

# LOCAL ADAPTATION IN EMERGING MARKETS – in theory and reality

Study of the Swedish subsidiaries in China

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#### **ABSTRACT**

Some MNEs encounter frustration or failures when they enter a new market. The main reason is due to a lack of adaptation. There is a lack of theoretical study about the local adaptation phenomenon of Swedish MNEs in China. Most studies are at the level of experience. Therefore, the purpose of this study is to find out the dimensions subject to local adaptation and their degree for the Swedish MNEs in China.

Culture and business practices, government demands, competition intensity, product customization, distribution channels and organizational structure, are the six main dimensions subject to local adaptation. The degree of their adaptation varies depending on different factors (established network, the MNE strategic choice, entry mode, etc). We have developed eight hypotheses to test the theories and find new factors influencing the need of local adaptation. A new model is developed by applying existing models and with the new insights specific to the Chinese market. The central dimension in this model is the culture and business practices, as it influences the other dimensions to different extents.

<u>Key words</u>: Local adaptation/responsiveness, Global integration, standardization, Emerging markets, Chinese market, and subsidiary

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Anne Barbaroux Li Miao

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#### **DEFINITIONS**

Here we will introduce some definitions of the terms used in this dissertation. Other definitions from the researchers in this dissertation are integrated throughout the text.

- **Local adaptation/responsiveness:** "is the ability to react in an appropriate timescale to events, opportunities and threats in order to be or maintain a competitive advantage" (Barcley, 1996). In this dissertation the terms adaptation and responsiveness have the same meaning and we will brief them as LR or LA.
- **Emerging Market:** "is an economy in the early stages of developments whose markets have sufficient size and liquidity and are receptive to foreign investment. Examples include China, Greece and Brazil" (Alberta Finance, Heritage Fund Glossary, [http://...1]).
- **Multinational enterprise:** "A MNE is a corporation which own, in whole or in part, controls and manages income-generating assets in more than one country. In doing so it engages in international production, namely across boundaries financed by foreign direct investment", (Hood & Young cited by J.Preston, 1993).
- **Subsidiary:** "is an entity which is controlled by another entity. The controlled entity is called a company or MNE and the controlling entity is called its parent (or the parent company). (Wikipedia, http://:...7)
- Global integration: is the centralization of the dispersed activities abroad in one management, (De Witt & Meyer, 1998). We will brief this term as G.I
- **Foreign Direct Investment:** "FDI is investment of foreign assets into domestic structures, equipment, and organizations" (Glossary of Economic terms, [http://...2]). When a firm goes to internationalisation, it has to decide its strategy to enter the new market. The firm has the choice between various mode of entry form: Exporting, Jointventure, Wholly-owned subsidiaries... In this case we talk about Foreign Direct Investment.

# **Chapter I: Introduction**

In this chapter, the dissertation background is introduced first of all. Then, the research purpose and problems are discussed. Further, the research questions and the hypotheses are presented as well as the limitations. Finally, the outline is described.

#### 1.1/ Background

The topic about local adaptation/responsiveness was initiated by the course "Environment of International Business". With this aroused interest, we observed and noticed that some Swedish MNEs did encounter frustrations or even failures in China due to the lack of adaptation. For example, IKEA and Volvo are both facing the dilemma to be more local adaptive or to keep their global strategies (Tang, 2006, Ma, 2006). There are also a lot of such reports on MNEs from other countries (Reasons for MNEs' failure in China, 2005, http://...9). Besides, we knew from the experience of some Swedish businessmen that they had difficulties related to a lack of knowledge about this market. Even though they are ambitious and have big interests in this country. Hence, we think it could be very interesting and meaningful to research on this topic. The economic relation between China and Sweden are increasing as the business world focus is on the Chinese market. However, the literature on this subject is about the general situation in the world. The studies about China in this field are more at an experience level than at a theoretical one. Moreover, there is very little literature about Swedish companies' adaptation in China.

Some authors such as Hill (2005) mentioned the pressure for cost reduction (global integration) and pressure for local adaptation. On the one hand, researchers like Theodore Levitt (1983), Dicken (1998), Dunning (1993) are pro-standardization due to the emergence of new communication, transport and technology devices. According to these authors, adaptation is decreasing in all these aspects and "the world begun to resemble a global village" (Dunning, 1993).

Many researchers such as De Witt and Meyer (1998) and Y. Luo(2000,2005) have developed theories to explain and analyse the factors that influence the MNEs' local

responsiveness. There are different definitions of local responsiveness. In this dissertation, LR is defined as the ability to react in an appropriate timescale to events, opportunities and threats in order to be or maintain a competitive advantage (Barcley, 1996).

Therefore, we are wondering if the local responsiveness is really important for the success of MNEs in China. Furthermore, we want to see whether the theories are applicable to reality or not. As the domestic and international business environment in China has been going through a dramatic change since its opening and reforms, such as its entry into the WTO. Thus, we consider it constructive to explore the current situation of the Swedish subsidiaries' local responsiveness in China.

#### 1.2/ Research problems

The problem is that we do not know what is going on concerning the situation of Swedish subsidiaries' local adaptation in China. Most of the existing theories on adaptation are about emerging markets in general. There are few studies about Swedish MNEs established in China.

#### 1.3/ Purposes

The first purpose is to find out the main dimensions and degree of local adaptation of our sample. Then, it is to test the existing theories about adaptation with our findings. Finally, it is to develop these current theories and models with new factors found within the sample.

# 1.4/ Research questions

With the background, problems and purposes in mind, we present our research questions:

- 1) What is the overview of the phenomenon of local adaptation?
- 2) What are the main dimensions subject to adaptation in China and their reasons?
- 3) What will be the new model if there are new factors concerning local adaptation in China?
- 4) What would be the trend of adaptation for Swedish subsidiaries in China?

### 1.5/ Hypotheses

We have developed eight hypotheses in order to test the theories and applied the models. With the results we would like to create a new model which could be specific to Swedish subsidiaries in China and answer our research questions.

#### 1.6/ Limitations

This dissertation has its limitations as any other dissertations. Firstly, we limited our research to the most recognized authors and to the most authoritative publications in this field. Secondly, we limited our study to Swedish subsidiaries established in China. Thirdly, we have limited the number of companies interviewed to ten. We made these limitations due to the constraints of time, resources and finance.

#### 1.7/ Outline

Here the outline of the dissertation is presented.

#### Chapter 2: Method

The choice of methodology, the data collection and the research approach are presented and described in this chapter.

#### Chapter 3: Theoretical framework

The purpose of this chapter is to provide an overview of the local adaptation. At first, the theories about local responsiveness and globalization are presented. Next, the characteristics of the emerging markets are introduced with a focus on the Chinese market. Latter, the different modes of entry in a new market are described. These theories provide local adaptation knowledge about what, where, and how. In the end, the hypotheses that we want to test are presented.

#### Chapter 4: Empirical method

This chapter is a complement of the chapter two. The research strategy is described, as well as the sample, the interview process and its limitations. We conclude this part with the validity, reliability and generalisability of the research.

#### Chapter 5: Interviews of the Swedish subsidiaries

The ten Swedish subsidiaries interviewed are described in this part. We also mention the main reasons for these companies to be in China and their view about local responsiveness.

#### Chapter 6: Analysis

In this part, based on the information from each company, we analyze the data collected to test our hypotheses and complete the models supported by the theories. Besides we answer the research questions.

#### Chapter 7: Conclusion

This last chapter summarizes the findings and puts forward questions for further research and investigation. A methodology criticism and a practical implication of the research are presented, as well.

The figure below represents how each chapter is linked to each others.

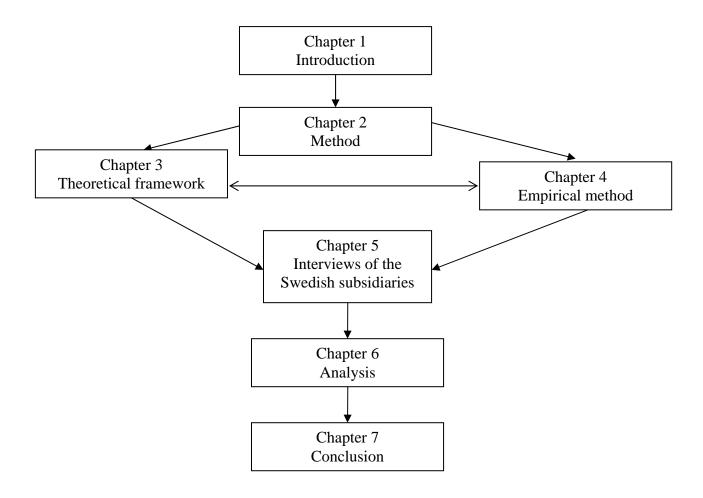


Figure 1.1: Dissertation guideline

# **Chapter II: Method**

We will present the choice of methodology chosen in this chapter. This choice is essential for conducting our study and reaching our goal. Firstly, the methodological approach choice will be introduced. Secondly, we will focus on the primary and secondary data. Thirdly, the methodology approach is presented.

#### 2.1/ Choice of methodology

At the beginning of our research, we wanted to compare the theory with the reality of the local adaptation with a case study of European multinational enterprises established in China. Then, we tried to narrow down to MNEs in one country. We decided to focus on Swedish subsidiaries. We knew there were some theories about local responsiveness, but we did not know what was going on in reality, especially in an emerging market as China.

We have looked at various literature about local responsiveness, global integration, and globalization in emerging markets. We also searched for literature about the differences in business cultures between Western countries and emerging markets with a focal point on China.

The purpose of this study is to find out to what degree Swedish companies adapt to the Chinese market and what challenges they face. We based our research on two types of data. The secondary data were the first data that we sought by reviewing the literature in this field. Then, to have a deeper understanding on what is going on in China, we interviewed Swedish subsidiaries established there. From the Consulate General of Sweden in China we received a list of around 200 subsidiaries. Thereafter, we checked on the companies' websites to find e-mail addresses and telephone numbers of the managers who could be our interviewees. We have made the compilation of the data from the literature review and the data from the interviews. Hereafter, we applied this information to the models found in the literature. We wanted to develop those models with the new insights from primary data, based on the experience of the Swedish subsidiaries.

#### 2.2/ Data

#### 2.2.1 Secondary data

In the field of local adaptation, the literature is more or less up to date, but only few authors really studied this aspect under the trend of internationalisation. Most of the famous writers talked about globalisation and shortly on the responsiveness aspect. Authors get started to be interested in the phenomenon of local adaptation since the beginning of the internationalisation of firms. We know that since the 1980's all the biggest companies all around the world undertook the expansion of their activities and especially in emerging markets. Knowing that few authors wrote about this phenomenon, we did not limit the date of the literature. Most of the secondary data are around ten years old.

We divided our secondary data research strategy into three steps. First we looked at local responsiveness and found various authors explaining the factors of this phenomenon as Hill (2005), De Wit & Meyer (1998), and Barckley (1996). Going further with this research, we found such different authors debating the adaptation and global integration as Dunning (1993), Dicken (1998) and T.Levitt (1983). The second step was to find information about the various modes of entry into a new market. In fact, the selected entry mode correlates with the strategy that an MNE wants to pursue. It also determines the degree of responsiveness or global integration. The last step was to read books and articles about emerging markets in general, and about China in particular. The goal was to seek business and culture differences that could influence the degree of local adaptation. We found some literature about the business and culture differences as it is a popular topic nowadays.

#### 2.2.2 Primary data

In order to obtain empirical data, we conducted some interviews with Swedish subsidiaries established in China. The interview questions are linked to the theories and the hypotheses that we want to study. These hypotheses have been developed through models illustrated in the literature review. Our aim was to interview at least 10 companies to increase the validity of our research. We tested the questions on two managers having experiences in the field of foreign subsidiaries before starting the interviews. These tests were really important to improve the interview. According to

their answers and comments, we adjusted the questions to achieve our goal and avoid any incomprehension on the part of the interviewees.

Then, we sent emails to 60 Swedish subsidiaries with the questions of the interview and a cover letter explaining our research. We have to admit that the reply rate was lower than expected. Some companies answered our questions directly by email, but without real contact it is difficult to have a real insight into the subsidiaries. We conducted phone interviews with the ones that agreed to participate. There were three among the 60 subsidiaries contacted with the first e-mail. To increase the reply rate we renewed the e-mail and searched on the companies' websites to contact the managers of the subsidiaries. We noticed that the positive returns were higher when we succeeded to contact the general managers directly. We received seven more replies. At the end, we had obtained the ten interviews as we had planned at the beginning of our method choice and design.

