Contextualizing Experience Effects in International Business: A Study of Ownership Strategies

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forthcoming in Journal of World Business

this version: June 2008

www.klausmeyer.co.uk
when citing please refer to the published verision

Keywords: international experience, country-specific experience, ownership strategy, emerging economies, ownership strategies

Acknowledgements: We thank editor Yadong Luo and two anonymous reviewers as well as Keith Brouthers, Michael A. Hitt, Kristian Jakobsen, Alan Rugman, Danchi Tan and Joseph Yu for helpful comments on earlier versions of this manuscript. Financial support from the National Science Council of Taiwan is greatly appreciated. Both authors have been affiliated with University of Reading when first working on this paper, and acknowledge support received from their colleagues.

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Abstract

Experienced firms act differently than newcomers, yet such differences vary with the context and with the type of experience. We thus investigate the effects of international experience on MNEs' ownership strategy across a range of developed and developing economies. We distinguish competence building and partner selection effects of experience, which vary between general international experience and country-specific experience, and across host contexts. This contextualization of the theoretical arguments suggests that the predicted effects hold in some host countries, but not in others.

In support of these arguments, our empirical study of subsidiaries of Taiwanese electronics forms finds that general international experience facilitates wholly owned operations in developed economies in Asia and Europe, while country-specific experience facilitates joint ownership in China.

Keywords: international experience, country-specific experience, ownership strategy, emerging economies

Introduction

Experienced actors can do things that novices cannot do, or do less well. Therefore, experienced multinational enterprises (MNEs) have a wider range of options than inexperienced firms (Chetty, Eriksson & Lindbergh, 2006; Johanson & Vahlne, 1977). International business researchers have studied the effects of such experience on MNEs' strategies, yet some of their results appear contradictory (Brouthers, 2002; Zhao, Luo & Suh, 2004). Therefore, a more differentiated analysis of the benefits of experience is required to explain its impact.

We focus on the ownership strategies for subsidiaries abroad, and argue that experience has (at least) two distinct effects. Traditionally, scholars have argued that experienced firms develop competences to operate independently, and therefore are less likely to need resources from local partners (Gomes-Casseres, 1989; Makino & Delios, 1996) and less willing to share control (Anderson & Gatignon, 1986; Brouthers & Hennart, 2007; Hennart, 1991). This argument is exemplified in the internationalization process model, which stipulates a typical path of gradual deepening of operating modes from contractual cooperation to joint-ventures and to wholly owned subsidiaries (Johanson & Vahlne, 1990). We call it the competence building effect.

However, a different effect may have an opposite impact. A joint venture is not only a legal contract, but an intensive relationship with another firm, that creates a mutual interdependence between the two or more parent firms (Hennart, 1988; Luo, 1997). It locks investors into a relationship, and thus limits the option of developing strategic alternatives that might compete with the joint ventures (Hamel, 1991; Meyer & Tran, 2006). Before committing to such a relationship, an investor would need to get to know the partner and its business contexts, check its capabilities and reputation, and build trust. This, however, requires tacit knowledge that can be gained through experience. Hence, experienced firms would be better prepared to enter a joint venture. We call this

the partner selection effect.

The relative importance of the two effects varies with different types of experience. General international experience (GIE) facilitates knowledge accumulation, but it provides little intelligence about specific local markets. Therefore, MNEs that have accumulated business experience all over the world would be more able to set-up new operations on their own (Terpstra & Yu, 1988; Yu, 1990, Knight & Kim, 2008). On the other hand, experience in a specific country may be beneficial for assessing alternative potential partners, and for building a relationship that can support a mutually beneficial and sustainable joint venture (Geringer & Hebert, 1991; Luo, 1997). Hence, country-specific experience (CSE) may facilitate the *creation* of joint ventures.

The relative importance of the two effects of experience also varies across contexts. Thus, the theoretical arguments have to be contextualized for empirical testing (Geppert & Mayer, 2006; Meyer, 2006; Rousseau & Fried, 2001; Tsui, 2007). In developed economies, markets are fairly transparent and efficient, while regulatory institutions are clearly defined. Thus, experience from one context may be relevant for another context, and facilitate the operation of a business there (Johanson & Vahlne, 1977; Terpstra & Yu, 1988). In contrast, emerging economies are often highly idiosyncratic in their institutional arrangements, and networks are essential for businesses (Peng, Wang & Jiang, 2008; Wright, Filatotchev, Hoskisson & Peng, 2005). Thus, experience from other contexts may be less transferable, while it is more important to get to know potential partners before committing to a joint venture. Hence, different types of experience may have opposite effects in emerging and developed economies.

We develop hypotheses based on these lines of argument, and test them on a dataset of MNEs that has a large variation in their international activities and experiences, and invested in a wide range of host countries. At the same time, we control for origin and industry by focusing on a single industry from a single place of origin, namely the

Taiwanese electronics industry. The study benefits from population level data with a total of 1506 observations.

The theoretical contribution of this study outlines two distinct effects of international experience, namely competence and partner selection effects. This helps explain puzzles in the empirical literature on MNEs' ownership strategy, notably differences between the impact of GIE and CSE. Moreover, we establish theoretically and empirically the contextual boundaries of these effects. We find a positive influence of GIE on ownership strategies when firms invest in some developed countries, and a negative effect of CSE on ownership strategies in China.

The epistemological view adapted in this paper is that empirical management knowledge is context specific unless evidence of its generalizability has been provided (Chang, 1995; Tsang & Kwan, 1999; Meyer, 2006; 2007; Tsui, 2007). Our results re-enforce this view by demonstrating that experience effects operate differently in different host environments. Hence, empirical results can not be assumed to be generalizable to other contexts. This logically also applies to our own empirical study: We cannot claim that firms outside the Taiwanese electronics industry would exhibit exactly the same experience effects. However, we contend that our main insight, namely that experience causes multiple effects which vary across host contexts, also applies to other MNEs.

The theoretical discussion in the next section discusses the arguments underlying the two theoretical effects, and their varying relevance for different types of experience and in different contexts. On this basis, section three develops hypotheses. The fourth section describes the sample and the methodology. The fifth and sixth sections present research findings and discuss them in light of our main argument. We conclude with managerial implications, research limitations, and suggestions for future research.

