THE IMPACT OF INTERNATIONALIZATION ON CRISES RECOVERING: A preliminary study on the Portuguese banking sector

1. Introduction

Portuguese banks, like most of their counterparts through Europe, recently managed to overcome the financial crisis which has affected the world on the last two years. In fact, the extensive internationalization of the banking sector has intensified the emergence and diffusion of financial crises. Therefore, the question is not whether they will face another crisis; the coming of new crises in the future is definite. The crucial question is rather if the banks' management can confront and reduce the impact of emerging new crises. Learning from history and comparing the behaviour of different banks may provide us some hints that can aid in reducing the impact of the future crises. In this respect, there has recently been a lively debate going among researchers and in media about the world-wide financial crises and its varying impact on multinational banks´ (MNB) enterprises. Among recent studies, Arena (2007) relate the crises to external issues like government intervention; Connolly (2008) connects the bank crises to the risk taking of the firms while Laeven and Levine (2009) explain the impact as a result of the mismatch and failure of banks and governments. Common for the studies in this vein is an emphasis on the homogeneity of crisis' impacts on banks. The homogeneity in the view of the impact provides no insights into to the specific situations for different MNBs.

The purpose of this paper is, therefore, to study the varying vulnerability of international banks in crisis. Our starting point is that crises are mainly the consequence of radical environment changes. Radical changes in environment tend to turn obsolete the organizations' stock of knowledge. Therefore the process to overcome a crisis is, essentially, a process of learning the new environment changes, and, thus, the greater the learning capacity the faster the organizations can overcome crises. Our perspective supports that the learning processes which able firms to overcome crises are similar to those comprehended in the firm's internationalization process. The border line, we argue, is that crises foster new environments that must be learned by the established economic actors in a similar way of that needed by the firms to learn the new markets' specificities where they enter to.

Considering the above introductory paragraphs, we propose to study the intersection between the banks' different internationalization components and their capacity to overcome the crisis effects. The existing studies provide few answers to explain the different impacts on different MNBs. In fact, there are some valuable contributions to understand companies' internationalization and heterogeneity towards the choice of expansion strategies like alliances or to path-dependence (Johanson and Vahlne, 1977; 1992) in the setting of relatively stable market conditions. The often undisclosed side of these strategies, i.e., the connection between critical crisis and internationalization, has not attracted researchers yet (Van Heerde, et al., 2007). Therefore, the pertinence of this paper to International Business literature and, particularly, to the conference theme. i.e., the role of International Business in building a better and stronger global economy.

The next section of the paper is a brief review on earlier literature and precedes the hypothesis formulation section. Section four explains simply the procedure taken. The preliminary results are shown in section five. The last section closes the paper with the conclusions.

2 . Contributions on earlier research

After the 90s' financial crisis a vast number of research contributions have emerged in economic and business fields concerning the impact of the crisis on banks (Khaaoubi, 2007; Bae et al., 2002; Bello, 2006). Furusten, (2009) and Engwall, (1995) state in their studies of bank crisis that the main streams of the research are on economic, political or organizational factors while leaving the relationship between customers and banks under critical situations untreated. Also, the issues of how the market activities are related to the uncertainty or why the firms' crisis experiences vary are left untouched. The earlier contributions within the scope of this project can be divided into three streams; (1) macro-economic theories; (2) firm level behavioural theories and; (3) theories on bank service internationalization.

In the first stream, those employing macro-economic theories, a large number of studies concern the impact of the financial crises on banks. While some observe crises as a government and political issue (Svensson et al., 2006), others relate it to deficiencies in trade (see for example, Love et al., 2006, Canbas et al., 2004; Carmona, 2007) or issues like credit and liquidity (Khaaoubi, 2007; Petersen and Rajan, 1994) and inflation (Hua Jiang, 2008) or banks/business firms risk taking behaviour (Laeven and Levine, 2009).

The second stream focuses on firm level and elaborates behavioural views for different types of crisis (Engwall, 1995; 1997). Among the few studies that concern the firms' relationship in financial crises, Furusten, (2009) and Engwall, (1995) on banks' organizational change, Gandemo and Olofsson, (1994) on the change process in the bank-customer relationships, Hedelin, (1999) on the relationships between banks-business firms and depositors and Bae et al., (2002) and Gianetti (2003) aiming to elaborate relationship concepts to examine the value of relationships between different actors in 1990th critical condition, provide insights. However, bank researches, like Limpaphayon and Polwitoon, (2004) and Bae, et al, (2002) on the value of long-term relationships in critical conditions, do not have internationalization strategy under their scoop.

