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Herausgegeben von Peter Kajüter

Thomas Poplat

Foreign Investments in BRIC Countries

Empirical Evidence from Multinational Corporations

Band 10

PL ACADEMIC RESEARCH

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Preface

In the course of their internationalization strategies, multinational companies undertake significant investments to establish subsidiaries and production sites in foreign countries. In 2012, worldwide foreign direct investment flows more than doubled compared to 2002 accounting for USD 1.4 trillion. Investments in emerging economies were a main driver of the significant increase of worldwide foreign investment flows in recent years. In particular during the times of stagnating growth in North America and Europe, emerging economies offer substantial opportunities for multinational companies, but they also entail significant risks. Specifically investments in BRIC countries are exposed to various challenges, as institutional voids, host governments and national champions dictate the local business conditions for multinationals. A systematic investment decision process is necessary to anticipate upcoming opportunities and mitigate arising risks.

In spite of the high failure rate of cross-border investments the design of foreign investment decision processes in multinational corporations is largely unexplored. The work of Thomas Poplat is therefore addressing an important research gap. His focus on investment projects in BRIC countries further enhances the practical relevance of his study. Based on a multiple-case study design involving two multinational companies, Thomas Poplat interviewed more than 50 managers, business developers and management accountants about their experiences with decision processes for BRIC investments. The author analyzes the empirical data on the firm- and country-level and consolidates his findings in a cross-level analysis.

On the firm-level, Thomas Poplat reconstructed the two company specific investment decision processes in their real-life context based on a pre-developed foreign investment decision process model. The author analyzes the two firm-specific decision processes from various perspectives and provides explanations for cross-company differences based on his conceptual framework. Thomas Poplat argues that decision process speed and decision process comprehensiveness are the two adjusting screws for efficient investment decision-making. Thereby, he shows how industry specifics and organizational characteristics determine the investment decision uncertainty and complexity which in turn influence the underlying decision process speed and comprehensiveness. Finally, the author recommends that a troika of power, process and technology promoters represents a reasonable role constellation to balance decision process speed and comprehensiveness.

The country-level analysis is focused on identifying political-economic and socio-cultural challenges for foreign multinational corporations in each of the four BRIC countries. Thomas Poplat combines his archival analysis with the interview evidence and thereby provides valuable insights for corporations which consider investing in the BRIC countries. In the cross-level analysis he finally consolidates the firm- and country-level in order to evaluate whether the identified country-specific challenges demand for higher decision process speed or comprehensiveness.

Overall, the empirical findings provide interesting insights into corporate investment decision-making in MNEs. They are highly relevant to both researchers and practitioners. Moreover, the study presents several suggestions how to improve foreign investment decision processes. It thereby significantly contributes to the research stream of foreign investments. Considering the valuable scientific contribution and the practical relevance of Thomas Poplat's work, I wish that his thesis will gain a lot of attention in academia and practice.

Münster, July 2013 Prof. Dr. Peter Kajüter

Acknowledgement

This study was conducted during my time as a PhD student at the Chair of International Accounting at the University of Münster. The thesis was accepted as a dissertation by the Münster School of Business and Economics in July 2013.

In this acknowledgment I want to express my sincere gratitude to everyone who supported me during my thesis. First of all, I would like to thank my academic teacher Prof. Dr. Peter Kajüter who has always been approachable for discussions and proposed both effective ideas as well as solutions. He greatly contributed to the success of this study and I deeply appreciate the amount of time and energy he invested in my work. I would also like to thank Prof. Dr. Gerhard Schewe who reviewed and evaluated my study as a second referee. My sincere thanks are further given to Prof. Dr. Ulrich van Suntum for being the third referee at my disputation.

The empirical part of this thesis is based on case studies with multinational corporations. I am grateful for the support and energy all the interviewed persons dedicated to my study. Particularly, I want to thank Tom Blades who established the research partnerships for my study and enabled me to conduct this research project in the first place. I would further like to thank my sister Sabine Poplat and my colleagues Julius Hannemann and Gregor Hagemann for reviewing my thesis. Furthermore, I also want to thank Martin Merschdorf who has always been willing to discuss the research design during our frequent coffee breaks. Moreover, I am grateful to all the student assistants who transcribed the interview data for my thesis and supported me in literature research.

Nonetheless, my thesis would not have been possible without the mental support of my dear friends at the Chair of International Accounting. They made my time at the chair really enjoyable. With great pleasure I remember and will never forget the sailing cruises on the Ijsselmeer, chair excursions, the WiWi-Cup, spontaneous office parties as well as various nightlife trips in Münster, Amsterdam and Berlin. Specifically, I would like to thank Marcel Baki for the entire administrative support at the final stages of my thesis, in particular prior to my disputation. Special thanks are dedicated to Daniel Blaesing who is a perfect host for doctorial seminar preparations. Moreover, I want to thank Max Saucke and Stefan Hannen for great soccer matches which helped to clear my mind. My sincere thanks are further given to Moritz Schröder and Gregor Hagemann for spontaneous half-marathons and distracting cycling workouts. Also, I would like to thank our IUR ladies Christina Voets, Stephanie Eckerth and Daniela Peters who enriched the entire working atmosphere at our chair. I want to thank Martin Merschdorf, Kristian Bachert and Martin Nienhaus for legendary nights at Jüdefelder Street. With great joy I remember fun times at the chair with Ashly Bills, Leila Prousch and Christian Reisloh. Finally, I want to thank Matthias Moeschler for providing me with fruitful comments in accounting.

