The Two Waves of Outward FDI: The Role of Institutions on the Evolution of Emerging Multinationals

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1. Introduction

Outward foreign direct investment (FDI) from emerging multinational enterprises (EMNEs) has been a rising theme within international business literature due to the growth and anticipated increase in outward FDI from a group of emerging markets (Narula 2010; Kang and Jiang, 2010). There was very little outward FDI from emerging economies in 1990 but this has increased at an exceptional rate with outward FDI flows reaching above $570 billion in 2010 (UNCTAD, 2011). Developing and emerging countries are now becoming more integrated in the world economy with them accounting for 23.48% of all FDI outflows in 2010 (UNCTAD, 2010). The majority of FDI outflows from developing countries come from Asia and Latin America with a handful of countries accounting for a significant percentage of FDI within particular regions. The BRICS play an important role within their regions with China and India accounting for a large percentage of FDI in Asia, while, South Africa, Brazil and Russia being a large source of outward FDI in Africa, Latin America and in transition economies respectively. Although the most affluent and largest emerging countries are home to the most significant outward FDI from emerging markets (Narula and Nguyen, 2011), there are more developing and emerging countries increasingly being involved in outward FDI (Gammeltoft et al, 2010).

While there is currently a significant increase in research being done on EMNEs, the phenomenon of enterprises originating from developing countries investing abroad is not a recent development with examples of Argentinean firms going multinational in the end of the nineteenth century (Lall, 1983). Moreover, there is literature on the field of MNEs from developing countries, especially in Asia and Latin America, since the 1970s to the early 1990s (e.g. Lecraw, 1977, Wells, 1983; Lall, 1983; Tolentino, 1993). Despite the high level of interest in the internationalisation of EMNEs and the vast research on the topic, there are still debates on the extent to which traditional FDI theories explain the internationalisation process of EMNEs. One of the main issues against using traditional theories of FDI in explaining how EMNEs internationalise is due to their emphasis on ownership advantages in explaining the MNEs ability to go abroad. EMNEs have been able to venture abroad despite holding weaker ownership advantages compared to MNEs from developed countries which seems to be a direct conflict with traditional theories on FDI (Matthews 2002).

According to Peng et al (2008), an institutional- based view on strategy has emerged from literature on EMNEs and they argue that this has to be incorporated in future theories. They argue that the omission of institutional conditions in past theories is because previous theories on MNEs have primarily focused on developed markets. Research on EMNEs has shown, however, that institutions play a role in explaining their internationalisation process and this may explain their ability to internationalise despite holding weaker ownership advantages (e.g. Child and Rodrigues, 2005; Buckley et al, 2007; Cuervo-Cazurra and Genc 2008, Ramamurti 2008).

In the long run, there are three options for future research to take when analysing outward FDI from EMNEs. First, to extend the advantage which makes up an ownership advantage, this includes adding political skills and the advantage of being able to compete in unfavourable conditions (Ramamurti and Singh, 2008; Garcia-Canal and Guillen, 2008). This does have a drawback in that, the ownership advantage in Dunning's eclectic paradigm already distinguishes between asset advantages and transaction advantages and adding more variables will potentially mean that everything becomes an advantage in itself, thus making the theory too broad (Gammeltoft, 2010).

Second, there is the option of just extending the current theory beyond the scope and to re-examine the relationships, concepts and causalities. Buckley et al. (2007) believes that rejecting mainstream FDI theories is not necessary and only modifications are needed so they fit better for EMNEs. They continue to add that institutional factors, such as government support and capital market imperfections which include preferential lending could be incorporated in existing theory. Child and Rodrigues (2005) concluded in a similar way to Buckley et al (2007) in that theories need to be extended as opposed to replaced and introduced four potential extension areas. These were to accommodate EMNEs internationalising to compensate for their competitive weakness as opposed to taking advantage of their competitive advantages, government supporting internationalisation of EMNEs, the EMNEs ability to compete in heavily government involved countries and their ability to adapt their business practices to be able to deal with the institutional conditions of the host countries. Ramamurti (2008) argues that mainstream theory does explain why EMNEs internationalise, but an extended theory is needed to understand the competitive advantages of EMNEs and how they are developed and how they are able to compete with MNEs from developed countries.

The third option would be to start a new theory completely, Luo and Tung (2007) introduced the concept 'springboarding' and Matthews (2002) introduced 'linkage, leverage and learning' (LLL model). However, some scholars have argued that such a radical position is ultimately 'throwing out the baby with the bathwater'; this was most notable on Narula's (2006) commentary on Matthews' LLL Model.

This paper agrees that theories on FDI have to be extended to incorporate the differences in findings and observations between traditional MNEs and EMNEs internationalisation process. However, the paper will adopt the position of the first option of just extending the ownership advantages believing that would help explain the internationalisation process of EMNEs.

This paper will be split into five parts. The first part will briefly look at Dunning's (1981) eclectic paradigm and how well it sits with research on EMNEs. The second part will describe the first and second wave of EMNEs. The third part will look at liability of foreignness through psychic distance literature and the Uppsala Model and how well it is received in the context of MNEs from developing and emerging countries. The forth part will look at ownership advantages and institutions. The fifth part will conclude the paper and propose some research questions that if answered can help develop our understanding of EMNEs.