In the third stream, among those concerning bank service internationalization, some in the early years of 1970th, emphasize on economic theories and competitive advantages (Dunning, 1971), while others employ behavioural views (Engwall and Johanson, 1990). In the latter stream, researchers explain the differences between bank and industrial firms' internationalization by whether the strategic path-dependency is customer or provider driven (See also Engwall, 1992; Oviatt and McDougall, 1995). Other researchers, in contrast to path-dependence views, promote the notion of penetration strategies like joint ventures or strategic alliances (ul-Haq and

Howcroft, 2007; Lei and Slocum, 1992). These strategies are argued to be easier for bank services than industrial firms, due to the low level of resource commitment in the facilities (Engwall, 1995; Kathuria et al, 2008). However, both researchers advocating incremental investments and penetration by large investments emphasize on the cooperation with foreign partners to avoid uncertainty.

In these contributions the degrees of uncertainties associated with different types of strategies have not explicitly been within the scope of research. But, implicitly they elevate the crucial fact that banks are related to a heterogeneous number of actors which explicitly is called by Engwall and Johanson (1990) bank network of relationships. Within the context of bank business network, a group of researchers refer to incrementality in relationship development and uncertainty reduction. Moreover, Eriksson, et al., (2000) with emphasis on knowledge and path dependence, and Blomstermo, et al., (2002) on experiential knowledge, have the assumption that uncertainty is challenged by incremental bank strategies. Contrasting to the stable gradual strategic change in the network, some explicitly connect crises to internationalization strategies and develop notions on varieties in business network crises. With emphasis on heterogeneity in the crisis impacts they elevate views like deinternationalization and decommitment in business network relationship (Hadjikhani, 1996).

This paper follows the latter stream of research and experience a call for new conceptual tools and empirical study in line with the stipulation of Nilson (1995) and Engwall (1995) and Furusten (2009) on the need for further research on bank crisis. Studies on the firms' internationalization strategy behaviour before, during and after the crisis can open new doors to understand the behaviour of firms in international markets.

3. Hypothesis formulation

This research employs a learning view for its empirical study of Portuguese banks internationalization experience to overcome crisis. In another words, it is assumed that the banks' foreign market behaviour during and after the crisis is interlocked with their past behaviour before the crisis. Crisis is defined as a situation of distortion in some or all important relationships where actors involved are unable to cope by using normal routines (Booth, 1993). It can have its origin in some important relationships or may reach the focal relationships for their embeddedness in a context far away in the horizon of the network. In cases like the recent mammoth crises, as Milburn (1972) states, even those actors which have undertaken cautious attitude before the crisis, they also, become affected because of turbulence far from the firm. This is very true for international banking because of their extensive embeddedness in an international financial system. An unwelcome unexpected event can rapidly diffuses in the network and induce change in all relationships. But as Engwall (1995) and Hadjikhani (1996) declare, the impact is diversified and is not uniform. The crucial distinction of this project, compared to the earlier studies, lies in the ambition of adding new knowledge on the Swedish international banks' process of crisis management. It can provide further knowledge on path-dependency in the internationalization strategies of these banks. Moreover, it also can increase the understanding of the heterogeneity in the impacts of crisis and the management of it.

The relationships between banks and their foreign partners are presumed to be embedded in a network context containing relationships with not only business but also non-business counterparts. Bearing a process view, the path-dependence of their internationalization expresses that sudden grievous situations somewhere in the network diffuse in the network and change the relationship construction. Concerning the level and character of impact, the assumption is that every internationalization strategy is inhibited by specific relationship investments and accordingly also network context. The specificity of the network context means that the impact of crisis will be different for every bank and accordingly the type of crisis management. Still the impact of the crisis is not unique in every instance as the crisis causing the impact is common meaning strong possibilities of generating knowledge. On this perspective, the first hypothesis:

1) The more extensive the bank’s international operations the better the overall performance in overcoming a crisis.

Stability in change grounds the theoretical views of studies on international business network. No matter if the firms’ internationalization modes in the foreign market development follow the incremental knowledge and commitment or if the decision is to form joint-ventures or strategic alliances, uncertainty in foreign markets underlies the foreign market behaviour (Jay Hyuk and Cheng, 2002). The banks’ challenge of uncertainty is by some explained to be due to the incrementality of knowledge and by some others the result of the reliance on the obtained knowledge in the relationships with partners in the banks’ foreign markets (Eriksson, et al., 2000, Engwall and Wallenstål, 1988). In terms of network, firms’ knowledge and uncertainty in internationalization encompasses both relational, business connections and contextual factors.

In this construction the future dimension relies on the past and present and a sudden change in the relationships which leaps firms into the unknown (Hadjikhani and Johanson, 2001) is not under consideration (see also Engwall, 1995). But, empirical evidence from the crisis of the 1990-ties (Engwall, 1995; 1997; Euh and Ree, 2007) manifest that firms’ knowledge suddenly may become insufficient or even distorted meaning that the investments in building the knowledge disappears. During periods of stable change firms have invested in the relationship and obtained useful knowledge while in the following period of crisis, the very same knowledge suddenly becomes invalid and thus, it turns necessary to investments in relationships in order to know what to learn for. In this sense, long international experience is an enabler to the banks’ performance during the crisis period, thus:

2) The more the bank’s international experience the better the overall performance in overcoming a crisis.

