Internationalization of Firms from Emerging Economies:
An Organizational Learning Framework

Sunil Sharma

INDIAN INSTITUTE OF MANAGEMENT
AHMEDABAD-380 015
INDIA

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Sunil Sharma
Indian Institute of Management, Ahmedabad
sunilsharma@iimahd.ernet.in

Abstract

Increasing globalization of economy has provided fresh impetus to internationalization efforts of firms from both developed and emerging economies. Extant research in this area has been carried out with the perspective of firms from developed economies. The issue of internationalization efforts by firms from emerging economies has received sparse attention. Further, multiple theories have been applied to examine this subject. Rarely the issue has been seen as multidimensional and as set of decisions that involve tradeoff. This paper attempts to bridge this gap by suggesting an integrative framework to look at internationalization as a multidimensional phenomenon. The framework is grounded in resource based view, organizational learning, and institutional theories. In addition, internationalization effort by a firm has been treated, as a separate decision not related with earlier or concurrent internationalization efforts with its own unique dimensions. This essentially means that internationalization process is highly context specific.

Introduction

In recent years, globalization of business has picked up at a frenetic pace to the extent that firms are increasingly looking at world as one market. This has given a fresh impetus to firms to internationalize their operations. However, the growth this time is triggered more by emerging economies, which has led to growing ambitions among firms from emerging economies to expand globally partly because of increased competition at home, and partly because of their new found confidence. Figures suggest that emerging economies are increasingly acquiring important position in world economy. In 2013 investment in developing countries accounted for 52% of total investment. Firms from emerging economies like China, India, South Africa, Vietnam, and many Latin American countries have made international forays to strengthen their competitive position. This emerging trend has invited attention of both scholar and practitioners. As recognition of growing importance of emerging economies, Hoskisson and colleagues (2000) carried out first major overview of the field.

While the phenomenon has become important, research on cross border acquisition (form of internationalization) is rare (Shimizu et al., 2004) and fragmented, especially for firms from emerging economies (Wright et al., 2005). Besides there is no integrated approach in the field of international strategic management that can effectively address this issue. In a review of ISM research Bruton et al. (2004) found that ISM research uses theory and frameworks drawn mainly from other disciplines. In fact since 1995, institutional theory, social network theory, organizational learning theory and resource based theory (RBV) have acquired prominent position in ISM discourse. Each of these theories only partially explains internationalization process. Besides they have been

applied in the context of firms from developed economies. For example, while institutional theory addresses concern of organizational adaptation to the external environment (Selznick, 1957), homogeneity of organizational forms (DiMaggio and Powell, 1983), and decision embedded ness of firms in institutional environment (Meyer and Rowen, 1977, Scott, 1987), it fails to explain acquisition of capabilities by firms in response to increased competition. Hence, there is a strong need to have a comprehensive framework embedded in theories/theory which can provide insights into the process of internationalization by firms from emerging economies. Further, the objectives of firms from developed and developing world may be different. For instance, the concept of knowledge as a valuable strategic asset in today's knowledge intensive environment has gained wider acceptance both among researchers and practitioners. So, possession of unique capabilities has become a source of success in highly competitive industries. Integration of value-added activities seem to be the primary motivations for internationalization (Kogut, 1985). As knowledge and learning go hand in hand, success demands identification, acquisition, and development of knowledge-based capabilities. This indicates that intent of the firms may decide on the applicability of the theory. Among the dominant theories, organizational learning and resource based view can be combined to explain internationalization process of firms from emerging economies.

It is assumed that a firm with global market advantage will be able to realize better strategic and financial returns, firms aim to develop new set of competencies that can provide firms a global market advantage. I found that most of the current research on internationalization has been conducted keeping firms from developed world as context. Further, there is very little research available on internationalization process of firms

from emerging economies. Resource based view to develop competencies seems most suitable paradigm to explore this phenomenon, especially in relation to the scope of inquiry for this paper. This paper makes an attempt to bridge this gap by developing a multidimensional framework to predict and explain internationalization behaviour of firms from emerging economies. The aim is to identify incorporate those elements in the framework which relevant and specific to the decision situation. While this may affect generalizability of the framework, it may still have strong explanatory value for large number of internationalization processes. However, in the absence of concrete support from past research, this paper is more of a conceptual paper drawing concepts and ideas from strategy and international strategic management literature. Further corroboration would require development of theory and supporting empirical studies.

This paper employs the resource-based view of the organization and combines it with organizational learning theory to explore the following set of research questions. The paper has been organized around following themes.

