

HOW TO BETTER GOVERN EMERGING MULTINATIONAL CORPORATIONS: DO CEO

CHARACTERISTICS MATTER?

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ABSTRACT

There has been a wide array of research on corporate governance and its impact on firm internationalization in the field of management. Scholars have looked at what governance elements may become critical in different contexts while multinational corporations are adopting to international markets. In general, emerging economies offer such a unique context in terms of understanding how different macro-level factors may influence the performance of these local businesses globally. In this paper, after providing a brief review on widely-used theories in firm internationalization including motivators for such efforts, I examine the impact of some CEO characteristics on the performance of emerging multinational corporations (EMNCs). In particular, I argue that younger CEOs of EMNCs will help their companies better perform in other foreign markets and this relationship is positively moderated by the CEO international experience. I also argue that the CEO duality will (not) become helpful for these EMNCs' international performance if the host country is an emerging economy (a developed economy). This theoretical work is grounded in upper echelons perspective and agency theory.

Keywords: Firm internationalization, Emerging multinational corporations (EMNCs), CEO age, CEO duality, CEO international experience.

INTRODUCTION

Firm internationalization has been widely researched in the field of international business (IB) in order to understand critical antecedents for such efforts, motivators leading companies towards this strategic path, and challenges that they may face including possible consequences. Andersen (1997: 29) defines the very concept of internationalization as follows: "Internationalization is the process of adapting exchange transaction modality to international markets." Sanders, Carpenter, and Gregersen (2001) enhance this definition by arguing that the firm internationalization enables multinational corporations (MNCs) to explore unique business ideas overseas and leverage resources without limitations of geographic distances.

An important context for the firm internationalization is emerging economies. According to Hoskisson, Eden, Lau, and Wright (2000), emerging economies are defined as the "low-income, rapid-growth countries using economic liberalization as their primary engine of growth" (p. 249). They further argue that in order to identify a country as an emerging market, there are two particular criteria that need to be met: "a rapid pace of economic development and government policies favoring economic liberalization as well as the adoption of a free-market system" (Hoskisson et al., 2000: 249). Because of their unique characteristics, these markets provide a "rich-setting" for testing theories (Bruton, Ahlstrom, & Obloj, 2008). More specifically, since emerging economies possess many unique resemblances among each other and distinctions compared to developed markets, it can be argued that researching in this context may provide some novel perspectives to those scholars who examine how these similarities and differences are actually expected to affect firm performance.

In this paper, after briefly discussing motivators for internationalization and related theories that help to explain this very process, I look at the impact of CEO characteristics on the EMNCs' performance overseas. In particular, I examine how the CEO age, duality, and international experience may or may not help to improve firm performance. According to the upper echelons perspective, younger top executives have the ability to process critical information better and faster and therefore, they can take bold actions in order to support the growth of their companies instead of being committed to the status quo. In this context, younger CEOs can be expected to better contribute to the success of their companies by also relying on the information and experience that they have gained throughout their international appointments. According to the agency theory, the CEO duality may prevent from potential conflicts in decision-making at the top level since it gives the whole executive power to only one individual, which might also result in less effective board monitoring. In this context, depending on whether the economy is either emerging or developed, I argue that the CEO duality may show different effects on either economy. In particular, the CEO duality can become a useful corporate practice in terms of improving the performance of EMNCs in other emerging markets; however, it is quite possible to observe an opposite effect in other developed markets.

LITERATURE REVIEW: MOTIVATIONS FOR INTERNATIONALIZATION AND RELATED THEORIES

Emerging economy firms have to deal with challenging environmental conditions that they may not be familiar with while entering other foreign markets. In order to be perform well overseas, they have to adapt their existing strategies to specific conditions of those new

markets where they enter (Aulakh, Rotate, & Teegeen, 2000). Entering emerging economies is particularly very unique because of these two aspects: “institutional development in different emerging economies directly affects entry strategies, and investors’ needs for local resources impact entry strategies in different ways in different institutional contexts” (Meyer, Estrin, Bhaumik, & Peng, 2009: 62). Basically, different types of institutional structures and uniqueness of local resources can be considered distinct characteristics of these markets. Therefore, it is extremely important to examine and understand what actually motivates these cross-border transactions over domestic ones.

