

CAUSALITY OF THE MULTINATIONALITY-PERFORMANCE RELATIONSHIP: SEARCHING FOR CONSENSUS

ABSTRACT

This paper reviews recent and prominent literature covering the causal direction of the multinationality-performance (M-P) relationship. It draws on articles from the international management, finance, and economics literature. International management's traditional view of M leading to P has primarily been championed with theoretical arguments. A review of the debate on the validity of those arguments indicates that they are unsatisfactorily founded. The relatively few explicit tests of the causal direction provide strong support for the notion that superior firms expand abroad, i.e. P as the antecedent to M and that the frequent finding of a positive correlation between M and P is best explained with a self-selection bias. A discussion of the emerging consensus of competitive advantage as an antecedent to both performance and multinationality explains the seemingly contradictory findings of the M-P literature stream and identifies new research directions for the literature stream.

INTRODUCTION

Imagine a world without borders, with only one nation. In this world there are businesses, large and small. Imagine then that we add borders, trade barriers, cultural differences and other aspects from the current real world to our imaginary world. Would this add value to the businesses that find themselves operating across borders compared to similar firms that find

themselves contained within one geography? Would multinationality, per se, enhance performance? Such a causal relationship where multinationality leads to performance is a fundamental assumption of international management research, especially in the large literature stream on the relation between multinationality (M) and performance (P) (Contractor, Kundu, & Hsu, 2003). In spite of this, the efforts to find a generic relationship between M and P have, essentially, failed (Verbeke, Li, & Goerzen, 2009). The findings have been inconclusive and often even contradicting. If we turn to the closely related research on international trade, on the other hand, the general view is that it is superior firms that choose to go abroad rather than multinationality causing superiority. Bernard and Jensen (1999) claim that “for most academic economists, the statement that ‘good firms become exporters’ is almost a waste of breath, producing knowing nods of agreement.”

Given that (1) this causal relationship is so fundamental to much international management research, (2) there is an apparent divide in researchers’ views on the direction of causality, and (3) that the research community has been unable to find a stable relation between multinationality and performance, it is important to investigate what research has been done on the causality issue, if we are moving towards a consensus, and what the major implications are for international management research. A lack of consensus on this matter is not sustainable because of the topic’s importance to international management research as a whole.

In this paper I argue that one main reason for the lack of consistency in the findings is that the causality assumption of M leading to P is incorrect. I argue that the causality relation, if anything, is the opposite, i.e. that it is performance, or more precisely, competitive advantage

that leads to multinationality. If it was the case that M, per se, on average, leads to P, there should be an observable relation between the degree of internationalization and performance. Much of the most important international management research focuses on studying just that relationship and has frequently found it to be positive (Ruigrok & Wagner, 2004). Normally, the causality direction of M leading to P is assumed. The assumption is not strange. On an individual firm level it is a very valid question to ask whether it should expand into or withdraw from foreign markets. There is, however, a difference between firm-level studies, where internationalization undeniably can be found to lead to performance improvements, and higher-level studies where averages are studied. For example, through looking at all multinational firms in one country – or some other high-level view – studies of average performance and multinationality must, for example, assume that multinationality, per se, causes a competitive advantage, which in turn must assume that multinationality is not available to all firms. If there was no such barrier to multinationality, all firms could find the optimal level and then competition would drive away any average excess profits stemming from multinationality¹. It is difficult to see a barrier to internationalization that would be systematic, present across geographies, and that would be unevenly distributed in such a way that it causes average performance superiority for firms with high degrees of multinationality compared to those with lower.

How, then, could we explain that many researchers have found a positive M-P relationship? If we take the opposite stand, that it is the firms that have a competitive advantage that will go

¹ This argumentation does not require perfect markets, as Contractor (2007) claims, because it only regards profits stemming directly from multinationality.

abroad, the logic is very simple. Firms with a competitive advantage will seek profitable growth through finding new markets where they can use their competitive advantage, which would cause a self-selection bias as superior firms would expand more into new geographies.

Interestingly, this view is firmly rooted amongst economists studying international trade, even though it, too, does not exclude the possibility of both causality directions being simultaneously true (Bernard & Jensen, 1999). The view that competitive advantage leads to international expansion is also supported in other parts of international management research. It should be noted here that there is a difference between competitive advantage and performance. It is, however, the case that performance is almost only used as an independent variable in discussions of agency costs while scholars viewing multinationality as a consequence of superiority mostly use some version of competitive advantage as the antecedent.