Finally but foremost, this thesis would not have been possible without my beloved family who helped me through the difficult times of my research project. I owe my deepest gratitude to my fiancé Kristin Blades. Her endless love, understanding and patience motivated me to never give up. With great anticipation I look forward to our common future in Dubai. In this regard, I also want to thank her parents Heike and Tom for their great encouragement over the past seven years and for the warm welcome into their family. Moreover, I want to thank my sister Sabine and my grandmother Emma for their great support and their positive attitudes during the final stages of my study. Most importantly, I would like to thank my parents Monika and Klaus Poplat who accompanied me during my entire life and showed great enthusiasm in my projects. I am deeply grateful for their trust, unconditional support and love. To my entire family I dedicate this thesis.

Münster, July 2013 Thomas Poplat

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Index of abbreviations

ARR	Accounting rate of return
BB	Betriebs-Berater (journal)
BCG	Boston Consulting Group
Bd.	Band
BRIC	Brazil, Russia, India and China
Capex	Capital expenditures
CAPM	Capital asset pricing model
CDBA	Costs of doing business abroad
CEO	Chief Executive Officer
Cf.	Compare for
CFO	Chief Financial Officer
CFROI	Cash flow return on investment
CIMA	Chartered Institute of Management Accounting
CINC	Composite Index of National Capabilities
CMA	Comparative management accounting
COO	Country of origin
CPI	Corruption Perception Index
CSF	Critical success factor
DAC	Development assistance committee
DAX	Deutscher Aktienindex
DCF	Discounted cash flow
DPC	Decision process comprehensiveness
DPS	Decision process speed
EBIT	Earnings before interest and taxes
E.G.	Exempli gratia
EMNC	Emerging market multinationals
EVA	Economic value added
FDI	Foreign direct investment
FiCo	Finance & Controlling
GAINS	Gestalt approach of international business strategies
GDP	Gross domestic product
GNI	Gross national income
HR	Human resources

I-proposal	Investment proposal
IC	Investment Committee
IMF	International Monetary Fund
IPC	Intellectual property rights
IPO	Initial Public Offering
IRR	Internal rate of return
IT	Information technology
KPI	Key performance indicators
LOF	Liability of foreignness
LOO	Liability of outsidership
M&A	Mergers and acquisitions
MAS	Management Accounting Systems
MNC	Multinational corporations
MNE	Multinational enterprise
MRTP	Monopoly and Restrictive Trade Practices Act
NPV	Net Present Value
OECD	Organization of Economic Development and Cooperation
OPEX	Operational expenditures
P	Page
P&L	Profit and loss
p-proposal	project proposal
PAC	Growth Acceleration Program
PESTEL	Political, Economic, Social, Technological, Environmental
PPP	Purchasing power parity
QDA	Qualitative data analysis
R&D	Research and development
ROCE	Return on capital employed
ROIC	Return on invested capital
RTE	Free and Compulsory Education Act
SCM	Supply chain management
SMART	Simple, maintenance-friendly, affordable, reliable, timely-to-market
SME	Small and medium-sized enterprise
SOE	State-owned enterprises
SVA	Shareholder Value Added
TFS	TechCo financial services

TRE	TechCo real estate
TSR	Total shareholder return
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
US	United States
WACC	Weighted average cost of capital
WTO	World Trade Organization
WWW	Worldwide web

1 Foundation

1.1 Introduction

1.1.1 Motivation and research goals

> *"Today the changing nature of competition and the increasing pressure of globalization make investment the most critical determinant of competitive advantage."*[1]

In 1998, *Michael E. Porter* – who is one of the most-cited strategy researchers – already highlighted the importance of investment decisions within increasingly globalized economies for creating and defending competitive advantages. In 2013, globalization has entered a new phase in which the global economic power is shifting to emerging economies.[2] As a consequence, this **rebalancing of the global economy** creates new challenges for internationally operating companies.

According to the *International Monetary Fund* (IMF), 2013 is expected to be a turning point within the world economy. In this year the industrial production of emerging markets will overtake those of the developed economies[3] for the first time in history. In 2020, almost 50% of the worldwide GDP growth will be attributed to the **BRIC** countries[4]. The dynamic economic development will inevitably create emerging market multi-nationals (EMNCs)[5] which are serious competitors in their host markets. Moreover, these national champions will seek to dominate their industries on a global scale.[6]

In return, multinational corporations (MNCs) take their business overseas to the developing world in order to strengthen their positions in growth markets. However, developing markets also entail **significant risks**. In particular, BRIC investments are exposed to various challenges, as institutional voids, host governments and "national champions" dictate local business conditions for MNCs.[7] The failure of the *ThyssenKrupp* investment in a steel plant in Brazil is a current example in this respect.[8] Therefore, it seems necessary to design systematic investment decision processes to mitigate these arising risks and exploit upcoming opportunities.

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1 *Porter* (1998), p. 431.

2 Cf. *Roberts* (2011), p. 6. The terms "emerging" and "developing" economies, markets or countries will be used interchangeably hereafter.

3 The terms "developed" and "advanced" economies, markets or countries will be used synonymously in the following.

4 The acronym BRIC means Brazil, Russia, India and China and was invented by Jim O'Neill, a chief economist at *Goldman Sachs* in 2001; cf. *O'Neill* (2001).

5 Emerging market multinational (EMNC) will be used for multinational corporations having their origin in one of the BRIC countries.