1.1. Eclectic paradigm vs. Theories on developing country MNEs

Dunning's (1981, 1988) eclectic paradigm is based on three advantages: ownership specific advantages, location specific advantages and internalisation advantages (OLI). According to the theory, for a firm to be seen as an MNE, it must engage in international value-adding activities and follow the three conditions of OLI. The firm must hold certain comparative advantages, known as ownership advantages and can include, a trademark, superior entrepreneurial skills and production techniques that they own and can harness over the local competitors. Ownership advantage is seen as a prerequisite of an international activity and the ownership advantages have to outweigh the cost of liability of foreignness. Dunning's OLI theory is built upon the work of Hymer's (1960) monopolistic advantages. Hymer 's (1960) work was based on the market imperfections assumption and argued that MNEs' monopolistic advantages (or unique advantages) which other foreign enterprises do not have are a key motive why MNEs engage in FDI. MNEs have to possess a monopolistic advantage in order to overcome the costs associated with foreign investment, the disadvantaged position they face against the host countries' indigenous firms and to ensure their foreign investment is a profitable one (Dunning and Rugman, 1985). Monopolistic advantage, a term now replaced by ownership advantages and firm specific advantages (FSA)[2] has had its definition broaden with subsequent work by Dunning (1988) leading to ownership advantage to be categorised as either asset type ownership or transaction-type ownership. Ownership asset advantages (Oa) are the proprietary ownership of specific assets including intangible assets, for example, technology, product innovations, trademark and reputation, management expertise or property rights. Ownership transaction advantages (Ot), is the ability of the firm to benefit from the transactional benefits (which are less than that of the transaction costs) during international production. Dunning's broader definition and introducing two types of ownership advantages was well received without much contest with regards to explaining outward FDI from developed countries (Dunning and Lundan, 2008; Goldstein, 2007).

Internalisation advantages are important for the MNE to engage in further international activities. Internalisation theory is based on 3 assumptions put forth by Buckley and Casson (1976:p33): 1) Firms maximise profit in a world of imperfect markets. 2) When markets in intermediate products are imperfect, there is an incentive to bypass them by creating internal and control the activities which are linked by the market. 3) Internationalisation of markets across national boundaries generates MNEs. Internalisation theory is the retaining of monopolistic advantages within the actually firm as the benefits of doing so outweigh the costs. When the firm has both ownership and internalisation advantage, location advantage determines whether or not the firm will engage in FDI. If the firm possess ownership and internalisation advantages but there is no location advantage in the host country, then the firm will opt for domestic production and exporting. If the firm only has ownership advantages, they will not be able to transfer comparative advantages within the firm and will have to opt for licensing (Dunning 1980; 1986; 1988).

[2] Ownership advantages and firm specific advantages are seen as interchangeable in this paper.

The OLI framework has faced criticism for the omission of provisions for explaining the internationalisation of EMNEs and the criticism is twofold. Firstly, EMNEs may not pose the same competitive advantages as traditional MNEs and so “if they invest abroad, it is not on the basis of “O”, and the parameters that determine the degree of “I” in their foreign operations are different” (Goldstein, 2007: 81). Moreover, early research on MNEs argued that the direct foreign investment is based on ‘monopolistic advantages’ the firms possess and these monopolistic advantages are akin to the entry barriers of new entrants (Lall 1983). Thus the multinationals deriving from developing countries entering into developed markets had to have monopolistic advantages that the host country firms did not have, which was not the case. This led to the notion that in fact EMNEs in developed markets did not always exploit their assets and in fact, they engage in asset exploration. In this asset exploration perspective, EMNEs internationalise as they need access to strategic resources and the ‘learning objectives that allow these firms to overcome the initial resource hurdles arising due to technological gaps and late mover disadvantages in international markets” (Aulakh, 2007: 237). Therefore, the strategy and the motivation of the internationalisation of EMNEs are to strengthen themselves through the addition of resources not available to them in the home country. Secondly, the OLI framework is viewed by some as a relatively static paradigm by only looking at the pre-existing advantages prior to making an FDI decision and it does not explain the accumulated advantages and experience from international involvement experience. This will lead to the evolution and development opportunities of improving the firms’ capabilities (Matthews, 2002a).

Matthews (2002a) proposed a theoretical framework based on observations on Asia-Pacific firms dubbed the ‘Dragon Multinationals’ and a series of subsequent work by (Matthews 2002b, 2006abcd, 2007) focused on resource based analysis which he argued is unexplained by the eclectic paradigm and other existing theories. Matthews argues that EMNEs do not hold domestic assets which are strong enough to be exploited abroad, which is how traditional MNEs have internationalised: “Rather their international expansion has been undertaken as much for the search for new resources to underpin new strategic options, as it has been to exploit existing resources. This is why they have to expand quickly, to consolidate gains that are fleetingly won. This is why they tend to rely on partnerships and joint ventures, to reduce the high level of risk involved in their leveraged strategies” (Matthews, 2006b: 17). Matthews (2002a) proposed the Linkage, Leverage and Learning (LLL) framework to conceptualise his observed gaps of the eclectic paradigm and the internationalisation of the ‘Dragon Multinationals’. Linkages are the collaborations with foreign firms such as joint ventures and other partnership forms within the global value chains, which is a method of accessing resources that the EMNEs lack internally. Leverage depicts the exploitation of global linkages and to become a ‘latecomer’ firm through harnessing their resources and cost advantages to compete at the international stage. Learning is the stage when the EMNE acquires competitive advantage sources and learn how to compete at an international level. The LLL framework, argues the global economy is a set of resources of the firm which is acquired through time before the internationalisation process happens and the EMNE becomes integrated in international activities (Matthews, 2006b). Research supports that the latecomer position is seen as an advantage in itself as many EMNEs and born global firms were exposed to an international dimension since they started their business operations (Li, 2003) and this has led them to catch up at a faster rate to traditional MNEs in terms of best practices and technologies. Other research that supports the LLL model from different countries include Klein and Wocke’s (2007) research on South Africa, Li’s (2007) research on China, Pananond’s (2007) research on Thailand and Elango and Pattnaik’s (2007) study on India. All these studies found that participation of global networks played a vital role in the internationalisation process and the building up of the EMNEs ownerships advantages.