4. The procedure

The research hypotheses posed aim to perceive if the internationalization enrolment matters to deal with the crises, and, secondarily, to verify if international crisis impacts differently for international banks. The model proposed is framed within three constructs: international experience, international degree and overall performance.

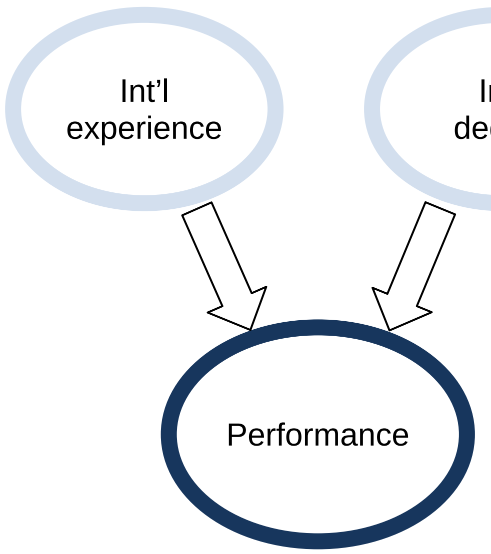


Figure 1

The international experience construct, as introduced by Young-Ybarra and Wiersema (1999), is characterized by the variables of number of years and number of countries of international presence. Relatively to the international degree, we opted to frame it under the Welch and Loustarinen's (1988) Model of the Dimensions of Internationalization and the incremental establishment of resources as illustrated by Johanson and Vahlne's (1977). Thus, to the international degree construct, we have considered the variables number of employees and number of front desk points, and international establishment modes as commercial protocols, representation offices, branches and local bank acquisition or "greenfield" investment. As for performance applied to banking sector, we intend to make a construct with five variables: total assets, banking product, credit to clients, clients' resources and profit. The performance values are the aggregated values for national and international activity, since the proposed objective of overall performance.

The present study is a working paper version; subsequently we will stay on the preliminary essay of two Portuguese banks: Banco Português de Investimento (BPI) and Banco Comercial Português (BCP). In this preliminary essay the idea is to design graphically the results with some of the above indentified variables. The initial data collected is primarily based on secondary data in form of annual reports. The further steps will consist in gathering all the secondary data available to assure all constructs variables, namely some complementary documents from the banks and media. Additionally, primary data such as interviews to banks managers are meant to be made in order to cross and accurate the secondary data collected. On the final version we intend to cover all the Portuguese banks and store it in a database allowing for various analyses, i.e. descriptive, factorial and relational/causal using both univariate and multivariate statistical techniques.

Within this context and study phase, we have constructed a longitudinal data series from 2000 to 2010(estimate) in order to perceive the stable period, the crisis' effect and the recover starting point and amplitude. The procedure will consist in the comparison of the linear regression of the respective performance variables' values available through the periods from 2000 to 2007 and 2008 to 2010. The sensing variables used are the assets and profit for performance and the number of employees and front desks for international degree.

5. Preliminary Results

The banks in focus are rather similar in what concerns the international experience's construct. BPI was founded on 1981 and started its internationalization process on 1996, while BCP initiated its activities on 1985 and proceeded to internationalization on 1995. Nowadays, BPI's international operations are settled in 12 countries. As for BCP, its activities are now covering 17 countries.

Relatively to the international degree, we have gathered an eleven year data series on number of employees and number of front desk offices, nationally and internationally. The differences are evident. Considering the aggregated activity, national and international, BPI foreign operations are lower than those on BCP. If we take the last year values, BPI's foreign employees only represent 14% of total, while foreign employees do not exceed 22% of total front desks offices (see figures 2 and 3).