6 Cf. *Khanna/Palepu* (2006), p. 62.

7 Cf. *Holtbrügge/Baron* (2011), p. 109.

8 For a documentation of *ThyssenKrupp's* investment project in Brazil see *Blasberg/Kotynek* (2012).

Yet, investment decision-making is not solely germane to implement corporate strategies and create future performance potentials from a firm-level perspective but is also a main determinant for the overall **economic development** and **social well-being**, e.g. by creating new employment.[9] Foreign investment projects are not always positively perceived in the home country due to the associated negative consequences for domestic corporate locations, such as relocations of labor to foreign low-wage countries. But in particular **German MNCs** are able to offset or even overcompensate their domestic declining demand by strengthening their international presence in emerging economies, as it can be observed during the recent European sovereign-debt crisis. This illustrates that foreign investment projects may have positive influences on the domestic position of MNCs and their environment due to stabilizing effects from foreign activities and growth markets.

The increasing practical relevance of foreign investments in Germany is also underpinned by the significantly increasing **foreign direct investment (FDI) activity** of German firms. The total outward FDI flows of German companies rose from USD 39 billion in 1995 to its peak of USD 164 billion in 2007.[10] The cumulative outward stock of German FDI amounted to USD 1.4 trillion in 2011.[11] These numbers indicate Germany's long-term globalization process. In contrast to small and midsize companies (SMEs) from other countries, German SMEs managed to emerge as world leaders in their niche markets.[12] This tendency may explain that the country was the world export champion between 2003 and 2008.[13] Thereby, exporting generally represents a preliminary stage of internationalization with further resource commitments – such as Greenfield investment or cross-border acquisitions – as foreign market know-how increases.[14] Therefore, the number and volume of FDIs is expected to further increase in the future.

However, as opposed to foreign entry modes with lower resource commitments, FDIs involve **complex decision processes**. A variety of investment configuration decisions has to be made, e.g. the target market selection, which are not relevant for domestic investments. Due to the international dimensions further external influences, such as exchange or inflation rates, have to be controlled.[15] Process complexity and **uncertainty** are driven by multiple agency-relations, unfamiliar economic environments or cultural distances, to name just a few.[16] Surprisingly, the review of prior research indicates that foreign investment decision processes within MNCs are almost unexplored. *Swoboda* criticized that the international management literature fails to provide practical recommendations concerning the design of internationalization processes.[17] From a

9 Cf. *Harris/Raviv* (1996), p. 1139.
10 Cf. *OECD* (2010b), p. 81.
11 Cf. *UNCTAD* (2012), p. 173.
12 Cf. *Simon* (2007a), p. 11.
13 Cf. *Jeremias* (2012), p. 239.
14 Cf. *Mutinelli/Piscitello* (1998), p. 495.
15 Cf. *Becker* (2005), p. 2.
16 Cf. *Fox* (1999), p. 47.
17 Cf. *Swoboda* (2001), p. 4.

theoretical point of view, foreign investment decision processes offer a variety of interesting research aspects due to their multidisciplinary nature.

Nonetheless, prior research is biased by focusing too narrowly on the investment decision evaluation with more or less sophisticated capital budgeting techniques. However, the investigated theory-practice gap of the 1970s – between theoretically proposed and practically applied capital budgeting models – was closed by the development of computer technologies and the rise of consulting firms which accelerated the **diffusion of sophisticated capital budgeting tools**.[18] Furthermore, this work takes the view that shareholder value is not solely created by applying sophisticated capital budgeting methods, but particularly through the investment case development in creating shareholder value accumulation. For this reason, this study is primarily interested in gaining a deeper understanding of the investment decision process as well as the underlying critical success factors.[19]

Certainly, investment decisions rely on business experience and intuition. But irreversible strategic investments involving high capital expenditures (Capex) should be thoroughly reflected, prepared and decided. For instance, *Barkema et al.* identified that it is crucial to adapt management tools to the challenges of internationalization in order to create shareholder value via foreign direct investments.[20] Structured investment decision processes and sophisticated capital budgeting models are assumed to be capable of supporting these requirements. Thereby, MNCs have to balance the conflicting demands of **decision process speed** and **decision process comprehensiveness** to keep pace with the dynamic environment within the BRIC countries.

To sum up, only a few studies have been undertaken to understand unfolding foreign investment decision processes within MNCs, so that the present work intends to address this research gap. Due to the low state of exploratory research and the high practical relevance of emerging market investments, the **overall objective** is to investigate decision processes for cross-border investments into BRIC countries in its real-life context within MNCs. This general goal can be divided into three sub-goals:

- The **first sub-goal** is to describe the foreign investment decision process of multinational corporations. Therefore, a multiple case study design is applied to empirically investigate two company-specific foreign investment decision processes. A cross-company analysis intends to explain process-related similarities and differences. Subsequently, critical success factors for the design of investment decision processes are discussed against the theoretical foundation **(firm-level)**.
- The **second sub-goal** is to explore country-specific challenges related to Greenfield investment projects in BRIC countries. Based on the investigated BRIC investments within the two MNCs, country-specific challenges are described and compared by political-economic and socio-cultural aspects **(country-level)**.

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18 Cf. *Haka* (2007), p. 705.
19 Cf. *Mittermüller/von Nitzsch* (2008), p. 779.
20 Cf. *Barkema et al.* (1997).

- The **third sub-goal** is to evaluate country-specific challenges along the investigated foreign investment decision processes by consolidating the firm-level and country-level results of the two preceding sub-goals. Thereby, the influence of the country-specific challenges on the identified critical success factors is discussed to draw analytical recommendations for the design of decision processes for investments in the BRIC countries **(cross-level)**.

