EDITORIAL

Letter from the Editor-in-Chief

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Editor-in-Chief

Journal of International Business Studies
(2008) 39, 333–336.
doi:10.1057/palgrave.jibs.8400367

Volume 39, issue 3 consists of one Perspectives article, nine Articles and one Research Note, all accepted for publication by former *JIBS* Editor-in-Chief Arie Lewin. Two themes run through this issue. The first is uncertainty and its effects on firms' internationalization patterns and timing through exporting and foreign direct investment (FDI). The second is conflict and cooperation in international quasi-hierarchical organizational forms.

The issue begins with Morck, Yeung and Zhao's, "Perspectives on China's Outward Foreign Direct Investment", which analyzes China's outward foreign direct investment (OFDI) from the late 1970s to the present. With the characteristics of both an emerging economy (high growth, high volatility) and a transition economy (movement from a communist to a market-based system), China is a relative newcomer to OFDI. Its OFDI is relatively small, mostly conducted by state-owned monopolies, and biased towards tax havens and southeast Asian countries. At the home-country level, the authors argue that China's high savings rate, its corporate ownership structure dominated by state-owned monopolies in the natural resource and infrastructure sectors, and bank-dominated capital allocation are important, potentially distortionary influences that can lead to misallocated and wasteful OFDI. The authors also identify several possible firm-level influences on Chinese OFDI patterns; for example, state-owned monopolies have developed strong political wiles, which can be a firm-specific advantage in emerging economies with institutional voids and high corruption.

The Uppsala model of internationalization argues that lack of experiential knowledge creates psychic distance, a critical barrier to internationalization of the firm. Firms therefore start the internationalization process through exporting to countries that are psychically close to their home country. Ellis's article, "Does Psychic Distance Moderate the Market Size-Entry Sequence Relationship?", argues that the behavioral school is incorrect; firms do not expand into new markets through exports based on increasing psychic distance (i.e., psychic distance has no direct effect on market entry), but rather psychic distance is a moderator, weakening the negative relationship between market size and market entry sequence. Moreover, psychic distance interaction effects with country size are stronger for exporter-initiated than importer-initiated trade, and psychic distance asymmetries depend on differences in managers' experience and learning. Ellis finds support for his arguments with a sample of 924 foreign market entries made by Chinese exporters.

Fisch's article, "Investment in New Foreign Subsidiaries under Receding Perception of Uncertainty," applies real options theory to

sequential investment decisions in a host country. In real options theory, growth option value is the difference between a firm's current value and the value of its assets in place; it proxies for the firm's growth opportunities as valued by the market. Growth options affect firms' incentives for making strategic investments and the timing and structuring of investment. FDI provides growth options for firms, both as platforms for investment within a host country and across host countries. Fisch argues that high uncertainty raises growth option value and deters sequential investment whereas lower uncertainty raises net present value and encourages investment. Two forms of uncertainty are assumed: exogenous host-country uncertainty and endogenous uncertainty about foreign subsidiary performance. The author hypothesizes that investors make decisions based on subjective perceptions rather than objective measures of uncertainty, and that subjective uncertainty is high with initial entry and drops off over time due to learning in the host country. As a result, investors perceive receding levels of uncertainty and shift their metric for FDI from option value to net present value. A panel data study of 634 German subsidiaries provides support for the model. Fisch concludes that real options theory can improve our understanding of internationalization processes.

Real options theory is also the theoretical lens in Tong, Alessandri, Reuer and Chintakananda's, "How Much Does Country Matter? An Analysis of Firms' Growth Options". The authors observe that firms' growth options vary across countries due to country-, industry- and firm-level factors. The authors argue that previous researchers have focused on firm and industry levels, paying less attention to home-country explanations for growth options. Using a database of 12 home countries, the authors find that firm-level effects are most important for growth options, followed by country–industry interaction effects; the direct effects of industry and country are relatively small. Firm-level effects are larger and country–industry interaction effects smaller for domestic firms compared with MNEs.

Relationship-oriented banking systems characterize Japan, Germany, Switzerland, the Netherlands and most emerging economies. Wan, Yiu, Hoskisson and Kim in, "The Performance Implications of Relationship Banking During Macroeconomic Expansion and Contraction: A Study of Japanese Banks' Social Relationships and Overseas Expansion", examine the benefits and costs of relationship banking in the context of home-country

uncertainty. The authors argue that the financial performance of banks in relationship-oriented banking systems varies with the business cycle depending on the strength of bank–firm social ties. Strong bank–firm ties improve bank performance during upswings, but constrain bank performance during downturns. Strong bank–firm ties at home, however, are weakened when the banks follow their customers by going international. The greater the international diversification of the banks, the weaker are home-country bank–firm ties and therefore the weaker the impact of home-country volatility on bank performance in relationship-oriented banking systems. The authors find support for their arguments for Japanese banks over the 1990s.

The second set of articles in this issue focus on quasi-hierarchical modes of entry, including global strategic alliances as loosely coupled systems, partial acquisitions as a forgotten entry strategy, the greenfield-acquisition choice, joint ventures that tip over into acquisitions by one of the partners, and failed mergers due to incompatible resource deployment strategies. The issue concludes with a Research Note that brings us full circle, on how uncertainty and asset specificity affect the choice between relational ties and contracts for domestic and foreign firms in China.

