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Exploitation versus exploration in multinational firms: Implications for the future of international business

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ABSTRACT

Given the economic weight of multinational corporations and their privileged access to resources, many different scenarios can be built about the future of international business and about the future impact of international business on economic, technological, and social development. In this paper, we argue that multinationals do not form a uniform organisational population, and we provide empirical evidence of the existence of traditional, rigid entities seeking benefits from low-risk exploitative strategies on one hand, and of flexible multinationals seeking higher performance levels by balancing the trade-offs between exploration and exploitation on the other hand. As these two sub-populations compete with one another for resources, we use a population ecology perspective to study likely ecological scenarios for the future. Our conclusion is that traditional multinationals tend to prevail over flexible multinationals, and the conditions required for a future society to allow a genuine growth of flexible multinationals are unlikely. This implies that multinationals remain primarily exploitative, and that as such, they will only be associated with marginal economic, technological, and social developments in the future. Other organisational forms, such as entrepreneurial small business and communities of practices are shown to be much more likely vehicles through which society can progress and innovate.

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1. Introduction

The multinational corporation (MNC) and models of MNCs [1] have always been central concepts in international business theory. Thus, when investigating the future of international business, one direction for reflection is the future forms of MNCs and their future economic roles.

Back in the 1980s, in parallel with the business literature on globalisation, international business theory was promising radical change and the emergence of highly competitive and resilient large scale businesses. Multinational corporations (MNCs) were said to be more flexible [1], benefiting from unique economies of scale, economies of scope, learning and real options opportunities [2], and having access to more sources of (cheaper) funds from international markets [3]. The predictions from these theories of “*multinational advantage*” is that MNCs should be naturally more competitive than domestic firms, and that they should dominate the realm of economic activities through the management of their knowledge reserves, flexibility platforms, and portfolio of real options. Such superiority should naturally be reflected in the MNCs overall value and corporate performance. There is a significant empirical literature in international business research investigating this proposition and the relationship between multinationality and performance, but it reports inconsistent and

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controversial results [4,5]. Most of this research, however, investigates a population of MNCs assumed to be uniform. If this assumption is relaxed, then the theory of multinational advantage would only hold:

- (1) if MNCs really seek, rather than avoid, strategic flexibility; and
- (2) if flexible MNCs can remain competitive when compared with MNCs using alternative strategies.

The specifications of the flexible MNC [1,2] match those of an explorative firm, as described by March [6]. March describes exploration as being associated with activities such as “*search, variation, risk taking, experimentation, play, flexibility, discovery, and innovation*”. Exploitation is associated with activities such as “*refinement, choice, production, efficiency, selection, implementation, execution*” [6]. March demonstrates the existence of a delicate trade-off between exploration and exploitation. He also shows that because adaptive processes refine exploitation more rapidly than innovation, organisations naturally tend to exploit rather than explore. As a result, organisations become very effective in the short-run but do so at the cost of compromising or “self-destructing” long run economic prospects. Conversely, a firm investing solely in exploration processes operates at such a level of risk that it would be difficult for it to secure enough short-term returns to fund long-term growth.

Therefore, if several types of MNCs compete with one another through different strategies, the rather ambivalent nature of the relationship between multinational flexibility and performance in MNCs can be revisited in a different light. Specifically, some firms will tend to forego valuable exploration opportunities (e.g. learning and real options) for exploitation activities. For example, these MNCs could seek growth by replicating their existing business models over a broader portfolio of markets, in what could be described as a “copy and paste” approach to strategy. At the other end of the spectrum, one would find MNCs systematically investing in flexibility and seeking an optimal trade-off between exploration and exploitation. In this work, we assume that managers’ propensity to detect and appraise real options as resources and tools for flexibility management in MNCs is one way of differentiating flexible MNCs from traditional ones in the current international business landscape (consistently with [1,2,9]). We argue that to appreciate the future of the international business landscape, one needs to investigate the validity of theories of multinational advantage. Thus our main research question is: Is the flexible multinational a reality or a theoretical fiction? In other words, does the flexible multinational, once the hot topic of international business research, have a future? Is it able to recognise, explore, and exploit its (flexible) real options platforms? For example, Reuer and Leiblein [7] and Tong and Reuer [8] empirical findings, both focusing on real options as determinants of performance in MNCs, are that multinationality and international joint-ventures as flexibility options do not necessarily equate with a lower exposure to risk or higher performance.

This paper is organised as follows. In Section 2, we use empirical data to investigate whether or not all MNCs are identical when it comes to flexibility. Our findings confirm the existence of two distinct sub-populations: traditional (non-flexible) MNCs and flexible MNCs. Having established the existence of two competing species of MNCs, we turn to the question of their likely co-existence, in the present and the future. Section 3 discusses our futures methodologies and our choice of a population ecology framework to assess the survival likelihood of both species on the basis of their ability to compete for resources. Section 4 discusses the application of this framework in the case where traditional and flexible multinationals are competing with one another. Section 5 extends this analysis by enlarging the set of species with small and medium enterprises (SMEs) and communities of practice (COP). Section 6 concludes the paper by discussing implications for the future of international business and its role in society.

2. Multinational advantage: an empirical investigation

2.1. Background

The pioneering theory of Kogut’s [2] multinational advantage has been reinforced with a steady stream of conceptual, normative, and axiomatic research studies about the specific paradigm of real options and its implications for flexible MNCs [1,9–11]. Most converge toward a model of the multinational enterprise as a rich portfolio of capabilities, which can be updated, adapted, and deployed as opportunities arise.

The literature, however, is much thinner when it comes to empirical evidence to validate this view. When one would expect a steady empirical counterpart of research studies setting themselves to test the mediating role of flexibility between multinationality and performance, only a few papers directly address this issue [7,8,12,13]. In Reuer and Leiblein’s [7] empirical study for example, results indicate that contrarily to the authors’ expectations, multinationality as a platform for real options is not associated with reduced organisational downside risk, thereby partly refuting the theory of the flexibility advantages of multinationals. To confound these negative findings, the literature on real options now includes a stream of critical research positions [14–16]. It is within this ongoing debate that this section inscribes itself. It empirically contributes to the study of the link between real options thinking, multinationality, and performance as a way of validating whether or not all MNCs are identical when it comes to flexibility.

2.2. Research framework

Fig. 1 provides a comparative display of the first research objective of this paper in the context of the multinationality–flexibility–performance debate discussed above. It highlights the distinction between the existence of opportunities

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