To achieve these goals, foreign investment decision processes and their underlying success factors are empirically investigated in two German MNCs by applying a multiple case study design. Country-specific challenges for foreign MNCs are explored by focusing on interviews regarding investment projects targeting BRIC economies. This study aspires to reach **practical relevance** by identifying elements of the decision process that are critical for foreign investment strategies in BRIC countries. Country-specific challenges are evaluated according to their importance for the investment decision process.

The **theoretical relevance** arises due to the low state of research regarding foreign investment decision processes in MNCs. Furthermore, the future economic importance of the BRIC countries creates the necessity to deal with their country-specific challenges and related solutions to cope with them. Therefore, business administration – as an applied science – should deliver starting points for managers to overcome these country-specific challenges. Building on this, the **main contributions** of this study are threefold. First, this study contributes to a more **comprehensive understanding** of foreign investment decision processes in MNCs based on a broad interview database. Second, **BRIC country challenges** are explored for the first time taking a German MNCs perspective, so that results may differ compared to studies based on Anglo-American MNCs. Third, this investigation provides a **multi-perspective view** on foreign investment decision processes by analyzing interviews with managers, business developers and management accountants in order to consider the interdisciplinary character of the research object. Due to the practical barriers in business administration of gaining access to qualified interviewees, the broad and differentiated interview data base represents a strength of this study.

To sum up, this process-oriented study[21] contributes in gaining a better understanding of the dynamics in MNCs by observing sequences of events and their underlying generative mechanisms that are germane for foreign investments to be implemented in real-life contexts.[22]

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21 A detailed description of the characteristics of process studies and theories can be found at *Mohr* (1982). One important aspect is to differentiate between a process theory and a variance theory. A process theory aims to explain how certain outcomes come about rather than to explain different variances in outcomes. Similarly, a process theory comprises a temporal order of states and phases rather than relations of dependent on independent variables without temporal structure, c.f. *van de Ven/Huber* (1990), p. 213.

22 Cf. *Tsoukas* (1989), p. 522.

1.1.2 Outline of the investigation

The outline of the investigation is depicted in Figure 1-1 showing that the present study consists of five chapters. Following the introductory elaborations on the research motivation and the underlying goals, **chapter one** continues with a presentation of the main scientific objectives and epistemological streams of business administration in order to position the present work. Subsequently, relevant terms and definitions for the further analysis are elaborated. A basic comprehension of investment decision processes within the context of shareholder-value oriented corporations is subsequently provided. Besides the illustration of a process understanding, this section serves to highlight the interdependent relationship between corporate objectives and investment decisions. The section closes with a brief description of decision parameters that have to be specifically considered within foreign investment decision processes. The investigation proceeds by explaining the background of the BRIC phenomenon and its growing importance for MNCs which represents the main selection criterion for the underlying study. Finally, a research gap is identified by reviewing prior research with respect to foreign investment decision processes.

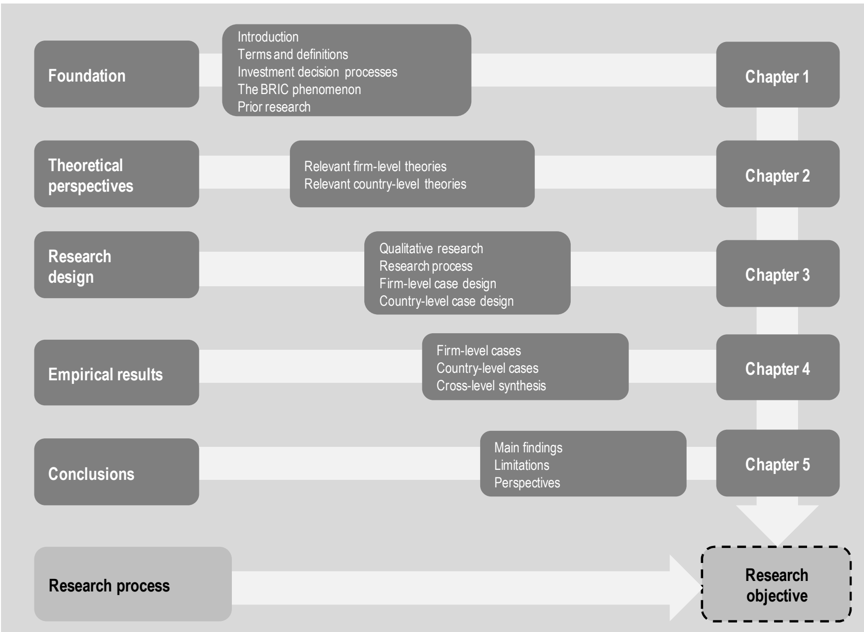

Figure 1-1: Outline of the investigation

Chapter two lays the theoretical foundation of this study. Firm-level theories in general and international firm-level theories are differentiated. The behavioral decision theory, agency theory and the promotor model have been selected as general firm-level theories. Subsequently, two international firm-level theories are introduced. The behavioral theory of *Aharoni* and the internationalization process model of the *Uppsala school* are explicitly concentrated on internationalization processes on the firm-level. This "analytical toolkit" or "theoretical lens" serves to analyze the empirical findings on the firm-level against this theoretical background. The next section presents relevant country-level theories which focus on explaining why and how country-specific challenges are related to foreign investments. Moreover, these concepts are introduced in order to highlight the influence of the internationality on the investment decision process and why country-specific challenges in the BRIC countries can be expected.