In a contradiction to the OLI framework, where asset exploitation is the attended first motive, according to the LLL model the first phase is likely to be an asset-exploring motive (Matthews, 2006b). This is concurrent with other research which argues that the early stage of the firm’s ability to internationalise is a consequence of inward FDI activity from the country of origin of the EMNE, where local enterprises that establish into foreign production networks are able to enhance their capabilities (Luo and Tung, 2007; Li, 2007). Luo and Tung (2007) outline the EMNEs capacity to exploit the advantages from inward FDI (through participation in global value chains) which allows the participating firm to upgrade their capabilities and then they become competitive abroad through experimental learning. However, this depends on the ability of the participating firm, to take advantage of the resources taken though being part of the global value chain and the extent to which they are able and the foreign firm is willing to get access to the resources. It is also dependent of the domestic firm’s absorption capacity which is defined by Cohen and Levinthal (1990:p128) “the ability of a firm to recognize the value of new, external information, assimilate it, and apply it to commercial ends… to its innovative capabilities.”

The LLL framework has come under some criticism most notably that it exclusively focuses on EMNEs originating from Asia Pacific region (Narula, 2006). Moreover, there is growing evidence that some latecomer EMNEs in fact hold some unique competitive advantages that explains their internationalisation strategies (Dunning, 2006). Dunning et al (2008) accepted that EMNEs lack firm specific O-advantages, but they compensate this through their country origin specific ownership advantages which determines their outward FDI activities. Matthews also argued that being the latecomer in the global scene can be an advantage itself. The reason for this is that the opportunity the latecomer has on imitation of technologies and innovations which will lead to an accelerated catch-up process to other MNEs (Matthews, 2006 and 2007).

2.2. First wave and second wave of EMNEs

Research on EMNEs have come in two periods and have been sparked by the two waves of EMNEs, the first wave, is depicted by the early research in the latter period of the 1970s to early 1990s and are described by Ramamurti (2008) as infant MNEs. Lecraw's 1977 paper marked the first wave of research by introducing a new kind of MNE, one that differed from traditional MNEs from developed countries. Questions in subsequent studies started to ask how developing countries have been able to engage in outward FDI and what this would mean in terms of economic development for developing countries. This new involvement of outward FDI from emerging markets was greeted with great expectations with the hope that there will be more cooperation between emerging countries and an increase in the inflow of capital and skills coming into emerging markets (UN, 1993).

The first wave of EMNEs have similar patterns and characteristics, such as only internationalising to neighbouring and other developing countries and their main motivation being resource and/or market seeking. The earlier studies and edited books (e.g. Kumar and McLeod,1981; Lall, 1983; Wells, 1983), all argued that the main differences between traditional MNEs and EMNEs were the latter has weaker institutions in their home market, weaker proprietary advantages, latecomer status and so forth. In fact, a lot of these EMNEs only held fundamental Oa advantages and had very little Ot advantages. This was very different to traditional MNEs from developed countries that were internationalising on a global basis and their main motivation was efficiency seeking and held advanced Oa and Ot advantages (Dunning et al, 1997; Gammeltoft, 2008; Guillen and Garcıa-Canal, 2009; Narula and Nguyen, 2011). EMNEs internationalisation to neighbouring and other developing countries is due to their lack of international experience and lacking the ownership advantages to expand to countries with stronger economic development (Narula and Nguyen, 2011). The Uppsala Model in fact argues that companies' internationalisation process is taken in incremental stages first to countries that exhibited similar characteristics and then venture into other countries once they acquire international experience to able to compete in other countries (Johanson and Wiedersheim-Paul 1975; Johanson and Vahlne's 1977). Research found that the first wave of EMNEs internationalised by using mature technologies and that they internationalised to countries with similar or lower levels of industrial and economic development. This shows that the first waves of EMNEs O advantages were outdated and thus were only able to generate rents in host countries that exhibit similar conditions to theirs. Moreover, 81% of the FDI originating from developing countries came from only 15 countries (Narula and Nguyen, 2011).