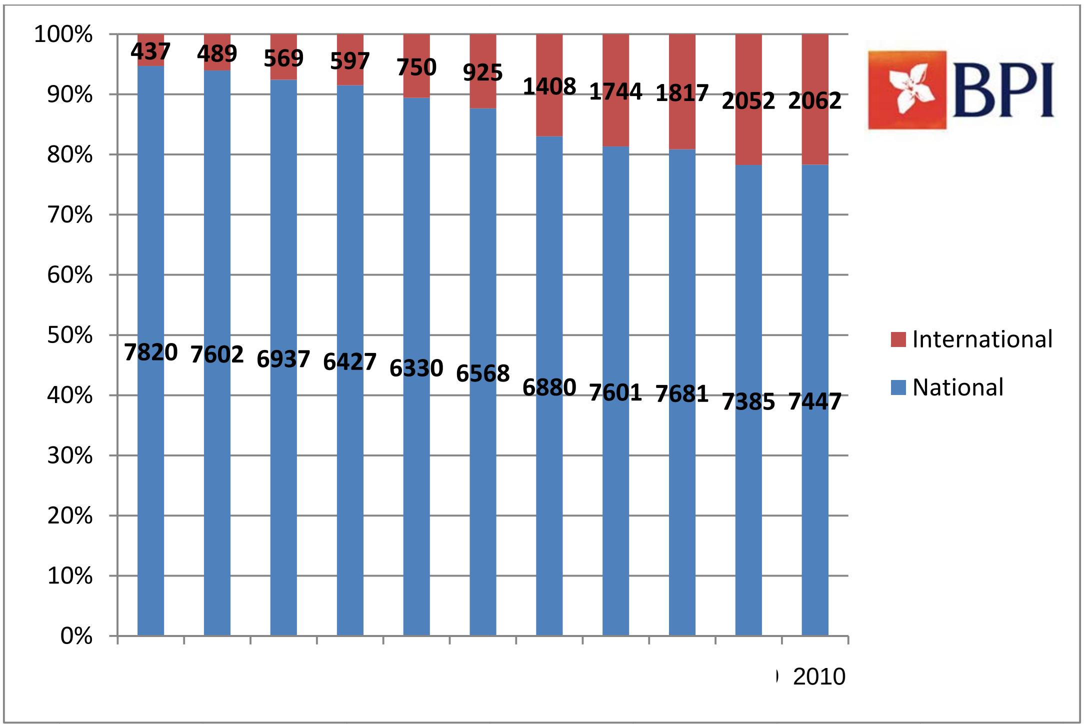


Figure 2

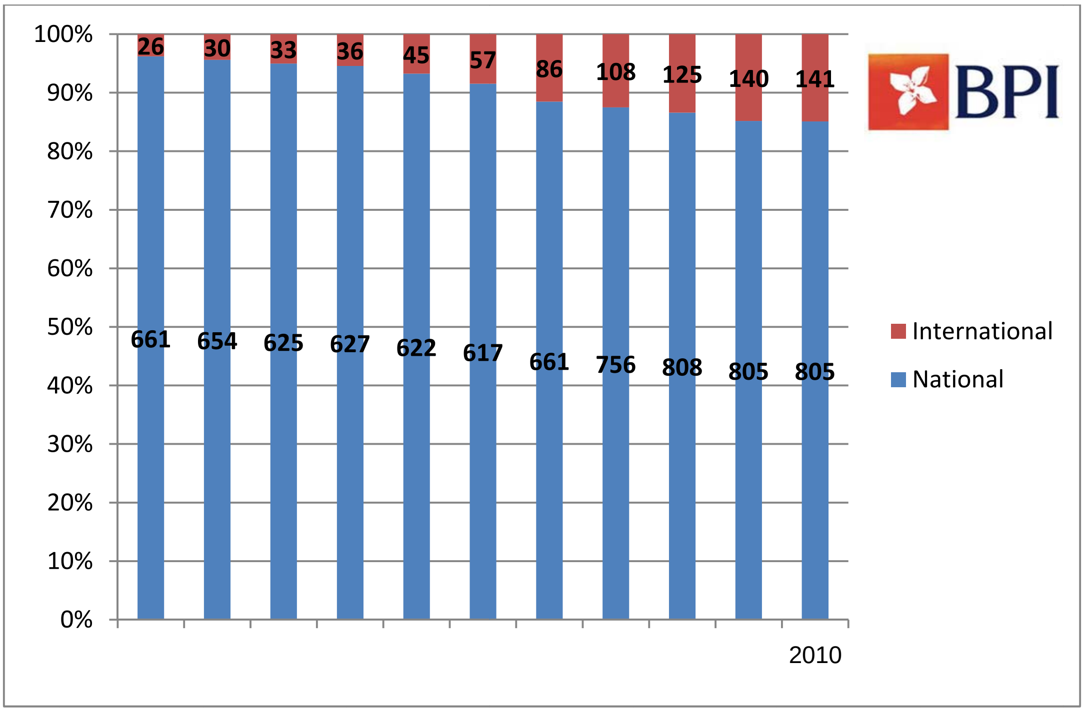


Figure 3

Comparatively, BCP has reached a higher internationalization degree. The number of foreign employees is just a few less compared to total; and foreign offices surpass slightly the total aggregated numbers (see figures 4 and 5).

