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MINIMISING INVESTMENT AND POLITICAL RISK IN CHOICE OF MARKET ENTRY STRATEGY BY MULTI-NATIONAL CORPORATION

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ABSTRACT: ***The study examined how the Multi-national corporations use their choice of market entry strategies to minimize investment and political risk in foreign operations. The study was based on extant literature which involved content analysis. The international market entry strategy is regarded as an established agreement that makes possible the entry of a multinational company's products and other resources into a foreign economy; risks involved evaluated before the decision procedure. MNCs take appropriate decisions for minimizing investment and political risks favouring internationalization involving a gradual increase in international involvement. In the course of the work, market entry strategies of MNCs (e.g, BP into Nigeria, Belco corporation into Peru, Enron into India, Occidental petroleum corporation into Peru, Huawei Technology Corporation into USA) were analysed. A hypothetical case of Marks and Spencer proposing to enter Nigeria was examined. It is recommended that appropriate mode of entry into Nigeria is franchise for reasons in order to avoid risks; such strategy of entry being not equity-based.***

Key words: MNCs, Market entry strategies, Investment

INTRODUCTION

Multinational corporations (MNCs) are the firms that operate in many economies thus operating in multiple-country markets arising from international growth and development, which creates values for firms with unique technological, marketing and managerial capabilities. (Martin & Salomon 2003) MNCs' entry in foreign markets is usually regarded as foreign direct investment in host countries because such entry into foreign markets by MNCs involves long-term inflow of capital by intangible assets (technological knowledge) for investment and operations. (Ito & Fukao, 2005)

The purpose of pursuing foreign investments by MNCs can also be precipitated by factors such as domestic currency increase, protectionism, higher labour costs, protracted domestic growth, and the need to acquire resources (particularly raw materials), alongside with the quest for entry into foreign markets. (Ghahroudi & Hoshino 2007)

The entry into foreign markets through investments by MNCs is not devoid of risks among which are political and investment risks. In this discourse, the proposal by Mark and Spencer, a clothing company in UK, to enter into Nigerian market, will be researched into, as a case study, in order to offer advice on suitable mode of entry that will help the company to minimise such risks. The purpose of this study is to investigate minimization of investment and political risk in choice of market entry strategy by MNCs.

LITERATURE REVIEW

Political and Investment Risk of MNCs' Operations

Political problems include: nationalization of the British Petroleum (BP) investment by government in Nigeria in 1975; problems faced by Belco Petroleum Corporation in Peru in the 1980s; that of Enron Corporation in India in the 1990s. The Nigerian case was caused by a change in military regime, emergence of a new ruling party resulted in a new government in Peru that embraced anti-foreign investment attitude that differed significantly from that of the previous government, and in the case of Enron in India, a regional government adopted policy that differs from public interest (Bradley, 1997; Mawanza, 2015). Wagner (2000), cited in Mawanza, 2015), explains that political risk can be explained in relation to distinct government policy that constitute a threat to the investment of MNCs; firm and country specific. Firm specific political risks arising from discriminatory policies directed at a particular organisation.

In essence, firm specific risks arising from government factors are discriminatory directives, expropriation, and breach of contract while country level risks arising from government operations include mass nationalizations, regulatory changes, and currency inconvertibility. Firm specific risks arising from political instability include Sabotage, kidnappings, and firm-specific boycotts while country level risks arising from political instability include mass labour strikes unrest, urban rioting, and civil wars (Mawanza, 2015; Meleka, 2012; Stover, 1985; Beamish, 1987; Henisz, 2003; Arrey, 2013).

In line with the practice of domestic companies, foreign MNCs must also learn about the political and interest groups of countries in which they invest on individual, organisational, and institutional levels (Harrison & Elaydi, 2014). Those firms (MNCs) that have learned and internalized the static and dynamic ability to effectively scan their external environment will achieve competitive advantage and mitigate political uncertainty when integrated with decision making processes and put into action accordingly (Prebel et al., 1988). Nevertheless, most multinational corporations (MNCs) do not adequately indulge in these practices, which tend to increase the political and investment risks inherent in their operations in the host countries (Keegan, 2009).

Minimising Investment and Political Risks through Choice of Market Entry Strategy by Multinational Corporations

The international market entry strategy is regarded as an established agreement that makes possible the entry of a multinational company's products, technology, human skills, management, and other resources into a foreign economy. This process revolves round combination of risks which are evaluated ahead of the decision procedure (Polesello, Amal & Hoeltgebaum, 2013). The choice of entry strategy by multinational corporations plays a significant role in determining the success or failure recorded by a firm and effects all the future decision and operations of the firm in the new marketplace (Reger, Duhaime & Stimper, 1992).

