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Chinese enterprises in Germany: Establishment modes and strategies to mitigate the liability of foreignness[☆]

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ABSTRACT

Although China shows an impressive increase of outward foreign direct investment, research on internationalization strategies of Chinese companies is still in its infancies. It remains unclear, for example, how Chinese MNEs cope with the specific institutional hurdles of a developed country such as Germany and to reduce their liability of foreignness (LOF). Given a remarkable lack of in-depth empirical studies, we present insights from 31 semi-structured face-to-face interviews with employees belonging to seven Chinese MNEs and stakeholders. Our findings suggest that Chinese MNEs have gained international experience, whereas strategies to reduce their LOF depend on the establishment mode chosen.

1. Introduction

Although the internationalization of firms from emerging markets is not new to scholars and practitioners (e.g., Bartlett & Ghoshal, 2000), one observes a remarkable increase in recent years, spurred by huge trade surpluses and engaged senior managers. More specifically, the outward foreign direct investment "stock from emerging markets grew sevenfold between 1990 and 2003 ... as compared with 3.5 times for developed countries." (UNCTAD, 2005). While large firms such as Haier or Lenovo received major attention regarding their bids to acquire competitors from developed countries, many unknown Chinese firms from different industries pursue a challenging internationalization strategy as well. Obviously, foreign direct investment (FDI) is no longer a one-way street from developed to developing and emerging countries.

A brief review shows that some researchers have already directed their attention towards this new phenomenon. On the one hand, there have been studies by consulting firms like The Boston Consulting Group (2006) or Deloitte (2007) and practitioner-oriented articles (e.g., Boateng, Qian, & Tianle, 2008; Dietz, Orr, & Xing, 2008; Hirt & Orr, 2006; Luedi, 2007), which prove the relevance of this phenomenon by referring to the sheer numbers of internationalizing firms from emerging markets and by highlighting basic motives and strategies. On the other hand, there have been academic synopses that aim at providing a more sophisticated picture of internationalization objectives, strategies, and behavior of emerging market firms, especially those coming from China (e.g., Aulakh, 2007; Buckley et al., 2007; Buckley, Cross, Tan, Liu, & Voss, 2008; Child & Rodrigues, 2005; Luo & Tung, 2007; Mathews, 2006; Morck, Yeung, & Zhao, 2008). Morck et al. (2008), for example, conclude that Chinese outward FDI may have been driven much more by national interests (such as stated in the five-year-plan) and governmental intervention compensating for market and institutional imperfections than resulting from strategic planning processes of individual firms. As target markets are changing to developed countries, however, governmental intervention may not compensate for strategic positioning any more so that Chinese companies may be forced to change (Morck et al., 2008). According to Buckley et al. (2007), this change *may* have already begun during recent years; it seems that it already *has* begun in companies like Lenovo (Huang, 2009).

Results remain inconclusive whether such change has yet occurred in Chinese multinational enterprises (MNEs) on a broader scale. Studies predominantly used a quantitative approach based on secondary data (e.g., archival data). Only a few studies base their findings on primary data (Bell, 2008; Deng, 2008; Li, 2007; Liu, 2007; Liu & Li, 2002;). However, despite insights based on primary data, these studies show several shortcomings. First, all studies solely

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focus on large Chinese MNEs. While one may argue that large firms are forerunners, it remains unclear whether the internationalization of Chinese firms is restricted to these large firms and whether and how smaller enterprises rely on different approaches to internationalization. Second, none of these studies applies a multi-level methodological approach that includes employees from different hierarchical levels, functions, and nationalities. Furthermore, perspectives from important external stakeholders are missing. Yet, such an approach is needed in order to ensure the validity of findings through triangulation (Eisenhardt & Graebner, 2007; Gibbert, Ruigrok, & Wicki, 2008; Miles & Huberman, 1994; Yin, 2003).

Our study fills this void by conducting in-depth case-based analyses of seven Chinese enterprises of different sizes and from different industries that entered Germany by using either acquisition or greenfield entry modes. More specifically, the objectives of our study are to identify and to describe how entry mode choice impacts the strategies adopted by Chinese firms to cope (or not to cope) with the specific institutional and competitive hurdles in Germany, and how they mitigate their specific 'liability of foreignness (LOF)' (Zaheer, 1995), a liability that may result in additional costs and competitive disadvantage for firms that are new to a certain foreign market. Germany was chosen as an exemplary market because of (a) significant Chinese investments (German Central Bank, 2008), (b) Germany's good representativeness for other developed Western markets, and (c) a considerably high LOF as a result of the high cultural distance between Chinese and German cultures (cf. Child & Markoczy, 1993).