### 2.3/ Methodological approach

We used a positivistic research philosophy because we used existing theories to test our hypotheses. We were external to the data collection. That is to say, that we could not alter the process as we were not directly affected by the results of the data collections. We tried to stay as neutral as possible so as not to influence our research. This dissertation is also interpretative as we cannot generalize our sample. We interpret the phenomena according to our own perspectives (Saunders, Lewis & Thornhill, 2006).

Our study is a mix of a deductive and an inductive approach, as we apply theories and models with the data collected and tries to develop these theories and create a new model with new insights. Moreover, we also test eight hypotheses to verify these theories. These eight hypotheses are mainly developed from the theories and models of Luo and Hill respectively. The dissertation adopts a qualitative analysis carried out by interviews. Our research is an exploratory study (Saunders, Lewis & Thornhill, 2006). We want to see what is happening with Swedish MNEs and their local responsiveness in China.

## **2.4**/ **Summary**

To sum up, this part explained the methodology that we used to conduct this dissertation. We sought secondary data by reviewing literature on our topic. Then, we collected primary data trough interviews with Swedish subsidiaries managers established in China in order to have qualitative data. The research philosophy is a mix of positivism and interpretivism. In this study, we used a combination of a deductive and an inductive approach. The dissertation is an exploratory study.

# **Chapter III: Theoretical Framework**

In this chapter the theoretical framework will be presented. Firstly, we will give an overview of the theories on local responsiveness and global integration. Secondly, the emerging markets and an example of the Chinese market will be introduced. Then, we will talk about the two main modes of entry chosen by multinational companies and the levels of adaptation these investments involve.

#### 3.1/ Integration versus Responsiveness

The literature in the field of adaptation presents always two main streams of theories. The first one is about the need of local adaptation of foreign subsidiary when established in a host country. The second stream emphasizes the trend of globalization. When a company goes abroad, two elements drive its strategy, the pressure for local responsiveness and the pressure for global integration. In this part, the type of pressure that a foreign company faces will be presented and the debate between the two streams is to be discussed. Thus, we will have an overview of adaptation and integration and understand local adaptation under the background of global integration.

#### 3.1.1 Strategic Choice

A multinational enterprise can have two choices for its international strategy: multidomestic or global orientation.

The multidomestic strategy brings autonomy to the local subsidiaries in order to emphasize local responsiveness, (Peter J.Kidger, 2004). The subsidiaries behave as they were national companies. In this international strategy, the subsidiaries are freer to respond to different demands; the pressure of economic efficiency is lower and each subsidiary has to make local optimization, (Yves Doz, 1985). With a multidomestic strategy, a subsidiary may take more risks than a national company due to the counterbalance of the losses and gains among subsidiaries. The transfer of know-how and the share of the risks with the headquarters could create competitive advantages.

Global orientation strategy requires various degrees of policy and operations coordination (Peter J.Kidger, 2004). This strategy involves the integration of the activities of the MNEs. The foreign plants are integrated into a multinational production and distribution network. There is a specialization of the product and the process. The benefit of this strategy is an opportunity to reduce costs. The management is centralized and each subsidiary has a well-defined part in the integrated multinational system (Yves Doz, 1985).

The choice of international strategy is influenced by the industry of the multinational. Firms are looking for global economic scale; nevertheless, they have to meet the needs of their customers; therefore, they have to be local responsive (Peter J.Kidger, 2004)

#### 3.1.2 Pressure for Local Responsiveness

When a firm chooses a multidomestic strategy, it has to face the pressure for local responsiveness. In the following part, we will present the components of local responsiveness.

#### 3.1.2.1 Hill

Four dimensions constitute the need for local responsiveness (Hill, 2005). The first dimension is the differences in costumer taste and preferences. These differences are due to historical and cultural reasons. Therefore the product or service needs to be customized to attract the foreign customers. Thus, the parent company has to delegate the production and the marketing function to the countries of the subsidiaries. The second dimension, the infrastructure, involves the need of responsiveness due to the differences within the infrastructure and traditional practices. The product or service needs to be customized to the new countries infrastructure and practices. In consequence, the parent company has to delegate the manufacturing. The third dimension, which is about the differences in the distribution channels, implies the differences in marketing practices. Hence, the parent firm needs to adapt its distribution channel to the new country and to adapt its marketing to the country's tradition. The last but not least dimension is the specific requirements of the host government's economic and politic demands. These demands could include nationalism, protectionism and local content requests.

#### 3.1.2.2 De Witt & Meyer

De Witt and Meyer (1998) define local responsiveness as "the need of a subsidiary to take autonomous resource commitment decisions to react to the primarily local competitive or customer demands". The companies with a pressure for local responsiveness have a lower need of economy of scale and/or there is no need to protect the technology propriety. The authors also mention that the need for a meaningful adaptation of product or distribution across national markets involves a need for local responsiveness. As for Hill, the authors identified the same four dimensions, but gave more details. For instance, the more substitutes on the market exist; the more there is a need of product adaptation; especially when it is a domestic substitute. Thus, the need of product customization is higher to be locally competitive. These authors also discussed the reasons of the specific demands imposed by the host government. These demands should contribute to the development of the nation and the general security. Another detail given by the authors is the need to adapt the price strategy and the product positioning which could vary from country to country.

#### 3.1.2.3 Other theories

Other authors studied the phenomenon of local adaptation, as well. Sharifi and Zhang (1999) define the local responsiveness as "the ability of company to gather information from its commercial environment, to identify changes and respond quickly to them, reactively or proactively, and recover from them". LR implies three other related categories: competency, flexibility, and quickness. In this sense, "zero waste total cycle time" and "zero waste information flows" are the conditions to enable responsiveness (Mason-Jones and Towill, 1999). We have defined LR, in the introduction, as the capability to react within an appropriate timescale to significant events, opportunities or threats from the external environment in order to increase or maintain competitive advantage (Barcley, 1996). The efficiency of a company depends on the company's environment. Barcley has established a model including six factors determining LR which can be seen in the table 3.1 below (Responsiveness of the order fulfilment process, Duangpun Kritchanchai and B.L. MacCarthy, http://...5).

Drivers	Providers
Timescale	Capability
Focus	Strategy

Table 3.1: Local Responsiveness factors (Barckley, 1996)

We can divide these six factors into three main themes (D.Kritchanchai and B.L Mac Carthy, 2004).

- 1) The events or influencing factors to which the company has to respond.
- 2) The capability to react and/or predict events in order to manage, control and take advantage.
- 3) The approaches to achieve responsiveness.

According to these authors, we have drawn a figure summarizing their models.

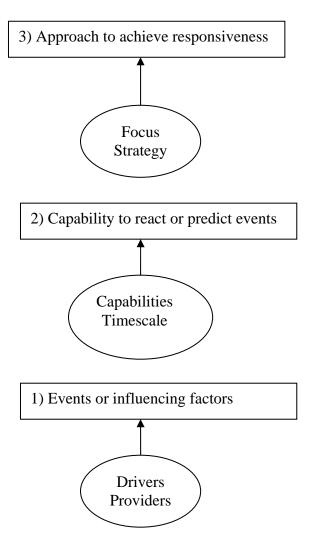


Figure 3.1: Local responsiveness themes including Barckley LR factors

The Figure 3.1 shows the relations between the six factors driving local responsiveness of Barckley and the themes identified by D.Kritchanchai and B.L MacCarthy. The drivers and providers of a company highlight the events and influencing factors that the company has to respond. In a good timescale and with its own capabilities, the company will react or prevent these events and take the advantage of the competitors. To respond to the demands and to achieve responsiveness, the company will focus on these demands and change its strategy in order to achieve its new goal.

In conclusion, the local responsiveness is driven by the strategy of a company and the market environment. According to Y.Doz (1985) the local responsiveness allows MNEs to supply similar goods from different national locations. Therefore, the MNEs coordinate actions for the optimization of their competitiveness and can alternate their policies from country to country.

#### 3.1.3 Pressure for Global Integration

A company choosing a global integration strategy faces the pressure of costs and needs to integrate its subsidiaries in one network.

#### 3.1.3.1 De Witt & Meyer

Global integration (GI) of activities is the centralization of the dispersed activities abroad in one management. The integration is in response to the cost pressure and the investment optimization. The consequences of a global integration is the delocalization of the plants in low labour cost countries. GI leads to economy of scale by building large-scale and highly specialized production (De Witt and Meyer, 1998). In general, global integration leads to globalization.

Global strategic coordination consists of the centralization of management resource commitments across national boundaries; for example the coordination of R&D across many laboratories or the coordination of prices to global customers. The goal of a strategic coordination is to recognize, build, and defend long-term competitive advantages. The pressure for global strategic coordination is divided into seven aspects, according to De Witt and Meyer (1998).

- 1) The pressure depends on the importance of multinational customers.
- 2) The presence of multinational competitors who operate in multiple markets.
- 3) The intensity of the technology, especially when the markets are extended.
- 4) The intensity of the investment; the need to leverage investment increases the need for global coordination.
- 5) The sourcing pressure for cost reduction requires a product sourcing from low cost location or to take advantage of economy of scale.
- 6) The universal need requires little adaptation across national markets, thus the global integration is obviously facilitated.
- 7) The need to access to cheap raw materials and supply of energy.

#### 3.1.3.2 Dicken

Dicken, in his book, Global Shift (1998), explains the debate between hyperglobalist and those who have a sceptical stance. As said by, the hyperglobalist we are living in a world without borders and nation states. The products standardized by global corporations create a homogenization of the customer tastes and cultures. Companies do not stick to one place or one community when they produce these goods. The main idea is the "end" of geography. As said Ohmae, 1995:

"Today's global economy is genuinely borderless. Information, capital and innovation flow all over the world at top speed, enabled by technology and fuelled by consumers' desires for access to the best and least expensive products".

The sceptics about this idea claim that the world is far from being globalized and the national forces are highly significant. As said Glyn & Sutcliffe? 1992:

"The system has... become more integrated or globalized in many respects... Nonetheless what as result is still very far from globally integrated economy... In short, the world economy is more globalized than 50 years ago; but much less so than is theoretically possible. In many ways it is less globalized then 100 years ago. The widespread view that the present degree of globalization is in some way new and unprecedented is, therefore, false."

According to Dicken, the forces of globalization exist but we still do not have a complete globalized world economy. The aspects of globalization are too complex to say that is the end of the states. He has distinguished two processes:

- Internationalizing processes involve the extension of economic activities across national boundaries. It is more an extensive geographical pattern of the economic activity.
- Globalizing processes involve not only the geographical extension of economic activities across national boundaries but also the functional integration of such internationally dispersed activities.

In conclusion, Dicken believes in the globalisation stream but time is needed before to say that we are living in a world without frontiers as the hyperglobalist movement is advocating. At the extreme, the world is depicted as a globalized world in which global corporations are more powerful than nation states and provide standard product to the world market.

#### 3.1.3.3 Dunning, Hirst & Thompson, Hill

Other authors explain the need for global integration as Hirst & Thompson (1996) and Dunning (1993). In accordance with Hirst & Thompson, the multinational enterprises are increasing the globalization of the world by being the engines of the economic activity. Today the global process determines the social life. The national cultures, economies and borders are melting into one piece. The transnational corporations can dictate the world process by being located all around the world. The new generation of advanced technology and organizations has transformed the structure of the international firms. The MNEs are aware of the needs of responsiveness in the countries where they operate even though the world becomes to resemble a "global village" (Dunning, 1993). To survive in the new world, companies have to change and become more global. Thereby, they can drop their costs. The international dimension of MNEs creates a need for flexible production and marketing systems; therefore, organizations have to be changed. The increase of the concentration and asymmetry are the causes of the globalization. In fact, asymmetry implies the need of strategy collaboration. MNEs are the economic leaders of the world with a more integrated governance of their operations even though they take in to account the specificities of the market. Multinationals mainly pursue ethnocentric or polycentric strategy in their subsidiaries.

The governments' attitude changes toward more economic collaboration between countries. To conclude these arguments mentioned by these authors, we can say that the global market is characterised by the convergence of the consumer needs and preferences (Dunning, 1993). The hyperglobalists draw the world as a free set of business with free competition in order to serve customers. Therefore, the national authorities should not intervene in the global market to control economic outcomes (Hirst & Thompson, 1996).

Local responsiveness could affect companies by increasing the costs and reducing the economy of scale. In his book, Hill concludes that a company having a local responsiveness strategy does not gain full benefits from experience curve. In addition, they cannot leverage their skills and there is no location economy.