The research design of the present work is presented in **chapter three**, which is split into four major sections. In the first part, a brief overview of qualitative research and its underlying research principles is given. Characteristics of case study research are elaborated by illustrating alternative research design configurations. The selection rationale for the case study method in the present research context is disclosed thereinafter. Subsequently, the research process is revealed by describing the data collection and data analysis procedures. The specific firm-level and country-level case designs are elaborated in the last two main sections in chapter three.

Chapter four presents the empirical results in three main sections. First, the firm-level case study results are described in order to achieve the first research objective. For this, the two case studies of the German MNCs focus on delivering a detailed description of the company-specific foreign investment decisions processes. Subsequently, critical success factors of investment decision processes and company-specific process differences are discussed against the background of the introduced firm-level theories. The second section presents the empirical results on the country-level to indicate country-specific challenges for MNCs in the BRIC countries. In order to accomplish the second research objective a following cross-country discussion confronts the country-specific political-legal as well as socio-cultural challenges. Chapter four closes with a cross-level synthesis by consolidating the firm-level and country-level results to achieve the third research objective.

The detailed empirical results disclosed in the preceding chapter are briefly summarized in **chapter five**. Based on the empirical findings, managerial implications are derived for those corporations which consider investing in BRIC countries or other emerging economies. Moreover, the empirical findings shall deliver implications for invested MNCs to improve the performance of their foreign business in BRIC countries. This work has to be measured against the aspiration to achieve practical relevance or usefulness. The investigation closes with a discussion of its limitations and suggestions for further research.

1.1.3 Scientific positioning

This section serves to briefly introduce the philosophy of sciences and the underlying scientific position of the present study. Philosophy of sciences ("science of science") involves the question of *how* scientific progress can be achieved and new knowledge can be obtained. For this reason business administration as a centerpiece of economic sciences is subject to considerations of the philosophy of science.[23] Philosophy of science can be classified as a **meta-scientific discipline** to the individual sciences because it reflects what science is and what science could be. It articulates hypotheses about the science itself. In addition, the philosophy of science deals with the term, the classification, the principles of knowledge, the methods, the languages, the assumptions, the objectives and results of the single scientific disciplines.[24]

The discussion of objectives and basic procedures of science to generate knowledge are also parts of the philosophy of science. Science is not exercised as an end in itself, but to pursue designated objectives. For science in business management **four main objectives** prevail.[25]

(1) **Descriptive target of science**: A fundamental target of sciences in business management is the precise description of the subjects under consideration. In order to create a clear communication, terms, elements and features in business management must be defined.

(2) **Theoretical target of science**: The explanation and prediction of the subjects under consideration are elements of the theoretical target. For this reason, theoretical statements must be formulated as hypotheses ("cause-and-effect-relationships").

(3) **Pragmatic target of science**: If research in business management aims to provide decision support, a pragmatic target of science is followed. Through predictive abilities of a theory, recommendations for the composition of corporate structures can be derived. The former "cause-and-effect-relationships" are transformed into instructions for achieving practical objectives.

(4) **Normative target of science**: If science claims to articulate values how a corporation *should* act in specific contexts, an exchange between practice and theory is needed. These statements are usually not based on empirical data.

This work pursues an explorative descriptive target as corporate investment decision processes are reconstructed in their real-life context and country-specific challenges are presented. Furthermore, this study aims to provide recommendation with respect to efficient decision process designs. In order to highlight *how* these new insights can be gained, the **main epistemological schools** are presented hereinafter. Highly simplified, four epistemological basic positions are identified.[26] The four epistemological schools can be roughly displayed in a two-dimensional coordinate system. *Rationalism* and *empiricism* constitute the dichotomy regarding the importance of **experiences** on the horizontal axis; while *constructivism* and *realism* are the opposites concerning **reality construction** on the vertical axis.

The classical *rationalism* has its roots in the ancient science. Knowledge is based on understanding and logical reasoning, independently of experience. Consequently, the

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23 Cf. *Fülbier* (2004), p. 271; or *Kornmeier* (2007), p. 3f.

24 Cf. *Fülbier* (2004), p. 266.

25 Cf. *Schweitzer* (1978), p. 2ff.

26 Cf. *Kornmeier* (2007), p. 29.

strict rationalism is dominated by **deductive reasoning** ("from the general to the specific"). In *empiricism*, the sensory perception or experience are considered as the main source of epistemological progress. In contrast to the rationalism, the empiricism is characterized by **inductive reasoning**. For instance, an explorative investigation of decision processes without a theoretical preconception would be characterized as a purely inductive study. According to the empiricism, theories or rules are derived from a limited number of individual cases (from the specific to the general). This work combines deductive and inductive elements by developing an investment decision process model prior to the empirical investigations which is further refined within the course of the explorative case studies.

Representatives of the *realism* assume that there is an **independent reality**. Through human perception or thinking substantial parts of the reality can be reconstructed. Hence, humans can perceive things, phenomena or events without distortion.[27] The *constructivism* takes the view that reality depends on the individual subject and is a construct of the human spirit. This obviously means that a **subjectively perceived reality** differs among individuals and is not objectively describable.[28] All knowledge is constructed in as much as it is contingent on convention, human perception, and social experience.[29] Constructivism proposes new definitions for knowledge and truth that form a new paradigm based on inter-subjectivity and viability instead of objectivity and truth. Since generation of knowledge is dependent on humans, a subject independent reality cannot be described. For this reason, the value or quality of a theory is measured by the adequacy for predictions and practical recommendations for action.