It is not only important to examine this causal relationship because it is fundamental to the M-P literature stream, which is the largest single literature stream in international management research (Hitt, Tihanyi, Miller, & Connelly, 2006). It is also important from a practitioner point of view. M-P researchers typically advise firms to find ideal levels of multinationality by expanding into or withdrawing from markets. If, as I argue, it is not multinationality that leads to performance, such recommendations are misplaced and can be directly harmful for businesses. It will also mean that multinationality is not an independent variable to manage but rather a result of other strategic choices. Managers take much interest in how international their firms should be, but if we as researchers are going to advise them based on an observed ideal

level of multinationality, we must be very sure that it really is differences in that degree that causes a significant share of performance differences.

The direction of causality of the M-P relationship is an old issue in international management research and does not need yet another review that summarizes previous findings. What is needed is to contribute to and look for a consensus view on an issue that has divided international management scholars for too long. Because of this, I have chosen to focus on recent literature.

In a special issue of *Management International Review* in 2007, Hennart (2007) and Contractor (2007) Debates the theoretical foundation of the M-P relationship. As it is essential to have a sound theoretical foundation in an argument of a causal direction, I use that debate as a backbone for a review of the theoretical reasons that have been suggested to facilitate an M to P causation. Because very little research has been done to explicitly investigate the causality of the M-P relationship and because the issue not only involves international management scholars, I also include findings from the finance and economics research communities.

Before the literature review, it is necessary to discuss the meaning of the key terms of this paper, performance and multinationality. To be meaningful in comparisons, performance must measure some risk-adjusted return on investment. Absolute measures of performance are meaningless from an investor's point of view as are measures that do not adjust for risk, as absolute return levels can be chosen by managers through for example leverage and expansion. Risk-adjusted relative performance, however, is what rational investors are seeking (see any corporate finance textbook).

I see multinationality as marketing products or services to several geographies. I choose not to make a difference between for example exporting and foreign direct investments as these are alternative entry modes and the decision is based on a number of factors, such as industry, technology, and risk preference (Castellani & Zanfei, 2004; Johanson & Vahlne, 1977). If we are to look at the effect of multinationality in isolation the term should include all forms of multinationality.

The literature review will start with a brief overview of the M-P literature stream. Thereafter follows a review of its most important theoretical underpinnings. The last part of the literature review section focuses on the research that more directly addresses the causal direction. The discussion focuses on how the confusing and contradicting findings can be fit into one view.

LITERATURE REVIEW

The multinationality-performance relationship

The relationship between multinationality and performance is probably the most studied part of international management research (Hitt, Tihanyi, Miller, & Connelly, 2006). Unfortunately, the findings have been inconsistent and often contradictory. Some researchers have found a U-shaped relationship between multinationality and performance (Ruigrok & Wagner, 2003; Capar & Kotabe, 2003), while others have found an *inverted* U-shape (Gomes & Ramaswamy, 1999). Some authors have tried to merge the contradictory findings through suggesting an S-shaped relationship (Contractor, Kundu, & Hsu, 2003; Ruigrok, Amann, & Wagner, 2007; Lu & Beamish, 2004; Riahi-Belkaoui, 1998; Contractor, 2007). Such curves have been observed but the shapes of the S-curves are very different in different samples so these efforts, too, have been

inconclusive. Other researchers have even found that international diversification destroys value (Denis, Denis, & Yos, 2002; Click & Harrison, 2000; Fauver, Houston, & Naranjo, 2004) or that the relationship is inconclusive (Morck & Yeung, 1991). Dastidar (2009) found that multinational firms create value but that it depends on the observed time period. For example, Dastidar observed negative value creation when using the same period (1991 to 1995) as Fauver et al. (2004), who found a negative relationship. The general view is, however, that the relationship is found to be positive more often than negative (Ruigrok & Wagner, 2004).

It is clear that simply observing the relationship between multinationality and performance is not enough to produce a meaningful understanding. The amount of research effort that has gone into testing the M-P relationship is astonishing, yet we are not even approaching a common understanding of the relationship. The inconsistency of the findings in the literature stream has primarily been explained with the suggestion that the relationship is much more complex (Hitt, Hoskisson, & Kim, 1997). A result of this has been a large number of suggested antecedents and moderators (for a review see Hitt et al., 2006).

