Emerging multinationals, emerging theory: Macro- and micro-level perspectives

Recent years have witnessed an unprecedented rise in FDI from emerging economies. From a relatively minuscule amount in 1990, outward FDI flows from emerging economies reached more than $350 billion in 2008 (UNCTAD, 2009). Though multinational corporations (MNCs) from the largest or most affluent emerging economies have led the pack (e.g. China, Russia, Brazil and India), the phenomenon is fairly widespread, with firms from countries such as Mexico, Chile, Malaysia, Indonesia, Egypt, Turkey and many others also being ever more active overseas. Generally speaking, it is increasingly recognized, both by practitioners (Sirk et al., 2008a,b; Van Agtmael, 2007) as well as academics (Ramamurti and Singh, 2008; Gammeltoft, 2008; Luo and Tung, 2007) that a surge of MNC activity from what is traditionally considered the periphery of global commerce is reshaping the structure of international business. Indeed, the positive connotations of the term ‘emerging multinational’ mirror the increasingly positive assessment of their contribution to the global economy.

As helpful as the ‘emerging multinationals’ category is it can conceal as much as it reveals. In terms of domestic market size, there are considerable differences between countries like Argentina and South Africa with populations of about 50 million, countries like Nigeria, Indonesia and Brazil with populations of about 300 million people, and the very populous India and China. The institutions and histories of developing countries are at least as varied as those of countries in the developed world. Most developing countries have a colonial background, often leaving them with very different legacies (e.g. Spanish versus British ex-colonies). In addition, some of the most successful ‘emerging MNCs’ are not recognized as such: firms that have shifted their place of incorporation or primary stock exchange listing, like Anglo-American, SABMiller and HSBC are often not considered to be from developing countries, even though they have a long history in the developing world, are institutionally rooted there, and often have top management teams that are heavily dominated by nationals from the original home country.

In other words, emerging and developing economies constitute a tremendously diverse population of countries. Consequently, generalizations across the group of countries should only be asserted with the utmost caution. Nevertheless, a variety of features do set emerging economies and their firms apart from their developed-world counterparts and a range of stylized differences can be identified.

First, in many emerging economies, central and local government plays a larger and more active role in the economy, and firms tend to be more attuned to government priorities and preferences. Government support also provides emerging economy firms with privileged access to certain inputs, preferential financing, subsidies and other support. Moreover, internationalizing state-owned or state-controlled companies can operate according to somewhat different logics than conventional commercial ones. Governments may specifically target internationalization and actively encourage their national firms to internationalize in order to strengthen international competitiveness. On the other hand, efforts to escape bureaucratic restrictions or volatility at home also occasionally feature as a motive for emerging economy firms (Peng et al., 2008; Kalotay and Sulstarova, this issue).

Second, the economic institutional environments of EMNCs tend to be ‘thinner’ and less sophisticated. This has implications for firm organization and governance. For example, emerging economy firms tend to be more horizontally and vertically integrated and provide for themselves internally what in more advanced economies might be procured through more established and well-functioning markets. In order to economize on scarcer technological, managerial, physical and other resources, large emerging economy firms have a greater propensity to organize themselves in diversified business groups, related as well as unrelated (Khanna and Yafeh, 2007; Tan and Meyer, this issue-a). In addition to addressing efficiency concerns, this provides additional advantages of cross-utilization of resources between units. The group structure also has implications for how EMNCs organize themselves internationally and specifically the openness of their international networks.

Third, emerging economy firms are often more reliant on social networks with ethnic, linguistic or cultural affinities, i.e. relational assets (Dunning and Narula, 2004). The limited experience with international operations of many emerging economy firms implies that they tend to operate with more closed networks and more personalized governance and control systems, e.g. expats play a very important role (Cho and Lee, 2003; Saxenian and Hsu, 2001).

