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MNE performance during a crisis: An evolutionary perspective on the role of dynamic managerial capabilities and industry context

Stav Fainshmidt[a,*], Anil Nair[b], Mark R. Mallon[c]

[a] Department of Management and International Business, College of Business, Florida International University, Miami, FL 33174, United States
[b] Department of Management, Strome College of Business, Old Dominion University, Norfolk, VA 23529, United States
[c] Department of Management and Entrepreneurship, Martha and Spencer Love School of Business, Elon University, Elon, NC 27244, United States

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ABSTRACT

As the likelihood of worldwide crises increases due to globalization and the resulting economic contagion, understanding why some multinational enterprises (MNEs) prevail in such environments becomes ever more critical. Drawing from the concept of dynamic managerial capabilities, we posit that MNE in-crisis performance is associated with the pre-crisis development of *asset management capabilities*, or the capacity of managers to orchestrate assets so as to extract more value from the firm's resource pool. Specifically, we argue that because dynamic managerial capabilities evolve as a response to a firm's task environment, MNEs that operate in dynamic industries develop stronger asset management capabilities. However, we also posit that whether these capabilities contribute to in-crisis performance is contingent upon the munificence of the industry environment in which the capability evolves. Asset management capabilities that evolve in munificent environments would encompass a wider spectrum of routine-altering activities, and thus increase the ability of the MNE to react to more revolutionary events, such as global economic crises. Conversely, asset management capabilities that evolve in resource-scarce environments will result in more strategic lock-in due to firms' constrained ability to experiment with novel resource configurations, resulting in poorer in-crisis performance. We test our hypotheses using a sample of 854 MNEs in the context of the global financial crisis of 2008, and find support for our hypotheses. We discuss implications for the dynamic capabilities view and MNE resilience.

1. Introduction

Crises often surprise and catch organizations unprepared. The global financial crisis in 2008 resulted in a worldwide market capitalization loss of 19.4 USD trillion, a 46 percent drop compared to 2007 (Garelli, 2009). The staggering costs of low preparedness and ineffective action in the context of environmental jolts (Meyer, 1982), as well as the rising frequency of such events (Taleb, 2012), create a pressing need to study the ability of firms to not only survive, but also perform well amid major environmental setbacks (Carmeli & Markman, 2011; Goll & Rasheed, 2011; Park & Mezias, 2005; Sutcliffe & Vogus, 2003; Wan & Yiu, 2009). Unfortunately, although failing organizations pose great economic and social risk, it remains unclear why firms decline or thrive during crises (Kunc & Bandahari, 2011). This issue is especially pertinent – yet understudied – for multinational enterprises (MNEs). While the multinational network structure of MNEs may provide them with the operational flexibility needed to expand or contract operations in troubled markets or regions (Chung, Lee, Beamish, & Isobe, 2010), such intra-firm shifts may be problematic in the face of a *global* crisis, such as the economic crisis of 2008, whereby adversity is worldwide (Westney, 2011). We therefore pose the following research question: *what factors explain performance differentials among MNEs during a global crisis?*

To begin answering our research question, we rely on the concept of dynamic managerial capabilities – "the capabilities with which managers create, extend, and modify the ways in which firms make a living" (Helfat & Martin, 2014: 2). These capabilities encompass activities by which managers continuously orchestrate assets into valuable resource combinations (Sirmon & Hitt, 2009), which makes them well-suited to explain performance differentials of MNEs during crises. We focus our attention on one key capability, namely, *asset management capability*, which captures the extent to which managers are able to configure resources so as to extract more value from the firm's resource base. Drawing from theory on industry recipes and managerial mental models (Shinkle & Kriauciunas, 2012; Spender, 1989), we leverage an evolutionary logic to argue that because dynamic managerial capabilities are partially shaped by a firm's task environment, MNEs that had been operating in dynamic global industries before the crisis would

* Corresponding author.
E-mail addresses: sfainshm@fiu.edu (S. Fainshmidt), anair@odu.edu (A. Nair), mallon87@gmail.com (M.R. Mallon).

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develop stronger asset management capabilities.

However, we also posit that whether asset management capabilities contribute to in-crisis performance is contingent upon the munificence of the industry environment in which the capability evolved before the crisis. Specifically, we theorize that asset management capabilities that evolve in munificent environments would encourage greater experimentation, and thus increase the ability of the MNE to react to more revolutionary events, such as global economic crises. Conversely, asset management capabilities that evolve in resource-scarce environments will result in more strategic lock-in due to firms' constrained ability to experiment with novel resource configurations, resulting in poorer in-crisis performance. Because asset management capabilities evolve as a means to adapt to a particular environment, they may result in overspecialization and lock-in that translate into a disadvantage amid unforeseen change (Burgelman, 2002). Yet, when these capabilities evolve in more munificent contexts, access to abundant growth resources in an industry encourages a wider spectrum of routine-altering activities and thus diminishes the path-dependent evolution of these routines when atypical change takes place (Daniel, Lohrke, Fornaciari, & Turner, 2004).

Overall, our research rests on the premise that performance during a crisis may be a function of pre-crisis strategic activities and the context that shapes these activities (Kraatz & Zajac, 2001; Meyer, 1982). While Jallat and Shultz (2011: 483) have noted that "[s]uccessfully diffusing a crisis requires an understanding of how to handle a crisis before it occurs," our research highlights the notion that performing well during a crisis may depend not only on preparedness, but also on the capabilities that evolve within the task environment, which may have little to do with addressing crises per se. This is consistent with Ritchie's (2004) call for a more strategic and holistic approach to crisis management that takes into account both crisis and non-crisis activities.