Another explanation for the lack of consistent findings has been that the M-P literature has a poor theoretical foundation (Hennart, 2007). Such critique is very important because the causal direction of the M-P relationship has rarely been tested and therefore the underlying theories are the only thing supporting the causality. And, if the causality direction goes from performance to multinationality, the inconclusiveness is predictable and we may expect a positive tendency from self-selection bias, i.e. that multinationals are better as a group, not because of their multinationality but because better firms become multinationals. Contractor

(2007) claims that a majority of the previous studies have at least some segment of the M-P curve with a positive slope and therefore draws the conclusion that “[t]his demonstrates beyond cavil that international expansion produces a net positive effect for companies for some, or considerable, portion of the internationalization range” (2007, p. 472). The statement clearly expresses a causal link (“*produces a net positive effect*”) but refers only to a correlation. Instead Contractor builds his argument on a theoretical foundation of the causal direction and therefore it is necessary for this paper to assess that theory.

Critique against the theoretical foundation of M-P studies

If we are going to be able to conclude that the causal direction of the M-P relationship is the traditional one (multinationality leading to performance), there should also be a theoretical argumentation explaining it. Hennart (2007), however, criticized the literature stream as a whole, pointing to its poor theoretical foundation. Hennart’s article, which has received much praise (Verbeke, Li, & Goerzen, 2009), criticized the four main arguments that have been used to suggest an M-P relationship, that is, risk reduction, scale economies, flexibility, and learning. Verbeke et al. later even concluded that “there is no valid theoretical rationale that would predict a generalizable M-P relationship” (2009, p. 149) but never referred to an article by Contractor (2007) that defended some of the theoretical reasons for an M-P relationship that Hennart (2007) criticized. Because of this lack of consensus, I see it as necessary to go through the main theoretical arguments and their critique.

The first argument is ‘risk reduction’. Hennart (2007) used transaction cost theory to claim that investors can diversify more cheaply, through transactions on financial markets, than firms can do through investing in foreign countries. The logic is well established in financial theory and

therefore the proposition that international diversification leads to higher performance through risk reduction can be rejected. The relevant risk metric, from an investor's perspective is systematic risk (Shapiro, 1978) and, contrary to the risk reduction proposition, this has been found to increase with the level of multinationality (Reeb, Kwok, & Baek, 1998; Siegel, Omer, Rigsby, & Theerathorn, 1995). Contractor (2007) argues that multinationality does reduce risk, for example because business cycles are not perfectly correlated across geographies. This unfortunately disregards that investors can diversify through markets and thus the defense on this particular point falls flat.

The second argument to be scrutinized is 'scale economies'. These, too, cannot motivate an M-P relationship because it is not shown how economies of scale from multinationality lead to a competitive advantage. When a market is too small to operate efficiently it does motivate firms to expand abroad but it does not explain any systematic competitive advantage. To reach an efficient scale, firms might have to expand abroad. If a firm is to achieve a sustainable competitive advantage from this, however, this option must be closed to, or at least costlier to its competitors. No argument has been put forward for why internationalized firms would systematically find such an advantage. Firms that are forced abroad because they have too small home markets would rather be at a competitive disadvantage to firms that can reach an efficient scale at home (Hennart, 2007).

Also Contractor (2007) argues that firms are forced abroad in search of scale. He also agrees that it is unclear in the literature why it would create a competitive advantage. Instead, he points especially to the large R&D expenditures in high-tech industries, which suggests a need for

multinationality. Strangely, Contractor never argues why this would create a competitive advantage and thus misses Hennart's point. The question is not whether multi-market presence allows for scale economies (which is undeniably true) but why only some firms are able to exploit them, which would cause performance differences from multinationality.

The third argument, 'flexibility', has been suggested to lead to performance through multinational firms being more able than home market focused ones to adapt to changing market conditions. For this to be true there must be some reason why internal adaptations, such as moving production from one site to another, would be superior to market-based adaptations, such as shifting suppliers. This would only be the case with very high transaction costs and inefficient markets. It even seems plausible that a market-solution is more flexible (Hennart, 2007).

The fourth argument, 'learning', states that firms with multi-market presence would be able to learn more than domestically focused firms. A fundamental idea behind this is that knowledge is transferred across units of the MNE to create a common pool of knowledge that is not attainable to less multinational firms (Kogut & Zander, 1993). Hennart (2007) claims that the knowledge transfer that is observed in reality usually goes from headquarters to subsidiaries and not the other way around. Contractor (2007), on the other hand, said that this pattern is changing with firms setting up R&D activities in multiple locations, for example. On the other hand, several authors have suggested that internalization of foreign units is not the only way to learn as it is possible to learn from suppliers or customers, for example, and that learning therefore does not cause any significant M-P relationship (Hennart, 2007).