#### 3.1.4 Integration-Responsiveness Grid

#### 3.1.4.1 *I-R Grid and industry types*

Daniels, Radebaugh & Sullivan (2004) distinguish the degree of responsiveness or integration depending on the type of a company's industry. Figure 3.2 below shows the link between the industry types and the level of adaptation. We can point out that high technology industries (square n°1) involve less adaptation. However, the more service-oriented an industry is (retail banking, health care...square n°3), the higher is the degree of adaptation.

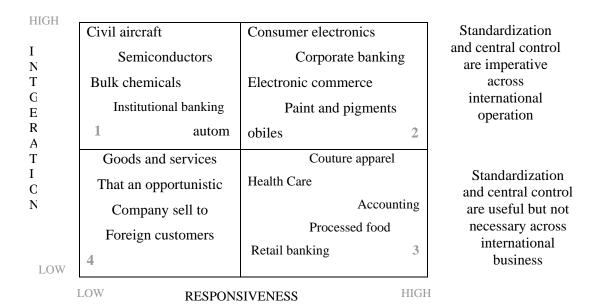


Figure 3.2: Integration-Responsive Grid and industry types (Daniels, Radebaugh & Sullivan, 2004)

#### 3.1.4.2 I-R Grid: strategic focus and organizational adaptation

Now, we will present the grid that Yves Doz and C.K Prahalad (1986) have drawn in their study about balancing local demands and global vision. The grid represents the characteristics of a business concerning LR and GI.

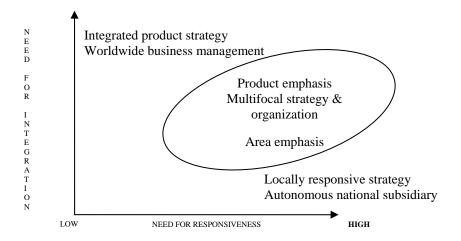


Figure 3.3: Integration-Responsive grid, strategic focus and organizational adaptation (Y. Doz & C.K Prahalad, 1986).

Figure 3.3 shows that the more a company has an integrated product strategy, the more the product is standardized as well as the international management; therefore the need of integration is high. On the contrary, if a subsidiary operates like a local firm, their autonomy is highest with an important need for local responsiveness. When a company emphasizes the geographical area and its organization, then there is a complementation between integration and responsiveness.

#### **3.1.5 Summary**

In this part we have seen the different stances concerning the international strategy of multinational enterprises. MNEs have two main choices: to be more local responsive, so to give more autonomy to the subsidiaries; or to be more integrated and adopt a global orientation strategy. After the literature review, we think that international firms should counterbalance these two aspects and find their place in the grid studied above. The type of industry and the market entered should be taken into account by an MNE in its strategy decision.

### 3.2/ Emerging Markets

The emerging market is an important factor when an MNE positions itself in the grid of local responsiveness and global integration. In this section, we will introduce the concept of emerging market, its features and its current situation, as well. Then, we will present the determinants of local responsiveness and the needs for global integration in emerging markets.

#### 3.2.1 Understanding the emerging markets

There are different definitions about emerging markets. Here we define it as "An economy in the early stages of development whose markets have sufficient size and liquidity and are receptive to foreign investment. Examples include China, Greece and Brazil" (Alberta Finance, Heritage Fund Glossary, [http://...1]).

#### 3.2.1.1 Commonalities

Although there are many emerging markets in the world, they still possess some commonalities. The first commonality is that the legal infrastructure, including legal system development and enforcement, is generally weak. The political, social, historical, and cultural factors often impede the implementations of the new laws. That is why many emerging markets have unique commercial practices and operations. The second commonality is the weakness of the market and the institutional support needed for economic development and business growth. The third one considers the uncertainties and the volatilities of the fast economic growth of emerging markets (e.g. Thailand in Asian Financial Crisis). The fourth commonality is that emerging markets have an emerging middle-class consumer (e.g. in China and India). There is a huge market opportunity characterized by its differentiation, such as the consumption behaviours, income levels, social norms and cultural traits (Y Luo, 2002).

#### 3.2.1.2 Government policy shifts

The government policy shifts on FDI characterize the current situation in most of emerging markets. The deregulation of the national economies, the structural transformation of various economic sectors, the fast economic growth in some emerging markets such as Brazil and Poland, and the increase of the global integration are the

forces which have affected these policy changes on FDI. These changes include (Y. Luo, 2002, 48):

- 1. Shift from entry intervention to operational interference.
- 2. Shift from separation from domestic policies to convergence with domestic policies.
- 3. Shift from overt control to covert intervention.
- 4. Shift from regulatory homogeneity to regulatory heterogeneity.
- 5. Shift from policy rigidity to treatment elasticity.

However Y. Luo said: "Pressures for increased global integration and for more inbound FDI drive the shift from conflict to cooperation with MNEs, while continuous economic, bureaucratic, and political transformations give rise to greater unpredictability of policy changes and the directions. Such unpredictability is evident in newly open yet still rigorously regulatory industrial sectors." (Luo, 2002, 41)

Besides the commonalities and current policy shifts, emerging markets also vary from country to country in its particularities.

#### 3.2.1.3 Particularities

Emerging markets can vary in political, economical, social-cultural, technological, environmental and legal systems. Since the culture is a basic aspect, which can influence other related aspects and takes long time to change. Thus, we decided to focus on the specificity of the culture.

#### 3.2.1.3.1 Culture

There are many scholars who have studied the culture issue. Here, we introduced the theory of the five dimensions of Hofstede, a Dutch scholar. It is about the national cultural differences and was conducted in business context. The results of the 5-D model have been updated with the development within each nation. Therefore it is relevant to our study. Hofstede's theory can be described briefly as following (Hofstede, 2003).

- Power distance index (PDI): the unequal distribution of powers in a society and organisation.
- Individualism (IDV): the relationship between an individual with collectives in a society.

- Masculinity (MAS): the different roles of women and men and their distribution between genders in a society.
- Uncertainty avoidance (UAI): the degree of tolerance of a social member to uncertainty
- Long-term orientation (LTO): a society's value to long-term commitments and respect for tradition.

If we check Hofstede's model, we can find scores for each nation in the five dimensions. As culture varies from country to country, we will leave the detailed discussion about cultural distance in the part of Sino-Swedish cultural distance.

#### 3.2.1.3.2 Business practices

Related to the cultural differences, emerging markets have also special practices. Different countries have different ways in terms of social customs, dress code and appearance, verbal expressions and accepted behaviours on different occasions. These practices, in fact, are the reflection of the value systems and norms of that culture. Doing business in different cultures requires adaptation to these practices as well. As the old saying states, "When in Rome, do as Romans do". A refusal to adapt may lead to inconvenience and failure. Adaptation can include in which way deals are negotiated, incentive pay systems for salespeople are set up, organizations are structured, the manner in which the product is promoted, and the like (Chaney, Martin, 2004).

#### 3.2.1.3.3 Business ethics

Business ethics is another factor which needs adaptation in the emerging markets. Many ethical principles are universally held across cultures. For example, basic moral principles such as do not kill or do not steal apply everywhere, despite differences in local culture (Hill, 2005). In business world, it is also universally held that it is unethical to break business agreements without a good reason, and those who do that will face sanctions either legally or culturally (Y. Luo, 2000).

Although many ethical principles are universal, some are culturally bound. One of widely cited examples is gift giving, which is regarded as normal way to build a network in Asia and especially in China, but it is regarded as unethical or bribery in some Western countries. Reflecting on such dilemmas, the ethicist Thomas Donaldson

has argued that when thinking through ethical problems in international business, firms should be guided by three principles (Thomas Donaldson cited by Luo, 2000,119):

- Respect for core human values that determine the absolute moral threshold for all business activities.
- 2. Respect for local tradition.
- 3. Believe that context matters when deciding what is right and what is wrong.

There are many other particularities that we cannot cover all. But we can be aware of those when doing international business in emerging markets.

#### 3.2.1.4 Needs for global integration

As we said, global integration is one of the forces driving emerging government policy shifts. Strategic capability, organizational infrastructure and strategic needs, can explain the need for global integration. Firstly, the immature and underdeveloped nature of emerging markets' legal systems limits the property protection of MNEs, especially tacit knowledge and strategic resources. Secondly, organizational infrastructure is important to global integration in terms of information flow, coordination system and resource flow. An advanced coordination mechanism can enhance the efficiency and effectiveness of an MNE. Thus, it facilitates its global operation. Thirdly, from the perspective of strategic needs, an MNE's global integration in an emerging market can diversify its risks and exploit factor endowments (Luo, 2002)

Consequently, there is a need for global integration in the emerging markets but there is also a need for local adaptation in the emerging markets. In the next part, we will talk about MNEs needs for LR.

#### 3.2.1.5 Needs for local responsiveness

Some authors as Y.Luo, (2000), argued that there is a need for local responsiveness in emerging markets. According to him and other scholars, the LR can be determined by environmental, industrial and organizational factors. Here, we will explain these factors and the model will be presented later in figure 3.5.

#### 1. Environmental Factors

• Environmental complexity: Environmental complexity in emerging

markets means high uncertainty and risks, which requires high adaptation to respond to the dynamic situations and reduce or diversify the risks.

- Business specificity: It is a country-specific knowledge, which can reduce MNE's liability of foreignness and promote its financial efficiency and competitive advantages (Dunning cited by Luo, 2000). Thus, local responsiveness is needed to reach the goals of efficiency and competitive advantages.
- Cultural distance: Most MNEs' original cultures are distant from the culture of emerging markets. According to the transactional cost theory, the more distant the cultures are; the more costly the internationalization is. Therefore, adaptation is necessary to reduce the transactional cost in foreign emerging markets.

#### 2. Industrial Factors

- Competition intensity: If an emerging market has many domestic and international competitors, then MNEs have to adapt to keep customers and business.
- *Demand heterogeneity:* Some emerging market has highly segmented and differentiated market (like China and India). Hence MNEs should adapt to different customer needs and preferences if they want to keep and expand their market share.
- Component localization: In order to protect national industries, emerging governments usually use component localization policies. Thus, they are in a dominant position driving MNE's local responsiveness according to the government demands (Luo, 2000).

#### 3. Organizational Factors

- *Previous experience:* previous experience or accumulated knowledge can help business operation. This experience is in fact the process of adaptation or responsiveness to local markets.
- Established network: Relationship building is a social investment that
  requires socialization, commitment as adaptation (Burt, 1997, cited by
  Luo). No matter which emerging market, it is important to have an
  established network to utilize the local resources, thus, adaptation is
  necessary.

 Market orientation: Market orientation means export or local market orientation. The first one does not need much local adaptation but the latter requires much adaptation as it faces local market, customers and authorities as well.

To sum up, we can conclude that the three factors (environmental, industrial and organizational) above and their elements dynamically and interactively determine the emerging market's LR. Facing the needs for integration and the needs for responsiveness, it is important for an MNE to deal properly with the parent-subsidiary relation in such a complex and dynamic environment.

#### 3.2.1.6 MNEs response: Parents-subsidiary relation

To understand the type and nature of parent-subsidiary relation, we can refer to Luo's view. There are two branches of views of parent-subsidiary links, one is resource dependence view and another is performance effects view. The first view is when many emerging markets cannot supply all needed resources for foreign businesses; parental support will increase the subsidiary's competitive advantages in the industry. This implies that the lack of parent resource support may increase transaction costs in various stages of operations in a host country (Teece, 1986, cited by Luo). The second view is that MNEs may gain greater returns from resource commitment and local responsiveness with favourable and opportunistic external conditions (Barlett and Ghoshal, 1989, cited by Luo).

We cannot separate the two views, both internal and external relations are important for MNEs in emerging markets. As we can see, many MNEs are increasingly integrating emerging market operations into their globally coordinated network through vertical integration: supply chain, production rationalization, or resource combination (Luo, 2000).

#### *3.2.1.7 Summary*

In this part, we have illustrated the emerging markets in terms of its commonalities and specificities. The needs for GI or LR, as well as, the proper way to deal with the parent-subsidiaries are presented. MNEs must take into account environmental conditions, organizational dynamics, and strategic objectives when they think globally and act

locally to balance global integration needs and local adaptation requirements (Luo, 2000). Indeed, the I-R grid addresses the importance of these two dimensions and offers insight into the mind-range balance between these two dimensions (Bartlett & Ghoshal, 1989; Doz & Prahalad, 1991, cited by Luo, 2000). In the next part, we will give an example of an emerging market.