- What is the dominant paradigm to explain process of internationalization?

- What is the current status of research on internationalization process of firms from emerging economies?

- Which theory can best explain the process of internationalization of firms from emerging economies?

- Develop propositions on choices of mode, direction, and size for the internationalization process of firms from emerging economies.

Based on conclusions and extant literature, few propositions have been developed. Secondary data collected for Indian firms for the last few yrs show that the propositions

are pointers in the right direction. However, further research scope would possibly attempt to include more dimensions of internationalization and to conduct empirical studies to test propositions.

Internationalization by firms from developed countries

Since the objective of this paper is to develop a framework for the internationalization process for firms from emerging economies, it would be appropriate to begin by developing a nomological map of the internationalization process drawn from extant literature. Towards that objective, this paper has mainly relied on two papers written by, Werner, 2002 and Wright et al., 2005. While the first paper outlines comprehensive review of literature on internationalization, the second paper puts it in a proper perspective by observing that the majority of papers take the perspective of firms from developed countries. Together the two papers present complete coverage of relevant studies on internationalization process.

Studies on internationalization have covered antecedents, consequences, and descriptions and measurement of internationalization. The topics covered on antecedents of internationalization can be broadly grouped into Motives (diversification, capability enhancement, growth), Facilitators/gaps (Top management's domestic/international experience, networks, exploiting capabilities, cultural distance), and Firm level factors (Age, international experience, foreign partners, level and speed). The research on consequence side mostly probes the relationship of internationalization with firm's performance. This conclusion or field of inquiry is probably based on premise that internationalization contributes to the performance of firm especially when I link

internationalization with the context of firm motives viz. to get scale or scope economies to reduce cost. The most heavily researched topic on internationalization is its relationship with measures of firm performance (i.e., growth, survival, etc.). Motives other than performance appear to be a potential research area not currently addressed in top management journals (Werner, 2002**).** *This provides direction and motivation to explore firm's motives for internationalization other than that for increasing profitability and growth.*

The paper by Wright et al. (2005) provides useful insights into the applicability of various theories to the process of internationalization. As per the authors, researchers have examined internationalization process of firms from developed world from perspective of four theories: Transaction cost theory, Agency Theory, Institutional theory and Resource based theory. However, popularity of Transaction cost theory has declined over a period of time. Further, researchers have also pointed towards contextual difference between firms from developed and emerging economies viz. higher transaction costs in emerging economies than those in developed economies, institutional differences between developed economies and emerging economies. In contrast, both institutional and resource-based theory (Barney et al., 2001; Peng, 2001) has gained in popularity. Agency theory is the least applied theory in internationalization research. Given complexities of the internationalization phenomenon, some researchers have adopted a mixed perspective to analyze internationalization process. The authors conclude that in order to extend research on emerging economies, there is a need for new business models and an understanding of how formal and informal institutions i.e. institutional environment affect firms. This calls for integration among various theories.

Internationalization by firms from emerging economies

Internationalization research has focused on globalization of firms from developed world (Wright et al., 2005), however research on internationalization experience of firms from emerging economies is sparse. The absence of rich research material handicaps efforts to develop a comprehensive framework for internationalization process of firms from emerging economies. The sparse research in this area covers topics like adoption of country specific strategies by firms (Brouthers et al., 2005), enhancing specific capability viz. R&D capabilities by Korean firms, and unique characteristics of firms from emerging economies (Chang, 1995; Hu, 1995). These studies show that firms from emerging economies have certain disadvantages because of underdeveloped institutions and economic resources. Hu (1995) further argues that firms internationalizing from one emerging economy to another prefer exploitation to exploration (March, 1991). In the next section I briefly describe the concepts of resource based view and organizational learning.

Concepts of organizational learning, RBV, and capabilities

RBV (Barney, 1991) provides an important theoretical anchoring to explore the question of sustained competitive advantage in a global market place. RBV conceptualizes firms as a bundle of resources (Penrose, 1959). Heterogeneity (Amit & Schoemaker, 1993; Barney, 1991; Wernerfelt, 1984) in these resources (i.e valuable, non-substitutable, rare, and inimitable) is a source of competitive advantage. In internationalization literature, focus is on acquisition of capabilities (McEvily and

Marcus, 2005). The process of capability development is incremental, path dependent (Nelson and Winter, 1982) and expansive.