Besides the critique of learning as a source of value from international expansion, learning has an intuitive appeal. Learning is often analyzed in relation to the concept of 'liability of foreignness', which means "costs of doing business abroad that result in a competitive disadvantage for an MNE subunit" (Zaheer, 1995, p. 342). In the case of liability of foreignness, learning should, over time, help overcome that liability (Ruigrok, Amann, & Wagner, 2007; Contractor, Kundu, & Hsu, 2003). If learning is to cause a performance improvement for the firm as a whole, however, new knowledge must be transferred back from the new geography and be applied in other parts of the firm, otherwise it only reduces a disadvantage. That is what the learning perspective suggests, but the liability of foreignness must always be taken into account when knowledge is transferred across geographies. Therefore, the knowledge that is transferred back from a new region will also be flawed by what could be called a 'return-direction liability of foreignness'. This gives further support to the argument that multinationality will not cause performance increases through learning. It is also in line with Hennart's observation that knowledge seems to flow from home to foreign rather than the other way around. Especially, the learning perspective acknowledges the liability of foreignness but never argues for learning economies from multinationality that would cause increased efficiency in learning.

One important issue that neither Hennart nor Contractor addresses regarding how knowledge could cause relative performance differences is whether multinational firms learn more efficiently. Instead they focus on if firms are able to exploit the learning opportunities that arise from multinationality. A multi-geography presence clearly creates opportunities to learn and

find new opportunities but so do other things, for instance having more employees, a more diverse workforce, or more dispersed operations within geographies, following the same logic. That does not mean that large, diverse, and multinational firms necessarily show higher returns, as resources come with costs and it has not been shown that there are any net learning economies of scale.

Although the M-P literature normally assumes multinationality to be the antecedent in the M-P relationship, other areas of international management research have often taken the opposite stance, seeing multinationality as the consequent. This is, for example, normally the case in literature that is based on core competencies and the resource-based view (Zaheer, 1995) or ownership advantages in the eclectic paradigm, which states that ownership of a competitive advantage causes internationalization (Dunning, 2000).

Generally, it seems improbable that an international configuration, per se, would be more profitable than a purely domestic configuration, especially considering that most trade barriers do not discriminate between individual firms. The core message is that if multinationality is to cause a systematic performance increase it must first cause a competitive advantage, and this has been overlooked in the M-P literature. This literature has rather looked at all reasons for internationalization, not just the things leading to competitive advantage.

Causality directly addressed

It is somewhat surprising that two such contradictory views can coexist in the same research community. Vermeulen and Barkema (2002) take this contradiction as a starting point in their study of the process of international expansion. When they differentiated between general

expansion and foreign expansion they found that the number of foreign subsidiaries had a consistently positive influence on performance, in their sample, while the geographic scope even had a negative influence. This means that new subsidiaries – not new countries – add profit, which clearly contradicts the notion of multinationality as the antecedent in the M-P relationship.

Howenstine and Zeile (1994) used plant level data to observe that foreign firms operating in the U.S. had higher productivity than domestic firms, although they thought this could be attributed to factors such as plant size and capital intensity. Globerman, Ries, and Vertinsky (1994) make the same finding in Canada. Doms and Jensen (1998) found that foreign-owned plants in the U.S. are more productive than domestic ones (11-13% more productive).

Interestingly, when they distinguish between pure domestic and domestic multinational firms, they find that U.S. multinationals is the most productive group of firms and that it is multinationals, as a group, that are more productive than domestic firms. This does not say anything about the causal direction of the link but the fact that exporters are more productive than purely domestic firms is an interesting starting point for testing the causal relationship.

Bernard and Jensen (1999) set out specifically to test the causal direction of the M-P relationship. They also saw higher productivity at exporters (12-19%) but they also looked at differences before and after the choice to start exporting. They saw that firms and plants that later became exporters were more productive than their peers already several years before they started to export. The evidence that good firms become exporters is therefore clear in Bernard and Jensen's test. They also found that productivity growth after plants started to export grew at the

same rate or slower than at domestic plants. This, I argue, is a good reason to reject the hypothesis of multinationality as an antecedent to performance. Interestingly, the low productivity growth of exporters was even more accentuated (and significant) over long time horizons, which is the opposite of what the learning argument of the M-P literature would predict. Other economists have focused specifically on testing the learning hypothesis but have also found that exports do not lead to the anticipated productivity increases and that the superior performance of exporters is due to self selection (Clerides, Lach, & Tybout, 1998; Delgado, Farinas, & Ruano, 2002). The view that it is the most productive firms that start exporting rather than exporting leading to productivity is strongly supported in economics literature and is an important trigger of the development of the "new, new trade theory" (see Melitz, 2003). There are, however, some indications that learning from exporting does take place for firms from under-developed countries (Blalock & Gertler, 2004) and young exporters (Delgado, Farinas, & Ruano, 2002).

