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Control and Ownership Tradeoff in Resource Sourcing Cross-border M and A of Chinese Enterprises Based on the Bargaining Power, Institution and Institution Imprint

Yongcong Huang, Manli Huang and Xiaomei Chen
School of Business Administration, South China University of Technology,
381 Wushan Road, Tianhe, Guangzhou, China

Abstract: More and more Chinese resource companies, such as CNPC, have achieved the foreign countries' resource through cross-border M and A. However they found that the resource sourcing cross-border M and A processes was not easy, because nature resource is the most important for the any host countries' sustain development and safety. From reviewing previous literatures, we found that control, not the ownership, is the critical determinant in cross-border M and A. Control means achieving the strategic goal and the ownership just means the cost. The most of previous literature about strategic decision of the control and ownership tradeoff assumed that the decision maker is rational, but more and more research found that the decision maker is influenced by their history which means that the they are irrational. Drawing on bargaining power, intuition intuitional imprint, this study tried to combine the rational and irrational variables which would give the whole picture of how to make the strategic decision and proposes a model of control for Chinese enterprises' Resource Sourcing cross-border M and A.

Key words: Control, institution, resource sourcing cross-border M and A

INTRODUCTION

With foreign countries' resource being depreciated financial crisis from 2008. Many Chinese Resource companies take this opportunity to going out through cross-border M and A. With the rise of neo-institutional economics, institution content which has richer connotation than environment, gradually become the main research trend in the field of international business. But pervious studies just found that the institution can moderated the control and ownership (Huang *et al*., 2013), not clarified which dimension of institution respectively influenced the control and ownership. We think this question is important because that control stands for ability and ownership stands for commitment. They are two distinct concepts and should be influenced by different variables. Further more, there are some room for informal institution about cognition variables will make the decision maker influenced by the mental model based on the historical behavior.

Though some literatures have reviewed that control and ownership is primarily the result of the bargaining power of both sides in Chinese cross-border M and A (Huang *et al*., 2013). However, they focused on technology sourcing M and A, but no matter strategic goal or type of target company is quite different in Chinese resource sourcing M and A. It call us to explore what the feature of control and ownership negations in Chinese resource sourcing M and A. Drawing on bargaining power, intuition intuitional imprint theory, this study tried to combine the rational and irrational variables which would give the whole picture of how to make the strategic decision and proposes a model of control for Chinese enterprises' Resource Sourcing cross-border M and A.

Control and Ownership: Two Distinct Concepts: From the perspective of organization arrangement, the various FDI modes depend on the choice of the ownership and control. Organization arrangement includes ownership and control. The "Control" and "Ownership" concept in cross-border M and A comes from the FDI research. The goal of FDI is to obtain strategic resources to achieve strategic goals and among all issues, organization arrangement is crucial to realize the strategic goals in FDI. There are many FDI modes, such as Greenfield investment and Cross-border M and A. The enterprises choose a proper mode according to their FDI aims. Previous researches on international business mostly equated control to ownership. Earlier studies did not distinguish ownership from control in FDI, because developed countries with competitive advantages can obtain corresponding control from the ownership. Most early

Corresponding Author: Yongcong Huang, School of Business Administration, South China University of Technology, 381 Wushan Road, Tianhe, Guangzhou, China

studies claimed that equity is a synonym for corporate control, so obtain all or a majority of stake of the target enterprise is the key to access control.

However, more and more foreign studies found that there is no linear relationship between ownership and control (Lecraw, 1984). Emerging economies enterprises in the process of internationalization, often have higher ownership stakes and lower level of control. Therefore, ownership and control are separate. It must be clear that the key to achieve strategic goals lies in control rather than ownership. Therefore, scholars come to realize that it is necessary to clear that ownership and control are two completely different concepts in FDI. By the definition of ownership, it represents the enterprise owners' commitment to the target enterprise's resources and the degree to obtain surplus value, reflecting the controlling stake of both sides in FDI; control refers to organizational ability to affect the behavior of its members to attain the strategic objective which is the actual extent of controlling resources. Control is divided into three dimensions: scope, degree and mechanism. Control scope refers to the fields under control during the operation process; Control degree refers to the influence of control behavior; Control mechanism refers to the control method (Geringer and Hebert, 1989).