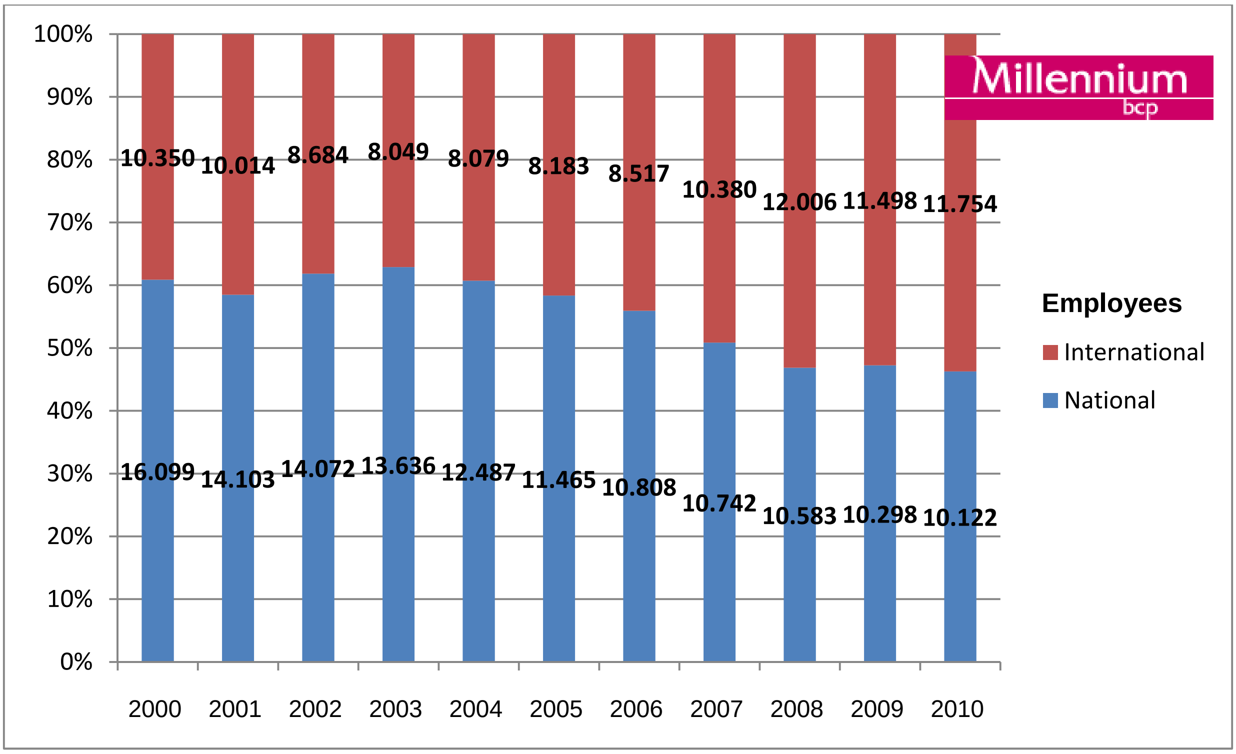


Figure 4

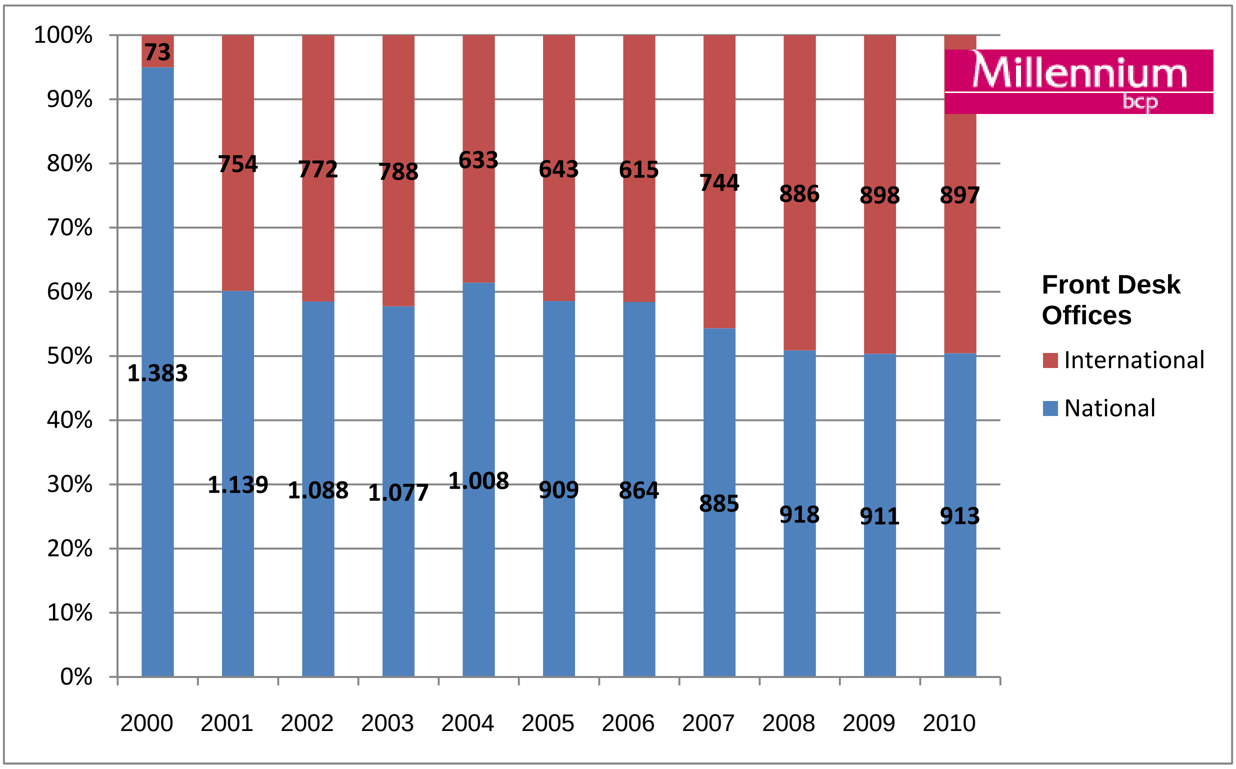
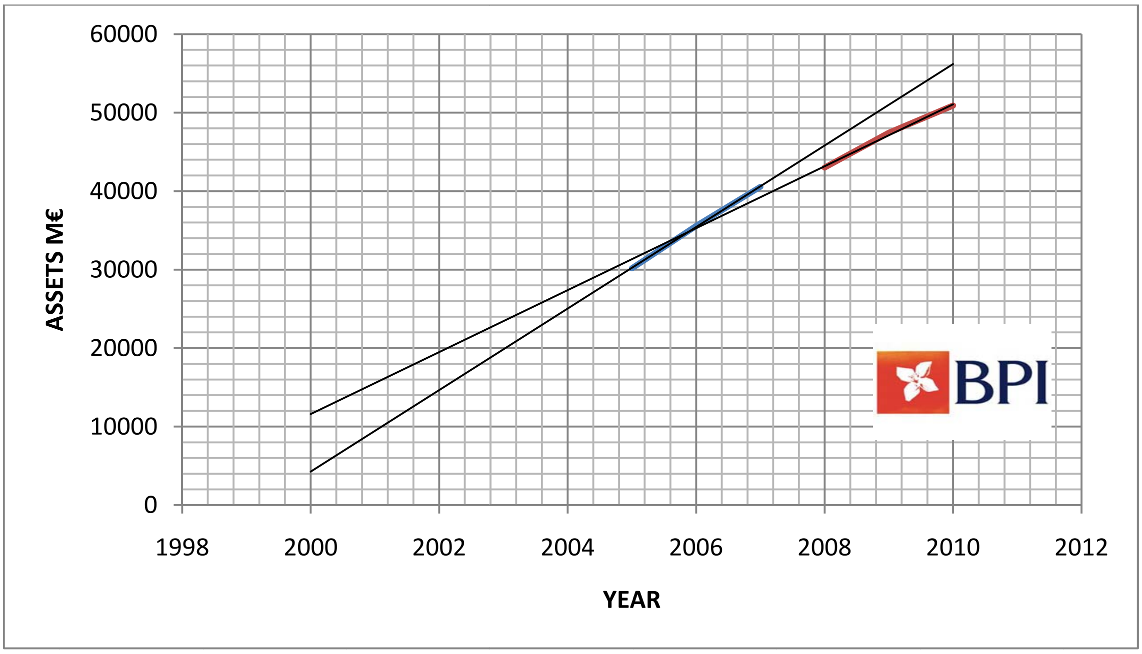


Figure 5

Within such a difference on the internationalization degree variables, it is expected that BCP, which international activities are approximately half of the global activities,tol have better performance to overpass the crisis effects. As drawn in the hypothesis, as deeper the internationalization process the more exposed to learning process the banks are, and, thus, more able they will be in overcoming crises.

In fact, our preliminary results give some hints which prospect the hypotheses confirmation in further studies. The linear regression of the assets and profit evolution in the two periods of the time series manifests a better crisis recovering behaviour of BCP towards BPI (see figures 6, 7, 8 and 9)