Economists have found that only a small share of all firms are exporting, let alone investing, abroad.² This implies that national borders are indeed significant barriers to overcome. Bernard and Jensen (2004) find significant costs of entry into the export market and Castellani and Zanfei (2004) have shown that investing abroad is even more expensive than just exporting. This is the same effect that is referred to as a liability of foreignness in the IM literature (Zaheer, 1995). These two notions, that there is a liability of foreignness and that few firms actually

² In America, for example, the top 10% of exporters account for 96% of the country's foreign sales, and only 4% of firms export at all (Economist, 2008).

export, puts the idea that internationalization leads to higher performance in serious doubt.

Admittedly, most studies testing the I-M relationship finds it to be positive but this finding can just as well be explained by a causal relationship where performance leads to internationalization. If it is the case that firms with competitive advantages are exporting and investing abroad to a greater extent than other firms, it could lead to an overrepresentation of successful firms in samples of international firms, a so called self-selection bias.

Some tests have indicated that multinationality per se causes performance improvements.

Delios and Beamish (1999), for example, found that multinationality is positively correlated to performance. They then tested whether this could be explained by differences in technological and marketing assets, measured by R&D and marketing expenditures. These two variables explained a significant share of the performance differences but not all of it and the authors drew the conclusion that multinationality was the cause of this. Dastidar (2009) made similar findings through a test using excess value as the dependent variable and a larger number of endogenous factors. The results are interesting but such cross-sectional tests do not exclude other potential sources of the performance differences, such as prior performance or added subsidiaries. Instead, the causality is assumed for the variance that is not explained by a number of control factors. Specific tests of causality should preferably be longitudinal and the tests of that type reviewed here indicate multinationality as an outcome rather than an antecedent.

DISCUSSION

When causality is tested there are normally three criteria that should be fulfilled; there should be a theoretical link, it should be possible to exclude alternative explanations, and the effect

between variables should be possible to measure with at least some degree of isolation. In the M-P literature that suggests an M to P causality, so far neither of these can be said to be convincingly fulfilled. The first, and arguably most important, criterion – a theoretical link – is far from being fulfilled. This paper reviews the academic discussion on the topic but cannot find convincing support for any of the main theoretical arguments for multinationality causing relative performance improvements. Still, a large number of studies show a positive M-P relationship. This is intriguing but far from proving an actual M to P causation. A self-selection bias is a fully plausible alternative explanation and has empirical support. Therefore also the second causality criterion – exclusion of alternative explanations – is unfulfilled. For the third criterion – a measurable effect – the inconclusiveness of findings, in spite of a vast literature, indicates that any possible M to P causation is poorly captured, at best, and only seen in cross-sectional tests. Specific and longitudinal tests of the causality relationship even show that rather than the opposite, it is P that causes M. Such a finding does not necessarily exclude that both directions are present simultaneously but without convincing theoretical argumentation the notion of multinationality as a source of competitive advantage is fighting a tough uphill battle.

The only solid consensus I see about why firms choose to go abroad is that they do it to exploit some competitive advantage they possess and that this is necessary for overcoming the liability of foreignness. The question therefore is if it is possible to combine all the confusing findings into one view.