Loosely coupled systems have components that are responsive to each other but maintain separate identities and physical locations. Luo, Shenkar and Gurnani in, "Control-Cooperation Interfaces in Global Strategic Alliances: A Situational Typology and Strategic Responses", apply the lens of loosely coupled systems to analyze global strategic alliances. Coupling facilitates cooperation among alliance partners, whereas looseness allows private control and opportunism. The authors develop a typology that varies by type of control (control for private gain vs control for collective gain) and level of cooperation (high vs low). They break control with cooperation into a 2×2 matrix with four cells, illustrate the range of strategic responses in each cell, and develop hypotheses exploring how these strategic responses are affected by relational characteristics such as goal congruity, resource complementarity, and bargaining asymmetry between foreign and local partners.

Mode of entry decision-making has been one of the most popular themes in *JIBS* for decades. Despite the huge number of articles on this subject, Chen argues, in "The Motives for International

Acquisitions: Capability Procurements, Strategic Considerations, and the role of Ownership Structures”, that researchers have ignored one mode of entry: the partial acquisition. When firms enter a host country, they can choose to set up a new operation (greenfield FDI) or acquire an existing firm (brownfield FDI). The firm can also choose to go alone or with a partner. These two decisions set up a 2×2 matrix. Greenfield investments break into two subcategories: “go alone” (a new, wholly owned subsidiary) or “with a partner” (a new joint venture, where the partner is either a host-country firm or another foreign firm). The same is true for an acquisition; it can either be alone (full acquisition) or with a partner (partial acquisition). In effect, a partial acquisition is a brownfield “with a partner” investment where the joint venture partner is the domestic acquisition. Chen argues that full acquisitions are motivated primarily by MNEs seeking complementary capabilities from host-country firms, whereas partial acquisitions are driven by other strategic motivations. Moreover, he argues that MNEs self-select full or partial ownership to justify their choice of a greenfield or brownfield entry strategy. Ownership and entry strategies are therefore not sequential, separate choices, but interdependent. Chen finds support for his arguments in a sample of Japanese investments in the United States in the 1980s.

The Chen paper implies that researchers who want to compare greenfield and acquisition investments as modes of entry must clarify whether the entries are alone or with a partner since the results can be confounded if, for example, the greenfields are all “with partner” entries whereas the acquisitions are all “alone”. Slangen and Hennart, in “Do Multinationals Really Prefer to Enter Culturally-Distance Countries through Greenfields rather than through Acquisitions? The Role of Parent Experience and Subsidiary Autonomy?”, take this point into account and focus only on the greenfield-acquisition choice for MNEs entering without a partner into culturally distant countries. When firms enter alone, the authors argue that MNEs generally prefer greenfield entries. This preference is lower when the MNEs have little international experience or plan to grant the focal subsidiary marketing autonomy; in such cases, MNEs prefer full acquisitions to greenfield investments. The authors find support for their arguments on a dataset comparing wholly owned greenfield entries with full acquisitions in 35 countries, made by Dutch MNEs over the 1995–2003 period.

International joint ventures are notoriously unstable due to their shared ownership. Previous researchers have focused on learning races, trust and host-country uncertainty as important predictors of joint venture instability. Steensma, Barden, Dhanaraj, Lyles and Tihanyi, in “The Evolution and Internationalization of International Joint Ventures in a Transitioning Economy”, contribute to this literature by asking, first, what factors influence whether a joint venture remains as a joint venture or converts to a wholly owned subsidiary? Second, of those joint ventures that do tip over and convert, which partner (local or foreign) takes control of the venture? Using a sample of Hungarian joint ventures, the authors find that the tipping point only occurs when there is *both* a power imbalance and high levels of conflict between the partner firms. A power imbalance provides the potential for, but not the inevitability of, exploitation by the stronger partner. Only when accompanied by conflict does a power imbalance appear to trigger the tipping point. Which partner takes over the joint venture depends on knowledge transfers and the degree of conflict. High knowledge transfers to the joint venture coupled with high conflict increase the likelihood of the foreign firm taking over the joint venture; in low conflict situations takeover by the local partner is more likely.

Meyer and Altenborg, in “Incompatible Strategies in International Mergers: The Failed Merger between Telia and Telenor”, explore the failed merger of two state-owned firms: Norwegian Telenor and Swedish Telia in 1999. Despite good organizational fit and high resource complementarity between the firms, they had incompatible strategies (e.g., differing answers to the question: “How should we deploy our combined resources?”). Given national governance structures established to protect national interests, the two state-owned firms could not resolve their strategic incompatibilities and the merger failed. The authors conclude that potential synergies may not be realizable when strategies are incompatible. Firms contemplating a merger should therefore watch out for incompatible strategies.

The issue concludes with a Research Note by Zhou, Poppo and Yang, “Relational Ties or Customized Contracts? An Examination of Alternative Governance Choices in China”. The authors hypothesize that as business transactions have become more complex in China, managers rely more heavily on relational ties as asset specificity and

uncertainty increase. Moreover, as uncertainty rises, managers turn to more customized contracts, regardless of the level of asset specificity. Interviews with 361 managers of firms in China in 2003 provide support for their argument. The authors also find that foreign ownership is negatively associated with relational ties and positively asso-

ciated with market contracts. When the sample is separated into domestic and foreign firms, uncertainty is positively related both to relational ties and to contracts for both subgroups; whereas asset specificity is positively related to only relational ties for both subgroups.