A firm's decision, management of limited resources mode of entry into selected market translate into company's loss, profit making or sustainable growth (Yung-Ming, 2006). Firms intending to enlarge their international market space have several entry options, which have been espoused on in the earlier part of this write-up; exporting, licensing/franchising, joint ventures and wholly owned subsidiaries such as acquisitions and green field investments. Each of these modes entails different levels of resource requirements, organizational control, expected future returns and risk exposure (Mujtaba & Martina, 2011; Murray, Ju & Gao, 2012; Durmaz & Taşdemir, 2014) Tracing the development of an extensive global corporation today reveals a recurring, sequential pattern of expansion. This pattern of expansion in relation to internationalization involves several steps. Understanding the international marketing environment, particularly the international trade system is the initial step in internationalisation process. This is followed by company's consideration of what proportion of foreign to total sales to seek, whether to do business in a few or many countries and what types of countries to enter (Wu & Zhao, 2007).

Another step of internationalization involves deciding on which specific markets to enter and this calls for assessing the probable rate of return on investment against the level of risk in relation to market differences. Consequently, the company has to decide on how to enter each attractive market (Aulakh, Tamer & Sarkar, 1998). The stage of deciding on how to enter into target market, which involves the entry mode, is a frontier issue which is one of the most critical decisions in international marketing. (Sarkar & Cavusgil, 1996). Many companies start on the basis of indirect or direct export of goods produced form its own country or another country and then move to licensing, joint-venture and finally direct investment. Hence this company evolution has been regarded as the internationalization process (Aulakh, Tamer & Sarkar, 1998).

Analysis of Modes of entry by some MNCs towards minimizing political and investment risks in host countries

Some multinational corporations and the nature of the political and investment risks that confronted them in their host countries and the market entries strategies adopted towards minimising political and investment risks are analysed below.

British Petroleum (BP) entered into Nigeria through Joint Venture with Shell and Nigerian government but in 1979, the Nigerian Government nationalised BP's investment in the country by acquiring the investment of the multinational in the joint venture. Reason: government of UK's planned resumption of oil supplies to then Apartheid South Africa. BP divested and left to reduce risks in Nigeria, thus selling all of its concessions to Shell Petroleum Development Company (Genova, 2010). The company (BP) would have *leased the concessions* (investment) to Shell Petroleum Development Company for rental payments from the latter instead of total divestment from Nigeria.

Belco Petroleum Corporation (U.S.) entered Peru through Greenfield investment in offshore oil exploration and production in 1959. In 1985, it suffered political risk when Peruvian Government nationalized the company, froze its bank accounts and took control of its local assets because the firm refused to accept new condition, enacted by a new government then, for reinvesting its profits on new exploration and production. The government said the oil company did not invest enough of their profits in oil exploration, in spite of the given incentives to do so through tax breaks. The company refused to negotiate but left the country (Bradley, 1997; Gellene, 1985; Mawanza, 2015). Belco should have used *Joint venture* (JV), by way of investing its operating assets in another oil company through leasing, to cope with the unfavourable government action in Peru.

Occidental Petroleum Corporation (U.S.) entered into Peru through Greenfield investment in oil exploration and production. However, in 1985 Peruvian Government threatened to nationalise the company, seize it producing properties, freeze its bank accounts and take control of its local operations, for not investing enough of its profits in oil offshore exploration despite incentives to do so through tax breaks. The company negotiated and agreed to invest of its profit on oil exploration (Gellene, 1985). The company's agreement to hunt for oil in a new location within the southern part of Peru, in order to fulfill the Peruvian government's demand for new investment was an appropriate strategy for survival. The new investment went a long way to compliment the firm's existing investment.

Huawei Technologies (China) planned to enter U.S. via acquisition of server technology firm but in 2011 the US government blocked the deal on national security grounds; released warning on Huawei in 2011 accusing the firm of spying on behalf of the Chinese government because of Huawei CEO, Ren Zhengfei's past association with the People's Liberation Army. The action of The House was corroborated by U.S. Congress in 2012 who publicised a report warning U.S. companies that they could jeopardize American security by working with China-based Huawei and issue of intellectual property theft, consumers' privacy issue, and the firm's close relationship with the Chinese government. Huawei launched, in 2012, massive public relations campaign in U.S. to convince technology companies for patronage in area of contracts. Furthermore, Huawei announced this year (2016) of its intention to engage in *direct sale* of technology solutions (its Indoor Connected Solution products) to the consumers in U.S (DeGrasse, 2012; Osawa, 2013). However, Huawei should have explored *Joint Venture* (JV) arrangement with large multinational firms like Ericsson, Samsung and Alcatel which are being patronised by technology firms in U.S.