Disentangling multinationality, performance, and competitive advantage

Although multinationality seems not to lead directly to performance, firms do expand and stay profitable doing so. This must be explained. It is important to remember that the objective of most firms is value-creation, and not just performance. Simply put, value-creation can be said to be sales times performance in excess of investors' risk adjusted expectations. With this in mind, it is possible to outline a simple model (Figure 1) that is aligned with the findings presented in the literature review. The model takes its starting point with competitive advantage, which leads to performance (Newbert, 2008). The two constructs are not equal but a competitive advantage leads to performance through firms exploiting the advantage they possess. Firms can also be expected to expand abroad as a way to seek new markets where they can exploit their advantages to realize more rents (Dastidar, 2009). This is supported by the observation that exporters generally show superior performance prior to exporting (Bernard & Jensen, 1999). While exporting may lead to economic rents, it does not necessarily lead to enhanced performance, measured as risk-adjusted return on investment (ROI). Contrarily, it has been shown that the often superior performance of multinational firms can be explained by a self-selection bias (Clerides, Lach, & Tybout, 1998; Delgado, Farinas, & Ruano, 2002) and that multinationality, per se, often even reduces overall productivity (Bernard & Jensen, 1999). Performance reductions can be explained with the well established notion of liability of foreignness (Zaheer, 1995). Imagine, for example, a firm that has a strong competitive advantage and is able to realize a 30 per cent ROI in its home market but have no new expansion opportunities there. Imagine further that the firm can expand to a neighboring geography where it, because of its liability of foreignness, is able to realize a 20 per cent ROI. If

investors only require a 10 per cent ROI on the foreign investment, the firm will, rationally, choose to expand, creating an increased firm-value but reducing its ROI. This would explain a positive relationship from self-selection but cause a return towards average P for high levels of M.

Insert figure 1 about here

Considering that foreign expansion is generally seen as adding systematic risk (Reeb, Kwok, & Baek, 1998), multinational firms will arguably require a higher non-risk-adjusted ROI and will therefore have a neutral (or negative) risk-adjusted performance effect, as they move into riskier or less familiar markets. The same firms may simultaneously experience heightened non-adjusted ROIs. At what levels performance would increase or decrease would then be depending on, for instance, the size of home- and related markets (see discussion in Ruigrok & Wagner, 2003).

An important point here is that it is competitive advantage that is the source of gains in performance and economic rents. To better understand the M-P relationship it is therefore relevant to ask whether expansion causes changes to firms' competitive advantages, on an aggregate level. The literature review cast serious doubts on this. Multinationality does come with a number of side effects, such as learning opportunities, added complexity, changes in scale of production, necessary product adaptations, added country risk, first-mover effects, etc. For individual firms these may be decision-relevant but for the aggregate level, the argumentation and empirical findings have so far been unconvincing. The reason is that

multinationality in isolation cannot cause a competitive advantage unless there is a barrier to multinationality that discriminates among firms. A firm with a competitive advantage could be able to expand in a way its competitors cannot, because of a liability of foreignness, and, for example, realize scale economies from this. The source of those economies, however, is the competitive advantage, not the multinationality. On an aggregate level, this would cause a self-selection bias but not causality from multinationality to performance. Other strategic choices, such as high levels of R&D, can also cause increased multinationality (Dastidar, 2009) but must cause a competitive advantage to enhance performance. I believe that a shift in the M-P discussion to also include competitive advantage will be beneficial to future research as it may create more differentiated research questions that are more practice-relevant.

Suggestions for future research

Peng (2004) suggests that the question “what determines the international success and failure of firms” should be the guiding “big question” for international management research. This is well aligned with what appears as the most researched topics in international management research, namely antecedents, outcomes, and moderators of internationalization (Hitt, Tihanyi, Miller, & Connelly, 2006). Based on the emerging consensus around competitive advantage as the most important antecedent of multinationality, I predict that Peng’s research question will be complemented by a comeback of the process view in IM research (Johanson & Vahlne, 1977), focusing on the highly interesting questions of how to manage the internationalization process, including the questions *where to, how, when, and how fast* to expand abroad. It would, for example be highly interesting to relate the concept of competitive advantage to the process of international expansion through studying how the *nature* of different sources of competitive

advantages affect the expansion process. This could help answer questions such as into which markets a particular firm should expand, depending on the nature of its competitive advantage and where it will be easiest to transfer.

An example that has caught much attention recently is the speed of internationalization.

Vermeulen and Barkema (2002), for example, have shown that a high expansion speed negatively moderates the M-P relationship. The authors argue that this is caused by limits to firms' absorptive ability. Contradicting to this, Zahra (2005) discusses the phenomenon of 'international new ventures'. Such firms internationalize much more rapidly than expected from, for example, the Uppsala process model (Johanson & Vahlne, 1977). The literature on international new ventures explains this by a concept called 'learning advantages of newness', which essentially means that younger firms learn better and can therefore expand faster. A problem with this is that the empirics speak against learning effects of internationalization, as this article indicates. An alternative explanation, drawn from the view of competitive advantage as antecedent to multinationality, which is championed here, would be that international new ventures have less resources and capabilities in place to defend their competitive advantage and must therefore accelerate their expansion in order to circumvent other firms from copying their strategy in other markets.

