International Business Strategies after the GFC

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Abstract

International business strategies are affected by economic conditions, although the resource-based view would suggest that company resources are a more significant factor. This paper identifies differences in the international strategy behaviours of companies located in countries which; entered a deep recession as result of the GFC, a shallow recession and no recession at all. Empirical evidence is provided for companies with home country markets with each of these conditions. The ability of international strategy theories to explain these behaviours is considered. Based on observations of international businesses with home country markets in each of these categories, it is suggested that determinants of international strategy during financial crises (and immediately after) are influenced by the strength of the home country market, foreign market government protectionist behaviour, international exchange rate variations and local levels of rivalry.

1. INTRODUCTION

What are international businesses doing as the domestic and the global economy begins to recover? The answer to this is fairly complex. Some economies such as those of India and China have not experienced a recession and, whilst there has been a downturn in their international business activity - particularly in the area of development and internationalisation, the downturn has not occurred within the context of a recession in the company's home country. In other countries, notably the US and particularly, Iceland, the depth of the recession in the home country has had a much more profound effect on international businesses. In these countries, the GFC has lead to the collapse of major international businesses such as Lehman Bros and government decisions to bailout major international manufacturers such as GM (which would otherwise have collapsed).

A third category of country includes countries such as Australia and Singapore which briefly entered a recession, but not a deep recession. The recessions these countries experienced were predominately forced upon them by the increased cost of capital and the collapse of trade with trading partners who had entered deep recessions. Aggressive responses by their governments, greater inherent comparative advantages, larger central bank and commodity reserves and more robust financial and capital markets in these countries led to their economies rapidly returning to near normal trading conditions. As a result, the impact of these international businesses was much less. In some cases, the reduction in international competition allowed these businesses to increase their global

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market share to higher levels than preceding the GFC. For example, following Australia's return to economic growth, all four major Australian banks moved into the category of the 20 largest global banks.

This paper will consider the specific impacts of the GFC and responses of international businesses based in countries in each of the three following categories:

international businesses based with home countries that did not experienced recession
international businesses with home countries that did experienced recession, but strong financial and capital markets leading to rapid recovery
international businesses with home countries which experienced a deep recession

2. LITERATURE

Little research exists regarding frameworks of international business strategic behaviours during and immediately after recession environments. Economic theory predicts a reduction in internationalisation when the cost of capital is higher, which is experienced in a global financial crisis such as the one just experienced (Ricardo 1963). This prediction has been supported by a global reduction in foreign direct investment (FDI) of 30 % (UNCTAD 2009).

Empirical evidence from the 1991 -- 1992 world recession (which was not as deep as the 2008/2009 global recession) identified post recession international business responses of reducing internal costs. This was primarily achieved though flattening the hierarchies and outsourcing to lower cost countries. This outsourcing became viable due to these countries developing their technical and resource capacity to absorb such outsourced activities such as IT, accounting, basic manufacturing and call centre work in response to demands from international businesses based in developed countries (Sharpe 1997). The flattening of the hierarchical structures resulted from the removal of layers of middle management and the horizontal narrowing of their organisational structures as a result of outsourcing. This lead to more efficient domestic business operations. International comparative advantage theory predicts a reduced attractiveness for international activities resulting from the increased level of domestic efficiency. From an organisational design perspective, the reduction in management resources made strategic planning for internationalisation more difficult, reducing the rate with which companies internationalised (Jennings, 1997, Lei & Hitt, 1995).

A corporate strategy level perspective suggests that focusing on core activities also had the effect of directing these organisation's strategies away from diversification. Internationalisation is a form of geographical diversification. Supplying markets outside that of the home country requires the introduction of variations in products and services to suit local conditions and variations in the structure and operations of the local subsidiaries to match local work practices, regulations and conditions. Even companies producing global products and services (such as airlines and book publishers) found that the necessary level of organisational variation between that of the home country structure and that necessary to sustain subsidiaries in other countries was a sufficient barrier to internationalisation for companies with home countries recently recovered from a recession (Birkinshaw and Morrison 1995). The attractiveness of markets in host countries was reduced relative to the attractiveness of the home country markets because, having survived the recession, these organisations had learned to become more efficient and therefore more profitable in their home country markets.