### 3.2.2 Example of the Chinese market

#### 3.2.2.1 Overview of China

China is the biggest emerging market in the world, which possesses both commonalities and particularities as other emerging markets. Foreign Direct Investment in China has gone through three phrases since the beginning of the politic reforms. After its entry into the WTO, the increasing transparency of FDI policies speeded up the development of FDI in various industries. Since 2002, China has been the country utilizing most foreign funds, which amounted to USD 52.7 billion. So far, over 420 MNEs among Global 500 Fortunes have invested in China; among them 30 MNEs have established regional headquarters in China and 400 MNEs have R&D centres in China. This trend is ongoing, (2006, CEC-CEDA, oct. 2006, http://... 3). The table 3.2 below gives an overview of the industrial development in China and the various reforms since 1979.

1979-	First reforms in agriculture. 80% of the population is living in the		
1984	countryside; a higher living standard would therefore create a basis for		
	other reforms		
1984	First success in agriculture – reforms are expended to state industry		
1988-	General shutdown of reforms. The main reasons are the high inflation rate		
1991	and the student demonstrations in 1989.		
1992	Since the spring of 1992, the government is following new politic reforms.		
	In October 1992 the XIVth Congress of China's Communist party		
	approved Deng Xiaoping's concept of the "development of the Chinese"		
	socialism".		
1993	In march, the concept of the "socialist market economy" is adopted in		
	China's legislation. Decision of transformation to a market economy.		
	· · · · · · · · · · · · · · · · · · ·		
	Reformation of the financial and the taxe systems.		
1994	Theoretical development of Deng's ideas		
2001	China enters the WTO		

Table 3.2: Chronological overview of industrial development in CHINA, (Arch G.Woodside & Robert E.Pitts, Quorum Books, 1996, pp. 64)

#### 3.2.2.2 Government policy shifts

As many other emerging market governments, the Chinese government also shifted it FDI policies. From these shifts, we can see that Chinese government's administration is more and more mature towards MNEs' operation. Since the mid-1990s, FDI-related rules and regulations are largely part embodied in various laws in domestic economic, procedural, administrative, and civil legislation. Some vague regulations and laws were drawn up for more government interference into some industries where the government lacks experience. This means that the regulatory framework of FDI will become more complex. This complexity is reflected mainly in regulatory heterogeneity across regions, locations, sectors, and industries. In order to compete with other emerging markets for more FDI, the government adopted an elastic policy towards those MNEs in a favourable negotiation position in finance, operation, industry access and ownership requirement (Local responsiveness' reasons and impact on Chinese firms, 2005,http://...10, Li & Hao,2006, http://...13, Luo, 2000)

#### 3.2.2.3 Industries versus opportunities & challenges

The Chinese government is making a series of measures to transform its industrial structure. The FDI policy shifts will bring new opportunities and challenges to FDI in different industries. In this part, we single out the technological intensive industries for further discussion. We have considered FDI on service industries in China, since most Swedish subsidiaries established in China are in the technological intensive industries.

The technological intensive industries mainly include automobile industry, computer industry, pharmaceuticals and biomedicine, telecommunication equipments, electronics and machinery, and chemical industry.

- 1. The automobile industry: China's automobile industry is relatively small but the government made great efforts to develop it. One of the measures is to increase the percentage of local content used in manufacture. With the entry into the WTO, high tariffs and some previous barriers will phase out gradually. More and more foreign firms will compete with domestic firms and joint ventures.
- 2. The computer industry: China's IT industry began to grow in the early 1990s. Its personal computer sector is growing fast. Foreign firms are facing increased competition from the domestic firms. Its software sector lacks property rights protection, but things are in change now.

- 3. Pharmaceutical and biomedicine industries: They face stronger competition and many regulations. However, foreign drug companies still possess competitive advantage due to the better effects of their products. Currently, biomedicine is the industry strongly encouraged by the government. Foreign investors have a promising future in the Chinese market with less competition and favoured government policies.
- 4. Telecommunications Equipment: The Chinese government has invested greatly in this industry and which is expanding dramatically in China. Nevertheless, the world's telecommunication giants have occupied big market shares; small firms can only seek market and technological niches.
- 5. Electronics and Machinery: China's electronics industry produces mainly a wide range of household appliances (Luo, 2000). It is growing very fast but some sectors had to adjust their product lines as the products have far exceeded the demand. China's machinery industry includes 12 major sectors, from heavy and mining machinery to food processing and packaging machinery. Specific areas are given special priorities by the government. Moreover, packaging machinery is perhaps the most promising segment in this industry (Luo, 2000, pp.131-132).
- 6. Chemical Industry: The chemical industry is the first industry where the government is less involved. The government not only continues to invest in the weak areas of this industry, but also encourages foreign investment to improve domestic products and mitigate the financial pressure of some state-owned enterprises (Luo, 2000, pp.134). The biological industry is still in the infant stage.

Beside these industries, the retailing sector is in development due to the increase of the purchasing power. Nevertheless, China still needs FDI in this sector, even though it will increase the competition with the domestic retailers.

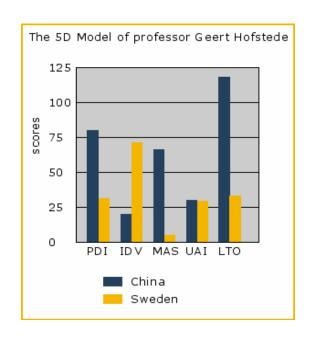
As we can see, the policy shifts and the entrance into the WTO, bring more opportunities than challenges to MNEs in these above industries. We will discuss it further in the analysis part.

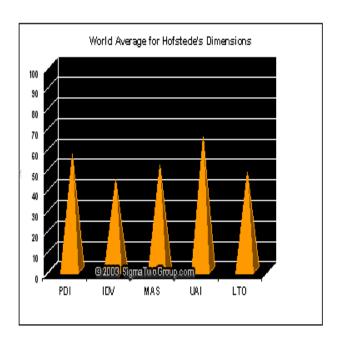
#### 3.2.2.4 Business culture and practices

China is a country with strong cultural tradition. No business can ignore its importance. Sweden is a western country far away from China but with an increasing bilateral trade. That is why, there is a necessity to know each other.

#### 3.2.2.4.1. Chinese versus Swedish culture

In the part of emerging markets (3.2.1.3.1), we have illustrated Hofstede's culture dimensions. In this part, we will compare Chinese culture with Swedish culture by applying Hofstede theory according to the figure 3.4:





World averages are 55 - 43 - 50 - 64 - 45

Figure 3.4: **PDI** Power Distance Index; **IDV** Individualism; **MAS** Masculinity; **UAI** Uncertainty Avoidance Index; **LTO** Long-term Orientation (G. Hofstede, 2003, <a href="http://...4">http://...4</a>)

PDI: China scores 80, Swede score 31 and world average is 55. This means China has centralized political power and exhibits all hierarchies in organizations with large differences in salary and status. Subordinates may view the "boss" as a benevolent dictator and are expected to do as they are told. Inequalities are expected, and may even be desired. In contrast, Swedish society and organizations are more flat and equal than Chinese society and organizations. Swedish manager delegate responsibilities to the employees. The result is a flat hierarchy. If we chase the cultural origins of PDI, we can

find the hierarchy is one of the basic Confucian teachings, which has influenced China for over two thousand years. While equality originated in 'The Jante Law' (in Swedish 'Jantelagen') saying that 'you should not think you are better than anyone else'.

- IDV: China scores 20, Sweden score 71 and world average is 43. Collectivism concept has root in Confucian teachings, which regard as harmony as the idealist state of China. Besides, collectivism was solidified by government's emphasis on collective social-economic interests over the individual. This aspect may invade private life and regulate opinions. In management, you will see that Chinese employees are less initiative than employees from more individualistic cultures. On the contrary, Sweden is a very individual nation. While typical Swedish management style is to think in an individualistic and collectivistic way at the same time. Generally a spirit of co-operation and flexibility will work better in Sweden. As a result Swedes will not want formal rules and procedures
- MAS: China scores 66, Sweden is 9 and the world average is 50. This indicates that China has a higher degree of gender differentiation. Males dominate a significant portion of the society and power structure. Sweden has a low level of differentiation and discrimination between genders. Females are treated equally to males in all aspects of the society.
- UAI: China scores 30 and Sweden scores 29, which is almost the same but still much lower than the world average which is 61. This indicates that both are uncertainty-accepting cultures, and more tolerant of different opinions from what they are used to. They try to have as few rules as possible. On the philosophical and religious level, they are relativists and allow many currents to flow side by side. People within these cultures are more phlegmatic and contemplative, and they are not expected by their environment to express emotions.
- LTO: China scores 118, Sweden is 33 and world average is 45. The high LTO indicates the strong influence of the Confucian teaching which values respect for tradition, fulfilling social obligations, and protecting one's "face". On the contrary, Swedish society is more short term oriented.

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<sup>&</sup>lt;sup>1</sup> Confucian, , an ancient philosopher and educator, whose ideas dominated the Chinese society for thousands of years and even spread over to some other Asian countries like Japan and Korea.

According to the comparisons, we know that Swedish and Chinese cultures differ greatly in four dimensions. The cultural differences will be reflected in management styles/practices. It is important for Swedish subsidiaries to know the differences and similarities between the two cultures while doing business in China. In short, Swedish subsidiaries should have high degree of LR in China due to the big cultural differences.

#### 3.2.2.4.2 International Business in China

Whenever we talk about doing business in China, *Guanxi (personal relationship or connections that could help the business)* and corruption are words frequently heard, thus it is important to distinguish between the two different concepts. Firstly, they differ in concrete attributes. Perceptual, contextual, power-related, illegal or norm-deviated, intentional and convert are the characteristics of corruption. While networking possesses different features as an ingredient of social norm, legal, built on exchange favour, involves implicit social reciprocity, without law risk, builds on a long-term orientation, does not specify a time limit, builds on trust and transferable. Second, they differ by nature. Corruption is evolutionary hazard, strategic impediment, competitive disadvantage and organizational deficiency. But a personal network is legal and reasonable. In one word, corruption is not equal to personal network (Luo, 2000, Four common problems for MNEs in China, Saike, 2005, http://...14).

According to many scholars (Gao Guopei, Oded Shenkar and Simcha Ronen, Paul W Beamish and Lorraine Speiss, 1995), the business environment in China is very complex, changing and risky.

### 3.2.2.4.3 Need for global integration

As in other emerging markets, MNEs in China have also the need for global integration. On the one hand, with its entry into the WTO, China will be more and more involved in the world economy. Hence, China will gradually do international business following international rules. On the other hand, MNEs have also the need for LR due to its particularities.

### 3.2.2.4.4 Need for adaptation

We can illustrate the need for local adaptation by applying the PESTEL model (Johnsson, Scholes & Whittington, 2005, pp.66-68). The PESTEL model is used in

order to see the weakness and the strengths of a market within six categories: Politic, economic, social-cultural, technology, environment and the legal system.

Politically, the Chinese government plays a very important role in policy and administration. Even the FDIs encouraged by the government have to realize this. Economically, the Chinese economic system is still transforming, thus, business cycles of different industries, money supply, interest rate and relevant financial institutions are not mature yet. Social-culturally, MNEs face big pollution, huge income distribution, dynamic social mobility, dramatic changes in lifestyles, consumerism, as well as, the uneven level of education. All these factors indicate that the Chinese market is not only segmented but also very complex. Technologically, the government is welcoming the FDIs that can bring technology transfer. To speed up this process, the government encourages Joint ventures. Environmentally, the government realized more and more the importance of the environmental protection, which is embodied through new laws. Legally, the legal system is developing. However, there are still some laws specific to China.

### *3.2.2.5 Summary*

In this part, we have introduced the overview of MNEs in China and their opportunities and challenges in different industries related to the government policy shifts. Then, Hofstede 5D model is applied to explain the cultural differences between China and Sweden. Finally, the needs for integration and adaptation are presented respectively. In conclusion, the particularities of this market, especially the cultural differences and its transforming industrial structure provide a need for Swedish MNEs to adapt in China. The entry mode is one of the first factors that the Swedish MNEs have to consider before entering this market.

# 3.3/ Mode of Entry in a new market

In this part the different modes of entry in a new emerging market will be presented. These modes are: exporting, licensing, franchising, wholly-owned subsidiaries, and joint-venture. We will browse briefly the three first modes of entry and in detail the two last ones, which are the most used modes in emerging markets. In our research, we find out that the mode of entry interferes in the need for integration or responsiveness.