The above discussion suggests that the durability of a competitive advantage would influence the speed of international expansion. It is easy to see other cases where the nature of a competitive advantage affects the internationalization process. Delios and Beamish (1999) found that R&D intensity is related to geographical scope with strong statistical significance but could

not find as strong statistical support for a general relationship between the possession of marketing assets and geographical scope. One explanation of this observation would be that technological sources of competitive advantage, like patents and unique designs, are easier to transfer across geographies than reputational assets. This would be aligned with the frequent findings of R&D intensity as a moderator of the M-P relationship and would fit well with the model presented above. Such research topics could provide insights that are highly relevant for individual firms and could become a valuable continuation of the M-P literature stream.

CONCLUSION

This paper argues that the traditional view of M leading to P does not hold. Empirically, the frequently observed positive correlation between M and P can be explained with a self-selection bias and specific causality tests show that it is P that leads to M and that there even are long-term negative effects from M. Just as important is that all major theoretical arguments for M leading to P have been rejected. This paper has argued that an emerging consensus view of competitive advantage as the primary antecedent to M offers an opportunity to reconcile the confusing findings of the past, which in turn opens up new and interesting research topics. If this paper helps breaking the deadlock between two contradictory views in international management research, it would surely make a valuable contribution. The paper is, however, limited by the fact that it uses a very diverse set of sources that uses a variety of definitions of the discussed constructs. As all theoretical papers of this kind, it also lacks explicit hypotheses and empirical support. On the other hand, the intention was never to propose new models and theories but rather to constructively try to help bring the M-P forward.

BIBLIOGRAPHY

- Bernard, A. B., & Jensen, J. B. (1999). Exceptional exporter performance: cause, effect, or both? *Journal of International Economics* , 47, 1–25.
- Bernard, A. B., & Jensen, J. B. (2004). Why some firms export. *Review of Economics and Statistics* , 86 (2), 561–569.
- Blalock, G., & Gertler, P. J. (2004). Learning from exporting revisited in a less developed setting. *Journal of Development Economics* , 75 (2), 397-416.
- Capar, N., & Kotabe, M. (2003). The relationship between international diversification and performance in service firms. *Journal of International Business Studies* , 34, 345-355.
- Castellani, D., & Zanfei, A. (2004). Cherry-picking and selfselection: Empirical evidence on ex-ante advantages of multinational firms in Italy. *Applied Economics Quarterly* , 50 (1), 5-20.
- Clerides, S. K., Lach, S., & Tybout, J. R. (1998). Is learning by exporting important? Micro-dynamic evidence from Colombia, Mexico, and Morocco. *Quarterly Journal of Economics* , 113 (3), 903-947.
- Click, R. W., & Harrison, P. (2000). *Does multinationality matter? Evidence of value destruction in US multinational corporations*. US Federal Reserve Board, FEDS Working Paper No. 2000-21.
- Contractor, F. J. (2007). Is international business good for companies? The evolutionary or multi-stage theory of internationalization vs. the transaction cost perspective. *Management International Review* , 47 (3), 453-475.
- Contractor, F. J., Kundu, K. S., & Hsu, C. (2003). A three-stage theory of international expansion: the link between multinationality and performance in the service sector. *Journal of International Business Studies* , 34, 5–18.
- Dastidar, P. (2009). International corporate diversification and performance: Does firm self-selection matter? *Journal of International Business Studies* , 40, 71–85.
- Delgado, M. A., Farinas, J. C., & Ruano, S. (2002). Firm productivity and export markets: a non-parametric approach. *Journal of international Economics* , 57, 397–422.
- Delios, A., & Beamish, P. W. (1999). Geographic scope, product diversification, and the corporate performance of Japanese firms. *Strategic Management Journal* , 20 (8), 711-727.
- Denis, D. J., Denis, D. K., & Yos, K. (2002). Global diversification, industrial diversification, and firm value. *Journal of Finance* , 67 (5), 1951-1979.

Doms, M. E., & Jensen, J. B. (1998). Comparing wages, skills, and productivity between domestically and foreign-owned manufacturing establishments in the United States. In R. E. Baldwin, R. E. Lipsey, & J. D. Richardson, *Geography and Ownership as Bases for Economic Accounting* (pp. 235–258). Chicago: University of Chicago Press.

Dunning, J. H. (2000). The eclectic paradigm as an envelope for economic and business theories of MNE activity. *International Business Review* , 9, 163–190.