Theoretical Perspectives

MNEs accumulate experience through their operations, which helps developing competences that facilitate the running of existing operations and the establishment of new ones (Chang, 1995; Luo & Peng, 1999). This experiential learning is a cumulative process over the time that a firm operates in a given context, or in international business in general (Luo, 1999). Prior research has explored in particular how experience affects the ownership strategies for foreign operations, yet the empirical results of this research show contradictory results. Two theoretical issues may cause these contradictions.

First, experience leads to the creation or enhancement of resources, especially experiental knowledge, and thus the lowering of costs of doing business. Resources developed through experience facilitate most forms of business; predictions on which form would be preferred by an experienced firm thus requires an assessment of the relative impact. Most prior studies argue, and find empirical support, for a positive effect, as experienced firms tend to have higher level of control and equity (Agarwal & Ramaswami, 1992; Chang & Rosenzweig, 2001; Delios & Beamish, 1999; Gatignon & Anderson, 1988; Hennart, 1991). However, some studies find no significant relationship (Brouthers, 2002; Brouthers, Brouthers & Werner, 2003; Kogut & Singh, 1988; Somlev & Hoshino, 2005), while others find a negative effect (Davidson & McFetridge, 1985; Erramilli, 1991). Based on a Meta analysis of this literature, Zhao, Luo & Suh (2004) conclude that international experience is inadequate to fully capture the effects of behavioral uncertainty and suggest to better control for the context.

Second, different types of experience may influence ownership preferences in different ways (Delios & Beamish, 1999; Gatignon and Anderson, 1988; Gomes-Casseres, 1989; Hennart, 1991; Padmanabhan & Cho, 1996; Pak & Park, 2004). In particular, GIE creates different types of capabilities than CSE, and thus may have different impact (Contractor & Kundu, 1998; Hennart, 1991; Terpstra & Yu, 1988; Wei,

Liu & Liu, 2005). Some suggestions have been made why this may be so (Chetty, et al., 2006), yet overall the evidence is not clear.

We argue that the conflicting results in the literature may be caused by the failure of previous studies to recognize the opposing effects of competence building and partner selection. These effects vary in their relative importance for different types of experience, and across contexts.

Competence Building

Experience is a key construct in several lines of theorizing in international business research, including transaction cost and organizational learning perspectives. Experience enables firms to build competences in their line of business, and thus to lower their internal operation and production costs (Ghemawat, 1985) as well as the transaction costs they incur in their markets. To some extent, these competences may be transferable, thus lowering costs of entering similar types of business.

Transaction cost theorists have emphasized the lowering of internal uncertainty as a result of experience-based competences (Anderson & Gatignon, 1986; Brouthers, 2002; Brouthers & Hennart, 2007). Experience is predicted to lower the costs of operating a fully owned operation, making higher ownership levels more likely. Moreover, inexperienced investors face high transaction costs in accessing local resources, and thus collaborate with a local partner to lower the costs of accessing local resources. However, experiential capabilities also lower the costs of negotiating and coordinating with a local partner, which makes the net effect less clear.

The organizational learning perspective develops arguments along similar lines, yet focusing on the *benefits* generated by experience rather than the lowering of *costs* (Chang, 1995; Luo & Peng, 1999). International experience is generated by a learning process in which firms acquire tacit knowledge about international business (Kogut,

1991; Prahalad & Hamel, 1990). Prior investments facilitate this learning process and thus the development of new capabilities that help to evaluate opportunities for new projects (Barkema & Vermeulen, 1998; Chang, 1995; Chang & Rosenzweig, 2001) and to compete in markets substantially different from home markets (Delios & Henisz, 2000). Firms are thus argued to start with small initial investments that are later increased once the firm has accumulated sufficient experience (Chang, 1995). Thus, over a series of entries, firms learn how to operate in foreign countries, which enables them to take higher levels of ownership (Chang & Rosenzweig, 2001; Chetty et al., 2006).

The predictions of the organizational learning perspective correspond with the internationalization process model. It suggests that firms' internationalization is an incremental process that depends on the firm's experiential knowledge of foreign markets (Johanson & Vahlne, 1977; 1990). Firms increase their commitment with their knowledge accumulation in local markets. Learning about the local environment enhances the firm's capabilities, lowers perceived uncertainty, and enhances opportunity recognition (Chetty et al., 2006; Eriksson, Johanson, Majkgard & Sharma, 1997). In this way, experiential knowledge allows firms to make greater commitments to foreign operations, and to take higher levels of ownership.

Partner selection

Local business partners can help in many ways to build an operation in a foreign country, yet building the relationship with that partner is also a challenge, albeit one less discussed in the scholarly literature (Kale, Singh & Perlmutter, 2000; Lin & Germain, 1998; Luo, 1997; Wang, Wee & Koh, 1999). The successful creation and operation of a joint venture requires a mutually supportive and trust based relationship between the co-owners (Gulati, 1995; Zaheer, McEvily & Perrone, 1998). Thus, successful joint

ventures often build on existing relationships rather than being the first step of collaboration, and studies have shown that a prior relationship enhances the longevity of the joint venture (Hennart, Kim & Zeng, 1998; Inkpen & Currall, 1998).

A joint venture establishes a long-term relationship based on a contract that, among other rules, normally prevents competing activities by either partner. Thus, the joint venture locks firms into a relationship that can only be terminated at a cost. However, firms from different countries vary in their resource endowments and capabilities, such that their strategic objectives and organizational cultures may not be compatible (Child & Faulkner, 1998). The divergence of the partners' objectives can undermine the profitability and stability of a joint venture (Yan & Zeng, 1999). MNEs with prior experience in a country may already have adapted to the particular context, which helps them to overcome such coordination problems. At the same time, they may be more able to identify local partners with compatible objectives (Harrigan, 1988).

Thus, MNEs with a prior presence are better prepared to cooperate with the partner effectively, even with low levels of equity control. Thus, new entrants may deliberately 'go slow' and first establish a small operation to learn about the local environment and to build business networks, before committing to an equity relationship with a local firm. Entrants may initially register a small sales office, which then serves as a platform to explore opportunities for larger business operations (Kogut & Kulatilaka, 1994). Once they identify a potential partner, they may first do a few small deals, such as a distribution agreement, before making a major commitment (Beamish & Banks, 1987).