The first wave of EMNEs led to influential work by the likes of Wells (1983) who looked at why "third world multinationals" (a term now replaced by EMNEs) opted to invest in joint ventures, branches and wholly owned subsidiaries abroad as opposed to licensing arrangements and exporting goods. His work was heavily influenced by the product-cycle model and the ability of EMNEs to change product technologies and processes to a low cost production and cheaper labour. Lall (1983: p. 261), looked at the ownership advantage in industrial technology and argued that EMNEs "develop advantages in specialized products and processes only if the localization of technical change … affords scope for the development of proprietary technological assets." Diaz-Alejandro's (1977) study on outward FDI by Latin American companies argued that technology at times is the main determinant of internationalisation of firms if they are entering into countries that are at a lower economic development level, while Tolentino (1993) added that the firm has to have the ability to go international in a learning-by-doing cumulative process. Oman (1986) also stressed that EMNEs offerings in terms of services and resources were better suited to match the needs of other developing and emerging countries. Different countries were able to internationalise for different reasons such as Argentinean and Indian companies having a stronger position on basic design capability and production engineering (Lall 1983), while in Brazil the EMNEs engineering contractors were able to execute specific technologies and large-scale projects under unfavourable environmental conditions (Guimaraes 1986). In Busjeet's (1980:p61, cf:

Goldstein, 2007) research on the Philippines and Mauritius he argued that “external market and cost considerations were more important in the foreign investment decision than the desire to exploit the skills and resources of the firm.”

Researchers started to see a change in the EMNEs characteristics during the end of the 1980s and early 1990s. This second wave of EMNEs is what Ramamurti (2008) calls ‘Adolescent’ MNEs. These MNEs are mainly still regional but are starting to expand more globally and the home CSA of where the EMNEs originate are also improving. Therefore, ownership advantages by virtue of being a function of location advantages are also improving, particularly the Oa advantages, however the Ot is still basic in the second wave of EMNEs. The location advantages have improved due to the increase in globalisation and thus access to more superior ownership advantages. However, not all the countries made the upgrade from infant MNEs to Adolescent MNEs such as Columbia and India (Guillen and Garcıa-Canal, 2009; Narula and Nguyen, 2011). Gammeltoft (2008) and Andreff (2003) argue that there is a third wave of FDI, however, as pointed out by Narula and Nquyen (2011) it seems to be an extension of the second wave of EMNEs. Gammeltoft (2008) paper shows that the motivation of the second wave includes asset seeking and thus the EMNE enters into developed regions not only to exploit their ownership advantage but for asset exploration. However, it is important to emphasise that the second wave of outward FDI from EMNEs simultaneously enter into both developed and developing countries. Table 1 summaries the differences between the first wave and second wave EMNEs against MNEs from developed countries.

Table 1: Characteristics of three types of emerging market MNEs

	"First wave"	"Second wave"	"Second wave+" (2000s)	"Conventional MNEs"
Ramamurti terminology	"Infant MNEs"	"Adolescent MNEs"		"Mature MNEs"
Destination	Regional FDI: neighbouring countries and other developing countries	Majority still regional, but expanding to a global basis		Global basis
Motivation	Resource seeking, market seeking in developing countries	In developing countries: resource and mark seeking In industrialized countries: asset seeking and market seeking		Efficiency seeking: MNE motivation aimed at optimizing use of each country's comparative and competitive advantages
Type of outward FDI	In developing countries: natural asset intensive, small scale production in light industries (Hecksher-Ohlin, moving towards undifferentiated Smithian industries)	In developing countries: natural asset intensive sectors as in first wave In industrialized countries: (a) assembly type, market seeking FDI primarily in Smithian industries (b) asset seeking investment in Schumpeterian industries	In between second wave and conventional MNEs	Capital and knowledge intensive (Schumpetrian) sectors capital/labour ratio dependent on natural/ created asset of host countries
Ownership advantages	Primarily country-of-specific. Fundamental Oa advantages, few Ot advantages	Both firm and country specific. Improving Oa advantages, Ot advanatges still basic		Mainly firms specific Advanced Oa and Ot advantages
Examples of ownership advantages	Conglomerate group ownership Technology (most adapted) Management adapted to emerging country conditions Low cost inputs (including managerial and technical personnel) "Ethnic" advantages	Conglomerate group ownership Management adapted to emerging country conditions Low cost inputs (including managerial and technical personnel) "Ethnic" advantages Some product differentiation Limited marketing skills Vertical control over factor/ product markets Subsidized capital		Large size – economies of scale Access to capital markets Technology Product differentiation Marketing know how Cross country management skills Globally efficient intra-firm activities Vertical control over factor/ product markets

Source: Narula and Nguyen (2011:p30)

2.3. Liability of Foreignness

While the general consensus is that Beckerman's (1956) paper coined the theory of psychic distance, the concept did not come into prominence until Johanson and Wiedersheim-Paul 1975; Johanson and Vahlne's 1977 studies of the internationalisation process of Nordic firms which subsequently led to the development of the Uppsala Model. The most commonly used definition for psychic distance is the one by Johanson and Wiedesheim- Paul (1975:308) who defines psychic distance as 'factors preventing or disturbing the flows of information between firm and market'. It is now widely accepted that psychic distance encompasses a wide range of factors and is not exclusively limited to transport or geographical factors; such factors include religion, education, culture, language, industry development and political systems (Boyacigiller 1990; Dow and Larimo 2009; Johanson and Wiedersheim-Paul 1975; Shenkar 2001). Some researchers (Bell 1995; Brewer, 2007; Pedersen & Petersen 2004) argue that the motive to enter into low psychic distance countries is that it is easier to gain knowledge from them as opposed to entering into large psychic distant countries. This is akin to the thoughts of Nordstrom and Vahlne (1994:42) who offered an adapted definition to the one of Johanson and Wiedesheim- Paul (1975): 'factors preventing or disturbing firm's learning about and understanding of a foreign environment'. Thus, it has been postulated that the greater the perceived dissimilarities, the more unlikely the country in question will be selected, due to the difficulties of transferring knowledge about the market. Therefore, psychic distance has an influential role on market selection, particularly in the initial stages of the internationalisation process (Petersen & Pedersen 1996; Stottinger & Schlegelmilch 1998a; Brewer, 2007). Moreover, the Uppsala Model argues that in the latter stages of the internationalisation process, the impact of psychic distance on market selection is reduced as the firm becomes more internationally active (Benito & Gripsrud 1992). If this is true, then arguably the firm does not in fact use objective methods to investigate future markets but depends more on subjective and on non-economic factors to screen markets (Brewer, 2007; Ellis 2000; Tornroos 1991; Cavusgil and Godiwalla, 1982).