### 3.3.1 Exporting, Licensing and Franchising

### *3.3.1.1 Exporting*

Export is the first step of expansion of a MNE. The exporting strategy avoids the costs and risks of establishment in a new foreign market. The drawbacks are the transportation costs, tariff barriers and the delegation of the sales and marketing to the new market (Hill, 2005). In this case there is no need for adaptation.

#### 3.3.1.2 Licensing

Licensing is an agreement, giving the right to the licensee to use the property right of the licensor for a specified period. In return of this service, the licensee has to give royalty to the licensor (Hill, 2005). With this entry mode, the firm does not need to bear the cost and risks of the development in the new market. The licensor has sold its knowhow to the foreign companies. Therefore there is a lack of control over technology and inability to engage in global strategic coordination (Hill, 2005). To conclude, when licensing a property, the firm does not need to adapt itself to a new market as it gives all the rights to the foreign operation in exchange of royalties.

#### 3.3.1.3 Franchising

"The franchising is a specialised form of licensing. The franchisor sells to an independent party, the franchisee gives the use of a trademark that is an essential asset for the franchisee's business and gives continual assistance in the operation of the business", (Daniel et al., 2004). The firms have less quality control power due to the distance. The franchisor gives the authorization to the franchisee to use the brand name including the quality of the service. As the licensing, the franchising does not allow the company to have global strategy coordination, (Hill, 2005). For a franchise, the franchisee needs to adapt a little the foreign service to the host country.

#### 3.3.2 Joint-Venture

### 3.3.2.1 Definition of Joint-Venture

A joint-venture (JV) could be characterised as a strategic alliance (Morris, 1998). A JV is a partnership between two or more firms from different countries in order to pursue a mutual interest by sharing resources and capabilities. There are two types of JV: equity JV and cooperative JV. The equity JV is the premium form of global strategic venture.

This form means that there is an equal ownership (50%-50%). Another alternative exists as the majority equity meaning that one partner owns more stakes in the venture than the other one. The partners should have a similar background, knowledge, short and long term objectives, and the same language (Luo, 2002). Through JV, companies can enter an emerging market (Morris, 1998).

### 3.3.2.2 Implication of Joint-venture

The creation of a joint-venture in an emerging market reduces the risks. The two partners can share their knowledge and improve the local recognition of the host company, making the entry in the new market easier. Even tough the local partners seem to be more sceptical about the success of the JV, this strategy provides business opportunities to the foreign MNEs (Luo, 2002). The costs decrease because the foreign partners can use the local partner distribution channels and its business network, (Woodside & Pitts, 1996). Moreover the MNEs can lower their costs by having lower labour cost, lower land price.... Therefore, the foreign company can increase its profitability, competitiveness and reduce uncertainty (Luo, 2002).

An MNE has to adjust its organization to the emerging market with a weak structure, regarding the property rights and uncertainty of the institutions. The foreign partners are assisted by the local partners who have specific understanding of the country in the government policies, the local business practices, operational conditions etc. The local partners have the knowledge about the environment as the distribution channels, promotional skills, local business practices, the relationship with the buyers, wholesalers and government authorities (Luo, 2002, Woodside & Pitts, 1996).

The creation of a JV in an emerging market can be very risky for the MNEs. In this paragraph, we will mention the type of difficulties that an MNE may encounter. The first difficulty is the relationship with the local partner. The organization between the two structures is different. The short-term and long-term expectation can differ. Therefore conflicts due to cross-cultural differences may arise between the two parts. The consequences of these conflicts could lead to the decrease of the JV outcome. The JV could loose its autonomy, its control and increase the internal instability. Another source of conflict could come from the parent company, which over intervenes in the JV decision making. To avoid this problem, MNEs need to maintain global integration and

to increase their global network controls (Luo, 2002). Nevertheless the need of adaptation is a real necessity for the survival of the partnership. We have noticed some important factors that should be adapted to the success of the JV. For example, the product has to be adapted to the new market. The two parts have to adapt their strategy for more cohesion. The management of the human resources shall be adapted to the new foreign operations, as well. The foreign partners need to adapt to communication and information device of the local partner. The business rules need to be coordinated between the partners. The most important step is the negotiation. Not only the western companies should adapt to local situation but the local firms also need to have knowledge about western management. The JV has to create a corporate culture in which western managerial style is acceptable by the local staff (Luo, 2002).

#### 3.3.2.3 Joint-Venture in China

The selection of the partner is important especially when the MNE enters an emerging market like China (Woodside & Pitts, 1996). China wants to enhance its agriculture, industry, science, technology and national defence to get closer to western countries. To accomplish this, the government undertook reforms to open the country and moved the "Chinese socialism" to a "socialist market system" (Woodside & Pitts, 1996).

In China, MNEs have to know and understand the economic, legal and socio-cultural environment, as we saw in the part above. It is important to establish a JV in an emerging market because of the economic and social environment complexity, (Luo, 2002). On the one side European MNEs gain with the access to the market, to the supply of raw materials and to low cost sourcing. On the other side, Chinese companies can take advantage of: production factors, technology, management and marketing know-how transferred from the foreign company. Thus, it improves the products and introduces new ones. The training of the employees to the business practices, the appearance of local managers improves also the economy independence (Woodside & Pitts, 1996). Emerging markets as China seek for technological innovation and managerial skills from the foreign firms. Their goals are the increase of the learning ability, the capability to assimilate the new knowledge and integrate it (Luo, 2002). In terms of human resources in China, the foreign companies should not take too many employees from a same nation but find a fair compromise. The MNEs have to resist the government demands and should not employ too many local workers. The patience and

flexibility are the key factors of success when looking for high-qualified local personnel. It is important for the managers of the JV to find among the local managers a trustworthy person who can help to deal with bureaucracy and institutions. In emerging markets the control of the JV by the foreign firms is very important.

Companies cannot expect an endless partnership. The end of the JV does not mean there was a failure, but that both parties achieved their goals. In China, the local partner does not specify explicitly in the contract the conflict resolution terms in order to be ambiguous about the long-term relationship (Luo, 2002). In conclusion, JV demands a great need of adaptation.

## 3.3.3 Wholly- owned subsidiaries

### 3.3.3.1 Definition of wholly-owned subsidiaries

As the JV, the wholly-owned subsidiaries (WOS) are established with foreign investors. WOS are owned at 100% by the foreign investor. Hence it is not considered as cooperation (Morris, 1998). There are two possibilities to establish wholly owned subsidiaries. The first one is to create a green-field venture meaning to set up a new operation in the foreign country. The second one is to acquire a firm in the host country and use this firm to launch its activity, (Hill, 2005).

### 3.3.3.2 Implication of integration

The WOS has many advantages; we will present here the three main ones. At first, this mode of entry protects the technological competence by increasing the control. Most of the companies in the high technology industry chose this entry mode. Next, the firm can increase the control over its operation in different countries. Later, the firm can realize location and experience curve economies. Nevertheless, the firm should bear the full capital costs and risks by setting up new operations abroad. The cultural aspects of the new market are not integrated as the JV. In fact, it is the most expensive entry mode in a foreign market, (Hill, 2005). We can conclude that setting up a green-field venture allows the company to protect is technology knowledge and increase the control but the risks and costs are high. The need of local adaptation to the new environment is lower for the company choosing this entry mode.

A firm can build its presence in the new market by acquiring an established enterprise really quickly. Companies save cost by acquiring other national companies than building new manufactories. The acquisition allows the company to pre-empt its competitor. The acquisition is, also, less risky than a green-field ventures because the buying company had already set up its recognition and asset in the host market. The acquisition of the assets is really important for the success in the new market, these assets are plants, distribution channels, brand name and knowledge of the business environment, as well (Hill, 2005). To sum up, acquisitions are less risky and ask more needs of adaptation. The needs of adaptation are mainly cultural. Managers need to deal with potential clash with the acquired firm. The managerial differences can slow the integration of the operations. Before acquisition the acquiring company has to analyze the benefits and costs.

It is difficult for companies to make a choice between green-field and acquisition. The choice will depend on the environment of the new market. If there are a lot of strong competitors, the acquisition may be the best mode of entry. On the contrary, if there is no competitor, the green-field venture may be the best one. The firm can base its new operation on its skills and culture.

### 3.3.3.3 Wholly-owned subsidiary in China

Although joint-venture is the most preferred mode of entry in China, we wanted to investigate the WOS in China, as it is the second type of FDI in this emerging market. We have seen that a JV could be risky for the foreign firm. For example MNEs used this strategy to enter a new market and after few years of operation they changed to WOS by buying the parts of the other (Woodside & Pitts, 1996). In fact, when well established and knowing the new market, companies prefer to stop the relationship and conduct their activities by their own (Morris, 1998).

### **3.3.4 Summary**

The entry mode and foreign direct investment of a company depend on the stage of its expansion process. The first step is the exporting mode. Then according to the environment of the foreign market, the firm has four other possibilities to go further in its internationalization. Each mode of entry offers various potentials to enter the new market. Exporting, licensing and franchising allow companies to save costs and risks

but they loose the control of their foreign operations. Wholly-owned subsidiaries give the full control of the activity with few local adaptations. However without knowledge about the environment the companies will meet difficulties to succeed in the new emerging market. Joint-venture seems to be the most appropriate and the most preferred entry mode chosen by companies willing to enter an emerging market. The local partnership is a real asset for the MNE even though there is a risk of cultural trouble. This last strategy includes large needs of local adaptation.

# 3.4/ Models and Hypotheses:

In this part, we will present you the models and hypotheses that we want to apply and test respectively, in order to answers our research questions.

#### 3.4.1 Presentation of the models

Through the literatures review we have mentioned some figures that we want to use for the analysis of the adaptation degree of the Swedish subsidiaries in China. Below, the models that we want to apply are presented.

Model 1: We have created this model from the dimensions of local responsiveness mentioned by Hill (2005). We want to apply this model in the environment of China to identify which factors are the most important ones in our study.

Model 2: This model is the I-R grid of strategic focus and organizational adaptations from Y.Doz & Prahalad/ Bartlett & Goshal. We want to know where the Swedish subsidiaries are situated in this grid (i.e. figure 3).

Model 3: The last model that we want to apply is the model of Y Luo, (2002): The determinants of LR. The components are defined in the part 3.2.1.5.

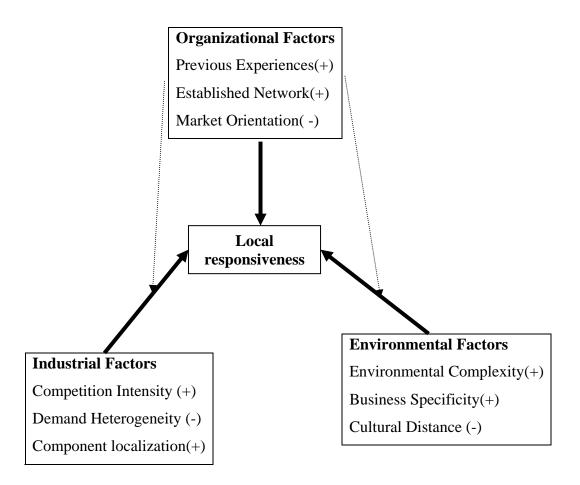


Figure 3.5: The determinants of local responsiveness (Y.Luo, 2002)

## 3.4.2 Hypotheses

As introduced in the section 1.5, we have developed eight hypotheses based on the literature review and the model presented above in order to obtain new insights and create our model.

H1: Having a previous experience in emerging market is positively associated with LR We presume that more a company has foreign experiences in other emerging markets and acquired knowledge more the company is willing and able to make local adaptation.

### *H2: An established network facilitates the LR.*

The need of a network in emerging markets is important to establish the business. We assume that a widely establish network and the mode of entry choice in a new market will bring a higher degree of adaptation.

H3: The cultural distance between Sweden and China has a high impact on LR, and increases the pressure for LR.

We believe that the culture distance between two countries influences the level of adaptation in the host country.

*H4:* The type of industry influences the degree of local adaptation.

According to the model 3 from Daniel & al. 2004, the type of industry has an impact on the local responsiveness.

*H5: The more the market is segmented, the higher is the need for LR.* 

We believe that a segmented market increases the degree of local responsiveness.

*H6: The higher the competition is, the higher the need for LR is.* 

We presume that the competition intensity on a market is positively linked to the degree of local adaptation.

H7: Component localization policy is one of the most important government demands that determine the degree of LR.