The remainder of the paper is structured as follows: first, we explain our research methodology including, for instance, the data selection process. Second, we briefly describe our sample with regard to the history of the respective firms' international orientation and provide an analysis of the particular motives and establishment modes (i.e., acquisition or greenfield investment) followed. Third, we elaborate on strategies the analyzed firms have chosen to reduce their respective LOF and derive propositions. Fourthly, we discuss important findings and pinpoint possible directions for future research in this important field. Finally, we draw implications for practitioners.

2. Research methodology

For the purpose of this study we approached Chinese MNEs that (1) have already entered the German market and over the time have built a market presence in Germany, that (2) seemed to pursue long-term objectives regarding their German investment, implying no 'hit-and-run'-mentality, which might bias our analysis and findings, and that (3) are heterogeneous in terms of sector or industry affiliation, firm size, level of international diversification, and state ownership. In the early 2006 preparatory stage of this study, information was requested from German and Chinese chambers of commerce and local business development institutions that significantly supported the identification of companies that complied with requirements (1) and (2). We additionally screened newspaper articles and ad-hoc announcements, compared the total amount of FDI invested between 2007 and 2008 with the industry average, and spoke to experts from consulting, law, and private equity firms who knew the respective market entries well and offered different perspectives and insights. In order to comply with calls for a rich variety of empirical evidence (Eisenhardt, 1991; Eisenhardt & Graebner, 2007; Yin, 2003), companies that made it on the short list were evaluated against requirement (3), i.e., to show a high degree of heterogeneity. As a result of this selection process, seven Chinese MNEs were approached for in-depth analyses.

Between February and September 2008, we conducted 31 face-to-face interviews with firm representatives that were all at least 90 minutes in length. These followed a semi-structured interview protocol. We interviewed employees from a broad range of organizational levels and units in order to ensure a good approximation of firm population (Eisenhardt & Graebner, 2007; Miles & Huberman, 1994; Yin, 2003). Interviewees originated from (1) diverse hierarchical levels, spanning from general managers responsible for Europe, Middle East, and Africa to team assistants; from (2) different functional fields such as business development, controlling, finance, marketing, procurement, or sales; and from (3) different national cultures, i.e., employees from China and Germany (see Appendix A for more information).

When developing our interview protocol, we accounted for common methods variance, a potential bias often observed in cross-sectional studies. We separated scale items in different places of the questionnaire, whereas items related to the "dependent" or criterion variable (i.e., liability of foreignness) followed those related to the "independent" variables (i.e., acquisition vs. greenfield investment as well as due diligence, reputation building and reliability enhancement, prior experience, share of control, share of work, and key employee roles). This is useful for reducing the effects that stem from artifactual covariance and, thereby, to decrease common methods variance to a certain degree (Podsakoff & Organ, 1986).

All interviews were recorded, transcribed, and evaluated through multiple rounds of independent assessments by the authors in order to ensure the reliability of findings (Yin, 2003). In every case, archival data was used to bolster interview data. Construct validity was additionally ensured through conducting a pilot test. A preliminary case study about a large Chinese electronics company that had no direct investment in Germany at that time but that had built a strong foothold in the Netherlands was undertaken. The Netherlands is highly comparable to Germany with regard to, for instance, market conditions such as consumer behavior or governmental restrictions like labor laws. The pre-test corroborated the basic findings of our study, thus ensuring the construct validity of our case methodology (details on the measures that we used in order to ensure a rigorous case approach are shown in Table 1).[3]

We apply a multiple case approach in order to derive our conclusions and insights (Eisenhardt, 1991). In order to avoid long narratives and in order to provide a structured overview over the most important insights and findings, the following parts of the paper are of comparative nature.

3. Case descriptions

The seven Chinese MNEs that were selected (see Appendix B for company profiles) originate from a broad range of industries: whereas the Bank of Communications (BoC) belongs to the five largest banks in China, Baosteel is China's largest steel refiner and Minmetals China's largest metals trader, Haier and Lenovo are two big players in the electronics and white goods industries, and Beijing No. 1 and the Shanggong Group are mid-sized machine manufacturers. Besides differences in industry affiliation and firm size, the selected companies also differ with regard to the level of state ownership as well as regarding "the level of international diversification (i.e., the breadth of geographical coverage of international markets through outward investment)" (Luo & Tung, 2007, p. 483). In terms of Luo and Tung's typology, our companies are transnational agents (Baosteel), world-stage aspirants (Haier), commissioned specialists (Minmetals, Beijing No. 1), or are positioned somewhere between niche entrepreneurs and commissioned specialists (BoC, Shanggong Group) or between world-stage aspirants and transnational agents (Lenovo) (see Fig. 1).

[3] We would like to thank an anonymous reviewer for raising this point.