From the previous research it can be inferred that the objective of global expansion (internationalization is to exploit the current set of competencies and to augment the resource base. Internationalization is one way of acquiring competencies, which exist external to the firm. This argument is in line with dynamic capability model of Teece, 1997, and Eisenhardt, 2000. Both authors argue in favour of acquisition of capabilities through external route as one way of enhancing capabilities, Teece calls it path, and Eisenhardt calls it alliances.

Firms from emerging economies explore opportunities to acquire financial, technological, and intangible asset Hitt et al.(2000) whereas developed market firms look for resource exploiting opportunities.

Framework for internationalization by firms from emerging economies

Looking externally to its competitors, firms must be able to identify knowledge resources and capabilities required by the industry merely to "merely to play the game", to remain competitive or the one to become competitive. Cross border mergers and acquisitions involve multiple processes, such as due diligence, negotiation, and integration (Shimizu et al., 2004). However, focus of this paper is on pre-acquisition or pre-entry diligence process only. The limited focus stems from the reason that for most of the firms from emerging economies, their first overseas expansion would look more at broader pre-acquisition issues as they lack prior experience and have no repository from where knowledge from past acquisitions can be applied. Therefore post acquisition issues

will not be of overarching importance for such firms. Due diligence process largely confirms to organizational learning theory and exploratory learning(March, 1991, as cited by Shimizu at.al, 2004).

From the literature review of internationalization process, both of firms from developed countries and that of firms from emerging economies, it can be inferred that an integrated approach is required to explain internationalization process of the latter. This paper makes an attempt to develop and to use an integrated approach to develop hypothesis on internationalization process of firms from emerging economies. Figure-1 shows dimensions of this integrated approach: General antecedents of internationalization (defined by general factors like mode, direction, cultural distance and others common to firms from both developed and merging economies), Firm characteristics (defined by institutional factors of host county), Global market structure(industry structure driving internationalization) and all three aligning at strategic intent of the firm.

General Antecedents

Strategic Intent

Unique Firm
Characteristics
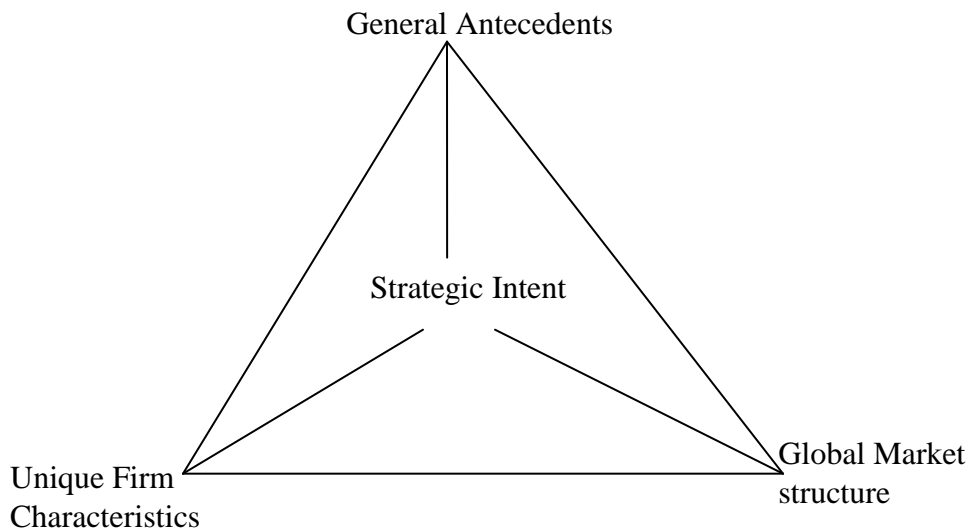
Global Market
structure

Figure-1

While an integrated approach can at best unravel the mechanism of internationalization, I use a combination of theory to explain this process. The dimensions of integrated approach outlined earlier points to certain degree of unique approach applicable to group of firms. This emerges from the fact that the model assumes homogeneous institutional environment for the firms. Therefore firms belonging to either a country or some industry would exhibit certain unique characteristics, which would define the path, or approach they adopt for internationalization.

As the topic of interest for this paper is internationalization process of firms from emerging economies, the underlying theory identified to explain this should reflect the overwhelming motive of such. For example, if increasing scale for profitability and growth is the dominant motive then transaction cost theory (Williamson, 1975) should be the apt theory to explain internationalization. However, as pointed by Wright et al., 2005, the early stage of internationalization can be better explained by institutional theory because the impact of government and society is stronger in emerging economy. However , later stages of internationalization can be better explained by transaction cost economics and resource based view. The fact that the entire global market has become very competitive and firms from emerging economies lack capabilities to effectively compete with international giants accentuate this. Moreover with increased globalization, many of these firms develop the confidence to compete with large MNEs . Bartlet and Ghoshal, 2000 in their HBR article cite numerous examples of firms from emerging economies which shrugged off their lack of confidence to go for internationalization.