Porter's theory of national competitive advantage points out that destination country features such as government and local industry supports are important factors in considering whether to internationalise to that country (Porter 2000). Post-recession, almost every government's policies (perhaps with the exception of China) have become more mercantile and focused on ensuring that the continuation of local industry. One of the main drivers of this mercantile policy is to support the needs of that country and in the face of uncertainty of supplying from other countries (Zhou and Vertinsky 2002). Porter's theory predicts the empirical observations above, in that less attractive government policy and a weakening of supporting industries (including capital markets) in almost every country as a result of the GFC, means that internationalisation should be less attractive until potential host countries have fully recovered from the impact of the recession.

Another of Porter's models, the five forces for industry attractiveness, predicts that, where the powers of suppliers are higher and the levels of rivalry are high, markets will be less attractive. This correctly supports the identified production internationalisation. Critical suppliers such as capital markets, finance and supporting industries will have high levels of power over their customers (i.e. the international business subsidiary) because of their rarity, whilst rivalry in markets will have increased due to a reduction in local demand resulting from local recessions.

The exchange-rate theoretical perspective suggests that the highly dynamic nature of international exchange rates, coupled with a high level of uncertainty of the value in the value of the US dollar (a currency frequently used for international trade transactions) increases the level of risk associated with international negotiations (Leung and Cheung 2007). Whilst currency hedging can be used to reduce the impact of currency variations, the cost of hedging (to provide the same level of risk as was possible prior to the GFC) has increased in response to the large currency exchange rate variations in the global market. In addition, just as it has become increasingly difficult to attract the capital necessary for large scale international transactions, it has also become much more difficult to acquire sufficient hedging for large scale international transactions. The cost and difficulty of hedging international operations to the same level of certainty as prior to the GFC, predicts a reduction in international transactions and internationalisation until such time as international exchange rate variations reduce.

Dunning's eclectic theory suggests that advantages such as prior internationalisation experience or a technological competency, the greater returns that international businesses have been experiencing with local subsidiaries and access to local country specialisations (such as raw materials in the case of South African diamond mines or low labour costs in the case of India) predicts a greater level of internationalisation and a more proactive internationalisation strategy (Dunning 2007). The high levels of internationalisation and aggressive internationalisation strategies in the economic boom preceding the GFC was supported by Dunning's eclectic theory. Dunning's theory also suggests that, when local market conditions are depressed, as a result of the local recession, the attractiveness of operating in those environments is also reduced. Demand conditions in many markets became less attractive as a result of the GFC and the local markets had less to offer international businesses, again due to the increased costs of capital and those countries governments' focus on ensuring the survival of domestic industries. For example, manufacturing cars in the US would have become less attractive because of the US government's moves to support the survival of the domestic US automotive industry. Dunning's eclectic theory, on balance, therefore predicts reduced internationalisation in the wake of the global recession.

The political theory perspective suggests that internationalisation, particularly into countries with unstable and risky political environments will be negatively affected. The impact of the GFC appears to have been to have reduced political activity levels in many countries and to have increased international and cooperative foreign affairs behaviours between fully developed countries (Ewing 2009; McMillan and Powles 2009). In poorly developed countries and some partially developed countries, such as some African countries and Middle Eastern countries, the impact of the global downturn appears to have been to increase political instability. Therefore, political theory predicts a shift in internationalisation towards internationalisation between moderately developed and fully developed countries with stable political environments as a result of the GFC.

3. EXAMPLES FROM INDUSTRY

These theories will now be considered in light of specific evidence of changes in the international strategy of companies with home country markets that: (a) never entered a recession, (b) briefly entered a recession and (c) deeply entered a recession, as identified in the introduction to this paper.

3.1 Companies with Home Country Markets in Deep Recession

International businesses based in countries such as Iceland, Japan and Ireland are continuing to display all time low levels of internationalisation and no medium-term plans to increase change this.