But the radical positions of rationalism, empiricism, realism and constructivism are more or less outdated and seldom applied in their strictest sense in business management research.[30] Moreover, modern business management research combines elements of the four concepts. Thereby, two **predominant research programs** have been evolved in business management research.[31] The concept of critical rationalism – advanced by *Popper* – and the constructivism of the *Erlangen school* – advanced by *Lorenzen* – are the prevailing research programs in business administration in recent years.[32]

Critical rationalists hold that scientific theories should be rationally criticized, and (if they have empirical content) must be tested to falsify them. The basic assumption is that human reason is fallible, why results of rationalistic argumentation are not irrefutable.[33] Hence, knowledge can never be proven as ultimately true. Instead, knowledge is only temporarily true until it is falsified. Hypotheses must be formulated in a way that they are consistent and falsifiable by empirical testing. Not falsifiable theories are

27 Cf. *Frank* (2007), sp. 2012.
28 Cf. *Jonassen* (1991), p. 9.
29 Cf. *Jonassen* (1991), p. 10.
30 Cf. *Kern* (1979), p. 16.
31 Cf. *Kornmeier* (2007), p. 39.
32 Cf. *Fülbier* (2004), p. 268.
33 Cf. *Fülbier* (2004), p. 269.

worthless or non-scientific because they cannot fail in reality.[34] Vice versa, hypotheses gain in scientific value if they provide greater opportunity for falsification, e.g. the hypothesis "*if company A invests ten percent of sales in R&D, it will be five percent more profitable than its competitors*" is easier to falsify than *"if company A invests ten percent of sales in R&D, it will be more profitable than its competitors"*. Consequently, the first hypothesis has higher information content and is scientifically more meaningful than the second. Critical rationalists regard the falsification of theories and hypotheses as the main procedure for achieving scientific cognition. By advancing theories through permanently setting up, testing and rejecting hypotheses, truth is approximated.[35]

The **constructivism** of the *Erlangen school* should not be mistaken for the radical constructivism. The *Erlangen* version represents an epistemological position which criticizes philosophy of science and science in general.[36] The knowledge is the result of argumentation and discussion of experts in a special field of studies. On the basis of theoretical considerations conclusions are drawn by the help of deductive reasoning. Since in this approach the fallibility of human reasoning performance is recognized, these statements are not irrefutable. Opposite to the critical rationalism the constructivism postulates that methodologically sound decisions can be made.[37]

This work basically assumes that reality is rather socially constructed or perceived than objectively observable. As a consequence this work is more strongly influenced by the constructivist concept of reality. Based on this reality comprehension an open, communicative and context considering research design is necessary for empirical analyses.[38] This is consistent to the applied **case study design** in the present context. For instance, inter-personal misunderstandings can be clarified during the interview sessions. In contrast, common survey-designs assume an objective reality which can be mirrored and is independent of human experience and perception.

Furthermore, the present study uses an **empirical research strategy**[39] to achieve its scientific objectives because a multiple case study design has been adopted which is based on empirical interview data. Thereby, theoretical conceptions are tested, further refined or explored based on empirical data in real-life contexts of MNCs. The present work is of **qualitative-explorative** character. Thus, statistical generalization from the setting to a broader population is not intended. Moreover, the aim is to understand the

34 Cf. *Kornmeier* (2007), p. 41.

35 Cf. *Popper* (1994), p. XXV; or *Brühl* (2006), p. 594.

36 Cf. *Kornmeier* (2007), p. 40.

37 Cf. *Raffée/Abel* (1979), p. 6f.

38 Cf. *Wrona* (2005), p. 4.

39 Three basic research strategies can be differentiated: analytical, conceptual and empirical research strategies; cf. *Grochla* (1978), p. 79ff. The analytical research strategy seeks to simplify reality and specific problems in order to develop models which can be applied to solve these specific problems; cf. *Kaplan* (1986), p. 439. The conceptual research strategy intends to formulate interpretative-descriptive hypotheses related to a research problem. Hypotheses are not based on empirical but derived from argumentative reasoning and plausibility; cf. *Al-Laham* (1997), p. 10.

deeper structure and context of foreign investment decision processes. From an interpretative position the validity of a generalization from individual cases depends not on the representativeness of such cases in a statistical meaning.[40] Generalization validity is based on plausibility and cogency of the logical reasoning used in describing the results from cases and drawing conclusions from them.[41]

Apart from the consistent scientific positioning, the present work shares the general view of pragmatist researchers that the priority should be on answering the research questions, rather than selecting the "right" scientific method. *Tashakkori and Teddlie* (2007) describe the **pragmatic approach** as follows:

> *"Pragmatist researchers consider the research question to be more important than either the method they use or the paradigm that underlines the method. We refer to this as the 'dictatorship of the research question'."*[42]

1.2 Terms and definitions

1.2.1 Foreign investment projects

An investment is a commitment of resources in order to generate future cash flows and returns. Investment decisions belong to the tasks of strategic management to save, respectively enhance future performance potential.[43] The investment definition of this work is constricted to **strategic investments**. Strategic investments have a significant influence on the organization and its long term performance. Hence, investment decisions represent crucial management responsibilities. Managers can use investments as instruments to implement corporate strategies in order to sustain or expand competitive advantages.[44] Investments are future oriented. Hence, assumptions are required for the evaluation of projects. This means that the decision maker is confronted with **uncertainty** concerning the future external and internal conditions.[45] Predicting the events of the next twelve months is difficult enough, but looking five or ten years ahead is almost impossible due to the inability to foresee external changes in market conditions.[46]

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40 Cf. *Yin* (2009), p. 38f.
41 Cf. *Eisenhardt/Graebner* (2007), p. 27.
42 *Tashakkori/Teddlie* (2003), p. 21.
43 Cf. *Haka* (2007), p. 698.
44 Cf. *Ott* (2000), p. 54.
45 Cf. *Haka* (2007), p. 699.
46 Cf. *Maritan* (2001), p. 515f.

