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Transaction cost determinants and advantage transferability's effect on international ownership strategy☆

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ABSTRACT

This research examines the complementary effect of transaction cost perspective and resource-based view on multinational enterprises' (MNEs) ownership strategies. Advantages may be location bounded, making certain advantages transferable and others non-transferable. Drawing on the concept of transferability of advantage, this study examines the advantage's location-boundedness and the effect of transaction cost on MNEs' ownership strategy. The empirical analysis combines survey data and secondary data from annual reports. The use of multiple sources avoids common method biases. Regression results show that both transaction cost perspective and location-boundedness of advantage greatly affect international ownership strategy. This study contributes to the literature by further examining this effect, thus allowing a better understanding of a firm's advantage. Firms can apply the findings to design an ownership strategy that considers both efficient and benefit lenses, fostering successful foreign investment.

1. Introduction

Entry mode plays a major role in MNEs' international expansion (Stopford & Wells, 1972). Transaction cost perspective has a lasting sustainable influence on foreign ownership with low transaction costs. Nevertheless, results vary depending on data sources (Pak & Park, 2004), and previous findings reveal not decisive of the transaction cost variables and ownership strategy (Anderson & Coughlan, 1987; Delios & Beamish, 1999; Erramilli & Rao, 1993; Hennart, 1991; Kim & Hwang, 1992; Osborn & Baughn, 1990). The transaction cost perspective focuses on efficiency and cost, and ignores value; therefore, this perspective cannot yield the optimal result (Ghoshal & Moran, 1996; Zajac & Olsen, 1993). MNEs' international ownership strategy obeys to multiple factors that a single theory cannot explain (Calvet, 1981), but different perspectives can provide explanations. This study, therefore, incorporates different theoretical perspectives to explain international ownership strategy.

Transaction cost perspective focuses on efficiency and cost and ignores other factors (Oliver, 1997). Resource-based view acknowledges the existence of MNEs not only on the minimum cost, but also on possession of advantage and value creation process. Those two perspectives explain MNEs' existence and are the major theoretical foundations of the international entry strategies (Anderson & Gatignon, 1986; Delios & Beamish, 1999). Transaction cost perspective focuses on cost. The resource-based view focuses on benefit. Both views are complementary. Scholars should consider both theories in international entry strategies (Tsang, 2000). Therefore, this study examines these two complementary perspectives' effect on the determinants of international ownership strategy.

Monopoly advantage theory proposes that MNEs that own monopolistic advantages can effectively conduct foreign direct investments (Kindleberger, 1969; Lall & Siddharthan, 1982). Conceptual models assume that ownership-specific advantages develop at firms' headquarters and then transfer to a network of foreign subsidiaries (Birkinshaw & Hood, 1998; Dunning, 1981; Vernon, 1966). Reports show that MNEs' degree of success in advantage transfer varies (Lo & Lin, 2015). In extreme cases, firms that are successful in their home country may face substantial problems and ultimately fail in foreign investments. Results of the analysis suggest that some firms lack the capability to transfer advantages to a host country or cannot capitalize effectively on such advantages outside the home market. Theoretically, subsidiaries can use headquarter resources to facilitate transferring advantages abroad (Martin & Salomon, 2003). Nevertheless, MNEs can transfer some advantages from parent firm to subsidiaries, but location-bounded advantages present difficulties and are not easy to transfer across borders (Rugman & Verbeke, 1992; Verbeke, 2013). The resource-based view may lack important perspectives to explain internationalization when a firm faces substantial barriers to advantage transfer.

Since transaction cost and resource-based perspectives, with their differing but complementary focus, provide sound explanations for the existence of MNEs, the two theories together serve as a basis to

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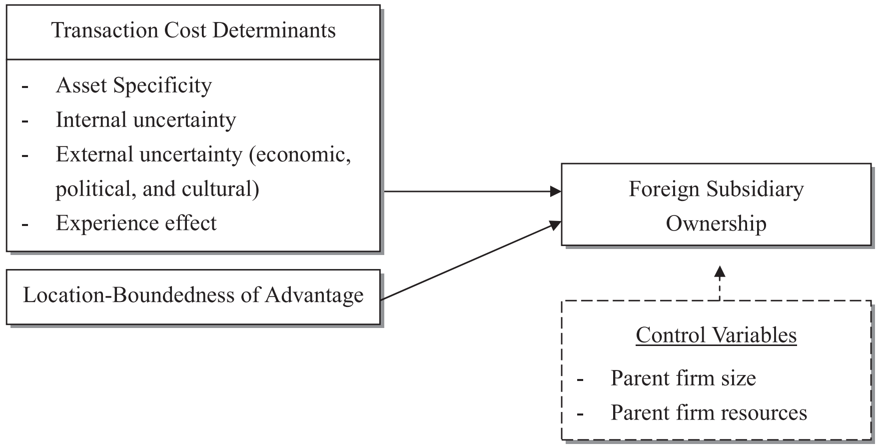

Fig. 1. Conceptual model.

explain MNEs' choice of ownership strategy. The structure of the study is as follows. Section 2: literature review and hypotheses; Section 3: research design, method, and findings; and Section 4: conclusion.