Toyota – Japan Toyota Motor Corp.'s profitability was badly affected by the GFC, resulting in a fall from record profits to record losses over 12 months (Greimel 2009). Whilst Toyota's industry rivals such as Honda Motor Co. and Nissan Motor Co. have been able to cut back operations, Toyota's Japanese operations were dependent on its export market and attractive exchange rates (Greimel 2009). In response, Toyota is planning to curtail all costs and get back to its original focus on quality. In reaction to global currency fluctuations, the lower value of currencies in countries such as the US and possibly mercantile behaviours of some of its host country market governments, it has decided to increase the percentage of local production in the products sells in its foreign markets (Bennett, Terlep 2009). This will be balanced by a reduction in production activity in

Japan (Automotive News 2009). It is also moving towards making its subsidiary in each country more independent of Toyota head office (Toyoda 2009).

Iceland -- Banking Industry Leading up to the GFC, FDI from Iceland had been quite substantial, including (in some cases) Icelandic companies acquiring foreign organisations larger than themselves. This internationalisation strategy was principally driven by the objectives of increasing economies of scale to globally competitive levels and gaining access to foreign markets (Óladóttir 2009). This internationalisation behaviour ended when Iceland entered a depression (OECD Economic Surveys 2009), precipitated by the collapse of the banking industry (Country Monitor a 2009).

Ireland -- all industry All international development activity in Ireland has ceased as a result of the weakness of the Irish economy which is in depression. For example, one of its major banks has already had to be nationalised to enable it to stay in operation and it is quite likely that most of the other Irish banks will also have to be nationalised to stop them from going out of business (Country Monitor b 2009).

US -- Exxon Mobil In response the GFC, Exxon Mobil reduced costs by outsourcing IT operations to lower cost Indian IT service providers (EmergingMarketsNOW a 2009). It also moved into related diversification such as research and development into biofuels. Interestingly, Exxon's website does not mention the GFC. The demand for energy in industries based in non-recession countries, Exxon Mobil has been able to maintain some internationalisation, but only using funds from international markets in the same regions. For example, it was able to finance a new liquefied natural gas project in Papua New Guinea with funding support from the International Finance Corporation, the Asian Development Bank, Italian credit agency Servizi Assicurativi del Commercio Estero and the Japan Bank for International Cooperation (Power Finance & Risk 2009).

These behaviours are strongly predicted by Porter's theory of national competitive advantage in that the increased cost of capital in foreign markets is an effective barrier to internationalisation. In addition, weak domestic exchange rates for countries still in significant recession will increase the cost of internationalisation, as predicted by international exchange rates theory. The political theory predicts this behaviour by suggesting that home country government initiatives will be focused on domestic business development, reducing the effective home country government support to internationalisation. Boeing's theory provides some explanation of this behaviour because organisations operating with home countries in deep recession are less likely to possess specific strengths of which the company can make use in foreign markets, as they contract back to core business in an effort to survive

3.2 Companies with Home Countries That Briefly Experienced a Recession

Countries such as Australia and Singapore experienced recession for only a few quarters and quickly return to economic growth because of strength in their domestic financial and capital markets, in conjunction with aggressive stimulatory behaviours of their governments. Companies from these home country markets quickly returned to internationalisation activities and maintained aggressive international strategies, but with some differences.

As a result of the relative stability of their home country environment, in conjunction with the exchange rate instability and reduction in attractiveness of domestic markets foreign markets companies with these home countries reduced their rate of internationalisation.

Australia – BHP Billiton response to the global financial crisis, BHP has reduced its international activities in the markets that have been most affected by the crisis (and in which demand for resources has been most affected). It is looking towards Asia, and particularly China, for the greatest opportunities and these are the markets where it will focus more of its attention (Argus 2009). BHP Billiton has also reduced its internationalisation in two regions where significant local development has been required. For example, it withdrew from negotiations with the Suriname government to mine alumina because of the lack of a local market (Mendes de Paula 2009).

Where BHP Billiton has continued internationalisation behaviours, it has attempted to use its size and position to create more attractive market. For example, the joint venture (JV) between BHP Billiton Ltd. and Rio Tinto PLC in iron ore mining in Western Australia will give the partnership an enormous bargaining power over the price of the iron ore that sells to one of its major markets. Twenty percent of BHP Billiton's sales are made in China (Argus 2009). Coupled with an iron ore pricing agreement which has also been established between Rio Tinto and Japan's Nippon Steel, these measures will create a more certain market for BHP Billiton.