The transaction cost theory gives an insight into the role which psychic distance plays in the internationalisation process. According to transaction cost theorists, psychic distance is correlated with transaction costs, with the greater the psychic distance the more transaction costs will occur due to the difficulties the distance presents when a company attempts to transfer their competencies and skills (Sousa and Bradely, 2008; Gatignon and Anderson 1988; Erramilli and Rao 1993; Williamson 1985).

Researchers (e.g.: Kogut and Singh 1988) in the past have concluded that firms find it easier to learn from foreign markets and are more likely to enjoy greater success when they enter into countries that are psychically close. However, O'Grady and Lane (1996) argued and found the opposite conclusion. As opposed to firms enjoying greater success when they enter into close psychic markets, they argue that: 'starting the internationalization process by entering a country psychically close to home may result in poor performance and, possibly, failure' (O'Grady and Lane, 1996). O'Grady and Lane (1996) argued through examples of Canadian firms that companies face a psychic distance paradox. The reason for this paradox is that the perceived familiarity causes the firm's decision makers to underestimate the dissimilarities between the domestic market and the new markets subsequently leading them to under prepare for the differences.

There has been little research on applying and testing the Uppsala Model and Psychic distance on EMNEs. While, Hong Kong is a developed market in it is own right, there was not many studies that tested psychic distance on non-western countries. Child et al (2003) examined the impact of psychic distance on the internationalisation process of Hong Kong firms through five case studies and found that three of the five companies had first internationalised to low psychic distant countries within South and South East Asia while the other two companies had opted for more psychic distant countries in Anglo-Saxon locations. However, it was made apparent that the latter was due to situations where psychic distance was either a) compressed or b) bridged. Compressing the psychic distance items depicts the narrowing of the perceived distance between the firm's home market and foreign countries. The compressing factors arise from macro developments, for example the influx of immigrants from Hong Kong entering into United States meant that one of the Hong Kong companies found an opportunity to enter into the American market to target the Hong Kong nationals and to have Hong Kong employees. Bridging factors are strategies the business uses to reduce the impact of the psychic distance items such as the use of a local partner to overcome some of the psychic distance uncertainties (Child 2009).

While the Uppsala Model is held with high regard, subsequent research has shown contradictory findings. For example, papers by Knight and Cavusgil (1996) and

Rialp et al (2005) found that born global firms contradict the notion that firms start their internationalisation process to psychically close markets and, more interestingly for this paper, firms that originate from emerging markets tend to ‘catch up’ and “leapfrog” over their established Western competitors through entering into developed markets that on the surface are psychically distant from their home market in order to build up their core competencies (Child and Rodrigues, 2005; Luo and Tung, 2007). While one could argue that this proves that the stages theory is weak and disproves the concept of psychic distance, Child et al (2009) argue and found that it actually disproves an assumption that businesses are unwilling to tackle the uncertainties that the psychic distance items generate. Thus, Child et al (2009) argue that despite the perceived uncertainties that high psychic distant markets present, businesses are still willing to enter into these markets particularly if the foreign market holds high attractiveness such as a big market size and a high growth rate. This is concurrent with Johanson and Wiedesheim- Paul (1975) who admitted that the size of the market may influence which markets to enter into. Furthermore, there has not been consistency within the literature of psychic distance; some have found that both cultural distance and psychic distance have a significant influence on the internationalisation process (Sousa and Bradley 2005; Pak and Park 2004; Evans and Mavondo 2002; Barkema and Vermeulen 1997) and others have not (Sethi et al. 2003; Mitra and Golder 2002; Stöttinger and Schlegelmilch 1998).

However, there are clear differences between traditional MNEs (i.e. does from the western developed countries) and which the Uppsala Model is built upon to EMNEs, table 2 shows some examples of differences. Traditional MNEs origins are based from the second industrial revolution with a surge of global expansion in the 1950s and 1960s with an accelerated shift toward liberalisation of trade and investment policies around the world (Guillen and Garcıa-Canal, 2009). These MNEs that originate from continental Europe and North America were able to expand through their superior tangible and intangible assets. They exploited these FSAs which were derived from their home country and then had a path dependent internationalisation process by gradually internationalising from country to country. These MNEs internationalisation process are thus likely to differ to that from EMNEs that have only really started to internationalise in the last three decades and already research has shown that some EMNEs have followed different patterns of international expansion (Guillen and Garcıa-Canal, 2009). There is also a contrast between the first and second wave of FDI from EMNEs with latter wave of EMNEs pushing to be leaders in their fields and not just marginal players within their industries which seemed to be the case with the first wave of EMNEs (Mathews, 2006a). Moreover, in contrast to traditional MNEs, EMNSs have used international alliances (Bonaglia et al., 2006; Garcıa-Canal et al. 2002) and acquisitions (Rui and Yip, 2008) to overcome the liability of foreignness in the host country. Therefore, there is a question mark on the extent to which the Uppsala Model is appropriate to explain the internationalisation process of EMNEs.

