Chapter 2
Strategic Options for MNEs Operating in Emerging Markets

Andreas M. Hartmann
Tecnológico de Monterrey, Mexico

ABSTRACT

This chapter outlines some of the basic opportunities, conditions, and strategic options for firms operating in emerging markets. Increasing FDI figures show that emerging markets offer many opportunities for foreign investors, but also pose specific challenges for doing business. Some factors are more abundant and less expensive, especially low to medium-skilled labor and natural resources, while sophisticated services are more difficult to obtain. A specific characteristic of emerging markets is the lack of business-enabling intermediaries. Therefore, foreign MNEs frequently need to fulfill tasks that are not within their range of activities in their home countries. Additionally, many governments in emerging economies act slowly and erratically; and laws are often not enforced systematically. In this context, foreign MNEs can choose between acquiring a local company, partnering up, or going it alone. The chapter looks at the pros and cons of these modes of internationalization and presents some concluding comments on the flexibility required by working under such conditions.

INTRODUCTION

Any company with significant operations in more than one country is a multinational enterprise (MNE) by definition. When the general conditions between the two or more countries are relatively similar, going international does not require major departures from the ways of doing business in the company's home base. Expanding operations from a developed country to an emerging economy, however, often demands significant changes. This chapter deals with the conditions and opportunities of such moves.

The traditional literature on multinational enterprises and their options for expanding into new markets has centered on two major themes: location choice and entry mode choice. For the first of these topics, there has been a certain discrepancy between the academic focus and the decision horizon for acting managers: While scholars prefer to look at the obstacles to internationalization that derive from cultural, administrative, geographic, and economic differences (Ghemawat, 2003), often under the label

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of "liability of foreignness" (cf. Denk, Kaufmann, & Roesch, 2012), practitioners are more concerned with opportunities opened through internationalization: On the supply side, the main motives are the availability of production factors, such as cheap or qualified labor, raw materials, or strategic locations, while on the demand side, growing and increasingly wealthy populations translate into market opportunities for goods and services to be sold to consumers, companies, and authorities. The second choice addressed by the scholarly literature on internationalization concerns the question whether a foreign enterprise should find a partner in the host country or whether it is preferable to establish a wholly owned subsidiary (either as a greenfield investment or through an acquisition), exposing the company to all the risks but also keeping full control and all of the expected benefits. Both research topics are typically framed as either-or decisions, where a company invests either in country A or in country B and then either operates with a partner or goes it alone.

The present chapter tries to deal with these issues a bit more from a practitioners' perspective: In many cases, the options for expanding are rather clear: Small firms need to consider issues of proximity or serendipity to expand into those countries where internationalization does not impose an excessive burden on their scarce financial and managerial resources. Large firms, on the other hand, need to access large markets with growth potential, such as the BRIC countries, or countries with abundant resources in order to keep up with international competitors. Once the location decision has been made, entry mode is often dictated by circumstances: The Chinese government, for example, requires foreign firms in many industries to work with a domestic partner. In other circumstances, finding a suitable partner might prove difficult. A third focus on strategic options for internationalization complements home-country activities with functions located in foreign country, thereby establishing internationally distributed value chains that take advantage of each location's particular strengths (cf. Coe, Dicken, & Hess, 2008).

This chapter is organized as follows: The first part establishes the general importance of emerging markets for MNEs from developed countries. The second part deals with the external conditions that these emerging markets offer to or impose on firms. The third part presents the option space for MNEs in the emerging market context. The concluding section looks at flexibility in investing abroad and at the special challenges of maintaining ethical business practices in countries with weak enforcement of regulations.

CONTEXT: THE INCREASING IMPORTANCE OF EMERGING MARKETS FOR MNES FROM DEVELOPED COUNTRIES

Even if the emerging economies still lag behind the developed countries in almost all socioeconomic indicators, they now have collectively become the target for more than half of the world's foreign direct investment. According to the 2014 World Investment Report, "FDI flows to developing economies reached a new high at $778 billion, accounting for 54 per cent of global inflows, although the growth rate slowed to 7 per cent, compared with an average growth rate over the past 10 years of 17 per cent" (UNCTAD, 2014: xiii). On the other hand, the developing economies accounted only for 32.3% of worldwide FDI outflows, which shows that the most common direction is still from developed to emerging countries.

The attractiveness of emerging economies as markets lies in their demographic and economic growth, which translates into growing markets for products and services. On the other hand, emerging economies often hold a plethora of underexploited resources ranging from raw materials to semi-qualified labor. These structural attractors are further enhanced by national governments inviting foreign firms through

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