Australia -- ANZ Banking Group In an approach similar to BHP, ANZ has continued to internationalise into nonrecession markets, such as those of Asia because of its access to home country capital markets and the growing demand in those foreign markets (Sibillin 2009). Also similar to BHP, ANZ attempted to make its foreign markets more attractive. In particular, ANZ aimed to become one of the top foreign banks in China by 2012 (Euroweek 2009), using a number of different approaches. For example, ANZ influenced the Chinese commercial banking industry to significantly increase the levels of corporate governance in that industry, to enable it to meet its corporate governance objectives (Ngee 2009). ANZ also invested in attractive acquisitions in nonrecession markets from competitors with home country markets in deep recession and capital shortages; for example, purchasing the Royal Bank of Scotland's retail and commercial Asian operations (MarketWatch 2009).

ANZ has also applied to the China Banking Regulator Commission for approval to set up wholly-owned local subsidiary and a rural bank in a West China province (Euroweek a 2009). These investments were funded with capital from its non-recession foreign markets as well. For example, ANZ raised 1 billion Australian dollars from the sale of bonds into Asian capital markets (Morrow 2009).

Singapore – Singtel SingTel also acquired businesses located in attractive markets, such as acquiring 30% of telecommunication operator Warid Telecom in Pakistan (Global Telecoms Business a 2009). It also negotiated with the Australian government to acquire a percentage of a proposed national broadband network (Venkat, et al 2009). In the same period, it entered into an international business partnership with Google and four other telecom companies to construct a high-speed communications cable between Los Angeles and Chikura in Japan (Global Telecoms Business b 2009), showing that it still has a longer term interest in both the US and Japanese markets. It also diversified in its home country market by acquiring the rights to show English Premier league football matches and other sport content there (Media 2009). SingTel also sourced capital from nonrecession markets, negotiating a US$713.3m loan with seven local banks (Euroweek b 2009).

In these countries, government intervention has made the home country markets quite attractive and has caused international businesses to switch some of their development investment up to their home country market rather than to foreign markets. International businesses with home markets such as Australia, which are located in geographical regions experiencing continued high economic growth, such as parts of Asia, and which had significant prior experience, still tended to internationalise in two these high economic growth rate foreign markets. Porter's five forces theory predicts a return to internationalisation activities in higher economic growth rate host countries because the threat of other new entrants (from other developed close countries) is reduced, internal rivalry in these countries is also lower because of the rapid rate of growth which means that companies can achieve growth on the basis of the country's economic growth rate without having to compete to increase their market share.

Exchange-rate theory also predicts this behaviour because, although the initial internationalisation investment outlay might be higher, interest rates in these home countries were generally at an all time low and the higher foreign markets currency exchange rates, resulting from the high levels of economic growth would result in greater profits to repatriate to the home country.

Porter's theory of national competitive advantage predicts continued internationalisation activities from international businesses with these home country markets into countries with high economic growth rates because the foreign market's government policy regarding FDI and the likely growth in supporting industries, as a result of that market's economic growth makes these regions attractive. For the same reasons, both Porter's five forces and national competitive advantage theory predict that companies with home markets recently emerged from recession and therefore more cautious than during boom times will find foreign markets still in recession unattractive due to the protectionist measures of local government, reduced size of these markets (reflecting reduced local spending power) and increased levels of rivalry (due to reduced market size).

3.3 Companies with Home Country Markets That Did Not Experience a Recession

Not surprisingly, countries with high economic growth rates leading into the GFC and which did not experience a recession maintained strong levels of internationalisation activity. The reduction in some of their foreign markets (particularly markets in countries that did enter a recession) meant that some international businesses were unable to maintain the same rate of internationalisation or, in some cases, were unable to survive due to their dependence on foreign markets that is entered deep recessions. Some international businesses took advantage of decline in share prices of their overseas competitors and attempted to acquire as many of these as possible as part of the corporate aspect of their internationalisation strategy.