The controlling party in FDI establishes abroad cooperation mechanism to influence target enterprise's operation decisions and resources allocation (Yan and Gray, 1994). Methods to access control include voting rights, the number of executives in the enterprise management and the control over specific operations which are based on technology or management skills, etc. In other words, even if the acquirer holds a minority of stake, it can also be able to control over the target enterprise owing to their advantages on R and D or managerial technique (Behrman, 1970). Therefore, in the course of FDI negotiation, it’s not necessary for enterprises to achieve control through higher equity, because for most of the time ownership is influenced by internal and external causes. From external causes, due to the legal restrictions on equity share in host country or when the target enterprise is state-owned, the host-country government tends to require occupying a majority of stake in FDI to maintain control over the state-owned assets and the acquirer will take a minority of stake (Gomes-Casseres, 1990). However, In this case, the acquirer still can gain control over the enterprise through controlling specific business activities or all of the operational activities in the negotiations. From internal cause, the acquirer may reduce the ownership share strategically to exchange for a specific control over business activities and ensure investment return. In addition, higher level of ownership means greater investment cost, so the acquirer may control the uncertainty risks through lowering the ownership (Lecraw, 1984).

To sum up, literature researches prove the separation of control and ownership in enterprises, suggested that actual control is the key to fulfill the FDI target which is reflected in enterprise organization arrangement. In other words, the acquirer with a minority of stakes may also be able to obtain control over the enterprise.

Development of Hypotheses: Bargaining Power, Control and Ownership: As mentioned above, the acquirer must clearly recognize the difference between ownership and control in FDI (Lecraw, 1984) and achieve strategic goal through the tradeoff between ownership and control. In cross-border M and A, there are a lot of negotiations between acquirer, target company and host intuition. In the negotiation, relative bargaining power of both sides is the most important (Lecraw, 1984). As Ring and Van de Ven (1994) argued that the essence of fair trade is the degree of reciprocity of the participants in the transaction, while the traders’ decisions will be greatly influenced by their culture, institution and resource.

In cross-border M and A, control is the core of achieving goal and the ownership is the legal means to ensure control realized. Bargaining power refers to the ability that the participants change the "set" when seek control from the other participant in the negotiation, in order cto achieve the optimal result of the negotiation (Lax and Sebenius, 1986). Compared with the efficiency standard of transaction cost theory, bargaining power theory emphasizes the importance that negotiators develop and implement reasonable organization arrangement on the premise of fair trade (Ring and Van de Ven, 1994).

Specific assets and bargaining power: From the resource-based theory, resources determine organization arrangement. The more value of resources owned the more bargaining power you have. The empirical research showed technology, marketing ability, management ability and capital advantage can really strengthen the bargaining power of the negotiators (Kim and Hwang, 1992).

The previous literatures found that the imputed resource dependency can also directly influence the bargaining power (Pfeffer and Salancik, 1978). The imputed resource dependence determinates the value of the resource in the negation. Huang *et al*. (2013) had found that in the technology-sourcing cross-border M and A, exclusive asset is the key of the resource dependency, but this study think that in the resource-sourcing cross-border M and A is quite different. Because exclusive asset focus on the asset which is depend on people such as technology and knowledge, but in cross-border M and A most strategic goal is about raw material which is not depend on the people. So we must further develop the notion of resource dependence in resource-sourcing M and A.

In the resource-sourcing M and A, Resource dependence mostly derives from the specific assets. Specific assets belong to the transaction cost theory, it means "without sacrificing its production value, the degree of preceding assets can be reconfigured to alternative uses, or be used instead of using the redeployment which is associated with sunk costs (Williamson, 1985). Williamson argued that specific asset; transaction uncertainty and transaction frequency determines different organization structure. Transaction cost theory emphasizes transaction cost minimization and they think that an organization or contractual arrangements aim to maintain the asset specificity away from the opportunism behavior. Previous studies have argued that specific assets are the key to the bargaining power of the negotiators. Aoki (1984) was the first one studied the bargaining power of specific asset in negation. Aoki considers worker ability as a kind of specific assets and introduced boldness as the reflection of their bargaining ability with the management. Final conclusion is that when relative importance of specific assets is higher, the assets owners share more organization residual and hold a stronger position in the negotiations. Specific assets include Tangible asset and intangible asset and the scarcity is the most influencing factors. If someone owns the resource which is scare in the market, then he get the relative bargaining power (Barney, 1988). In cross-border M and A, when the one of the negotiators get the unique nature resource or technology, it can in charge the negation.

Hypothesis 1: The more specific are the resources, the more dependent the resources of both sides.

Institutional factors moderate the relationship between ownership and control: With more and more countries involving the globalization, Context factors can't not be ignored, even then it can influence the relative bargaining power (Yan and Gray, 1994). With the rise of neo-institutional economics, institution content which has richer connotation than environment, gradually become the main research trend in the field of international business. But the studies about the institutional factors and the ownership and control has some limitations: First, pervious studies just found that the institution can moderated the control and ownership (Huang *et al*., 2013), but as above said, both of them are distant concepts, then we should further found that which institutional factors influences the ownership and which institutional factors control. Second, the pervious literatures just focused on the macro intuitional variables which still assumed that the decision maker is rational (Huang *et al*., 2013), but more and more studies found that making decisions is not always rational, some informal institution about cognition variables will make the decision maker influenced by the historical behavior rather than rational "benefit and cost".