Enron (U.S.) entered India through majority-owned subsidiary but suffered political risk between 1992 and 2001. There was a review of its ownership of power plant project (PPP) from 100% Enron to 50% but later to 64%, and review of the power purchase agreement on Enron's power project by the Maharashtra state government in India. Reason: political pressure from within the coalition government of Maharashtra state in India arising from the project costs and power tariffs considered higher than other power projects in India; fear of significant inflationary trend in prices in other areas. The contract dispute raged from 1992 to 2001, which was controversially counter-guaranteed by both the state and federal governments, threatened to bankrupt the State power board and the state exchequer itself, was mired in controversy, including protest rallies, environmental concerns, charges of human rights abuses, court cases and political skullduggery.

Thus Enron announced in 2001 its intention to sell its DPC stake because of payment disputes with its sole buyer, the Maharashtra State Electricity Board (MSEB) and the failure of the Indian central government to honour its counter-guarantee. The action of Enron by divesting from the project was appropriate because Enron has investment interest in many other viable and lucrative projects: LNG vessel construction joint venture; Metgas pipeline project; LNG terminal at Dabhol; Broadband services; and oil and gas fields in joint venture (Allison, 2001). The action was appropriate considering Enron's other investments in India.

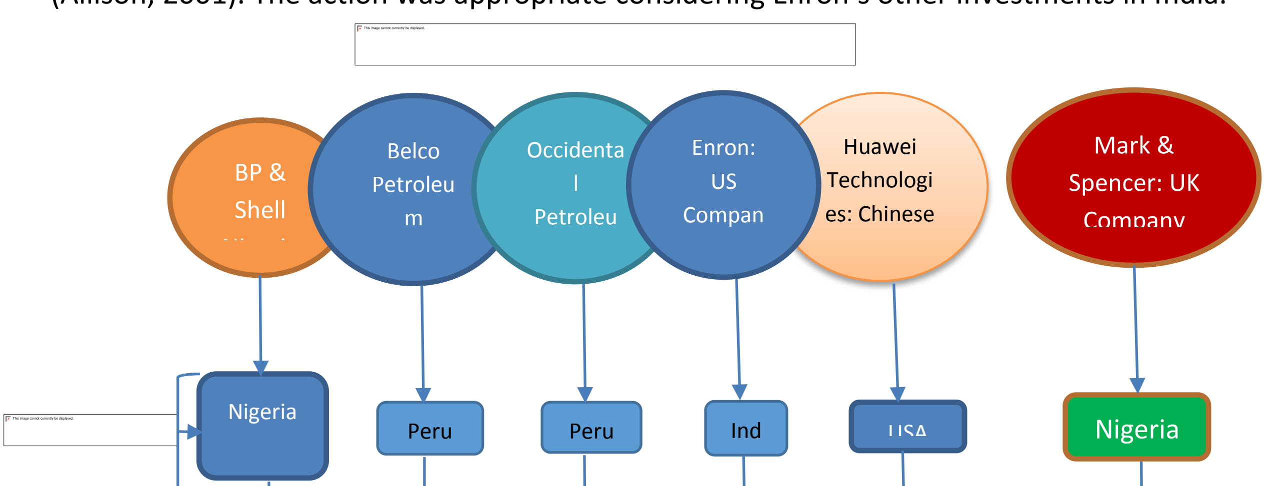

Figure 1: Summary of case study reviewed

Theoretical framework of minimizing political risk in host country

Institutional Theory

In respect of minimising political risks in host countries by MNCs, the tenets of *institutional theory* come into play. The paradoxical effects of firm foreignness, institutional learning is crucial as the landscape for foreign direct investment is defined by human constructed cognitive-cultural, normative, and regulative pillars that guide, constrain, and support social behaviour. Regulative elements of the landscape refer to formal rules and their enforcement including legal, political & economic arrangements; for example, those formal laws, rules, and rights. Normative elements pertain to values and norms, the former being conceptions of what is preferred or desirable, the latter suggesting the correct manner of activity or operations in terms of mores and protocols (Harrison & Elaydi, 2014).

Once there is deviation through the operations of MNCs from such lay down pillars that guide, constrain, and support social behavior, an element of jeopardy comes into play. For instance, Enron Corporation has problem in India over its power plant project because the contract for power supply to the host state contained many irregularities. Belco Petroleum Company has problem in Peru because it refused to accept legitimate government policies on investment in oil exploration and development of that country (Bradley, 1997; Gellene, 1985; Mawanza, 2015).

Internationalisation Theory

Another important consideration is the *internationalisation theory*. Internationalization portends momentous risks, such as investment and political risks, firms exposes itself to because of their entry into new markets that may be different from familiar domestic markets (Ramachandran et al., 2006; Zaheer, 1995). Unforeseen economic, political, and social challenges faced in a new business environment constitute fundamental risks in internationalisation; they will be greater if such environment is rapidly evolving. (Bartov et al.,1996; Reeb et al., 1998)

The risks that are associated with internationalization may be mitigated by an MNC's unique resources called ownership advantages (Delios & Henisz, 2003; Henisz & Delios, 2001; Kotabe et al., 2002). MNCs from developing countries such as Chinese MNCs may not possess strong ownership advantages and thus may face greater risks in their internationalization attempts (Nachum, 2014).