Consequently, experience may ease the process of selecting the most suitable partners, while making joint ventures more feasible and more viable. Hence, investors with prior operations in the same country may be more likely to share equity ownership with a local partner. In other words, experienced MNEs may be more inclined to entry by joint-venture (Delios & Henisz, 2000; Lu, 2002; Somlev & Hoshino, 2005).

Offsetting effects

The competence-building and partner-selection effects of experience may be offsetting each other: experience both reduces the need for a partner, while it also prepares partners for handling a partner relationship (Figure 1). The relative importance of the two effects, and thus the effect likely to dominate in an empirical study, depends on the type of experience under consideration as well as the host context and the investor's own context in terms of industry, time and home country.

****** Figure 1 approximately here ******

Types of international experience. Recent studies distinguish international experience that has been collected anywhere in the world, and experience in the specific country where the focal subsidiary is operating (Chetty et al., 2006; Delios & Henisz, 2000). General international experience (GIE) enhances many capabilities for managing international operations, whereas country-specific experience (CSE) enhances the understanding of the specific political and cultural context and of actors in that context.

The effects of these two types of experience may be different, even pointing in opposing directions. GIE may in particular support the competence building effect, as many competences (but not all) are transferable across contexts. CSE may in addition support the partner selection effect, and thus facilitate formation of joint ventures.

Empirical studies including both types of experience mostly hypothesize positive effects on both GIE and CSE, suggesting that these types of experience complement each other (Claver & Quer, 2005; Davidson & McFetridge, 1985; Delios & Beamish, 1999; Padmanabhan & Cho, 1996). However, some studies find opposite effects (Delios & Henisz, 2000; Pak & Park, 2004; Somlev & Hoshino, 2005).[1]

[1] Some studies moreover suggest that, in addition to GIE and CSE, more specific types of experience would be relevant in international business. Thus, concepts such as decision-specific experience (Chang

Host Context. Each country has its idiosyncrasies in terms of business practices, institutions and resource endowment, which affect the way businesses operate (Peng, Wang & Jiang, 2008; Dunning & Lundan, 2008; Meyer, Estrin, Bhaumik & Peng, 2008). Foreign investors gain tacit understanding of these idiosyncrasies through operating in the local context. Such local experience may be more important for business in emerging economies, where, for example, a weaker legal system may increase costs of contract enforcement, while regulatory ambiguities or corruption increase external uncertainty. Moreover, local firms in emerging economies may have weaker resource endowments, compared with their counterparts from industrialized nations (Hitt, Dacin, Levitas, Arregle & Borza, 2000). Thus, skills and practices developed through experience in developed countries may be inappropriate or impossible to apply in an emerging markets context (Tallman, 1992), and foreign investors may aim to compensate for their inexperience by partnering with a local firm (Makino & Delios, 1996; Meyer & Nguyen, 2005; Peng, 2003). This suggests that GIE may only to a limited degree be transferable, while CSE may be particularly relevant.

Investor Context. The context from which a firm originates may influence its resource endowment and its ability to operate in other contexts (Dong & Glaister, 2007; Geppert & Mayer, 2006; Harzing & Sorge, 2003). This context includes in particular location, industry and time. For example, the competence building effects of CSE may be less important for firms originating from areas with traditions, cultures and languages closely related to those of the host economy. Thus, Taiwanese businesses, our empirical field, may have unique features due to the close historical and cultural relationships between Taiwan and the mainland of China (Filatotchev, Strange, Piesse & Lien, 2007; Tan, Hung & Liu, 2007). Our study design aims to identify experience and host related

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& Rosenzweig, 2001; Padmanabhan & Cho, 1999) and operation-specific experience (Chetty et al., 2006) have been proposed. In the interest of parsimony we focus on the main types of experience in this study. We have tested for effects of a decision-specific experience measures in our empirical analysis, but we found them not to be statistically significant.

influences and thus controls for the investor's own context by choosing firms from a single home territory, and a single industry at a specific point in time. Thus, our hypotheses need to explore the impact of types of experience and of the host context.

Hypothesis Development

Our hypotheses bring the aforementioned theoretical arguments together. We analyze the main effects for the different types of experience, which however vary in their intensity across contexts. This leads us to hypotheses that predict the effects of experience in some contexts only.

General international experience

The competence building effect set out above suggests that firms with more experience in international business would be more likely to choose higher levels of ownership because they would be better positioned to recognize business opportunities (Barkema & Vermeulen, 1998; Delios & Beamish, 1999), to assess risk (Chang, 1995; Chang & Rosenzweig, 2001) and to operate in foreign markets independently (Agarwal & Ramaswami, 1992; Brouthers & Brouthers, 2002). Thus, as a general proposition, we would expect that *GIE has a positive effect on levels of ownership in foreign subsidiaries.*

This common line of argument, however, assumes that experience is transferable to the investors operation in another country (Chang & Rosenzweig, 2001; Johanson & Vahlne, 1977; Terpstra & Yu, 1988). This assumption may be appropriate for mature market economies with a transparent and stable institutional environment. Thus, firms may accumulate knowledge of foreign markets and apply it in similar markets.

However, it is much less clear to what extent experience from other countries is

transferable to emerging economies such as China, where investors face very idiosyncratic environments. These countries differ from mature markets, but they also vary widely amongst each other, which suggests that foreign investors may not be able to redeploy their organizational and managerial capabilities, unless these are specifically adapted to the particular emerging economy (Meyer & Peng, 2005). Within emerging economies, firms have to acquire local knowledge on how to operate in the unfamiliar informal and regulatory environment (Peng et al., 2008). This knowledge is generally tacit, which increases the time required to learn it from local businesses, and inhibits its transfer even within an MNE. Therefore, we hypothesize:

Hypothesis 1: General international experience has a positive effect on subsidiary ownership in developed economies, but not in emerging economics.

Country-specific experience

Knowledge about a particular context is often tacit (Kogut, 1991) and thus primarily generated by own experience on site. It provides important insights about the business environment and can help to recognize opportunities in a host country (Johansen & Vahlne, 1977), to overcome uncertainty from political hazards (Delios & Henisz, 2003) and to build relationships with local authorities (Luo, 2001).

CSE enhances a firm's knowledge about the local context, and thus supports not only competence building, but also the ability to select a partner. In other words, CSE makes it easier to build a joint venture, yet at the same time, it reduces the need for a joint venture partner.