2. Literature review and hypotheses

The transaction cost perspective suggests choosing the modes with the lowest cost to enter foreign markets (Lu, 2002). According to the literature, factors on evaluating transaction costs of entering foreign markets include asset specificity, complementary assets, factor market inefficiency, and uncertainty of the transaction (Anderson & Gatignon, 1986; Delios & Beamish, 1999; Lu, 2002; Tsang, 2000; Williamson, 1975, 1991). Williamson (1991) proposes that the most important factors that affect transaction costs are specificity, complementary, and frequency. Williamson (1991) proposes the concept of comparative dynamic analysis and calls for the incorporation of the external institutional environment in the future. This study draws on Williamson's (1991) viewpoint, and proposes the following hypotheses about transaction cost perspective.

2.1. Asset specificity

Asset specificity is an important core concept in transaction cost perspective (Delios & Beamish, 1999). According to transaction cost perspective, investment on specific assets over this transaction supposes a higher interdependence of the two parties, while the hierarchy mechanism allows maintaining the value of the specific asset (Williamson, 1991) and avoiding the risk of one transaction partner holding up the other (Anderson & Gatignon, 1986). High asset specificity also increases the difficulty of arm's length market transactions and the incentive of internalizing this activity (Hennart, 1991; Williamson, 1975), that is, to conduct a wholly-owned foreign subsidiary in the foreign investment (Caves, 1996). When MNEs entry a foreign market with high asset specificity, MNEs tend to use high ownership entry strategy.

H1. Asset specificity positively affects MNEs' international ownership.

2.2. Internal uncertainty

Uncertainty highly increases the transaction cost (Williamson, 1979). Anderson and Gatignon (1986) classify uncertainty as internal uncertainty or external uncertainty when examining the transaction cost variables and international entry strategy. This study also incorporates this classification because internal uncertainty captures the industry effect, and external uncertainty captures the host country environment.

Internal uncertainty comes from MNEs' industry. Industries with more structural changes create uncertainty within the industry's structure (Luo, 2003), thus increasing MNEs' internal uncertainty. Facing an ever-changing industry, firms need to be flexible and avoid ownership involvement to transfer the risk to other parties (Anderson & Gatignon, 1986). By sharing ownership with a joint venture partner, MNEs can share investment risk and get more information about the industry. Industry structure uncertainty also increases the risk of resource commitment (Luo, 2003); therefore, MNEs tend to invest with a lower ownership entry strategy.

H2. Internal uncertainty negatively affects MNEs' international ownership.

2.3. External uncertainty

External uncertainty is the unpredictable factors of the external environment for new entrants (Anderson & Gatignon, 1986). Williamson (1991) suggests increasing the external institutional environment in transaction cost considerations. MNEs' environment highly affects MNEs' strategy (Geringer, Tallman, & Olsen, 2000), and so, MNEs need to find more flexible resource allocation to respond to the external environment (Buckley & Casson, 1998). In MNEs' decisions, the host country is a relevant factor (Buckley & Casson, 1998). The institutional perspective suggests that the institutional environment perspective can examine the host country factor (Kwok & Reeb, 2000). If the institutional environments in the host and home country are similar, MNEs can understand and adapt to the local environment. Therefore, under low external uncertainty, MNEs tend to invest in high international ownership. A large difference in institutional environments increases external uncertainty. Hence, the difficulty and risk of the foreign investment rises (Brouthers, 2002). Therefore, MNEs seek other firms to co-invest, and thus lower the entry barrier and risk.

H3. External uncertainty negatively affects MNEs' international ownership.

2.4. Experience effect

Williamson (1979) mentions that the transaction frequency affects the governance structure. Regarding foreign investment, the effect of transaction frequency on the entry strategy depends on the MNE's international experience (Hennart, 1991; Pak & Park, 2004; Penner-Hahn, 1998). MNEs unfamiliar with foreign investment face the liabilities of foreignness (Hymer, 1976). After some time, MNEs gain experience that allows them to lower the investment cost (Johanson & Vahlne,