To sum up, it can be argued based on discussion so far that a firm must understand the relationship between its unique characteristics shaped by institutional

environment, global industry structure as in today's globalized economy there are no insulated environments, antecedents of internationalization and its strategic intent. The interface would determine the path a firm would adopt for internationalization. The context of study of this paper i.e. Internationalization process of Indian firms' makes resource based view apt for explaining internationalization because by acquiring competencies, these firms become stronger in both domestic as well as global market (Dewar & Frost, 1999). (hoskinson, 2000). This explains our preference for RBV as the underlying theory.

Based on our model, a working definition of 'internationalization' for this paper is proposed. Internationalization for firms from emerging economies is an introduction process in which the firms slowly increase their international involvement with focus on building distinctive competencies through gradual acquisition, integration, and use of knowledge. Here the basic assumption is that emerging economy firms lack capabilities to operate in international market and therefore rapid expansion is not possible. These firms gradually acquire necessary knowledge by having international operations.

Discussion

Internationalization for firms from emerging economies as defined by this paper is akin to gradual introduction or induction to the international market. This definition in combination with the model developed earlier becomes basis of our exploratory study. In this section, an attempt has been made to predict and understand following determinants of internationalization. Further*, Due diligence process largely confirms to organizational learning theory and exploratory learning(March, 1991, as cited by Shimizu et a.l, 2004)*

which conforms with this paper's argument that the main motive of firms from emerging economies would be to enhance their capability.

Due diligence process involves identification of appropriate acquisition targets, negotiation, and completion of the deal (Shimizu et al., 2004). In a way due diligence process is an objective, independent examination of all aspects of decision. In other words it is an assessment of 'what a firm has', 'what it wants to achieve' and 'how to accomplish that process' For a firm intending to internationalize its operation to enhance its resources and capabilities, the process can be divided into following elements.

- Assessment of strength or resources (firm Characteristics)

- Strategic intent

- How to achieve(antecedents defining path)

- Environment (Global market assessment: competitive intensity)

1. **Choice of mode (Greenfield or acquisition or Joint venture)**

Firms can internationalize in a number of ways viz. acquisition, joint venture, Greenfield (Dunning, 1980). Out of these three modes of entry, the dimension of acquisition is under researched (Melin, 1992). Previous research has examined influence of several factors (antecedents in our model) but has offered no coherent framework (Barkema and Vermeulen, 1998) to study entry mode choices. Cross border mergers and acquisitions involve multiple processes, such as due diligence, negotiation, and integration (Shimizu et al., 2004). However, focus of this paper is on pre-acquisition or pre-entry diligence process only. The limited focus stems from the reason that for most of the firms from emerging economies, their first overseas expansion would look more at

broader pre-acquisition issues as they lack prior experience and have no repository from where knowledge from past acquisitions can be applied. Therefore for such firms, post-acquisition issues will not be of overarching importance in their decision-making. This paper applies the earlier developed model to predict entry mode choice for firms from emerging economies and to develop general propositions.

Greenfield: Foreign start-up investment entails building an entirely new organization from scratch in a foreign country. Firms often use startups to exploit firm-specific advantages that are difficult to separate from the organizations i.e. tacit knowledge (Hennart and Park, 1993).

Acquisitions: By buying a part of equity in a foreign firm, the acquirer firm acquires new technological resources and increases their capabilities (Prahalad and Hammel, 1990). Firm's original stock of resources and capabilities determine its preferred option of expansion: through start-ups or through acquisitions (Hoskinson and Hitt, 1990). Firms from emerging economies explore opportunities to acquire financial, technological, and intangible asset Hitt et al.(2000). In contrast, firms from developed market search for resource exploiting opportunities. For emerging market firms, the objective of acquisition is to control idiosyncratic resources of the target firm, viz. best practices, knowledge , complementary resources and transfer them them back to the parent firm.

Joint Ventures: Joint ventures in strategy literature have been presented as an alternative to acquisitions with a view to explore new capabilities or Greenfield with a view to exploit existing capabilities. Joint ventures are entered to reduce transaction costs, for strategic motivations (as deterrent) or organizational learning(developing capability). The knowledge to be transferred is tacit in nature.