Traditionally, the literature has focused on the competence building effect: Firms with little host country experience acquire local knowledge by partnering with local firms. However, CSE is also important for assessing potential partners, negotiating a contract suitable for the local environment, and for managing a business interface with another firm. Thus, CSE facilitates the establishment of a joint venture in another country, more

so than GIE. The majority of prior studies has focused on the competence building effect, and thus associates CSE with higher levels of ownership (Delios & Beamish, 1999; Li, 1995). This literature leads us to expect that *CSE has a positive effect on levels of ownership in foreign subsidiaries in developed economies.*

These arguments, however, assume a dominance of the competence building effect over the partner selection effect; yet does this hold in every context? CSE is more important the more idiosyncratic a context is, because investors can transfer less of their established business practices. Hence, we would expect a stronger impact of CSE in emerging economies than in developed economies.

Moreover, the competence building effect may be counterbalanced by a strong partner selection effect. In emerging economies, such as China, businesses rely to a larger extent on business networks as means to coordinate economic activity and to overcome high transaction costs (Meyer & Peng, 2005; Peng et al., 2008). Thus, in these contexts, foreign investors have to integrate themselves into a relationship-oriented culture to conduct their business (Luo & Chen, 1996). At the same time, weak institutions inhibit the availability and reliability of information on potential partner firms, such as accounting data. Thus, it is particularly important to engage in due diligence and get to know the partner and its specific business environment before committing a major joint investment. Firms with CSE are thus better qualified to develop business relationships with influential local partner firms (Luo, 1999). Hence, we expect that *CSE has a negative effect on levels of ownership in foreign subsidiaries in emerging economies.*

Taking these arguments together leads us to our second hypothesis:

Hypothesis 2: Country specific experience has a negative effect on subsidiary ownership in emerging economies, but not in developed economics.

In addition to the moderating effects on experience, contextual variation also has a

direct effect on subsidiary ownership. It is fairly well established in the literature that foreign investors' access to local knowledge and resources is of particular concern in emerging economies, especially if the institutions are weak (Chan & Makino, 2007; Delios & Beamish, 1999; Meyer, 2001; Peng, 2003, Peng et al., 2008). In particular transition economies, such as China and Vietnam (Makino & Beamish, 1998; Meyer & Nguyen, 2005), have only gradually removed constraints on the level of foreign equity stakes. Thus, we expect ownership levels to be lower in emerging economies. This direct effect is incorporated in Figure 2 as a dotted line, and controlled for in the empirical analysis.

******Insert Figure 2 approximately here******

Methodology

Data and Sample

To test our hypotheses, we need a dataset that has a large variation across subsidiary locations and investor experience, while controlling for other pivotal variables such as home location and industry. We thus analyze subsidiaries of Taiwanese firms in the electronics industry listed in 2003 on the Taiwan Stock Exchange. Financial data and information such as parent firm's size, financial leverage and export intensity were taken from the Taiwan Economic Journal (TEJ) database. Foreign investment information has been obtained from annual reports, complemented with data from the Statistics Report on Overseas Chinese and Foreign Investment from Investment Commission of Ministry of Economic Affairs (MOEA). To check the reliability, we triangulated the data with data from company websites and the Taiwan Stock Exchange.

We excluded the foreign investment of holding companies and dropped 281 observations where the date of an initial entry was not entirely clear, or other values were missing. These missing values affected all types of investors, such that tests for

selection bias did not raise any concerns. Five subsidiaries in Australia were dropped as they do not clearly fit into any of our regional groupings and the sample is too small for a separate analysis. Our final dataset thus comprises total 1506 observations of overseas investments from 1980 to 2003 by 467 electronics firms.

In the empirical analysis, we distinguish host regions firstly in terms of the developed-versus-emerging dichotomy suggested by our theoretical arguments and by the prior literature. Secondly, we conduct a more detailed analysis of the moderating effects by distinguishing developed economies as developed North America (D-NA), developed Europe (D-Europe), and developed Asia (D-Asia)[2] and while categorizing emerging economies as other emerging economies (E-Other)[3] and China (E-China). We distinguish China because of its distinct context and the large volume of foreign investment in China in recent decades from Taiwan (Tan et al., 2007). Thus, we can test whether the hypothesized effects apply in similar ways to China as to other emerging economies. Table 1 presents the sample.

******Insert Table 1 approximately here******

Our empirical analysis employs an Ordered Logit model to make the most of the ordinal nature of ownership data (Chu & Anderson, 1992). We investigate the nature of the moderating effects in two alternative ways, which yield substantially identical results – thus enhancing our confidence in the results. First, we incorporate the moderating effects between experience and host contexts in a single equation using interaction effects (Tables 3 and 4). This method has the advantage that it exploits the full variation in the data, and generates more efficient estimators based on the higher degrees of freedom of the full sample. However, it assumes that coefficients on control variables are not moderated by the variation in host contexts.

[2] Developed Asia includes high income economies in the region: Japan, the Republic of Korea, Hong Kong, and Singapore.

[3] Other emerging economies include Indonesia, Malaysia, Philippines, Thailand, Vietnam, Brazil, Czech Republic, Georgia, Mexico, Hungry, Russia, and United Arab Emirates.

Second, we regress our empirical model for subsamples of each host context (following Peng and Luo, 2000), thus generating 14 separate regression equations (Table 5 and 6). This method relaxes the assumption of identical coefficient on control variables by estimating them separately for each sub-sample; yet, it suffers from smaller sample sizes (and thus lesser levels of significance) and possible imbalances or collinearity in the subsamples which we had to check separately for each sub-sample. In Developed Europe, most subsidiaries are wholly-owned such that the regression over this subsample has only low explanatory power.

Variables and Measurements

Ownership. The share of ownership is a variable with a non-normal distribution, and it is non-linearly related to a key theoretical construct, control over the operation. Therefore, we follow Chu and Anderson (1992) and operationalize the level of ownership as a 4 point categorical variable with the following steps: 0 = the ownership less than 50% as minor equity; 1 = 50% as equal equity; 2 = 50-95% as majority equity; 3 = 95-100% as wholly owned enterprises, using data from the 2003 annual reports.