We assume that the host government demands are important in the local responsiveness strategy especially in China.

H8: Environment complexity increases the requirement for LR

We presume that the complexity of a market environment is associated with the local responsiveness.

We will test these hypotheses by comparing them with the data obtained from the interviews in the analysis part.

# 3.5/ Summary

In this chapter, we have seen that a global orientated strategy involves a need for global integration. While a multidomestic strategy choice involves a need for local adaptation. Different authors have different stances between these two choices. We know that the emerging markets are complex. The government makes some policy shifts in order to

respond to the globalization trend. Therefore, these shifts generate a need for integration in MNEs strategy, in those markets. However, their environment particularities demand for specific adaptation. We focus on China as it is a very particular emerging market. China is changing its policy for more FDI. The type of FDI implies different levels of adaptation. The JV is the mode requiring the highest need for responsiveness. Through the theories and presented hypotheses, we want to find out what main dimensions are subject to adaptation in China. We will discuss this in the analysis part.

# **Chapter IV: Empirical Method**

In this chapter, the empirical method used in this dissertation will be explained. Firstly the research strategy will be presented, and then the sample, the limitations and the interviews will be described. Secondly, the validity, reliability and generalisability of the interviews will be discussed.

# 4.1/ Research Strategy

The purpose of this dissertation is to study the degree of local adaptation in emerging markets. We focused our research on the degree of adaptation of the Swedish subsidiaries on the Chinese market. As we explained in chapter two, our research is an exploratory study with a mix of a deductive and an inductive approach. That is to say, that we used existing theories to explain the reality and to develop them with new insights specific to the Chinese environment and Swedish subsidiaries. Through interviews, we expect to have new information about the factors influencing the degree and dimensions of responsiveness of the Swedish subsidiaries.

According to Saunders & al. (2006), there are three ways to conduct an exploratory study: a search of literature, interview of the experts in the subject and conducting focus group interviews. An extensive amount of literature was reviewed concerning our topic. We wanted to make a survey of Swedish subsidiaries to have the empirical data. A survey is usually used when you want to answer the questions: who, what, how much and how many. However, we realised that we need more qualitative answers to get deeper information and we were also unsure about the quantity of the replies. In our case, we want to see the reality and identify new elements of the LR. To achieve this goal, we chose the case study as a research strategy. A case study involves an empirical investigation to study a phenomenon in its reality. Furthermore, a case study gives a rich understanding of the reality (Morris & Wood, 1991, cited by Saunders & al., 2006). The techniques used to conduct this kind of investigation are interviews, observation, documentary analysis and questionnaires (Saunders & al., 2006). Thus, we have chosen to conduct interviews with Swedish subsidiaries established in China. There are several other reasons why we chose this method. Firstly, we think a qualitative study is suitable

for this topic, and it is also easier to operate. Secondly, the research questions of the dissertation can be better investigated by the use of interviews, from which we can obtain more information and a deeper understanding of the questions. Thirdly, we think that the usual response rate of survey is low. If we cannot have more than 30 replies on a list of 200 companies, then we cannot do the parametric statistics. We knew that the list found on the website of the General Consulate of Sweden in China was not complete and it is difficult in the time limit to make a new complete one. So we have chosen a qualitative method, as it is more operational and more controllable. Because of the distance constraint we chose to do it by telephone. The advantages of this method are the speed and the access to the appropriate people. Moreover, business people are more willing to accept a phone interview than a face-to-face interview, which is due to the time required.

We have chosen three models that we wanted to develop with examples from reality. These models are the LR dimensions of Hill, the I-R grid of Y.Doz & Prahalad and the model of LR responsiveness determinants of emerging markets of Y.Luo (2002). Then we set up eight hypotheses that we wanted to test. To complete these models and test our hypotheses, we needed a profound insight into the problems of subsidiaries established in China. We designed interview questions according to the hypotheses and models. Interviews were conducted with managers of Swedish subsidiaries in the Chinese market. The first step of the interview was to test it with some business people to see the validity and the time needed, as well as, to get some comments to improve it. We chose business people having an actual experience in a foreign subsidiary. Their comments helped us to refine and add some questions to avoid incomprehension and to increase the pertinence of the interview questions. Afterwards, we sent the interview questions by e-mail with a cover letter explaining our research to the sample subsidiaries. According to their replies, we have done telephone interviews with managers of the subsidiaries in China.

When you plan to do phone interviews in China you have to take into consideration the time differences and the cost of calling. That is why the first contact with a manager was by e-mail to arrange a phone meeting. The interview lasted around 30 minutes. We stayed as neutral as possible so as not to influence the answers and the analysis. As only few managers answered us after the first e-mail, we started the second step of our

interview process. This step was to call the subsidiaries and get in touch with a manager. Actually, these calls were also not very successful. The first contact in the companies was at the desk office and it was hard to go further even though we explained the purpose of our interview in Chinese. Therefore, we sought to find a direct address of one of the high managers of the subsidiary in order to send the e-mails for the second time. This has included e-mails to the Headquarters to find the correct addresses of the potential interviewee situated in China. In this way, we had more positive replies. At the end of the interview process we had more than 10 different comments from people who have insights into the local adaptation of Swedish subsidiaries. Normally, a case study involves few interviews. We planned more interviews to get more insights of the Chinese environment and to have a higher rate of validity.

## 4.2/ Sample

We focused our research on Swedish subsidiaries in China. We used a non-probability sample. According to Saunders et al., (2006), a non-probability sample means that you do not know the total selected samples and it is impossible to generalise and make statistical inferences. Our goal is not to generalise our findings to all the Swedish subsidiaries in China but to draw a conclusion from the ones interviewed. For a generalisation further researches have to be done. One of the main advantages of the non-probability sample is that the researchers have a total control over the participants. On the website of the Consulate General of Sweden in China, we found a list of around 200 Swedish subsidiaries. Due to the time and financial constraints, it would have been impossible to interview all the subsidiaries and analyse the results. Hence we chose a sample of subsidiaries. We reviewed the entire list and looked at their websites. We did not take into account the companies having no websites. We have carefully collected a sample of 60 companies according to certain criteria. The first criterion was to choose interview participants from Sweden with a managerial function, in order to have a coherent cultural interpretation. The second criterion was that the subsidiaries needed to produce and sell products or services on the Chinese market. The size and the type of industry of the subsidiaries were not included in our criteria. We wanted to have a sample representing all types of Swedish subsidiaries established in China.

### 4.3/ Limitations

This research has several limitations. First of all, we limited our sample to Swedish MNEs established in China. We thought of other European countries for our study and even collected data from European MNEs established in China such as German and French MNEs. Since we study in Sweden and one of us comes from China, we think it is easier to contact China and get feedbacks. Besides, Swedish companies have a reputation for being student friendly, which gave us easier access to interviewees. Since we studied at Kristianstad University, we acquired Swedish culture knowledge. This culture knowledge made the cultural interpretation of Swedish MNEs in China easier. We chose these two countries as the business between China and Sweden is increasing.

Secondly, we limited the number of questions in our interview, since more questions would act as a deterrent to the interviewees and reduce participants' willingness to answer the questions. The goal of this dissertation is to have as much insight as possible. One knows that the longer the interview is the more unwilling managers are to participate, due to the time constraints. Therefore, we limited the interview duration to thirty minutes and to 22 questions.

Thirdly, we had distance and financial limitations. Several subsidiaries in fact suggested that we come to China for a field trip to get valid and reliable data. Since it is far away and we do not have the budget for international trip, this type of study is not realistic for us. If we were in China, it would have been easier to make a more insightful research.

Finally, we also had a limitation in the interview process. We made telephone interview, instead of face-to-face interview, from which we can obtain more information from the interviewees' expressions, body language and longer time.

## 4.4/ Interviews

We adopted a qualitative research method for this dissertation. The method of this dissertation is to carry out with interview survey and qualitative analysis. One described interview survey as a mix of those two methods to collect qualitative data. We designed an interview composed of 22 questions, carefully written, which are based on the literature review, models and our hypotheses. We used a mix of open, probing and

closed questions to design the interview. We divided the questions into six parts. The first part, question number 1 to number 5, gives a background of the interviewed subsidiaries in China. We used closed questions to have specific answers except for question three, which is a probing question. A probing question is used to have a significant response, which has its importance for the research, (Saunders et all, 2006). The next four parts cover the four local responsiveness categories: differences in tastes and preferences, infrastructure and traditional practices, differences in distribution channels and host-government demands, according to Hill (2005). For these parts open questions were designed in order to encourage the interviewees to provide extensive and developmental answers. Open question may be used to reveal attitudes or obtain facts, as well, (Grummitt, 1980, cited by Saunders et al., 2006, pp. 329). The last part (question number 20 to 22) looks for personal opinions about the Chinese environment and how the interviewees see the future. The questions are all open because we looked for personal answers. With closed questions, we can avoid both interviewer and interviewee bias since they describe the facts or situations. However, the open questions increase our understanding of the interviewed subsidiaries.

The response rate was low at the beginning but due to our active procedure, we made finally ten interviews on 60 companies contacted. In total, we obtained 15 replies from the companies. Among them, three were unwilling or not able to participate in our research. Another company was willing for an interview, but the manager was not suitable before the deadline of this dissertation. We received also one interview from a company not anymore established in China, therefore it is ineligible. So, 15 divided with 60, the total response rate is 25%. The active response rate, which is the total of the replies minus the ineligible subsidiaries, is 17%. The likely response rate for such type of interview is usually higher. We were a little disappointed with the low reply rate after we sent the second run of emails and made phone calls. However, the number obtained is above of the minimum required for a case study. This makes our qualitative study trustworthy.

The interview was designed in English since both of us do not speak Swedish and most Swedes speak good English, especially the ones assigned to work in a foreign country. We did a self check and pilot test on several business people.

# 4.5/ Validity

According to Sanders et al., (2006), a case study involves unscientific interpretation. However, it is the best way to explore existing theory and provide new source of research questions. Validity is concerned with the degree of the measurement of what the scholar wants to measure. It includes internal and external validity (generalisability). Here, we discuss about the internal validity of this dissertation. Our dissertation has good face validity as it looks reasonable and well designed.

Our research seemed to have a lack of criterion related validity, or instrumental validity. That means that we did not compare our measure with another measure which has been demonstrated to be valid. We already mentioned that few studies have been made about this field. However, we did refer to the textbooks to know how to design qualitative interview.

The construct validity seeks agreement between a theoretical concept and a specific measuring device. The theoretical concept of this dissertation is local responsiveness. To test the degree of subsidiaries' local responsiveness in China, we adopted the measuring device of interview, which requires lower minimum number of studies and provides unscientific but new insights into existing theories. The interview questions were designed from the models and the hypotheses which were developed from the theories. The results of the interviews were derived from what we found in the literature. The interview device meets the theoretical concept of this dissertation, so this research has high construct validity.

The content validity refers to the degree to which a measurement reflects the specific intended domain of content (Carmines & Zeller, 1991, p.20). The questions of the interview cover all the contents of the phenomenon measured. We designed our interview mostly based on Hill's theory about the four aspects of local adaptation pressure and with other theories. Thus, the intended domain of content is well measured through the interview questions. As we did the interviews, it was possible to give further explanation, to avoid misleading questions. So we can say that the dissertation has high content validity.

# 4.6/ Reliability

Reliability refers to the degree to which the data collection techniques or analysis procedures will yield consistent findings each time it will be applied (Sunders, Lewis, Thornill, 2006, 149). That is to say, reliable measure will not change from time to time. Reliability can be evaluated by the following three criteria (Easterby-Smith et al., 2002:53, cited by Sunders et al., 2006, 149):

- 1. Will the measures yield the same results on other occasions?
- 2. Will other observers reach similar observations?
- 3. Is there transparency in how sense was made from the raw data?

In relation to qualitative research, reliability is concerned with whether alternative researchers would obtain similar information (Saunders et al., 2006, 318). One threat to the data collection reliability is interviewer bias. Bias may arise due to interviewer's comments, tone of voice or interviewer's attempts to impose his or her ideas on the questions (Saunders, 2006, 318). It can also result from the interviewer's own way of interpretation of the response given, in case there is no mutual trust between the interviewer and the interviewee. To avoid bias and increase the reliability of data quality, we did sufficient preparation for the interviews through literature review, discussion with tutor, research participants as well as Internet searching to be knowledgeable about the MNE subsidiaries and relevant concepts. We also tried to be neutral by paying attention to the tone and dictions when we made telephone interviews, in order not to lead the interviewees with our own ideas and comments. In addition, we planned to use audio recording, but due to the unsatisfying quality of the recording, had on-the-spot information saving by typing while listening. Further, right after the interview, we sorted out the information saved to avoid information missing and culturally biased interpretation later on.