The model developed in this paper positions decision on entry mode on four dimensions of antecedents (Firm's initial stock of knowledge), global market structure (Competitive intensity, capability distribution among competitors), unique firm characteristics(firms developed in capability and resource scarce environment), and strategic intent(intention to be among industry leaders) with RBV and organizational learning as the underlying theory. Since, firms from emerging economies lack strong technological capabilities; they will be more inclined to undertake acquisitions than start-ups. With regards to choice between acquisition and joint venture, it is suggested that firms from emerging economies may prefer the former for following two reasons. Due to increased globalizations, firms may have opportunity to enter into joint ventures in host country, and secondly the strategic intent of firms from developed firm may not be in favour of transferring tacit knowledge which is the source of competitive advantage for these firms. This is possible only if acquiring firms have complete control over the acquired firms. Further, for many of these firms, the acquisition being their first exposure to internationalization, post integration issues may not get important priority. Based on above discussion, following propositions are proposed.

Proposition 1a: Firms from emerging economies would internationalize primarily through acquisitions.

Proposition 1b: Firms from emerging economies adopting acquisition route to internationalization would go for majority stake in the acquired firm.

2. Choice of direction

Firms are part of social and cultural norms mainly determined by differences in institutional environments. Organizational cultures are different from national cultures (Hofstede, 1980). Firms from emerging economies develop competence in relationships(Khanna and Palepu, 2000; Guillen, 2000) as factor markets are not developed in their host countries which necessitate close liaising with external stake holders (government and institutions). In this case, the specific dimensions of model are antecedents (Cultural distance), global market structure (Competitive intensity, less difference in capability distribution among competitors), unique firm characteristics (high on relationship competencies), and strategic intent(growth/profitability) with RBV and organizational learning as the underlying theory. The model suggests that the firms with this configuration would prefer to go to countries with similar conditions i.e. in other emerging economies. This is especially true for firms which are part of Business groups as they internationalize to capitalize on their marketing or existing competencies. From the discussion following proposition is developed. However, it is possible that firms other than those belonging to business group may not have received patronage. These firms would path of entering developed world to explore competence development.

P2a: Firms belonging to business groups from emerging economies would internationalize by entering markets belonging to other emerging economies to exploit existing competence.

P2b: Firms not belonging to business groups from emerging economies would internationalize by entering markets belonging to developed economies to explore development of new competence (ies).

3. Choice of size:

Firms from emerging economies lack resources to undertake large scale internationalization. Further the intent is of developing capabilities, and many of these internationalizing firms are of big size. Recent acquisitions in pharmaceutical industry suggest that large firms are acquiring smaller R&D firms for complementary asset. Large Pharmaceutical firms have huge infrastructure, whereas small firms have research capabilities. In this case, the specific dimensions of model are antecedents (Size), global market structure (High Competitive intensity, large difference in capability distribution among competitors), unique firm characteristics (Low resource positions), and strategic intent (developing competence) with RBV and organizational learning as the underlying theory. Firms entering developed market would acquire smaller size companies to internationalize.

P3: Firms from emerging economies would go for small size acquisitions.

Conclusion

Secondary data collected for Indian firms suggest that P1a and P2a receive support. Testing of other propositions would require further firm specific data collection. This paper provides some useful insights into the process of internationalization. The first major conclusion is that there is a need to look towards internationalization as a multidimensional phenomenon. The choices faced by firms for international expansion are complex and multifaceted. Each choice has to be taken as a separate decision. Since, dominant factors for each choice are different there is a tradeoff involved, which calls for optimization of constraints. While extant research has thoroughly examined antecedents

of internationalization, it falls short on integrating firm specific factors shaped by institutional factors, Global market structure driving choice between exploiting and exploring competencies, and above all the strategic intent of the firm which is influenced by and influences all three dimensions. For example, if the strategic intent of the firm is reflected in its confidence is to become global leader; other factors may take lesser priority in decision making process. In nutshell, this paper provides an easy framework for practitioners to understand tradeoff involved in Internationalization, and for researchers to develop new perspective for the process.

However, it suffers from certain limitation. First, the model has been developed with to address phenomenon of internationalization by firms from emerging economies, which limits its generalizability. Second, this paper has considered only three decision choices involved in internationalization. Other choices may involve certain complexities requiring further development of this framework. Besides, the paper is conceptual and lacks rigour of empirical studies. The limitations are in a way scope for future research.

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