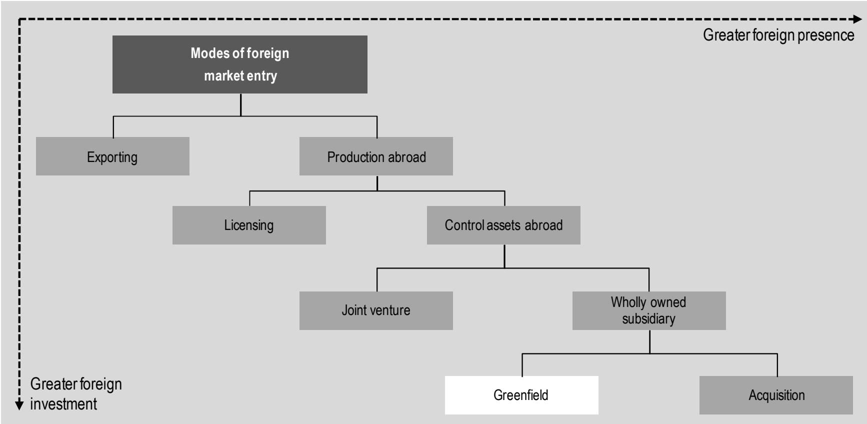

Figure 1-2: Foreign market entry modes
Adopted from *Eiteman et al.* (2010), p. 458.

Thereby, a central parameter within the foreign investment decision process is the **entry mode decision**.[47] Different criteria are germane to select an adequate market entry strategy, such as transaction costs, resource commitment, reversibility, flexibility or time-to-market.[48] As depicted in Figure 1-2 the two most challenging entry modes in terms of capital commitment and management requirements are Greenfield investments and cross-border acquisitions.[49] Partially, joint ventures could involve similar requirements due to the complexity arising from two or more joint venture partners with possible conflicting interests and high amounts of capital.[50] These three equity-based entry modes can be subsumed under the term **foreign direct investment (FDI)**.[51] Thereby, the investor intends to hold a long-term interest and influence in the investment.[52] Investors who undertake FDI are usually MNCs or on the development path to become a MNC.[53] As opposed to FDI, **foreign portfolio investments** are characterized by a short- to medium-term horizon of the investor.[54]

The present work intends to investigate expansion investments in foreign countries or so called **Greenfield investments**.[55] Greenfield investments occur when an investing

47 Cf. *Erramilli* (1991), p. 482.
48 Cf. *Erramilli* (1991), p. 483.
49 Cf. *Johnson/Tellis* (2008), p. 2.
50 Cf. *Gilroy/Lukas* (2006), p. 448.
51 Cf. *Chang/Rosenzweig* (2001), p. 748.
52 Cf. *Shimizu et al.* (2004), p. 311.
53 Cf. *Fox* (1999), p. 48.
54 The Organization of Economic Cooperation and Development (OECD) and the International Monetary Fund (IMF) have defined an interest of more than ten percent of the stocks or voting power of a foreign company as a threshold level for long-term interests; cf. *Betschinger* (2010), p. 11.
55 Although the term *Greenfield* may also refer to domestic investments, this work uses the term exclusively in the context of foreign investment projects.

company establishes new operations in a foreign country, e.g. the construction of a new plant in foreign markets.[56] Greenfields provide the highest control over the organization of internal resources, but involve the development of local know-how and establishment of relationships. Due to the high control over internal resources, technologically superior corporations may favor Greenfields in order to leverage their advantages.[57] In contrast, an acquisition of existing capacities in foreign markets is described as a **Brownfield investment**, e.g. the takeover of a foreign competitor.[58] The acquiring company intends to obtain the target's resources such as local knowledge bases, local market access and established supply or distribution networks.[59] In the following foreign investment projects, cross-border investments or international investment projects will be used synonymously to Greenfield investments.

1.2.2 Multinational corporations

This study aims to investigate foreign investment decision processes *within* MNCs. Therefore, it is necessary to disclose a working definition for MNCs in order to define the organizational context for the following investigation of foreign investment decision processes. Nevertheless, the term "multinational corporation" is **not consistently defined** respectively understood in literature, which makes it necessary to provide a comprehension of MNCs. This section intends to give a brief overview of the tedious theoretical discussion related to the definition of MNCs. Subsequently, the working definition of multinational corporations for this investigation will be presented.