Fourth, the tendency of firms from emerging economies to operate in more mature rather than technologically fast-paced industries has long been noted (Dunning et al., 1998; Ozawa, 1992). Given the nature of their domestic environments, they tend to
focus on the provision of cost-competitive goods and services and in certain specific sectors, e.g. steel, cement and white goods, many EMNCs are coming to play important roles as global industry consolidators (Ramamurti, 2008). At the same time, internationalization which is based less on prior accumulation of ownership advantages and more on the intent to acquire and augment such advantages abroad is also increasingly significant among emerging economy firms (Mathews, 2002).

1. Theoretical implications of the rise of EMNCs

Emerging economy firms originate from within a context that is unfavorable for generating significant firm-specific ownership advantages of the traditional kind. Unlike established MNCs, most of the sources of advantage at home, such as low operating costs, distribution systems, brands, customer relationships, government relationships, etc., are not particularly mobile. Consequently, there are few monopolistic advantages for EMNCs in foreign markets. Even though some of the strategies that EMNCs develop provide them with advantages in the least developed countries (Cuervo-Cazurra and Genc, 2008), their competitive advantage overseas, in particular in the advanced economies, tends to be based on price competition, which is not so easily sustainable, rather than on technology or brand.

Despite this, firms from emerging economies have increasingly surprised observers not only by how rapidly they are internationalizing, but also by their bold and aggressive methods in the early stages of their outward internationalization (Sirkin et al., 2008a,b). For example, emerging multinationals are entering not just other emerging economies but also advanced economies and, furthermore, making extensive use of acquisitions in the latter (UNCTAD, 2006). Much as this pattern of behavior is increasing, it is not entirely novel. In his early work on ‘third world enterprises’, Lall (1983) already noted the outward investment by Hong Kong enterprises through joint ventures in established technology industries which were neither well-established at home nor important export products of the colony.

Lall’s observation reminds us of the importance of not simplistically ascribing certain set characteristics to EMNCs compared to MNCs from the developed world. Although there often are differences between MNCs from more versus less developed countries, those differences are not cast in stone. Yet, the trajectories followed by EMNCs are often different from those of established MNCs, and the differences have consequences. For example, EMNCs suffer from comparative newness compared to more established MNCs who are already present in many markets. Their lack of international experience, lack of reputation, and the like put them at a disadvantage relative to the latter, and can further increase the liability of foreignness generally suffered by foreign firms (Zaheer and Mosakowski, 1997).

The current interest in EMNCs represents the latest wave of scholarly attention into the phenomenon. Although earlier researchers strongly emphasized the differences between EMNCs and established MNCs, their research relied heavily on extant theory. The very early scholarly work on MNCs from emerging economies – notably a collection edited by Kumar and McLeod (1981) and the work of Lall (1983) and Wells (1983) – emphasized contrasts between EMNCs and the more established MNCs, such as the lack of proprietary advantages, latecomer status, weaker institutions, etc., as mentioned above. However, their work assumed that the theories explaining the foreign investment and internationalization activities of firms, such as the international product lifecycle model (Vernon, 1966), the stages model of internationalization (Johanson and Vahlne, 1977) and the ownership–location–internalization framework (Dunning, 1980, 1988), remain useful, even though based mainly on the experiences of multinational firms from the US and Europe.

Of course, that emerging economy firms, considered in very general terms, deviate from their developed country counterparts does not in itself imply that separate theories are needed in order to understand and explain their evolution, organization and modus operandi. However, the recent and consistent increase of the international presence of EMNCs begins to test the limits of extant theory and it is increasingly being asked whether those theories are relevant to EMNCs that are internationalizing in a different era, with different starting points and possibly very different internationalization patterns and paths. The set of questions to which we seek answers is changing and the scope of existing theories, though valid, may not be the most appropriate. In other words, even if existing theories are correct, they may not be the most relevant to answer the specific research questions being posed. For example, the fact that extant theories are generated from experiences of North–North or North–South investment flows is likely to render them less useful to understanding issues related specifically to South–South and South–North investment flows, i.e. investment flows made from ‘thinner’ to ‘thicker’ institutional environments. By the same token, extant theories may be less applicable to understanding investments made by companies with relatively weak ownership advantages into environments already saturated with such advantages and this may have implications for location, entry modes and operational strategies for multinationals from emerging economies.