Empirical evidence provides that in order to neutralize the risks of internationalization, MNCs should acquire foreign market knowledge and cultivate mechanisms to foster organizational learning (Andersen, 1993; Barkema & Vermeulen, 1998; Erramilli & D'Souza, 1993; Inkpen & Beamish, 1997; Lord & Ranft, 2000; Zahra et al., 2000). The benefits of organizational learning involving process of assimilating new knowledge into organization's knowledge base (Autio et al., 2000; Zaheer, 1995), may compensate for absence of ownership advantages. Hence it is a key motivation for developing country MNCs for entering foreign markets (Luo & Tung, 2007). Not only will learning be useful in the particular host country but it could be also leveraged into other markets leading to competitive advantage and profitable operations (Harrison & Elaydi, 2014).

In accessing valuable knowledge and expertise in various host countries, Chinese MNCs', for instance, would be able to upgrade their existing knowledge of technology while developing new advantages (Harrison & Elaydi, 2014), which will be used to fill their resource gaps and compensating for their competitive disadvantages (Chung & Juan, 2002; Luo & Tung, 2007; Harrison & Elaydi, 2014). Hence it implies that learning advantages may be more important in counterbalancing the risks inherent in internationalization particularly for Chinese MNCs when compared to MNCs from the developed economies (Mathews, 2006; Peng, 2012).

Contingency Theory

It is also necessary to consider the *contingency theory* in applying it towards the discourse on necessary steps to take to minimise political and investment in host countries of MNCs. Different types of firms have different levels of embeddedness on a project, leading to more or less emergent dilemma in operations by MNCs and therefore, require knowledge of foreign markets. Given the large differences that occur between different firm's business goals, processes, and levels of embeddedness, it is always necessary to consider appropriate in guiding against political and investment risks in host countries by MNCs (Javernick-Will**,** 2013).

Hypothetical Case of proposal of Mark and Spencer (UK) Entry into Nigerian Market

Mark and Spencer is a British company that specializes in merchandising of cloths, which has many outlets in some countries around the world. The company has been chosen as a hypothetical case study due to the fact that, as a MNC, it has no sales outlet in Nigeria. The Nigeria market with a population of 170million is a well know consumer country of foreign made goods, and the country has political and economic ties with UK, the past political authority of the former.

Minimisation of political and investment risk in the home country being the focus of this paper, Mark and Spencer (M&S) proposes to entry into Nigerian market to reach the consumers of teeming population of about 170million. The use of cloths cuts across several strata of Nigerian society. The usage of clothing include uniforms for teeming pupils and students in primary and secondary schools, uniforms for factory workers, corporate workers in banks, insurance companies, and financial institutions, office workers in government establishments and other organizations, celebrities for occasions and ceremonies, elites in all the geo-political zones who are used to English dressings, and above all, youths constituting huge population in Nigeria.

The company is hereby advised to enter into the market through *Franchising* in order to avoid the political and investment risks suffered by the British Petroleum in Nigeria in the late 1970s as earlier analysed in this paper. The *Franchise* arrangement is considered appropriate because it involves form of contractual agreement between the firm and the agent to produce and market the products in Nigeria, as the foreign market in return for some form of economic rents (Shane, 1994).

The reasons for the choice of *Franchise* for Mark and Spencer's entry into Nigerian market include the fact that it: is not equity ownership; involves transfer of patent right to use its technology of clothing products for return of share of the franchisee's profits; does not involve transfer of physical assets to the franchisee; mar require secondment of M&S's production experts to mentor staff of the franchisee overtime; supports heightened campaign on patronage of home-made goods and the new government of President Muhammad Buhari can place outright ban on importation of cloths into Nigeria thus boosting M&S's returns.

CONCLUSION

The international market entry strategy is regarded as an established agreement that makes possible the entry of a multinational company's products, technology, human skills, management, and other resources into a foreign economy. The available entry strategies into foreign markets by MNCs include: exporting; licensing; franchising; joint ventures; acquisition of venture; and greenfield investment – full ownership of the venture.

The choice of entry strategy by MNCs normally plays an important role in determining the success or failure in its operations, which affect future decisions for a new marketplace. The implication is that MNCs take appropriate decisions to minimise investment and political risks by engaging in internationalization; a gradual increase in international involvement. And in the case of Mark and Spencer's proposal to enter Nigerian market, franchise mode is recommended in order to avoid political and investment risks.

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