Given the ordinal nature of this scale, we employ an Ordered Logit regression model for the analysis. We have also run the same equations with a simplified binary logit (wholly owned enterprise versus any other level), yet the results were substantively identical to the Ordered Logit model reported here.

General International Experience. We follow earlier studies in constructing our measures of experience. GIE has been measured in a variety of ways, including the number years of worldwide experience (Contractor & Kundu, 1998; Erramilli, 1991; Prasad & Kang, 1996), total number of foreign investment (Delios & Beamish, 1999; Gatignon & Anderson, 1988), the ratio of foreign to total number of investment (Contractor & Kundu, 1998), the ratio of a firm's foreign to total sales (Chang &

Rosenzweig, 2001; Yu, 1990), whether firms had subsidiaries in neighboring countries (Terpstra & Yu, 1998; Yu, 1990), the geographic spread of the company's international experience (Erramilli, 1991) or number of previous technology transfers (Davidson & McFetridge, 1985). We use the most common measure of GIE, namely number of years of foreign investment operations outside the home economy.

Country-Specific Experience. The construct of CSE has previously been measured as the number of years operated in the country (Luo & Peng, 1999) and the number of previous expansions in the same host country (Barkema, Bell & Pennings., 1996). We match our measure of CSE with that of GIE to allow a comparative analysis, and thus use the number of years of foreign investment operations in the specific country.

Control Variables. In investigating the effects of experience on ownership strategy, we need to control for other variables likely to influence this decision. This includes firstly parent specific variables: *export intensity,* proxied as the ratio of parent firm exports over parent firm sales (Chang, 1995; Terpstra & Yu, 1988), *R&D intensity* in terms of R&D expenditures as a percentage of sales, the parent *size* in terms of the number of employees. *Leverage* is a critical factor affecting firms' operational risks and proxied by total debts to total assets. Moreover, we control for the age of the specific subsidiary as ownership structures may change over the lifetime of a subsidiary.

******Table 2 approximately here******

Table 2 presents the means, standard deviations, and correlations matrix for the variables. The two concepts relating to experience, CSE and GIE, are correlated at 0.5 such that we include them in separate regression models. None of the other correlations are such that they would give rise to concerns.

******Table 3 and 4 about here******

Results

The results of our Ordered Logit regression analysis over the full sample are reported in Tables 3 and 4. The model statistics are satisfactory and the coefficients are signed in line with expectations.

Models 1 and 2 introduce the experience effects moderated by the broad categories of 'developed' and 'emerging'. GIE is positive and significant at 5% level for developed economies, in line with Hypothesis 1, while the effect is not significant for subsidiaries in emerging economies. We interpret this evidence that the competence building effect of GIE dominates in developed economies, but is ineffective in emerging economies where idiosyncratic local condition may prevail. CSE is negative significant at 1% level in emerging economies, suggesting that partner selection dominates over the competence building effect, as predicted in Hypothesis 2.

This analysis may be subject to aggregation biases, such that we next interact the experience effects with more specific host region dummies to test for the context specificity of the hypothesized effects (Table 4). Note that the dummies cover all five regions, such that the model is fully specified without a non-moderated experience effect.[4] The coefficients thus measure the effect in each of the host contexts.

Model 3 shows that GIE has a positive and significant influence on ownership in developed Asia and Europe, but is not significant in other regions. Thus, internationally experienced investors are more likely to pursue full ownership strategies in developed economies of Asia and Europe, as predicted by Hypothesis 1, but surprisingly no such effect emerges for North America. Thus, the competence building effect appears relevant in some developed regions but not in others.

CSE shows a different pattern, as predicted in Hypothesis 2. In Model 4, the relationship between CSE and ownership strategy is not significant for any developed

[4] Some earlier studies test for *differences* in the effect sizes, which requires omitting one of the categories for the moderators (say, GIE*China). In that case the coefficients would measure the difference of the effect sizes *compared to the base case*.

country region. On the other hand, CSE has a highly significant negative effect on ownership strategy in China in line with Hypothesis 2. Thus, the partner selection effect dominates in China, which appears to be distinct from other emerging economies, where the coefficient is positive and not significant. Model 5 combines GIE and CSE effects with substantially the same results as Models 3 and 4, thus showing that multicollinearity is not affecting the results.

Additional evidence on host country effects emerges from the region dummies. We use China as a base case. In a base model that excludes the experience effects (not reported), we find that subsidiaries in *D-Europe*, *D-Asia* and *E-Other* are significantly more likely to be wholly owned than those in China, with the effect size for *D-Europe* being considerably larger than for the other regions. However, these country effects are to some extent caused by investors' experience: Models 1 and 2 with interaction between host region and experience effects show a significant effect only for *D-Europe*, where affiliates are more likely to be wholly owned.

In all these regressions, results for the control variables show that higher levels of ownership are associated with smaller firms, highly leveraged firms, older subsidiaries, and possibly R&D intensive firms.

Next, we perform a sub-sample analysis for developed versus emerging economies (Table 5) and for more specific regions (Table 6). This form of analysis drops the assumption that other coefficients are context-invariant, yet each analysis has fewer degrees of freedom such that levels of significance would normally be lower. The regressions show the same patterns thus enhancing our confidence in the results.

In Models 6 to 9, we conduct the analysis over sub-samples for respectively developed and emerging economies. These show the same patterns as in Models 1 and 2, namely significant negative effects of CSE in emerging economies, and significant positive effects of GIE in developed countries. In Models 10 to 19, we use more specific

sub-samples for the categories employed in Model 3 and 4. These show the same patterns: Positive effects for GIE in *D-Europe* and *D-Asia*, and negative effects for CSE in *E-China*, while other effects remain insignificant.

Discussion

We have argued that investors' prior experience influences the ownership of foreign affiliates in two ways: a competence building effect enhances a firm's ability to manage independently and with full ownership, and a partner selection effect enhances a firm's ability to establish and manage a relationship with a local firm (Figure 1). Our results suggest that the competence building effect applies with respect to GIE for investments in developed Europe and Asia, while the partner selection effect dominates in China, but not in any other region.