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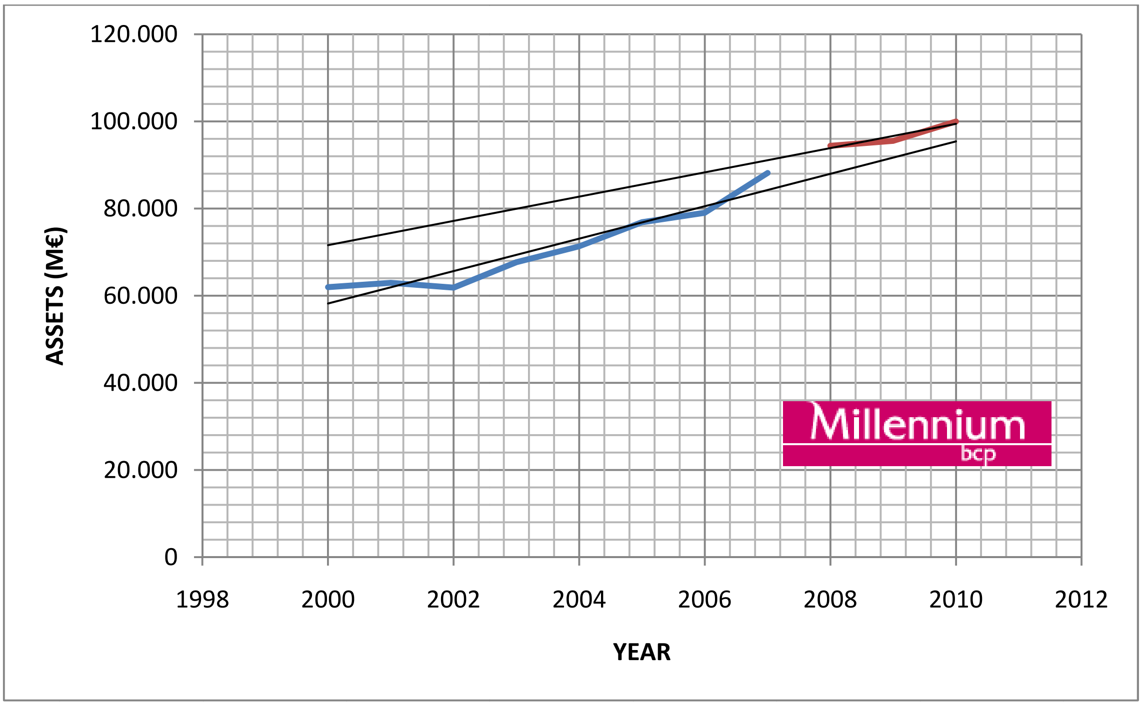
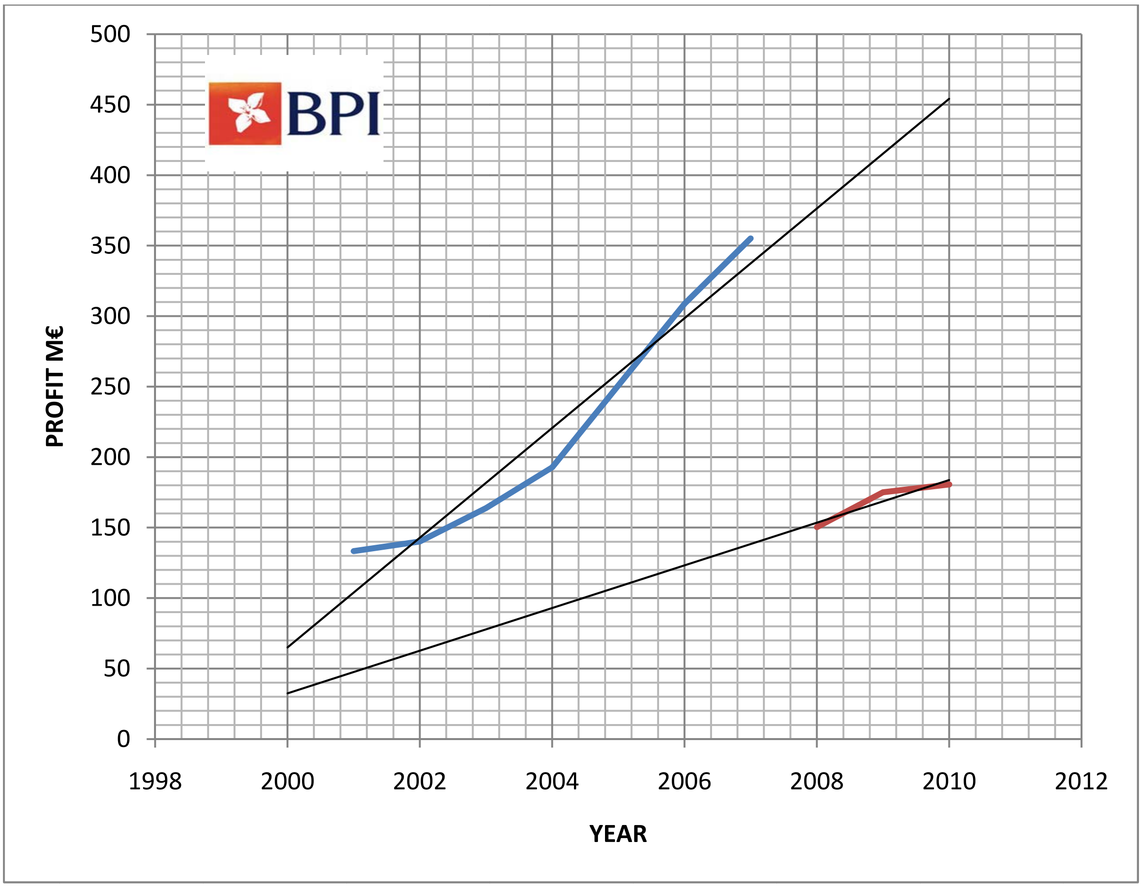


Figure 7

In both banks, the assets evolution rate during the crisis period is tendentially lower than the previously achieved. Nevertheless, in the BCP's case the regression lines' tendency is not so different than the BPI ones. As for the profits regression analysis, it leaves no doubts about the better performance of BCP in comparison with BPI.