The following definitions of MNCs illustrate the diversity of this terminology.[60]

> *"Corporations […] which have their home in one country but which operate and live under the laws and customs of other countries as well."*[61]
>
> *"A multinational firm is a firm owned by persons from many nations."*[62]
>
> *"The multinational enterprise is […] a closely controlled single enterprise, located in markets separated by national boundaries, and operating under several governments. Its essential feature is 'unity in diversity'."*[63]
>
> *"An 'international company' may be defined as one with foreign content of 25 per cent or more; 'foreign content' defined as the proportion of sales, investment, production or employment abroad."*[64]

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56 Cf. *Newburry/Zeira* (1997), p. 89.
57 Cf. *Hennart/Park* (1993), p. 1068.
58 Some authors only refer to the term Brownfield investment, when an acquired foreign target firm requires very deep restructuring; cf. *Meyer/Estrin* (2001), p. 575.
59 For a detailed meta-analysis of prior research regarding the influencing factors on foreign market entry mode decisions; cf. *Shimizu et al.* (2004).
60 For a detailed overview of different definitions for multinational corporations; cf. *Fischer* (2006), p. 15ff.
61 *Lilienthal* (1960), p. 119.
62 *Aharoni* (1971), p. 28.
63 *Behrmann* (1969), p. 62.

> *"A multinational company must possess the following five characteristics, (1) it must operate in many countries at different levels of economic development, (2) its local subsidiaries must be managed by nationals, (3) it must maintain complete industrial organizations, including research and development and manufacturing facilities, in several countries, (4) it must have a multinational central management, and (5) it must have multinational stock ownership."*[65]

> *"Transnational corporations are enterprises which own or control value-added activities in two or more countries. The usual mode of ownership and control is by foreign direct investment [...]."*[66]

A fundamental distinction between multinational and national corporations can be derived from the context and conditions in which they operate. Opposed to national enterprises, a multinational company operates in different social, political and economic conditions. Hence, MNCs are confronted with different socio-cultural norms and government regulations as well as with heterogeneous customer preferences. Therefore, the management across borders in MNCs is more **complex** and **diverse**, e.g. national corporations are concerned with the management and control of products and business functions, whereas the multinational management must also provide control over its **geographic diversity**.[67] Besides this additional global dimension, managers in MNCs are exposed to obstacles with respect to long geographic distances, time differences, language problems and national cultures.

This study uses the term multinational corporation for companies which have the two following main characteristics: (1) corporations must have **substantial foreign direct investments** in host countries, and (2) corporations must be engaged in the **active management** of these foreign assets opposed to passively managed portfolio investments.[68] The terms multinational corporation (MNC), multinational enterprise (MNE) and international corporation are interchangeably used for a corporation that conducts international business from a multitude of locations in different countries with employees from all over the world. Moreover, a significant characteristic of this understanding of MNCs is that the management disposes over a global mindset and outlook so that the operations of these corporations are not limited by national borders.[69]

1.2.3 Emerging markets

The focus of the present study is on investments in emerging economies – specifically the BRIC countries. Thus, a characterization of an emerging market country will be presented in the following. International institutions like *The World Bank, the Interna-*

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64 *Rolfe* (1970), p. 17.
65 *Maisonrouge* (1974), p. 8.
66 *Dunning* (1993), p. 1.
67 Important strategic management decisions within international contexts will be presented in detail in section 1.3.3.
68 Cf. *Bartlett/Ghoshal* (2000), p. 2.
69 Cf. *Khambata/Ajami* (1992), p. 5.

tional Monetary Fund (IMF) or the United Nations (UN) provide different country classification schemes. Finally, the understanding of the current work is disclosed.

The World Bank defines developing countries according to the annual gross national income (GNI) per capita.[70] This classification distinguishes between low, middle and high income countries, whereas middle income countries are subdivided into lower and upper middle income countries.[71] In 2012, the annual GNI per capita thresholds were as follows: low income countries equal USD 1,025 income per capita or less; lower middle income countries between USD 1,026 and 4,035 per capita; upper middle income between USD 4,036 and USD 12,475 per capita; high income countries equal USD 12,476 per capita or higher. Developing countries are referred to low and middle income countries. The World Bank does not use the term emerging economy on purpose because their country categorization scheme aspires to be objective and does not allow a judgment about the development status on the GNI per capita ratio.[72]

Advanced and emerging/developing countries are forming the two main country categories under the **IMF** country classification. This division of the world in two groups is not based on strict criteria and takes different country aspects into account. The IMF's intention is to facilitate analysis with a meaningful method of organizing data within a wider scope.[73] Per capita income level, export diversification and integration into the global financial system are expected to have a significant influence on the classification as this data is disclosed within the *World Economic Outlook* reports. But the respective weights or the influence of other aspects are not made explicit. Although the classification criteria are not publicly available, the IMF classification criteria for developed/advanced economies are more demanding than those of the other international institutions. The IMF classification has regularly the fewest countries categorized as developed or advanced.[74]

The **United Nations** country classification is based on the Human Development Index published within the Human Development Report.[75] This approach intends to capture the multilayered nature of a country's development. The Human Development Index is a summary composite index which covers the three human development aspects of health (measured by life expectancy at birth), knowledge (measured by a combined measure of actual and expected years of schooling) and income (measured by GNI per

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70 The main difference between GDP and GNI is that the latter comprises the market value of goods and services produced by state citizens and corporations regardless of their location, whereas GDP measures the market value of goods and services within a state; cf. *van den Bergh* (2009), p. 117.

71 Cf. *Gitlin/Fuentes* (2012), p. 298.

72 Cf. *The World Bank* (2012b).

73 Cf. *International Monetary Fund* (2012), p. 177.

74 One important reason for the fewer advanced economy classifications is obviously that export diversification is considered as a criterion. Oil-exporting countries such as Saudi Arabia and the United Arabic Emirates with very high GDP per capita are classified as emerging/developing country.

75 The Human Development Report is published since 1990 in order to create awareness for human development around the world. Opposed to other development reports, the well-being of people is placed within the center of this publication; cf. *The United Nations* (2012), p. 16.