This result confirms our main argument that context is very important for experience effects, even where it does not confirm with our exact predictions that were based on the distinction between emerging and developed economies. We expected that in developed countries, where institutions and the general business environment are more stable and transparent, investors would be able to apply their knowledge acquired in other countries. This expectation is confirmed with respect to developed economies in Asia and Europe. This finding is consistent with previous studies arguing that learning and knowledge accumulation are important for mode choice (Barkema & Vermeulen, 1998). These benefits arise more from GIE rather than CSE, because it can be transferred to other locations (Johanson & Vahlne, 1997). This result thus supports both organizational learning and internationalization process theories with respect to developed economies.

However, the insignificant relationship between GIE and ownership strategy in North America does not conform to our expectations. Principally, this could be caused by two effects:

a. Experience gained elsewhere, for example in Asia, is not relevant for operating in North America. In other words, the North American business environment creates unique challenges for entrants that render other experiences irrelevant.

b. A partner selection effect neutralizes the competence building effect such that firms with a lot of international experience know better how to set up a joint venture in the USA.

The partner selection effect is associated in particular with a lack of information about prospective business partners, low trust environments, and personal relationship-based business networks. However, as business in North America is comparatively transparent and markets are relatively efficient, explanation (b) seems rather unlikely. Thus, we follow (a) and interpret our results as an indication that the North American market – which here mainly implies the USA – is fairly unique from the perspective of an Asian business, for instance due to is sheer size, fierce competitiveness, and its complex (though largely codified) regulatory environment for imports and inward investment. Hence, the dynamics of competition may be substantially different, which limits the relevance of experiences gained in Asia for operations in North America.

Our results for CSE are consistent with some studies, although many studies found a positive relationship between CSE and ownership. The finding that *only in China* CSE has a significant *negative* influence on ownership points to a distinct nature of the Chinese business environment. The importance of building relationships prior to the establishment of a JV may be based on specific features of Chinese culture (Luo, 2007; Luo & Chen, 1996). Thus, China appears to be special in two ways – GIE does not matter and CSE matters because of the partner selection effect not found elsewhere.

China has a unique heritage of economic reform and a rapidly evolving institutional environment, which may limit the transferability of GIE from other countries. Moreover,

in the fast changing and highly uncertain environment of China (Luo, 2007), firms seem not to utilize CSE to establish subsequent investments as wholly owned operations, possibly because prior experience is not necessarily applicable to the next investment. However, CSE helps to cooperate with local partners and to tap into their business networks. This would explain why firms with more CSE tend to have lower levels of ownership in China.

In addition, a country-of-origin effect may have affected our results. We have studied firms from a specific geographic and industrial origin in this study. This allowed us to separate host country variations from home country or industry effects. However, a limitation of this approach is that the results may be specific to the chosen population of firms. It is remarkable that most prior studies that found a negative effect for CSE have been conducted on Japanese firms (Delios & Henisz, 2000; Lu, 2002; Somlev & Hoshino, 2005). Hence, there may be a country of origin effect shared by East Asian businesses. Other evidence suggests that experience effects may be moderated by the distance between host and home countries (Estrin, Baghdasaryan & Meyer, 2008). This reinforces concerns regarding the transferability of scholarly management knowledge to Asia (Meyer, 2006). Thus, we recommend that future studies on experience effects depart from the dominant strategy of using single source countries, and study investment from many sources into a single host country.

Further limitations arise from the choice of measures of experience. We follow the dominant practice to use the number of years of operational experience in global and host markets respectively to capture GIE and CSE. This measure captures the length of exposure but not necessarily its intensity. Future research may thus explore further variables for more comprehensive assessment of international experience. Future studies may also integrate the analysis of general forms of experience with decision-specific or mode-specific experience (Chang & Rosenzweig, 2001; Chetty et al., 2006) or with the

experience held by individuals in the top management team.

Conclusions

This study examines the relationship between international business experience and foreign investors' ownership strategy. We separate experience as GIE and CSE, and find that the results are highly dependent on the chosen host context. In particular, GIE has a positive effect on ownership levels for firms operating in developed Asia and Europe, while CSE has negative impact on ownership strategies in China.

Possibly the most important insight from this study is a reminder that all management knowledge – and empirical scholarly knowledge about management – should be considered context-specific unless empirical evidence supports its generalizability! Effects that are found to be significant in one context may not apply in another. This has been argued by many scholars (Hofstede, 1990; Meyer, 2006; 2007; Tsui, 2007), yet rarely has it been demonstrated as clearly as in this study. Thus, management researchers ought to prioritize both systematic comparative research designs (Redding, 1994; White, 2002; Jackson & Deeg, 2008) and replication studies (Peng, Zhou & York, 2006; Tsang & Kwan, 1999) in their research agendas.

The main message for management practice is to reinforce the 'importance of local knowledge'. This is probably less surprising to international managers than to scholars searching for the 'general theory' of management. Local knowledge has to be developed locally because of its tacit nature, while advice from consultants (or theorists) unfamiliar with the local context should be treated with great caution. This study has shown that this process is particularly important in idiosyncratic contexts, such as China.

Moreover, local experience may influence business strategies in different ways: it facilitates operating in a country (the competence building effect), but it also facilitates

managing a joint venture with a local partner (the partner selection effect). These sometimes offsetting effects make JV an appropriate mode for newcomers in some locations, but not in others.

The conventional view that the inexperienced would prefer a JV as means to gain experience is clearly not appropriate for everyone and everywhere. While an arranged marriage may serve some, most would prefer to get to know their partner before they tie the knot. Similarly, businesses would prefer to build relationships with prospective partners before committing substantial resources to a venture that is dependent on the partner.