We test our hypotheses using hierarchical linear modeling and a sample of 854 MNEs operating in 24 global industries. Consistent with our evolutionary predictions, we find support for a pre-crisis positive effect of global industry dynamism on asset management capability. During the crisis, however, the effect of asset management capabilities on MNE performance was only positive for MNEs operating in global industries that were munificent *before* the crisis. For asset management capabilities that were developed in more resource-scarce industries, their effect on in-crisis MNE performance was negative. These results suggest that while dynamic managerial capabilities may be a useful concept for explaining performance differentials during times of crisis, their relationship with in-crisis MNE performance is contingent upon the context in which such capabilities evolve.

Our study makes important contributions to two research streams. First, we provide insights to the bourgeoning literature on MNE resilience. For instance, previous literature has focused more on actions and implications at the subsidiary level in the context of crises (e.g., Chung et al., 2010, 2013). Other studies have focused more on pre-crisis and post-crisis performance in an international context (e.g., Lee, Beamish, Lee, & Park, 2009). We complement these studies by examining performance differentials *during* a crisis at the *enterprise* level (cf. Boubakri, Guedhami, & Mishra, 2010). Explicating the role of asset management capability and global industry context as sources of such performance differentials helps to "shed light on the nature of the MNE, and the foundations of SCA [sustainable competitive advantage]" (Teece, 2014: 9).[1]

Second, we offer novel insights to dynamic capabilities research. Whereas industry dynamism has often been cast as a boundary condition in the capabilities-performance relationship (Peteraf et al., 2013), we demonstrate that dynamic managerial capabilities may be an evolutionary *outcome* of operating in dynamic task environments (Wang & Ahmed, 2007). Further, few studies have examined the relationship between dynamic managerial capabilities and firm performance under extreme, unfavorable macro-environmental conditions (for two exceptions, see Makkonen et al., 2014 and Nair et al., 2014). Our study therefore sheds light on the performance implications of such capabilities, as well as their being contingent upon the context in which they develop. Importantly, existing literature has been heavily occupied with the role of environmental dynamism in the advantage-generating efficacy of dynamic capabilities, whereas our study offers theory regarding the role of other dimensions of the task environment, namely, munificence.

This paper is organized as follows. In the next section, we review relevant literature regarding crises and how MNEs respond to such unforeseen events, highlighting the theoretical gaps our study attempts to address. We then draw from the concept of dynamic managerial capabilities and evolutionary logic to develop theory regarding the development and in-crisis effectiveness of asset management capabilities. Next, we present the data and analyses of our study. A discussion of the theoretical and practical implications of our findings follows. We end with a discussion of limitations and future research avenues that could further bolster theory of MNE resilience and the dynamic capabilities view.

2. Theoretical framework

2.1. Crises: consequences and coping strategies

A crisis is "a low-probability, high-impact event that threatens the viability of the organization and is characterized by ambiguity of cause, effect, and means of resolution, as well as by a belief that decisions must be made swiftly" (Pearson & Clair, 1998: 60). According to Jallat and Shultz (2011: 477), "crises are becoming more complex; they increasingly transcend boundaries, and affect many institutions… corporate crisis management remains an evolving area in many MNCs [multinational corporations]." It is inevitable that in a world of increasing levels of global interconnectedness, growing exposure of organizations to worldwide environmental jolts would take place. The economic crisis of 2008, for instance, was so pervasive that for many MNEs, the task was not as simple as divesting or leveraging flexibility to reduce activity in one subsidiary, while doing the opposite elsewhere (Bartnar & Bodnar, 2009; Chung et al., 2013).

Scholars have examined several organizational characteristics and actions that may facilitate better performance during crises. For instance, Meyer (1982) posited that an entrepreneurial organizational culture and adaptive ideology are the main strategic drivers of organizational resilience because they allow firms to detect the tremors and prepare for jolts. Further, firms may also engage in alliance formations (Park & Mezias, 2005) and acquisitions (Wan & Yiu, 2009) during a crisis to increase stock price and profitability. Others have noted that the firm's human resource management system may create the human capital needed to thrive under adverse conditions (Lengnick-Hall et al., 2011), and that enterprise risk-management systems may help hedge against economic downturns (Nair et al., 2014). Firms also exhibit patterns of learning in dealing with severe crises. Venkataraman and van de Ven, (1998) discovered that firms that survived jolts gained valuable experience that allowed them to exhibit stronger resilience in subsequent jolts. According to Chakravarthy (1982), proactive strategies coupled with an organic structure facilitate strong resilience to crises, as managers are more likely to anticipate environmental changes and make innovative decisions.

Chung et al. (2010, 2013), using real-options logic, found that MNEs may benefit from building operational flexibility in foreign subsidiaries, which allows them to invest/divest in crisis-stricken areas. This is consistent with Chung et al.'s (2008) earlier finding that the latent flexibility residing in multinational networks of foreign subsidiaries

[1] By examining MNE performance during the economic crisis of 2008, this study contributes to emerging general theory of organizational resilience as well (e.g., Lengnick-Hall & Beck, 2009).