In general, primary motivators for firm internationalization between emerging economies and other foreign markets can be listed as *market seeking*, *resource seeking*, *cost reduction*, and *organizational learning and exploration*. According to Athreye and Kapur (2009), one of the most important reasons why emerging economy firms venture abroad is to “gain access and proximity to overseas markets” (p. 214). For instance, emerging economies such as India and China prefer investing abroad since they look for new markets via bringing in their products and services (Athreye & Kapur, 2009). Beule and Duanmu (2012) also argue that multinational firms usually look for relatively large markets in which they can bring their “market-, natural resource- or strategic asset-seeking investments” (p. 266). Therefore, having an access to new markets should be considered an important strategic path for EMNCs.

Resource seeking is the second important component for moving into another foreign economy for EMNCs. According to Carmody (2009), China shows a great deal of interest on African markets because of the availability of natural resources such as oil and mineral resources. Beule and Duanmu (2012) also argue that increased demand to EMNCs’ products

and/ or services make these firms move to other markets in order to seek more resources. Therefore, gaining an access to abundance of resources (raw material, labor, etc.) for both improving operations and reducing economic deficiencies will become another critical determinant of performing better for EMNCs (Shirokova & Covin, 2012).

Reducing the cost of goods is another important factor of internationalization for EMNCs. In this context, Athreye and Kapur (2009) define "*frugal engineering*" by stating that for some countries such as India and China, it is very important to manufacture its products at the lowest possible cost. That's why these countries tend to go to Africa to find cheap labor and material (Hart & Padayachee, 2000) so that they can reduce the overall cost of their production. As Baack and Boggs (2007) also argue, if EMNCs are able to reach efficiency in their production via having a direct access to economic assets and labor force, they will be better able to differentiate themselves from others towards becoming new "*cost leaders*" in the industry.

Organizational learning and exploration is the fourth critical component that EMNCs look for while entering other foreign markets. As Chittoor (2009) argues, once emerging economy firms decide to go international, one of their primary focuses is to explore resources and capabilities that already exist in those new markets as well as to exploit them. In addition, throughout internationalization, when an EMNC enters a new market, it can better expand its operations via using its existing know-how as well as acquiring novel know-how (Chittoor, 2009; Hitt, Tihanyi, Miller, & Connelly 2006). Thus, this very learning process overseas is expected to significantly benefit EMNCs towards long-term survival.

In the literature, there have been several theories and perspectives used to “explain why multinational firms exist” and how they function (Oviatt & McDougall, 1997: 86) including the transaction cost theory (TCT), agency theory (AT), eclectic theory (ET), resource-based theory (RBT), institutional theory (IT), and linkage-leverage-learning (LLL) perspective. First, according to Hoskisson et al. (2000: 254), the TCT focuses on “the firm-environment interface through a contractual or exchange-based approach.” The underlying consideration of this theory is how to minimize the cost while entering new markets (Andersen, 1997). Second, Jensen and Meckling (1976: 308) define the agency relationship as “a contract under which one or more persons engage another person to perform some service on their behalf which involves delegating some decision-making authority to the agent.” According to the AT, there is going to be some cost associated with decision-making processes done by the agent (Jensen & Meckling, 1976), which is required by the principal. Third, the ET explains internationalization activity of multinational corporations (Athreye and Kapur, 2009) by considering its three main aspects, namely the ownership, location, and internalization. As Brouthers, Brouthers, and Werner (1999) explain, the *ownership* dimension looks at control issues within firm’s transactions; the *location* dimension looks at resource-related issues such as availability and cost; and the *internalization* dimension looks at cost-related issues for transactions as well as firm’s coordination efforts. Fourth, the RBT is defined as “a theory of strategy and of sustainable rent” (Kogut & Zander, 1992: 509). They argue that choosing appropriate resources is a highly complex issue for firms, especially when there are high barriers to the entry and an uncertainty exists (Kogut & Zander, 1992). This theory becomes more critical in the context of foreign entry since it helps the entering firm better “develop the capability of combining the requisite foreign