Table 2

The New Multinational Enterprises Compared to Traditional Multinationals

Dimension	New MNEs	Traditional MNEs
Speed of internationalization	Accelerated	Gradual
Competitive advantages	Weak: Upgrading of resources required	Strong: Required resources available in-house
Political capabilities	Strong: Firms used to unstable political environments	Weak: Firms used to stable political environments
Expansion path	Dual path: Simultaneous entry into developed and developing countries	Simple path: From less to more distant countries
Default entry modes	External growth: Alliances and acquisitions	Internal growth: Wholly owned subsidiaries
Organizational adaptability	High, because of their meager international presence	Low, because of their ingrained structure and culture

Source: Guillen and Garcıa-Canal (2009:27)

The major problem with the work done Guillen and Garcia-Canal (2009) and others looking at applying the Uppsala Model and psychic distance to EMNEs is that is does not make a distinction between the two waves of outward FDI from EMNEs. The paper argues in fact that the first wave of EMNEs would have more of a gradual and path dependent internationalisation process. The assumption is based on the first wave of EMNEs being regional based and tended to enter exclusively into developing countries Therefore hypothesis one is

H1. The closer the psychic distance between the home and host country the more likely the first wave of EMNEs will first enter the market.

However, the second wave of EMNEs tends to internationalise simultaneously to both countries that are psychically close and distant. This leads to the second hypothesis:

H2. There is no relationship between psychic distance between the home and host country and likelihood of the second wave of EMNEs will enter

Entering into countries that are psychically distant leads the EMNE to have higher levels of liability of foreignness' then they would face if entering into countries that are more similar. Referring back to the work of Child et al (2009), there was evidence that multinationals use bridging strategies such as joint ventures and acquisitions to overcome these problems. This is supplemented by Bonaglia et al. (2006) and Garcıa-Canal et al. (2002) that EMNSs have used international alliances and Rui and Yip (2008) that some have used acquisitions to overcome liability of foreignness. Therefore hypothesis three is:

H3. EMNEs choosing to first enter into host countries that exhibit higher levels of psychic distance to that of their home country are more likely to use bridging strategies such as a joint venture or acquisition

2.4. Home country location disadvantages and the role of institutions in the internationalisation process of EMNEs

There is not a generally accepted definition for institutions, but they are often referred to as the rules of the game. North's (1990: 3) definition of institutions is the most cited definition: "the humanly devised constraints that shape interaction. In consequence, they structure incentives in human exchange, whether political, social, or economic." North also distinguishes between both formal and informal institutions, which have embedded constraints, enforcement mechanisms and formal rules. Literature on EMNEs has started to focus more on institutions and their acquired competitive advantages through domestic formal and informal institutions (Peng, 2002; Child and Rodrigues, 2005; Tan and Meyer, 2007; Goldstein and Pananond, 2007; Peng et al., 2008). There are two types of institutions, macro-level and micro levels of institutions (Marinova et al 2010). Marinova et al (2010) classify the role of government policies, legal environment and regulatory landscape, as examples of macro level institutions and micro level institutions such as cheap finance, preferential treatment, direct encouragement by key politicians and government support for acquisitions to the individual EMNE. However, they neglect the informal level intuitions such as culture which Dunning and Lundan (2008) give examples of at both micro and macro level.

Research on institutions have tended to focus more on the micro level institutions of EMNEs with more focus on the central government role in influencing the EMNEs internationalisation process (Tan and Meyer, 2007; Ramamurti, 2008). Research on EMNEs originating from China has emphasised the importance of the role of central government and this is because many Chinese MNEs are State Owned Enterprises (SOE). Moreover, some private firms are selected by the government to receive support to go international through their go global policy which offers several incentives such as favourable tax regimes, preferential loans and joint venture partner selection of international partners to encourage technology transfer (Child and Rodrigues, 2005; Buckley et al., 2007; Athreye and Kapur, 2009; Athreye and Godley, 2009). Yiu et al (2007) looked at the increase in international ventures of Chinese firms. They analysed institutional variables, which included linkages with domestic institutions, such as financial institutions, central and local governments, research centres, trade associations and business networks. They found that these linkages with domestic institutions play an important role in their internationalisation process. They concluded from their results that institutional network ties were an important ownership advantage in their internationalisation process for firms originating in countries that are in the early stages of development.