In essence, there are three options. First, should one just expand the scope of current theory? In such case, all that is required to address the emerging economy MNC phenomenon is to expand the types of advantage that qualify as an ownership advantage, for instance political skills, the ability to thrive in adverse circumstances, etc. (Garcia-Canal and Guillen, 2008; Ramamurti and Singh, 2008). Such an approach has precedent in the study of developed economies — for example, Dunning’s (Dunning, 2001) extension of the ‘ownership’ advantage concept into Oa (asset advantages) and Ot (transaction advantages). However, stretched to the limit, such an approach risks stripping the concept of its power of distinction since everything potentially becomes an advantage.

Second, should one extend current theory — not merely expand the scope of a theory, but also rethink the concepts, relationships and causalities it contains? Buckley et al. (2007) argue that rather than rejecting conventional theories, specific modifications to them are required to incorporate better, for example, capital market imperfections (such as preferential lending) and institutional factors (e.g. government support and guidance). Child and Rodrigues (2005) propose that existing theories should be extended rather than replaced, and point to four principal areas for such extension: to properly accommodate the

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occurrence of investments made not on the basis of already acquired advantages but to compensate for competitive weaknesses; the role of government in supporting internationalization; processes related to negotiating a space for entrepreneurship in environments of heavy government involvement; and whether EMNCs successfully reproduce their domestic business practices abroad or rather adapt to institutional conditions prevailing in host countries. In a somewhat similar vein, Ramamurti (2008) contends that existing theory accounts sufficiently for why EMNCs internationalize, the challenges they face in host countries and when they prefer hierarchies over markets, while new theory is required to account properly for their competitive advantages, how these advantages are developed, why they invest in developed economies and how they manage to compete successfully with developed country MNCs.

Third, should one disregard current theories for being inappropriate and then develop some fresh theoretical perspectives? From this perspective, the inadequacy of extant theories may reflect not only actual changes in the behaviors of EMNCs, but also the need for theoretical advancement in general. Although there is not yet consensus about what such a new theory could look like, a number of authors have proposed several avenues to explore. Luo and Tung (2007) argue that emerging economy MNCs internationalize through a distinct process dubbed ‘springboarding’, designed to achieve the dual purpose of acquiring strategic resources abroad and reducing their institutional and market constraints at home. Mathews (2002) also argues that EMNCs typically represent instances of accelerated internationalization and that they use their latecomer position to their advantage through repeated applications of a process of ‘linkage, leverage and learning’. They are not operating in a world where they seek to push monopolistic advantages as much as one where they seek to tap resources elsewhere and devise appropriate strategies and organizational forms for doing so.

Although some scholars have commented that this third position may be somewhat radical and risks ‘throwing out the baby with the bathwater’ (especially Narula, 2006), one can safely conclude that some healthy skepticism of extant theories embodied in such work is overdue, and that such research helps spur further efforts to address some of the key issues. For instance, since the conventional multinational firms came from more liberal and established institutional contexts rather than from those in institutional transition, the role of governments and the institutional context in home markets and how these impacted FDI behavior of firms has been comparatively neglected. If at all, it was addressed only indirectly, for instance as leading edge demand in home countries being conducive to innovation (Vernon, 1966) or the emergence of clusters (Porter, 1990).

It is not possible as yet to predict how future work will shape subsequent theoretical development, but it is likely that a sustained investigation of emerging multinationals will continue to challenge existing paradigms. Consider a statement like the following:

How should the MNE effectively compete with rising competitors from emerging markets who are imprinted with very different national institutional configurations, business models, belief systems and stakeholder relationships? (Cheng et al., 2009:1072)

The point of departure is still ‘the MNE’ and the emerging multinationals are the ‘very different’ challengers as well as future incumbents. Which theoretical gains can be realised by simply shifting the point of departure, and by exploring how the global economy operates from the point of view of what has been called ‘the periphery’?