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Figure 1: Competence Building and Partner Selection Effects

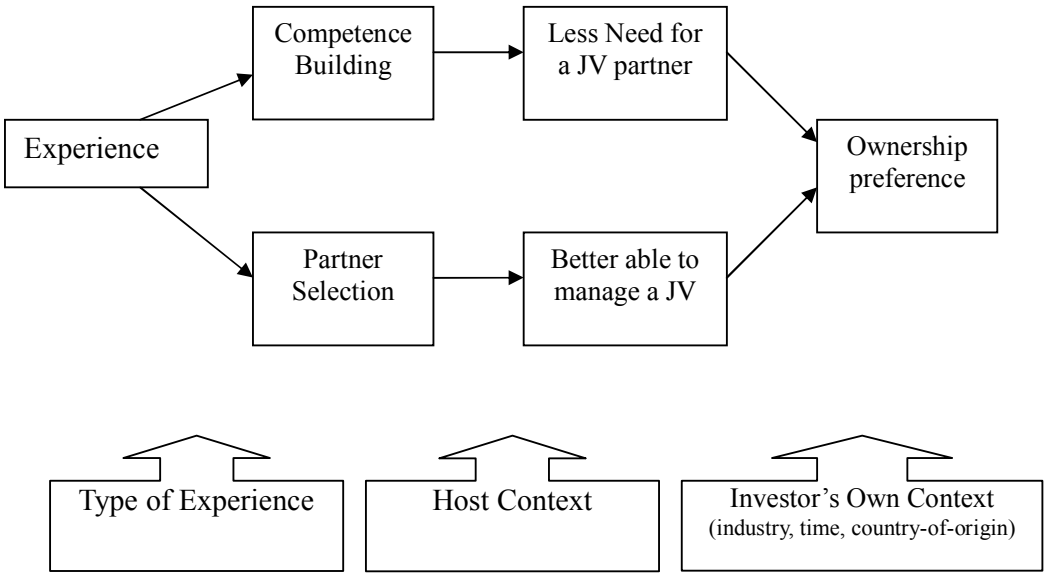

Figure 2: Experience Effects and Subsidiary Ownership in Different Contexts

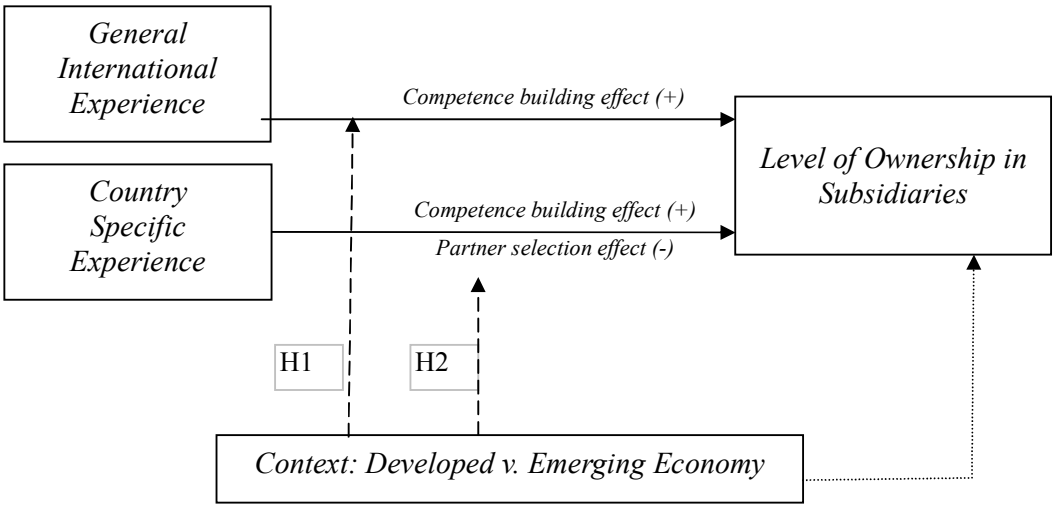

Table 1 Sample distribution

Location	number	International experience (mean)	Country-specific experience (mean)
Developed N-America	240	6.90	4.76
Developed Europe	144	7.74	1.01
Developed Asia	238	6.28	0.93
Emerging Other	87	8.44	1.11
Emerging China	797	7.85	3.01
Total	1506	7.46	2.63

Table 2 Means, Standard Deviations, and Correlations

Variables	Mean	S.D.	1	2	3	4	5	6	7	8	9	10	11	12	13
1. Size	905.574	1249.749	1.000												
2 Leverage	41.806	17.000	-0.058**	1.000											
3 Export Intensity	63.327	30.858	0.259***	-0.030	1.000										
4. R &D Intensity	3.607	5.660	-0.056**	-0.239***	-0.108***	1.000									
5 Subsidiary age	4.562	4.043	-0.081***	0.265***	-0.034	-0.044*	1.000								
6. Developed N-America	0.172	0.377	0.077**	0.018	0.045*	0.084***	0.138***	1.000							
7 Developed Europe	0.103	0.3040	0.040	0.046*	0.127***	0.015	0.086***	-0.154***	1.000						
8. Developed Asia-Pacific	0.164	0.371	-0.030	0.063**	-0.095***	0.004	0.120***	-0.202***	-0.150***	1.000					
9. Emerging Other	0.069	0.254	0.020	0.057**	0.070**	-0.056**	0.143***	-0.124***	-0.093***	-0.121***	1.000				
10. Emerging China	0.491	0.500	-0.069**	-0.116***	-0.070**	-0.047*	-0.319***	-0.448***	-0.333***	-0.436***	-0.268***	1.000*			
11. General International Experience	7.461	8.346	0.309***	-0.128***	0.285***	-0.092***	-0.267***	-0.031	0.011***	-0.063**	0.032	0.046**	1.000		
12. Country-specific Experience	2.632	4.685	0.139***	-0.101***	0.216***	-0.050**	-0.244***	0.207***	-0.118	-0.161***	-0.089***	0.080***	0.526***	1.000	
13 Ownership strategy	2.522	0.956	-0.068**	0.107***	0.006	0.049*	0.115***	0.080***	0.125***	0.028	0.021***	-0.168***	-0.028**	-0.081***	1.000

*p≦0.10, **p≦0.05, ***p≦0.01

Table 3 Ordered Logit on international experience and ownership strategy

	Model 1		Model 2	
	Coefficient	Wald	*Coefficient*	Wald
GIE * Developed	0.028**	4.386		
GIE * Emerging	0.002	0.061		
CSE * Developed			-0.002	0.014
CSE * Emerging			-0.075***	11.330
Developed N- America	0.341	2.289	0.319	1.990
Developed Europe	1.271***	14.206	1.222***	14.629
Developed Asia	0.052	0.062	0.010	0.003
Emerging Other	0.334	1.529	0.206	0.570
Emerging China [a]	0	.	0	.
Size	-0.000**	9.202	-0.000**	7.605
Leverage	0.010**	6.127	0.008**	4.401
Export Intensity	-0.000	0.034	0.002	1.410
R &D Intensity	0.026*	3.707	0.021	2.491
Subsidiary age	0.084***	12.638	0.064**	6.928
μ_1	-1.164***	22.640	-1.431***	32.719
μ_2	-1.084***	19.743	-1.350***	29.310
μ_3	-0.177	0.539	-0.437*	3.183
Observations	1506		1506	
Log-Likelihood	2097.464		2099.053	
Cox & Snell R^2	0.053		0.057	
Model χ^2	3843.648***		3892.595***	

Notes: China is used as base case for host region dummies. GIE = general international experience, CSE = country specific experience. μ_1, μ_2, μ_3 = shift parameter of Ordered Logit.