and domestic resources” (Guillen, 2000: 368). North (1993: 12) defines institutions as “rules of the game.” Fifth, the IT argues that “the role of institutions in an economy is to reduce both transaction and information costs through reducing uncertainty and establishing a stable structure that facilitates interactions” (Hoskisson et al., 2000: 252). And finally, the LLL perspective suggests that “multinational latecomers engage in foreign direct investment to achieve new competitive advantages via *external* linkage, leverage, and learning rather than exploiting existing internal advantages via *internal* control” (Li, 2007: 299). As Athreye and Kapur (2009) argue, the main idea of this perspective is that latecomers will have to utilize their global connections in order to both learn some new ways for improving their competitive advantage and leverage their current operational advantages so that they can minimize prospective problems related to finding resources, reducing transaction costs, and enhancing coordination efforts during their cross-border operations.

THEORY DEVELOPMENT: CEO CHARACTERISTICS AND EMNCs PERFORMANCE

Aguilera and Jackson (2003) define corporate governance as “the outcome of interactions among multiple stakeholders” (p. 449). In the literature, it has been argued that governance structure of the firm is expected to significantly affect firm performance via both harmonizing conflicts of interest between agents and principals and improving the wealth of shareholders (Baysinger & Hoskisson, 1990). Bell, Filatotchev, and Aguilera (2014) also argue that governance mechanisms may have important impacts on improving stock market valuation of the firm and in turn gaining legitimacy. Although corporate governance practices might vary significantly around the globe (Chizema & Shinozawa, 2012), enhancing value creation via

utilizing the most effective practices is at the core of this phenomena (Carney, 2005). Three main pillars of corporate governance include the board, top management, and shareholders of the company. In this paper, the main focus will be on the CEO as the highest rank executive officer within top management teams.

The CEO is considered “the central strategic decision-maker” (Barker & Mueller, 2002: 783) within the organization. These top-level executives possess very distinct decision-making attributes, which are closely related to their cognitive and demographic characteristics (Beber & Fabbri, 2012). According to the upper echelons perspective, executives’ characteristics can significantly affect how they make decisions and in turn the firm performance (Hambrick and Mason, 1984). These powerful actors can also influence the firm’s market value (Nelson, 2005). In addition, they are fully responsible for the effective information exchange and integration within the top management team (Buyl, Boone, Hendriks, and Matthyssens, 2011). Due to all these vital tasks that affect the organizational performance directly, it is crucial to examine critical linkages between CEO characteristics and EMNCs’ performance in foreign markets.

CEO Age

Some empirical research has found that younger executives are bigger advocates of strategic change (Johnson, Schnatterly, & Hill, 2013). Especially, younger CEOs tend to strongly support the change (Golden & Zajac, 2001) and new product introductions (Barker & Mueller, 2002) as a part of their firm’s growth efforts. As argued in the upper echelons theory, younger executives are more willing to take risks toward novel practices whereas older executives may prefer being risk-averse by embracing conservative approaches and being committed to the status-quo (Hambrick & Mason, 1984). In addition, as the information-processing perspective

argues, younger executives are expected to better process and integrate critical information so that they will make their decisions with more confidence compared to those of older executives. By combining these two main arguments, it can be stated that a younger CEO of an EMNC can better handle challenges, complexities, and ambiguities overseas due to his or her abilities in effective information-processing and good-quality decision-making. In other words, we can expect younger CEOs of EMNCs to better absorb the “newness” in an international setting by taking necessary actions immediately. Therefore, I argue that the CEO age is negatively related to the international performance of EMNC.

Proposition 1a: *The younger the CEO, the better the international performance of the EMNC.*

CEO International Experience

Executives’ previous experiences influence their strategic choices and managerial actions (Hambrick & Mason, 1984). Executives with international experience can encourage other upper echelons’ members to “consider internationalization a more viable avenue for expansion” (Carpenter, Pollock, & Leary, 2003: 808), which is a very critical aspect of CEO’s responsibilities within a firm trying to expand its operations globally. O’Reilly, Synder, and Boothe (1993) further argue that the experience factor is important for “key” decision-makers in organizations since they can better communicate their thoughts with their industry partners as well. Therefore, an executive experience should be considered a concept that has direct effects on both within-firm and within-industry relationships.