China -- Sinopec Sinopec is one of China's largest patrol petroleum companies. Local demand has ensured that it remained profitable during the GFC, actually experiencing a profit increase in 2009 off 50% (Country Monitor c 2009). Whilst Sinopec is investing heavily in establishing production facilities and in exploration in China, it is also investing heavily in acquisitions outside of China. One of these acquisitions was the Swiss Canadian petrochemical producer Addax Petroleum Corp. It planed to make foreign investments of $20 million US in 2010 and 2011 (Wall Street Journal -- Eastern Edition 2009). In addition, it established a partnership with Japanese company Mitsubishi Chemical (Tremblay 2009), as well as establishing partnerships with Indian petrochemical companies and aggressively investing in many other countries such as Kyrgyzstan. To fund its acquisition, it formed partnerships with companies such as Kuwait Petroleum Corporation and released bonds into the Chinese bond market (Company Monitor 2009). Sinopec's international strategy is to meet the increasing domestic demands through expansion of its direct access to oil and gas assets (King 2009).

India -- Tata Tata Motors took advantage of the weakness of competitors with home country markets in recession and acquired the UK Jaguar Land Rover company, taking. It also introduced the world's cheapest car in 2009. It now carries a high level of debt which it needs to refinance (Economist 2009), showing it is still susceptible to some of the issues facing international businesses with home country markets in recession. Its consulting arm (Tata Consultancy Services) announced a net profit of US$ 300 million and increase in revenue of 25%, indicating that business activity remains strong in its home country market (Sheth, et al 2009). It has also been increasing its internationalisation in Asian countries which have not experienced a deep recession (EmergingMarketsNOW b 2009). It has also strengthened its activities in its home market in response to the economic growth there. For example, it is entered into a partnership with Microsoft India to launch a centre of excellence to support the local Indian market EmergingMarketsNOW c (2009).

Maintenance of internationalisation plans by international businesses with these home country markets is predicted by exchange-rate theory. The weakening of the exchange rate of currencies whose countries that have experienced a recession, relative to the home country currency of the international business makes companies with these home country markets attractive acquisition targets. This advantage would have been moderated, however, by the reduced revenue that income generated in these markets would convert to in the international business's home country currency.

This behaviour is also predicted by Dunning's eclectic theory which notes that local conditions are attractive due to reduced resources and capital available to local companies with which to compete against a business international business acquiring businesses located in that country. The international business's sustained competencies and access to capital would be valuable in these environments. This advantage would have also been moderated by the increased level of rivalry and possible protectionist behaviour of the foreign country's government in reaction to takeover plans of larger local organisations.

Porter's five forces and national competitive advantage theory do not predict this international strategy behaviour of acquisition of companies in weak foreign markets as local levels of rivalry would be greater in markets in recession and the power of customers and possibly suppliers would be stronger due to their relative rarity (reduced spending power of customers and collapse of some suppliers). In addition, local government behaviour and weakened supporting industry would have made these environments unattractive for investment.

4. CONCLUSION

This paper has identified three different international strategy responses to the global emergence from the GFC. The different international strategy behaviours can be categorised on the basis of whether the company's home country market experienced a deep and lasting recession, a brief recession or no recession at all. In all three cases, international strategy was affected by the GFC, dramatically reducing internationalisation rates for countries with companies with home country markets that experience deep recession, creating reduced, but highly focused internationalisation behaviours from international businesses with home country markets that experienced a shallow recession and a greater level of acquisition as part of the international strategy from companies with home country markets that experienced no recession at all.

These findings suggest that two principal factors are dominant in determining international strategy during times of financial crisis -- home country market conditions and the level of domestic industry protection introduced by the foreign country government in response to the economic downturn. Other factors including the variability in relative exchange rates also influenced international strategy during financial crises.

The behaviours of international businesses under these conditions were accurately (but not completely) predicted by exchange-rate variation, Dunning's eclectic and political theory. Corporate strategy, Porter's five forces and Porter's theory of national competitive advantage correctly predicted some of the behaviours of international businesses with home country markets that experienced some level of recession, but did not correctly predict the behaviours of international businesses with home country markets that did not experience a recession during the global financial crisis GFC.

These findings suggest a model for international strategy at times of financial crisis could include the following factors:

1. Impact of home country markets and home country capital markets

2. Foreign country government protectionist behaviours

3. International exchange-rate variations variability and relative values

4. Local levels of rivalry

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