With the rise of emerging economies and firms from these economies, institutional theory has become much more visible in IB research in recent years (Peng et al., 2008) and can lend a useful and complementary lens to the more standard economics-based theories. More concretely, there may be certain significant differences between firms from advanced and emerging economies because of variations in local institutional context. For instance, emerging economy MNCs are often either state-owned or affiliated or family-owned and often comprise parts of conglomerates. Here, resources at the group level (e.g. international experience of managers, financial resources, etc.) would enable them to internationalize whereas other factors (e.g. reliance on expats) may hinder it. Moreover, with weaker shareholder pressures, it may be easier for emerging economy firms to accomplish rapid internationalization through acquisitions. These are just a couple of examples but point towards the enormous possibilities for research and theoretical development.

2. The institutional perspective: macro and micro-level considerations

Institutions, the ‘humanly devised constraints that structure human interaction’ (North, 1990), include formal rules as well as informal constraints. Firms and other organizations pursue their interests within institutional constraints (Oliver, 1997). They tend to conform to rules, expectations, and beliefs in their environment and take shape from them because such isomorphism (coercive, mimetic, and normative) confers them legitimacy (DiMaggio and Powell, 1983; Meyer and Rowan, 1977).

In classical economics, the invisible hand of perfect markets is presumed to guide the allocation of resources to their most efficient use. In this world there is no scope for strategy. In the real world, markets are usually fraught with failures. Firms then emerge as active creators (or co-creators) of economic systems and their organization and strategies significantly influence economic outcomes through the visible hand of managerial capitalism (Chandler, 1977).

Generally speaking, it is well recognized in the IB literature that MNCs in various ways reflect the institutional conditions of their home environment and that systematic differences prevail between MNCs of different national origins. Institutional environments supply the material from which firms build their resources and firms link their resources with environments through their strategies. Institutional forces influence firms’ strategy making through three principal channels: regulatory,
normative and cognitive (Scott, 1995) and the strategic choices of firms are therefore shaped by the institutional frameworks in which they are embedded (North, 1990; Peng, 2003).

In brief, there is clearly a dialectic relationship between the MNC and its institutional environment. The MNC will reflect the institutional context in which it evolves (e.g. internalizing weak markets); and MNC activities will spill over into the institutional context (e.g. through training and R&D), which will in turn more or less actively respond to its requirements (e.g. through regulations and supporting institutions). In other words, the MNC (micro) and its institutional and country (macro) environment progress in a co-evolutionary process. The specificities of emerging economy institutional environments may imply that they also bring about institutionally distinct MNCs and that EMNCs follow different evolutionary trajectories from developed economy MNCs.

With respect to FDI, the macro and micro-level approaches towards FDI, pursued by economic and management theorists respectively, dovetail neatly and complement one another well. At the macro level of the country, researchers, particularly economists, are interested in the overall patterns of FDI stocks and flows. However, what shows up at the macro level as inward or outward FDI is ultimately an aggregation of the activities of thousands of multinationals as they go about engaging in international commerce. At the micro-level of firms, researchers engage in understanding the internationalization strategies and actual activities of firms, i.e., the motivations and drivers and their speed, scope and means of internationalization. Similarly, what is referred to as technological development or sophistication at the more macro (or country) level is technology acquisition or accumulation and learning by firms.

Turning to outward FDI by emerging economies, it is understandable that the level has accelerated rapidly only this past decade. First, initially much of the emerging economy FDI was directed towards other emerging economies in low-technology industries since similarities not only in demand structures but also in institutional contexts rendered their skill sets more appropriate to these host countries (Cuervo-Cazurra and Genc, 2008). However, this alone becomes limiting in global competition since, as long argued by the 'process school' (e.g. Bartlett and Ghoshal, 1989) and recently by Guillen and Garcia-Canal (2009), firms need a balance between global reach and technology upgrading to enjoy the benefits of both learning and economies of scale. Second, post-liberalization, MNCs from these countries went through a process of inward internationalization, especially through tie-ups with foreign firms at home (Chittoor et al., 2009). As learning occurred and they gradually built up their competitiveness and knowledge base, they also became more able to benefit from investments not just at home but also in countries abroad and not just in other developing countries but also in advanced economies.