*p≦0.10, **p≦0.05, ***p≦0.01, [a] = omitted case

Table 4: Ordered Logit on international experience and ownership strategy: Region-specific effects

	Model 3		Model 4		Model 5	
	Coefficient	Wald	*Coefficient*	Wald	*Coefficient*	Wald
GIE * D-NA	-0.000	0.000			-0.010	0.158
GIE * D-EU	0.185**	5.145			0.218**	5.609
GIE * D-Asia	0.049**	4.619			0.067**	6.349
GIE * E-Other	0.043	2.111			0.040	1.828
GIE * E-China	-0.003	0.103			0.018	2.223
CSE * D-NA			0.000	0.000	0.013	0.188
CSE * D-EU			0.013	0.019	-0.152	1.257
CSE * D-Asia			-0.026	0.263	-0.100*	2.771
CSE * E-Other			0.043	0.240	0.033	0.137
CSE * E-China			-0.087***	13.750	-0.101***	14.630
Developed N-America	0.526**	4.219	0.264	1.308	0.403	2.394
Developed Europe	0.233	0.190	1.158***	11.445	0.052	0.009
Developed Asia	-0.128	0.298	-0.002	0.000	-0.273	1.295
Emerging Other	-0.156	0.151	-0.024	0.006	-0.329	0.651
Emerging China [a]	0 [a]	.	0 [a]	.	0[a]	.
Size	-0.000**	9.484	-0.000**	7.782	-0.000***	13.099
Leverage	0.011**	6.730	0.008**	4.264	0.009**	5.341
Export Intensity	0.000	0.046	0.003	1.716	0.002	0.704
R &D Intensity	0.025*	3.547	0.020	2.434	0.021	2.486
Subsidiary age	0.085**	12.748	0.062**	6.585	0.067**	7.343
μ_1	-1.193***	23.637	-1.469***	33.992	-1.423***	31.064
μ_2	-1.113***	20.677	-1.389***	30.538	-1.342***	27.788
μ_3	0.202	0.702	-0.474*	3.685	-0.421*	2.828
Observations	1506		1506		1506	
Log-Likelihood	2086.131		2096.119		2075.405	
Cox & Snell R^2	0.060		0.059		0.072	
Model χ^2	3808.927***		3899.732***		3935.451***	

*p≦0.10, **p≦0.05, ***p≦0.01, [a] = base case for host region dummies.

Table 5: Ordered Logit Sub-sample Analysis: Developed vs Emerging economies

	Developed economies		Emerging economies	
	Model 6	Model 7	Model 8	Model 9
GIE	0.035**		0.002	
CSE		-0.000		-0.065**
Developed N America	0.365	0.366		
Developed Europe	1.291***	1.286***		
Developed Asia [a]	0 [a]	0 [a]		
Emerging Other			0.292	0.185
Emerging China [a]			0 [a]	0 [a]
Size	-0.000***	-0.000***	-0.000	-0.000
Leverage	-0.005	-0.007	0.017***	0.016**
Export Intensity	0.001	0.003	-0.000	0.002
R & D Intensity	0.003	0.002	0.042**	0.035*
Subsidiary age	0.059	0.049	0.092**	0.068**
μ_1	-2.682***	-2.844***	-0.635**	-0.891**
μ_2	-2.575***	-2.737***	-0.559*	-0.814**
μ_3	-1.052**	-1.224**	0.150	0.099
Observations	622		884	
Log-Likelihood	694.354	706.919	1361.094	1354.650
Cox & Snell R^2	0.059	0.050	0.034	0.043
Model χ^2	1735.551***	1678.409***	2303.007***	2330.777***

*p≦0.10, **p≦0.05, ***p≦0.01, [a] = base case for host region dummies.

Table 6: Ordered Logit Sub-sample Analysis by Region

	Developed N America		Developed Europe		Developed Asia		Emerging Other		Emerging China	
	Model 10	Model 11	Model 12	Model 13	Model 14	Model 15	Model 16	Model 17	Model 18	Model 19
GIE	0.002		0.139*		0.081**		0.020		-0.003	
CSE		-0.009		0.007		-0.020		-0.007		-0.073**
Size	-0.000***	-0.000***	0.000	0.000	-0.000**	-0.000**	-0.000	-0.000	-0.000	-0.000
Leverage	-0.025**	-0.025**	-0.002	-0.002	0.021**	0.016	-0.009	-0.010	0.018***	0.018***
Export Intensity	0.006	0.005	0.003	0.009	-0.000	0.001	-0.000	-0.000	-0.000	0.002
R &D Intensity	-0.024	-0.025	0.188	0.196	0.077*	0.066	-0.225**	-0.236**	0.052**	0.046**
Subsidiary age	0.013	0.015	0.102	0.047	0.078*	0.067	0.018	0.000	0.100**	0.069**
μ_1	-4.591***	-4.591***	---	----	-1.033	-1.496**	-3.726**	-4.005**	-0.508*	-0.756**
μ_2	-4.392***	-4.392***	---	---	-0.976	-1.439**	-1.915	-2.198	0.428	-0.675**
μ_3	-2.771***	-2.771***	-0.032	-0.649	0.367	-0.139	---	---	0.224	-0.016
Observations	240		144		238		87		797	
Log-Likelihood	268.500	268.326	70.568	78.750	314.386	328.691	107.566	109.353	1231.053	1222.408
Cox & Snell R^2	0.078	0.078	0.073	0.039	0.089	0.047	0.083	0.078	0.040	0.05
Model χ^2	708.466***	702.944**	90.313	113.893	771.336***	733.533**	144.601	153.224	2138.689***	2154.190***

Note: In Models 12 and 13, the industry control dummies have been omitted due to multicollinearity.

*p≦0.10, **p≦0.05, ***p≦0.01,