At a macro level, institutions in the context of EMNEs tend to be discussed as home country specific disadvantages. There is a new stream of literature on EMNEs that has found that the EMNEs home country disadvantages gives the EMNE the ability to internationalise and compete successfully in the host country that have adverse conditions for businesses (Cuervo-Cazurra and Genc 2008, Ramamurti 2008). The literature on home country specific disadvantages is heavily influenced by the macro-level institutional factors. It is well documented that emerging markets have weaker location advantages than developed nations and this has led to EMNEs developing an ownership advantage. Ramamurti and Singh (2008) and Garcia-Canal and Guillen (2008) argue that as a result of operating in unfavourable conditions such as poor infrastructure and government restrictions in their home country, EMNEs have developed political skills and the advantage of being able to compete in adverse conditions that traditional MNEs are not used to. This is further supported by Child and Rodrigues (2005) who argued that academic research should focus more on the EMNEs ability to compete in heavily government involved countries and their ability to adapt their business practices to be able to deal with the institutional conditions of the host country.

Cuervo-Cazurran and Genc (2008) paper shows a high concentration of EMNEs is based in areas that are home to adverse business conditions. If one looks through the perspective of path dependence then their results should not be surprising. Eriksson et al (2000:308) define path dependence as an ‘incremental process where the pattern of behaviour by firms is contingent upon and a function of its past international experience. The knowledge accumulated in the past forms the trajectory for the future internationalization behaviour of firms’. Benito and Gripsurd (1992) found the sequence of locations that firms entered into was interrelated, suggesting that they were influenced by path dependence. Naidu and Rao (1993) and Bilkey (1978) suggest experimental knowledge, which is gained from the early stages of the internationalisation process and the knowledge from their home country is an important determinant of how much firms are willing to commit in terms of resources in their subsequent international ventures. In essence, the knowledge and learning have an impact on how the firm approaches the foreign markets (Forsgren, 2002). If one takes the concept of path dependence then it is feasible to argue that the firm will learn how to deal with adverse conditions in their home country and they can use this experience in other countries that have similar adverse conditions. This argument is also consistent with the Uppsala Model and psychic distance literature.

In a response for the strong research and calls by scholars to incorporate institutional factors to help explain how EMNEs internationalise, Dunning and Ludan (2008a) added a third advantage to Dunning’s Eclectic Paradigm. Institutional advantages (Oi), which argues that taking advantage of institutions in the internationalisation process is something that the firm owns and can leverage the advantage abroad. What is strong about Dunning and Lundan (2008) arguments is that they capture the macro and micro levels and distinguishes between the formal and informal institutions. Therefore, at a macro level if an EMNE is able to internationalise because they have developed the necessary ‘skills’ to engage in FDI in host countries with adverse business conditions due to their experiences in their home country than that is an advantage the EMNE has. Moreover, if an EMNE has home government support to internationalise (a micro-level institution), it is now an advantage they own and they can use this advantage to help to engage in outward FDI.

Past research has shown the EMNEs ability to compete in difficult institutional conditions that those MNEs from developed countries will struggle in (e.g. Cuervo-Cazurra and Genc, 2008). Traditional MNEs do not have the experience to deal with adverse business conditions in their home country. Thus when they enter into countries that have a difficult institutional environment, they face a higher level of liability of foreignness as they do not have the experience of dealing with such conditions in their home country. However, the EMNE can transfer its experiences of dealing with adverse conditions to the host country giving it an ownership advantage that traditional MNEs do not have. The paper has already postulated that the first wave of EMNEs internationalisation process is path dependent and tends to enter into developing countries. Developing countries tend to be home to countries with poor institutional environments and the first wave of EMNEs enter into countries that they can exploit their ownership advantages. Building upon the work of Dunning and Lundan (2008) and basing it on the theory of path dependence the paper supports the argument that EMNEs do possess Oi at a macro level and as the EMNE has learnt to deal with adverse institutions they will be able to compete in host countries with similar conditions to their home country (Garcia-Canal and Guillen, 2008). Thus hypotheses, four, five, six and seven are:

H4. The weaker the legal system of the host country the more likely the first wave of EMNEs will enter

H5. The higher the political risk of the host country the more likely the first wave of EMNE will enter

H6. The lower the control of corruption the more likely the first wave of EMNE will enter

H7. The weaker the regulation of the host country the more likely the first wave of EMNEs will enter

Referring back to the literature on second wave of EMNEs, one of the characteristics is that they tend to internationalise simultaneously to both countries that are from developing and developed markets. The process of second wave of EMNEs is not path dependent and thus hypotheses eight, nine, 10 and 11 are:

H8. There is no relationship between the conditions of the legal system of the host country the likelihood the second wave of EMNEs will enter

