. multichannel and omnichannel retailing, e-marketplaces) emerge to serve the fragmented demand. The accommodative forces brought about by the emergence of digital platforms began to counterweigh the first phase's assimilative forces. The digital platforms have evolved into powerful accommodative actors that enable the consumers and brand owners to bypass the traditional retail and channel structures.

The third phase is characterized by the dynamic interplay between the different assimilative and accommodative ecosystems. The digital platforms have evolved into ecosystems that expand themselves beyond the boundaries of different domains of digital business models. The changes within and between these ecosystems are the new drivers in the digital economy. They shape the competitive operating conditions of businesses and facilitate consumers' digital consumption practices.

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