Host country government intervention and ownership choice: Gomes-Casseres (1990) claimed that the acquirer will make concessions on ownership due to host-country government's restrictions on equity. It assumes that all the company is risk-averse and ownership means acquirer's resource commitment. If the uncertainty is too high, the acquirer will make the ownership concessions (Lecraw, 1984).

Previous researches focus on formal institution and uncertainty avoidance. Firstly, the legal restrictions of the host country imposing on foreign companies' operations will reduce the likelihood of holding or wholly-owned enterprises in cross-border M and A. Brouthers (2002) introduced transaction cost theory into the choice of ownership and control, proposed the composite structure of environmental theory and cultural differences and through empirical study, found that enterprises entering into market with high level of law enforcement tend to share equity with the target enterprise.

Hypothesis 2: The host-country government intervention will moderate the relationship between acquirer bargaining power and level of ownership: The acquirer's bargaining power will more strongly associated with higher ownership when the degree of host-country government intervention is low than when it is high.

Intuitional imprint and control choice: As above said, the decision maker are not always rational. In many times, people make the decision is not only based on the current environment but also the historical behavior which we call institutional imprint (Stinchcombe, 1965). The concept of imprint comes from the biology. Imprinting as a process whereby a focal entity develops characteristics that reflect prominent features of the environment and these characteristics continue to persist (Stinchcombe, 1965). Institution imprint emphasized that the key brief sensitive time, such as the founding time or IPO would shape the organizational behavior pattern which will be longstanding even the external environment change. However, the pervious literatures assumed that the imprint only existed when the external environment is the same, but recently Marquis and Huang (2009) found that even the external environment change, the imprint can also persist. So the cognitive of the organization can evolutes.

Pervious studies thought that the founding time is the most important sensitive time, because when start-up the enterprise, the organization will be constrained with different institution and try to adapt to the external environment gain legitimacy. The enterprises' strategic behavior will be internalized within the organization. All this behavior pattern, such as organizational process and structure shaped in the founding, can become a part of the intellectual enterprise storage for most enterprises. Because of the Organizational inertia, the organization will make decision relied on imprint cognitive map rather than current status when face the changing environment. The imprint of the enterprises can persist and explicitly or implicitly influences decision making and cognitive map (Helfat, 2003). In China, because of the market segmentation which the culture and other institutions are quite different among different provinces, the regional culture and the limitation of resource and uncertainty made the enterprises to choose regional operation or the national operation in the founding time. If the enterprises choose national operation and successfully survive, it can form the geographically dispersed subsidiaries coordination advantage which tends to persist and help these enterprises have more advantage to pursue higher level control in the cross-border M and A.

Hypothesis 2: Contrast by the regional operation enterprises, the national operation enterprises can take higher degree of control.

THEORETICAL MODEL

With a review of the literature, we found that making strategic decision is influenced by the rational and irrational variables. The factors influenced the decision between technology-sourcing and resource sourcing is quite different. The most important, the acquirer make the tradeoff between control and ownership is not only influenced by the relative bargaining power but also the host-country government intervention and institutional imprint will play a moderating role. Therefore, we put forward a model of Control and Ownership tradeoff in Resource Sourcing Cross-border M and A of Chinese

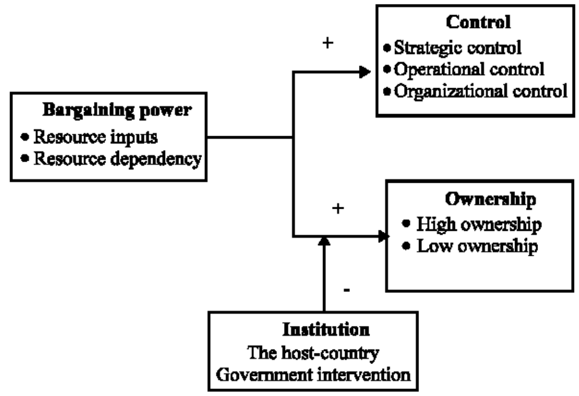

Fig. 1: Mmodel of chinese enterprise's resource sourcing cross-border M and a choice between control and ownership

enterprises Based on the Bargaining Power, institution and Institution Imprint (Fig. 1).

FUTURE RESEARCH

With the development of globalization, international research becomes a result of multiple factors. In the future, we will try to figure out more rational and irrational variables influencing the strategic decision making. Further more, we should in-depth explore what is the institutional imprint,what mechanism and process of imprint.

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