Through their international experience, top executives, in particular CEOs, can better analyze the external environment via using a global “lens” (Guna & Jalland, 1996). Possessing

knowledge about international business operations and cross-cultural management will make a significant contribution to the CEO's strategic decision-making efforts so that he or she can act up on all possible opportunities confidently. Having a younger CEO with an international experience becomes much more critical in the context of EMNCs since these CEOs are fully responsible for observing, analyzing, and understanding "brand new" environmental conditions before taking any sorts of strategic actions necessary. Therefore, I argue that the CEO international experience positively moderates the negative relationship between the CEO age and EMNC's international performance.

Proposition 1b: *The younger the CEO with an international experience, the much better the international performance of the EMNC.*

CEO Duality

In the management literature, there have been controversial views regarding effects of the CEO duality on organizational performance. According to Joseph, Ocasio, and McDonnell (2014), if both the CEO and chairperson are same persons, this duality perspective will provide the CEO with a broader authority over the board, which reduces the possibility of power conflicts at the top executive level and leads to reaching consensus within the top management team much faster. On the opposite side, the CEO non-duality can increase the effectiveness of board monitoring and provide the top management team with better strategic counseling and advice so that interests of shareholders can be better protected (Finkelstein & D'Aveni, 1994), which "fits" perfectly with the agency theory arguments.

From the duality perspective, keeping the CEO and chairman positions together can provide the firm with more effective leadership toward formulating and implementing strategies as well as avoiding potential rivalry and conflicts at the top level (Baliga, Moyer, & Rao, 1996). In this particular case, since only one person keeps the power within the top management team and board of directors (Davidson, Worrell, & Nemec, 1998), the duality perspective will help to “establish a unity of command at the top of the firm, with unambiguous leadership clarifying decision-making authority and sending reassuring signals to stakeholders” (Finkelstein & D’Aveni, 1994: 1081). On the opposite side, if the CEO and chairperson are not same individuals, this non-duality perspective can have the board better function in monitoring the top management team via becoming “truly” independent (Harris & Helfat, 1998). In other words, splitting up these two top-rank positions will remove possible constraints in making decisions towards better value creation for shareholders as well as major concerns on the board independence (Baliga et al., 1996).

In the context of EMNCs, if the host country is an emerging economy, it may be better to have a CEO-duality structure due to the fact that the CEO is already familiar with conditions of an emerging market from his or her home country and therefore, he or she should be able to make faster and good-quality decisions by gaining support from other top executives without a “big” necessity of “detailed” corporate monitoring. On the other side, if the host country is a developed economy, it is more likely that the CEO may get confused, feel pressured, and even might not process the information available to him or her correctly due to unfamiliar conditions of that host country. Thus, a more “strict” monitoring and strategic guidance may be required

by keeping the CEO and chairperson positions separated. As a result, I argue that the effect of CEO-(non)duality on the EMNCs' international performance is certainly context-dependent.

Proposition 2a: *The CEO duality will have a positive influence on the international performance of the EMNC if the host country is an emerging economy.*

Proposition 2b: *The CEO non-duality will have a positive influence on the international performance of the EMNC if the host country is a developed economy.*

CONCLUSION & DISCUSSION

This early-stage theoretical paper, which is grounded in the agency theory and upper echelons perspective, looks at how different CEO characteristics (age, international experience, and duality) affect the EMNCs' international performance. From the perspective of corporate governance, it is critical to examine how different governance elements may play some unique roles in the context of EMNCs since emerging markets are very much different than developed economies and therefore, "key" success factors for better firm performance may certainly vary.

This research contributes to the management literature in a couple different ways. First, it provides a brief review on widely-used theories in firm internationalization. Second, it emphasizes the importance of corporate governance on EMNCs' performance by particularly focusing on the CEO. Third, it argues that some relationships between independent and dependent variables can certainly be context-dependent. And finally, it examines the interaction effect of international experience on a proposed relationship.

This paper will certainly need to be improved in later stages. First, the theoretical model needs to be further developed by including more evidence from the literature. Second, by collecting the data, current propositions including moderating effects will need to be empirically tested. Third, instead of only focusing on the CEO, demographics of the top management team can be examined. And finally, it may be fruitful to look at whether a particular region or continent that an EMNC belongs to makes a difference in its international performance.

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CONCEPTUAL FRAMEWORK