One threat to reliability is interviewee bias. This bias can arise because of above-mentioned perception about the interviewer. It can also be the result of sensitivity to some probing questions that the interviewees do not wish, or are not empowered, to discuss with you (Saunders et al., 2006, 318). Another reason of interviewee bias is the nature of individuals or organizational participants. The time-consuming feature may reduce their willingness to give valuable or overall information. To avoid this bias and increase the reliability, we used emails to ask for options between email reply and

telephone interview. Only one company answered the interview questions by email. We tried to set up the interview at convenient time for the interviewees. We had also explained the purpose, themes, and other relevant information about the coming interview beforehand. In order to reduce their anxiety, we promised them the confidentiality of the information they do not want to publicize. Besides, we tried to create a relaxing, friendly atmosphere during the interviews to build a trust with the interviewees. We also tried to control the time spent on each interview.

By taking these measures, we did not encounter the bias as referred to above. We cannot say that the data collection is 100% reliable, but we can say that the data we obtained are quite reliable.

# 4.7/ Generalisability

Generalisability means that your findings may have the same results if you applied them in the same way to other research. Generalisability can be also referred to as external validity (Saunders et al., 2006, 151).

There is an important difference between quantitative and qualitative methods. Quantitative method gives less information but it is more generalizable than the qualitative method. Qualitative method gives more in-depth information but it is more difficult to generalize the results (Alasuutari, 2000). However, quantitative method needs a basis of sufficient numerical size of sample selected to be generalized. For a qualitative method, the generalization to other cases is not necessary and possible. In our research, we used a qualitative method. The purpose of this study is to test the existing theories of local responsiveness in China, to see whether news factors can be found to develop the theory, instead of inferring a new theory from data. To achieve this goal, we needed deep insights from the companies. We interviewed 10 Swedish subsidiaries; therefore the generalization is not possible. On the other hand, our study is not designed to produce a scientific generalization but to draw a generalization of the 10 subsamples interviewed. This research is focused on particulars therefore the "only generalization is: there is no generalization" (Lincoln & Guba, 1979, cited in Case Study Method, 2000).

# 4.8/ Summary

In this chapter, we presented our exploratory research strategy, which is the conduct of phone interviews to obtain empiric data. These data gave us the possibility to develop the models and test our hypotheses with the experience from the reality. Therefore, this dissertation is a combination of a deductive and an inductive approach. We carefully selected the company sample according to some criteria in order to increase the validity of this research. This dissertation as any dissertation has some limitations. The focus on Swedish subsidiaries established in China is one of the main limitations. The interview questions were designed based on the theories and models from the literature. Phone interviews were conducted in order to avoid bias from the interviewers and the interviewees. Hence this research is characterised by its validity and reliability. In the case of qualitative method as interview it is hard to generalize the results as you can do with a quantitative method. The goal of this study is not to obtain a scientific generalization but to draw a generalization based on the sample studied.

# **Chapter V: Interviews of the Swedish subsidiaries**

We have interviewed Swedish subsidiaries for our research. In this chapter, they will be introduced. We will present their environment and why they have chosen to establish on the Chinese market. Finally, their views about the local adaptation in China will be introduced. For this part, we based our analysis on the questions 1 to 5 and 20 to 22.

#### 5.1/ Lawson - Intentia

Intentia was created in Sweden in 1984. In 2006, Intentia merged with the American group Lawson Software to form Lawson. The company operates in 40 countries and has over 4,000 customers. Their operation is business to business. Lawson (initially Intentia) delivers software and implementations services in manufacturing, distribution and services industries. Its service is specialised in different categories as financials, human capital management, supply chain management, business intelligence, and asset management. The company helps its customers to improve their process and develop business performance through their software. Thus, the customers can lower their costs and increase their flexibility. (Lawson, 2006, http://lawson.com)

The company has experiences in emerging markets as they are established in Sri Lanka, Indonesia, Asia, Mexico and East Europe. The objective is to enter markets where their clients are. Lawson established a subsidiary in China almost ten years ago, in 1997. It has chosen China to serve the global market. In fact, China itself represents a huge market with a great potential. The company strategy was to have a global market as soon as possible to provide service to all potential customers. The first step in Asia was the entrance in Singapore, then Hong-Kong.

Mats Hedberg, consultant manager of technique service, was the interviewee of this company. He is established in China since 2004. For him few companies try to establish in China, as it is difficult to understand the environment, which is really different from the Swedish market. The interviewee explained that you have to get acquainted with the Chinese market and adjust to it otherwise you cannot be successful. The culture issue is really strong even though the language matter is decreasing due to

the fact that more and more Chinese speak English. Therefore, there will always be a need of responsiveness. One example of the Chinese culture is their link to their family. They are first loyal to their family. Chinese people are not considered as an individual like in western countries but as a whole part of the family. The interview ended with the question 22, about the main challenge for Swedish businessmen in China. For the interviewee the main challenge is to find the right people, who can help you to understand the client. The need of a good network is really important.

### 5.2/ Nolato

Nolato was created in Sweden in 1938. The company develops and manufactures polymer components and product system for telecommunications, automotive product, white goods, medical technology and other industries. The group has more than 5.000 employees in Sweden, China, Hungary, Estonia, Malaysia and Japan. Nolato sells in business to business. (Nolato, 2006, http://nolato.com)

The company has little experience in emerging markets (Estonia and Hungary). Nolato has been established in China since six years. Nolato Beijing is specialised in the creation of components for mobile phone. It sells their products to other phone companies as Ericsson, Siemens, Nokia (etc.), which are also established in China and ships components to European countries for manufacturing. Nolato chose to open a subsidiary in China to lower the costs. But the main reason was to follow the customers that went to this market. Nolato is a wholly-owned subsidiary, and they have no local partnership.

We interviewed Magnus Lindvall, the Director of marketing and sales in Asia. According to him, you have to adapt to the Chinese environment. If a manager does not try to develop the company by giving employees trust and tools to succeed then, the company will fail. Every businessman has to be aware of the risks and Guanxi. For a better success of a foreign company it is better to run it with a mix of local and foreign staff. According to the interviewee, the degree of local adaptation in China will be higher due to the deep value and tradition nevertheless it is continuously opening. The challenge for a Swedish company in China is to face the aggressive and dynamic environment. The more the Asian companies expand, the more aggressive they become.

In the telecommunication industry, Chinese firms try to compete by shaping their business to be more competitive and aggressive. Most of the Western companies have under estimated the huge competition of local companies. However, it is easier for a company as Nolato, as they can take advantage of the experience acquired from other western companies established there since 20 years. Another challenge is the tie with authority and customers. The network is very important. It will help you to find solutions to the issues faster. The laws are written for the local; therefore, it is difficult for foreigners to understand them. A good relationship with the authorities will help the company because the more they know you the more they will trust in you and make decision in your favour.

### 5.3/ Sandvik

Sandvik is a Swedish company created in 1862. The group Sandvik has 39,000 employees and operates in 130 countries. The company is the world leader of high-technology, engineering advanced products. They are in three core areas:

- cemented-carbide and high-speed steel tools for metalworking
- machinery and equipment for rock-excavation
- stainless and high-alloy steels, special metals and resistant materials

The company is divided in four business areas: Sandvik tooling, Sandvik mining and construction, Sandvik material technology and Seco tools. Sandvik sells in business to business. (Sandvik, 2006, http://sandvik.com)

The firm is established in China since fifteen years (1991). Sandvik has experiences in emerging markets as they are established in 130 countries like India. They moved there to be closer to the customers. Sandvik is a wholly-owned subsidiary

We interviewed, Svante Lindholm, the manager of Sandvik Steel which is a part of the business area Materials and Technology; and he has experiences in all main emerging markets. Sandvik in China does not seem to have encountered difficulties in this environment as they are established there since fifteen years. For the interviewee, Sandvik is already a Chinese company as they are completely adapted. According to the manager, there are two main challenges in China. Firstly, it is a challenge to find and make trade. Secondly, it is the challenge to keep people.

#### **5.4**/ Thule

The story of Thule started in Sweden in 1942. Thule is the world leader of transport solutions. They produce load carriers for cars as roof basket, roof rails, bike carriers, snow chains and trailers. The firm has 3,700 employees in all major car markets (North America, Europe, Africa and Asia). Thule is focused on the final customers but they reach them through retailers. (Thule, 2006, http://www.thulegroup.com)

Thule is established in China since five years. It does not have partnership except a small one for the import. It has set up a wholly-owned subsidiary. Thule chose the Chinese market due to its potential. There is a growing car market so they needed to be established there. It has sales office in Beijing and Shanghai. The company has experiences in emerging markets as East Europe, South America and Dubai. Its target markets are markets where there is a boom of the car industry and vacation trend. Therefore the emerging markets shall be at the latest stage of their development. Thule is situated in a niche market. Actually there is no real business opportunity but the market is going to develop quickly in China.

We interviewed Peter Kral, the vice president of business development. According to him, local adaptation will be higher in the future due to the dimension of the developing market. In the industry of Thule, the tradition aspect is not a cause of the local adaptation. The need for local adaptation is generated by the stage of the development of the Chinese market. For instance, the Chinese people need to have a car, a good road infrastructure and vacations. The challenge for a Swedish businessman who is in a niche market is to create a category of product and explain it. Thule needed to rewrite the logo and create a new name because of the language translation. There are no words in Chinese to explain their products. The constraints of the laws, regulation, Guanxi and the dictatorship are other challenges. An addition, the challenge is to find a way to fit the product with the society and the Government. Since China is a huge market, you have to be aware of the dimensions and the potential of the environment.

### 5.5/ Stora Enso

Stora Enso is the merger of Enso a norvegian-finnish company with Stora a Swedish company in 1998. Stora Enso produces publication, fine paper, packaging board and

wood products. The group has 46,000 employees. The company sells mainly in business to business. It set up their own local presence with sales and marketing network in 40 countries. Its customers are publishers, printing house, merchants, and packaging joinery and construction industries. (Stora Enso, 2006, http://www.storaenso.se)

Stora Enso created its subsidiary in Beijing in 1998, but before it had set up another subsidiary in Hong-Kong in 1985. The firm has set up a joint-venture where the capital share parts are more and more important for it. It went to China in order to lower the costs and to be closer to the customers. They have various experiences in other emerging markets as they are established in South America, Russia and India.

Markkus Pentikäinen, the interviewee, expects a higher need of local adaptation due to the long tradition in China. The biggest challenge for a Swedish businessman is to be well prepared in advance before to enter this market and use local services. The Chinese market is faster and the environment is more risky.

#### 5.6/ IKEA

IKEA is a world leading furniture manufacturer and retailer. IKEA was created by Ingvar Kamprad with the help of his father in 1943. Now, IKEA headquarter is in Älmhult, southern Sweden. IKEA has set up 237 franchising stores in 35 countries and employ 110 000 persons. The number of visitors of all IKEA stores worldwide in 2006 was 504,154,000. IKEA's concept is to offer a wide range of well-designed and functional home furniture products at prices acceptable for as many people as possible in the world. IKEA has adopted a global strategy. (Ikea, 2006, http://www.ikea.com)

IKEA started its business in China from Qingdao in 1989. But the operation of IKEA stores in China is quite recent. Shanghai, Beijing and Guangzhou were all set up after 2000. IKEA Chengdu is coming up. Today, China has become IKEA's top purchase country. At the beginning, they entered with a joint venture followed by acquisitions later. IKEA has chosen China for the lower costs. Before, IKEA did not have much knowledge neither about China nor about other emerging markets, since most of its overseas markets are in developed countries.

Thomas Ronnbolm was our interviewee. He used to be a regional market manger in IKEA Guangzhou, with 6 years experience in China. Now he came back to work in the IKEA headquarter in Amhult. According to Thomas, the major differences in doing business in China are time, distance and culture. Time and distance make the contact with the main office inconvenient, the employees' travel longer and slow down the supply of goods. He detailed the problem of cultural distance. For him, culture is very important for doing business in China. He said that IKEA China had always tried to find a balance between "think globally and act locally". They do not bribe to obtain more business opportunities. As he predicted that the local responsiveness in the future will be lower as China is getting more and more international. In conclusion, he thinks that there are many disadvantages to do business in China but at the same time it is still a big potential market. The main advantages are the salary costs, availability of raw materials, and the large supplier base. The challenge of doing business in China is the difficulties in finding the right partner because there are too many options. Other challenges are the vague legal system and the issues concerning corruption, product quality, culture and environment.