In the context of this paper, activities by EMNCs provide us with fertile ground to look either at somewhat novel phenomena or at existing ones in a somewhat novel manner. For instance, one noteworthy feature of outward FDI by emerging multinationals is the importance of M&As. Especially when investing in advanced economies, EMNCs have shown a frequent interest in acquisitions (UNCTAD, 2006), an aspect somewhat neglected by current theories. One reason why FDI in developed economies through acquisitions has accelerated is arguably that these economies are further up the technological ladder. With respect to M&As, acquisitions offer enhanced and faster opportunities for learning (Barkema and Vermeulen, 1998), an aspect that is somewhat neglected by current international business theory. Besides immediate access to needed skills and capabilities, ownership enables the emerging economy firm more discretion in how it taps into those skills for learning purposes.

Another separate though related point is that from a resource-based lens, the starting point and history of a firm would shape its approach towards acquisitions. For established firms that already possess an existing advantage and an international presence, an acquisition would more likely be approached more from more of an efficiency or power perspective, i.e., to rationalize and restructure operations, eliminate a potential competitor, etc. In contrast, to the extent that emerging economy firms acquire for purposes of learning and catch-up with their more established competitors, they have the motivation and incentive to preserve the target so as to be able to learn from it. Additionally, from the seller’s perspective, the complementary resources that emerging economy firms bring, e.g., reach in their domestic market and low cost, may be as valuable if not more so than a selling firm’s technology.

3. The content of this special issue

The special issue makes two main contributions to our understanding of FDI by developing countries, and international business theory generally. First, at the macro level, the contributions in the special issue in different ways engage with institutions and their role as the determinants and outcomes of outward direct investment. The papers also bring out different ways in which the interplay between organizations and institutional environments shape the behavior, organization and strategies of EMNCs. Second, at the micro-level, this issue advances both the institutional and the resource-based arguments with respect to firm strategy. Much as papers in this issue confirm the importance of firm resources, they suggest that the strategies and resources of EMNCs need to be conceptualized more broadly than is generally done in the literature on firms from the developed world. The prevalence of institutional features in contributions emphasizing both the macro and the micro-level is noteworthy, and is discussed below.

Implicit in a lot of the current attention directed at FDI from developing countries is an assumption that OFDI contributes to or at least reflects the growing competitiveness of those countries. Two papers in the volume directly investigate the assumption that outward FDI is in some way beneficial to the home country. The papers by Tolentino (this issue) and by Zhao, Liu and Zhao (this issue) both touch upon the relationships between home country institutional environments and outward investment. Tolentino asks how features of the macro-economic home environment influences outward investment flows in the cases of China and India while Zhao, Liu and Zhao analyze how, in the case of China, institutional as well as non-institutional factors mediate the home

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and resources that can be procured through the market, and looks mainly at highly sophisticated knowledge. In sum, Knoerich provides evidence that EMNCs can arbitrage between environments in home and host countries, and resulting from advanced R&D or embedded in tacit knowledge. There is also little serious work done on the speci

resources are highly context-speci

ty in the sense that both control substantial resources, and often across a variety of contexts. Their paper provides evidence not only of real synergies between the German and Chinese environments into the analysis when trying to understand how EMNCs emulate each other in their investments decisions, and suggests that EMNCs’ decision to engage in FDI into China is based as much on an assessment of various reference groups as on an assessment of their own capabilities. They find contingencies between firms’ mimetic strategies and the institutional environment in home and host settings: firms are influenced more by the entry decisions of EMNCs from their own home country than by firms from other countries, and are more likely to follow the example of other EMNCs than that of advanced MNCs. These EMNCs seem to be pursuing a ‘follow the leader’ (Knickerbocker, 1973) strategy, but the ‘leaders’ are not those firms with the richest internal resources, but instead the firms that are most similar to the investing EMNC. These findings provide clear support for (neo-) institutional theory, and also raise the question of the extent and way in which EMNCs make sense of and exploit their own resources.