Economist. (2008, December 30). *Emerging economists: International bright young things*. Retrieved May 12, 2009, from The Economist Web site:

http://www.economist.com/finance/displayStory.cfm?story_id=12851150

Fauver, L., Houston, J. F., & Naranjo, A. (2004). Cross-country evidence on the value of corporate industrial and international diversification. *Journal of Corporate Finance* , 10 (5), 729-752.

Globerman, S., Ries, J. C., & Vertinsky, I. (1994). The economic performance of foreign affiliates in Canada. *Canadian Journal of Economics* , 27 (1), 143-156.

Gomes, L., & Ramaswamy, K. (1999). An empirical examination of the form of the relationship between multinationality and performance. *Journal of International Business Studies* , 30 (1), 173-188.

Hennart, J. (2007). The theoretical rationale for a multinationality-performance relationship. *Management International Review* , 47 (3), 423 – 452.

Hitt, M. A., Hoskisson, R. E., & Kim, H. (1997). International diversification: Effects on innovation and firm performance. *Academy of Management Journal* , 40 (4), 767-796.

Hitt, M. A., Tihanyi, L., Miller, T., & Connelly, B. (2006). International diversification: Antecedents, outcomes, and moderators. *Journal of Management* , 32 (6), 831-867.

Howenstine, N. G., & Zeile, W. J. (1994). Characteristics of foreign-owned US manufacturing establishments. *Survey of Current Business* , 74, 34-59.

Johanson, J., & Vahlne, J.-E. (1977). The internationalization process of the firm—a model of knowledge development and increasing foreign market commitments. *Journal of International Business Studies* , 8 (1), 23-32.

Kogut, B., & Zander, U. (1993). Knowledge of the firm and the evolutionary theory of the multinational enterprise. *Journal of International Business Studies* , 24 (4), 625-645.

- Lu, J. W., & Beamish, P. W. (2004). International diversification and firm performance: The S-curve hypothesis. *Academy of Management Journal* , 47, 598-608.
- Melitz, M. J. (2003). The impact of trade on intra-industry reallocations and aggregate industry productivity. *Econometrica* , 71 (6), 1695-1725.
- Morck, R., & Yeung, B. (1991). Why investors value multinationality. *Journal of Business* , 64 (2), 165-187.
- Newbert, S. L. (2008). Value, rareness, competitive advantage, and performance: a conceptual-level empirical investigation of the resource-based view of the firm. *Strategic Management Journal* , 29, 745-768.
- Peng, M. W. (2004). Identifying the big question in international business research. *Journal of International Business Studies* , 35 (2), 99-108.
- Reeb, D. M., Kwok, C. C., & Baek, H. Y. (1998). Systematic Risk of the Multinational Corporation. *Journal of International Business Studies* , 29 (2), Systematic Risk of the Multinational Corporation.
- Riahi-Belkaoui, A. (1998). The effects of the degree of internationalization on firm performance. *International Business Review* , 7 (3), 315-321.
- Ruigrok, W., & Wagner, H. (2004). *Internationalization and firm performance: Meta-analytic review and future research directions*. Working Paper, University of St. Gallen.
- Ruigrok, W., & Wagner, H. (2003). Internationalization and performance: An organizational learning perspective. *Management International Review* , 43 (1), 63-83.
- Ruigrok, W., Amann, W., & Wagner, H. (2007). The internationalization-performance relationship at swiss firms: a test of the s-shape and extreme degrees of internationalization. *Management International Review* , 47 (3), 1 – 20.
- Shapiro, A. C. (1978). Financial structure and cost of capital in the multinational corporation. *Journal of Financial and Quantitative Analysis* , 13 (2), 211-226.
- Siegel, P. H., Omer, K., Rigsby, J. T., & Theerathorn, P. (1995). International Diversification: A Review and Analysis of Evidence. *Managerial Finance* , 21 (9), 50 - 77.
- Verbeke, A., Li, L., & Goerzen, A. (2009). Toward more effective research on the multinationality-performance relationship. *Management International Review* , 49, 149-162.

Vermeulen, F., & Barkema, H. (2002). Pace, rhythm, and scope: Process dependence in building a profitable multinational corporation. *Strategic Management Journal* , 23, 637–653.

Zaheer, S. (1995). Overcoming the liability of foreignness. *Academy of Management Journal* , 38 (2), 341-363.

Zahra, S. A. (2005). A theory of international new ventures: a decade of research. *Journal of International Business Studies* , 36, 20–28.

FIGURE 1

The interaction of competitive advantage, expansion, and performance