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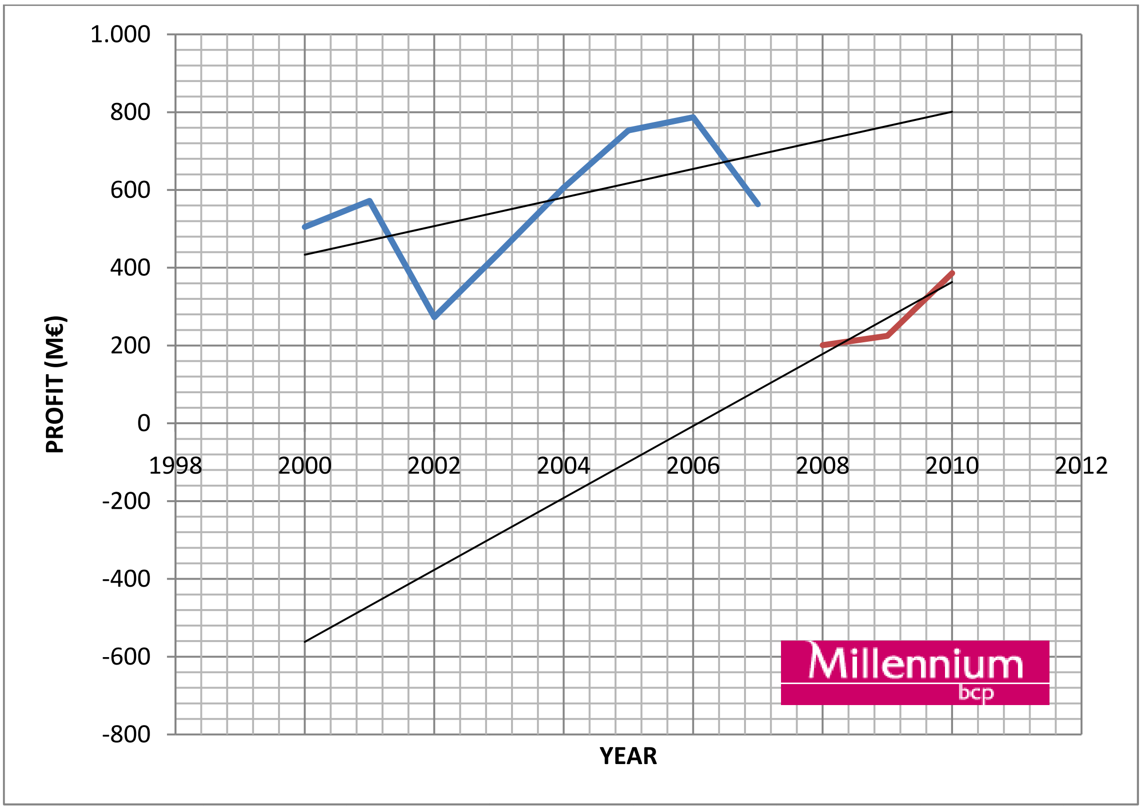

Figure 9

The figures show that BCP has better recovered from the crisis. Although the deep decrease on profits registered in both banks during the 2008/2010 period, the linear regression prospects that BCP will achieve faster the profits it used to before the crisis. As for BPI, the divergence between the two lines shows a poorer recovery of global profits.

6. Conclusions

This working paper was planned to find preliminary support for further research on the potential role of IB in the actual crisis context. The paper supports on the idea that the firm's internationalization path influences the firm's ability to deal with radical changes. The rationale is based on the learning processes that occur during the firm's internationalization. This underlying principle applied to the banking sector – where crisis effects were firstly issued – proposes that as more internationalized banks are the better prepared they will be to overcome crisis effects. In fact, internationalization exposes banks to different business settings that must be learned such as the radical changes during crisis periods. Thus, internationalization increases the learning ability for banks to handle the crisis impact.

The vulnerability of banks in terms of the impact degree from crisis was analysed by the imbalance in the development of three interdependent elements; internationalization experience, internationalization degree, and performance. The preliminary results have supported the first rationale and showed that banks with higher internationalization degree are, so far, achieving a better performance in overcoming the crisis effects.

With further developments of this working paper, we can hopefully provide a new awareness of the international banks' vulnerability through different strategies and furthermore how international banks can manage and develop crisis strategies holding higher tolerance towards critical situations. Bank crisis harming a few specific banks or massive crises like in the 1990-ties and in the last years will always occur and challenge the bank system. Therefore, the contribution of this study to improve the knowledge about the impacts of internationalization on organizations and to conscious managers for the benefits of internationalization learning processes, namely in their importance to overcome crises periods such as the world is passing through.

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