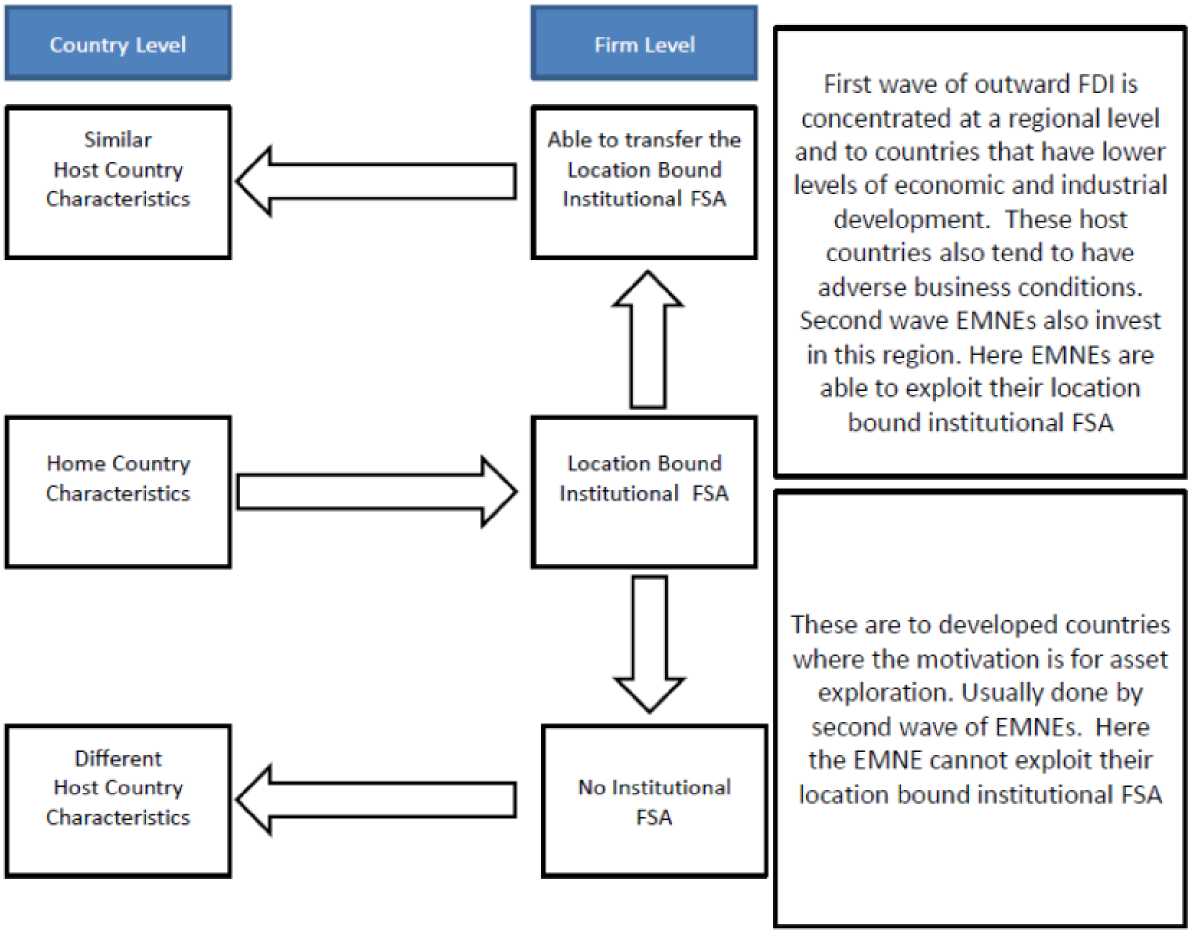
H9. There is no relationship between the political risk of the host country and the likelihood the second wave of EMNE will enter

H10. There is no relationship between the control of corruption of the host country and the likelihood the second wave of EMNE will enter

H11. There is no relationship between the regulations of the host country the likelihood the second wave of EMNEs will enter

This paper in fact argues that Oi is a location bound FSA and can only be an advantage in some countries. Looking at Oi at a macro level, it is only applicable when they enter into a host country that shares similar characteristics to that of the home country. The framework below is based on the literature from the first and second wave of outward FDI from EMNEs, psychic distance, the Uppsala Model, path dependence and institutions. It is important to emphasise that the framework is based on four assumptions; firstly, Oi is a location bound institutional FSA and can only be used in host countries that exhibit similar characteristics to the home country. Secondly, this Oi is developed from a learning process as depicted in path dependence literature, i.e. the EMNE has learnt how to deal with adverse business conditions and uses that knowledge to deal with adverse institutions in the host country. Thirdly, the internationalisation process of the first wave of EMNEs is path dependent and finally, the second wave of EMNEs tends to internationalise simultaneously to both developed and developing countries and when entering into countries with similar characteristics they take advantage of their location bound institutional FSA.

Framework: Institutional Advantages as a Location Bound FSA



2. Conclusion and Research Questions

The paper is based on the premise that the inclusion of Oi will suffice in explaining outward FDI from EMNEs. This will perhaps explain why EMNEs will enter into developing countries but less so on EMNEs entering into developed countries. The paper believes that the motivations put forward by Dunning's eclectic paradigm explains south-north FDI and that while the motive is not always to exploit the ownership advantage of the firm, it could be motivated to improve the EMNEs ownership advantage. Thus the ownership advantage still plays an important role. The paper argues that the EMNEs not only exploit their ownership advantages in developing countries but through their location bound institutional advantage they are able to leverage on their experiences of dealing in adverse institutional environments in their home country. Current research on EMNEs are limited in that majority of the generalisation of theories on EMNEs come from studies based heavily on Chinese MNEs. China itself holds very unique characteristics (Child and Rodrigues, 2005; Buckley et al, 2007) and thus it is questionable to what extent this research can be applied to other regions. The paper argues that addressing these following questions outside the context of China, will give us a better understanding of how EMNEs internationalise and answer the question; to what extent is Chinese MNEs a unique case?

- To what extent does "mainstream" FDI theory explain the internationalisation process of EMNEs? I.e. do EMNEs internationalise in a conventional way?

- What are the host country characteristics that attract EMNEs and do they influence the market entry strategy they take?

- Do EMNEs learn from their home location disadvantages and use their experiences to enter into countries with adverse institutional conditions?

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