Tan and Meyer (this issue-b) reframe the argument about business groups (as presented by amongst others Chang and Hong, 2002; Khanna and Yafeh, 2007) by arguing that business groups resemble the multinational corporations of the developed world in the sense that both control substantial resources, and often across a variety of contexts. Their paper provides evidence not only that the nature of business group resources shapes how expansion takes place, but also that home institutions shape the types of resources firms have at their disposal when internationalizing. They argue that since firm resources reflect a specific environment, they may be of limited use or even a disadvantage when the firms internationalize to dissimilar environments abroad. Thus if resources are highly context-specific, e.g. close ties with the local business community or government, there is a lower level internationalization. In contrast, there is a higher level of internationalization if managers have international work experience.

In turn, Barnard (this issue) documents the value of market-based resources. She shifts focus from the home to the host country and argues that liability of foreignness may be a more relative concept than conventionally assumed, and shows how the success of EMNC subsidiaries within their corporate network depends also on institutional features of the host countries. Her paper questions the view that tacit, knowledge-based resources are more valuable than market-based resources, which are seen as being too easily imitable to provide a lasting competitive advantage. Where firms suffer a significant liability of foreignness, they could overcome this as well as potentially derive a substantial advantage from procuring resources through the market. This suggests that not only the potential value but also the accessibility of resources must be considered when exploring how resources shape the firms’ competitive position.

Knoerich (this issue) focuses on the dimension of resource complementarity in his paper on German/Chinese M&As, and investigates why German firms in a long-established German industry, machine building, decide to sell to Chinese firms. He finds evidence of real synergies between the German and Chinese firms. For example, it is difficult to remain profitable in the research intensive top-end of the market that most German firms occupy, and a Chinese acquisition provides the Germans with access to the much larger lower end of the market as much as it provides the Chinese with access to new technology and an avenue for upgrading. The need and desire for technological upgrading tend to be better documented than the benefits of having access to the larger lower end of the market. Knoerich points out that recognizing how both partners contribute to the relationship – that an understanding and presence in low-cost markets is a comparable competitive advantage to technological expertise for the high end of the market – is an important insight for the acquired firm, and makes it more positively disposed to be acquired as well as cooperative in the exchange of knowledge. In sum, Knoerich provides evidence that EMNCs can arbitrage between environments in home and host countries, and establish conduits through which complimentary resources can be transferred from one environment to the other.

Contemporary work originating in and focused on firms from advanced economies tends to gloss over both business groups and resources that can be procured through the market, and looks mainly at highly sophisticated firm resources, e.g. those resulting from advanced R&D or embedded in tacit knowledge. There is also little serious work done on the specific requirements of serving the lower end of the market. The assumption seems to be that those markets can be served simply by providing technologically less sophisticated and cheaper products. While not denying the existence and even importance of other types of

resources, the extant research suggests that firms benefit most from those resources that are at the tip of a proverbial iceberg of capabilities in an organization. In contrast, the papers by Tan and Meyer, by Barnard and by Knoerich all investigate resources that are often hidden from view, and through their more inclusive approach, they expand our understanding of the development and functioning of firm resources generally.

4. Conclusion

To conclude, globalization has accelerated change processes that have previously taken decades or longer and, due especially to international and domestic liberalization, EMNCs are in certain ways both more able and more intensively challenged to internationalize earlier. This accelerated process provides a useful lens to understand the co-evolution of firms and their home and host economies.

The papers in this issue provide evidence of the potential and promise of theoretical gains that can be realised through a closer and more careful investigation of context. Buckley and Lessard (2005) recently contended that IB research may be running out of ‘big questions’. We question that contention and agree with Peng (2004) that the rise of emerging economy MNCs may infuse fresh life into IB research through a closer and more careful investigation of the particular institutional context of emerging economies and EMNCs. To more generally summarize from this special issue, there are three broad areas of inquiry that research needs to engage with to properly understand EMNCs from an institutional perspective: first, the co-evolution of firms and their institutional environment; second, the distinctiveness of emerging economy institutional settings as home countries, and third, the particularities of a firm with a given governance structure spanning a range of institutional settings, both more and less advanced. We invite and look forward to future work in this direction.

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Emerging multinationals, emerging theory: Macro- and micro-level perspectives

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