### 5.7/ Lorentzen & Wettre

L&W was founded in 1895 and is located in Kista, Sweden. It is the leading manufacturer of equipment for quality control and process optimisation for the paper industry world wide. L&W employs a total of 185 people. It has subsidiaries in USA, France, Canada, etc, and is represented in 35 other countries by distributors and agents. (L&W, 2006, http://lorentzen-wettre.com).

L&W set up its subsidiary two years ago in China, but it has fifteen years of experience in agency. Its global operation and success elsewhere encouraged it to choose WOS as its entry form in China. L&W came to China due to the big sale of mills in this area. It sells in B2B, and the main customers include pulp and paper mills, suppliers to pulp and paper mills, research institutions and so on.

Patrik Stophe, the general manager in China, answered our interview. According to him, L&W needs to stick to its goals and global strategy. However, it is important to react to the changes at the same time. As he predicted, it will be less adaptation in China. The rest of the world has to adapt to China and China has to adapt to the world mutually.

In conclusion, he thinks that it is not easy at all to do business in China, if you only think it is growing. Problems seem to be endless, for example, you have to be prepared for a lot of paper work to establish there, and even afterwards, there are still other new barriers to overcome. You have to be patient.

### 5.8/ Exir

Exir was founded in Sweden in 1985 and was acquired by its present owner in 1992. During the past ten years the company has developed well with an annual growth of more than 20%. The Exir Group consists of two production units, in Värnamo Sweden and Mezökövesd in Hungary and a purchase and sales department in China. Exir manufactures turned and milled components in the most of the processable materials and dimensions. (Exir, 2006, http://www.exir.se).

Exir China mainly produces the products that do not suit the headquarters' current machines. Exir has been in Beijing for 8 years and started its Wuxi factory in 2006. Exir China is the first emerging market of Exir, so it has no previous experience in other emerging markets. But the general manager in Wuxi has much experience in China. Exir came to China because of the market potential and lower costs. It sells in both B2B and B2C. They also chose WOS as the entry mode. Exir's main customers include BT, ABB, Tetra Pak, Siemens and other big MNEs. They do both selling in China and exporting. Lars Darwell, the general manger of Exir China, accepted the interview. According to him, the local responsiveness in China is hard to predict, because China has not executed a lot of regulations and laws yet.

In conclusion, doing business in China is fun, interesting and complicated for him. In his explanation, the complexity of doing business in China means they face unequal competition with the local companies. Local companies can solve problems without considering laws and they can communicate directly with the authorities since they have already established good relationships.

# 5.9/ Höganäs Aktiebolag

Höganäs has origins in coal mining, bricks and pottery, but today it focuses solely on metal powders. This company has a history of 200 years but its path to become the largest producer of metal powders started with the introduction of Hoganas Sponge Iron in 1910. The Company develops, produces and markets iron- and metal powder as well as non metallic raw materials in powder form. Furthermore, they administer real estate, securities and conduct other business connected hereto. It has established on the main continents in the world. (Höganäs, 2006, http://www.hoganas.com)

Hoganas entered China over a decade ago. It came to China to sell more of its products with some knowledge about the Chinese market in 1993 and experiences in other emerging markets like India and Brazil. It set up both Joint venture and wholly owned subsidiaries. It sells only in China and in B2B. Olof Andersson, the application manager, accepted our interview. He has extensive working experiences in China. According to him, the new factor about local responsiveness is the speed of their response to the customer needs which shall be quicker. An addition, some Swedish formalities are not required. He thinks that his company needs stronger adaptation for more business.

In conclusion, he thinks there is a common belief outside and inside China that products must be cheaper because they are from China. In the future that irrational reason will not be a valid argument anymore when prices for export rise and less Joint Ventures come to China. Besides, he thinks that small companies/customers/ J.V. partners have a different or insufficient understanding for economies/ calculation.

### 5.10/ SCA

SCA (Svenska Cellulosa Aktiebolaget) was founded in 1929 by Ivar Kreuger in North Sweden. SCA is a good and paper company developing, producing and marketing personal care products, tissue, packaging solution, publication papers and solid-wood products. The company has 51,000 employees in 50 countries. Their main customers are global companies as Sony Ericson, HP, Ikea, Canon...(SCA, 2006, http://sca.com)

SCA has established a subsidiary in China in 2002. The firm started with a joint-venture until 2004 where they bought the capital share parts of their partner to set up a WOS.

The company chose China mainly to follow their customers. It has experiences in other emerging markets as South America, India and other Asian countries.

Rijk Schipper the president of the Asia area, answered to our interview. He has worked in China since two years. According to him the need for local adaptation in China is as high as in other countries. In every new market you have to adapt and understand the environment. The local adaptation is the ultimate condition to success in an emerging market. For the interviewee, the need for local adaptation in the future would be as high as it is nowadays. The Chinese customers are more and more influenced by western products. However, it is a challenge to establish there. Firstly, you need to be flexible enough to face the changing environment. Secondly, you have to stay in line with the mother company. The last challenge is to have the right partners who can speak English and have business competencies.

## **5.11**/ **Summary**

We have interviewed ten Swedish subsidiaries which operate in China. Those interviews gave us a great insight of the adaptation of these subsidiaries on the Chinese market. Mainly, the Swedish subsidiaries studied are operating in the engineering, machinery and technology industries. According to the I-G and industry types, these industries do not need a high adaptation. In the next part we will analyse the interviews and test our hypotheses to see if the theories fit with this sample and whether there are new insights.

# **Chapter VI: Analysis**

In this chapter, we will analyse the answers of the interviews and point out the important factors of adaptation in the context of the Swedish subsidiaries established in China. Afterwards, we will either reject or accept the hypotheses and develop our models.

## 6.1/ Analysis of the interviews

In order to analyse the degree of local responsiveness of the subsidiaries studied, we have ranked them. Our interview is designed according to the theories. We have seen in the theoretical part that local responsiveness is mainly related to five dimensions: product customization, distribution channel, business practices and culture, competition intensity, and host government demands. We have added one dimension, the organizational structure which seems to be an important aspect for the investigated subsidiaries. For each dimension, we have graded the interview questions according to the companies' answers. Each dimension has a maximum of three points. Three points means that the subsidiary is well adapted in this investigated dimension. The highest total score possible for each subsidiary is 18 points. We will present the results of each dimension in the following part.

#### **6.1.1 Product customization**

The analysis of the product customization dimension is based on the interview questions n° 6 & 7. The scale system is divided into four categories: no, minor, some and high customization. When a company did not customize a product before entering the Chinese market, it obtains zero point. When the product is slightly modified to encounter some standards (e.g. electricity standard), the subsidiary has minor customisation, so the firm obtains one point. Some means that the product has been customized with cheaper materials and/or has had to meet the government requirements. The points gained here is two. High is when the company has made a total product customization to attract the Chinese customers. Therefore, the firm has a high

customisation degree, which gives it three points. The table 1 in the appendix shows the answers of the companies and their scores.

Three companies have a global strategy; that is why they did not customize their products. Moreover, these subsidiaries are operating in a high technology industry; therefore, as we explained in the literature their need of product adaptation is low. Two made few changes in order to adapt to the Chinese standards (such as, the adaptation to Chinese electricity system or adapting the logo). These two subsidiaries have a global strategy, that is to say, that they integrated and standardized their products. However, they need to be responsive to the local practices. Another one is currently in the process of their products customization. Three companies have some product changes because of cheaper materials and government requirements. Only one company has a high degree of product customization. This subsidiary's product is customized because of the customer demands.

To sum up, 30% of the subsidiaries studied did not change their products, 60% made some changes and only 10% made total changes to meet the demand of local customers. The product customization is not high for the subsidiaries investigated. Moreover, the main reasons for the product customization are not due to customers' taste differences but to cost reduction, government requirements and Chinese standards.

### **6.1.2 Distribution channels**

The distribution channels dimension refers to the price strategy, the product position, and the distribution channels, according to the theories. In order to rank the level of adaptation in the distribution channels, we graded questions n° 8, 9 and 10. When there is no different product position, no distribution channels adaptation and no price differences the subsidiary obtains 0 point. When there is differentiation in these aspects, they obtain 1 point for each adaptation; and the maximum grade per firm is 3 points (i.e. appendix table 2).

40% of the companies did not change their distribution channels, price strategy, and product position. 10% made a total adaptation in this category (subsidiary n° 7). Mainly, this subsidiary has a higher product position due to the recognition of the Swedish products. As China is a price sensitive market, this company also lowered the prices by

reducing the costs and it used special agents to sell the products. Two subsidiaries have 2 and 2.5 points. For both of them their product positions are higher due to the superior quality of the Swedish products and they have also lowered the price. One of them did not change the distribution and the other one had to create its own distribution channels. The subsidiary n°2 obtains one point as they just changed the product position. This subsidiary finds it has a lower product position because the lower product quality is caused by the lack of competence in the Chinese manufactory. The last subsidiary (n°10) only changed its distribution channels to be adapted to the fast changing environment.

To conclude, most of the subsidiaries did not adapt their distribution channels to the new environment. We can also explain this by the choice of the entry mode. Indeed, most of the subsidiaries operate in a WOS, which involves no need for distribution channels adaptation to the one used by the partner, like it is in a JV. The Swedish subsidiaries sell their products to other western MNEs. Therefore, they do not change their price strategy, which is similar with the Swedish market. When there is a different product position, it is caused mainly by the different perceptions of the product between the two countries.

# **6.1.3** Government demands

The government demands dimension is based on the questions  $n^{\circ}$  13, 14 & 15. According to the answers, we give 1 point to the subsidiaries having specific demands from the government. If there is a conflict or they do not respond to the demands, it is 0 point. If they argue in order to find a compromise with the government, they gain 1 additional point. If they obey they obtain 2 more points. (i.e. appendix table 3)

There are only three companies that do not have specific demands from the government. For two of them, the reason is that the Chinese government encourages their industry. For the third company, the cause is that there is no existing law concerning the regulation of their product. Therefore, each region of the country has its own arbitrary judgement. Most of the subsidiaries agree that they have to obey the authorities in order to succeed in this market, and to make sure not to put the mother company in trouble. Only one tries to discuss and find conciliation. For this aspect the need of a good network is very important. The government demands are various. For two companies,

these demands concern the export, and for the others, it concern specific local requirements.

The local policy requirements are important in China. Most of the subsidiaries have to respond to these specific demands, which could create some business barriers. However, the government encourages some industries in which they can gain economic development.

### **6.1.4 Business practices and Culture**

In order to analyse this dimension, we refer to the questions n° 16, 17, 18 & 19. The subsidiaries listed business differences. They gain 0 point if they have not made adaptation to these differences; otherwise, they obtain 1 point. The subsidiary that thinks culture is not important gains 0 points, 1 point if it thinks it is important, and 2 points if it is very important.

The table 4 (i.e. appendix) shows the high need for adaptation concerning the culture and business practices. The business practices are various and can be explained by the culture distance between the two countries. The major difference between the two countries is the general environment of China. Five companies answered that it is difficult to do business in China due to the size of the market, the volatility of the environment, the state policies and the immature market. Four companies meet difficulties with Guanxi and four others with the necessity to have a good network. All the interviewees agreed on the importance to know the environment, including the culture, to succeed in China.

To sum it up, business practices and culture seem to be the dimension asking for the highest degree of adaptation. Sometimes it is difficult to understand the different practices; however, to be successful in a market you have to understand and adapt to it.

### **6.1.5** Competition intensity

The competition intensity dimension refers to the availability of substitutes on the market. According to the literature, the more competitors the more substitutes are on the market; therefore, there is more need to adapt the product/service. For this dimension

we base our analysis on the questions n° 11 & 12. We have divided the answers in accordance with the intensity of the competition in each industry into four categories. When there are no competitors on the market, the subsidiary obtains 0 point. When there are less than five direct competitors, the subsidiary has a low number of competitors and gains 1 point. When there are between five to ten competitors, it gains 2 points; and 3 points when the number is over ten (i.e. appendix table 5).

There are two subsidiaries with less than five competitors and four have the highest degree of competition. The big companies as Ikea, SCA and Sandvik face an intensely competitive environment. All the main multinationals are established in China and the Swedish subsidiaries investigated compete with them. Most of them have moved to China to follow those MNEs that are their major customers. They have few real local competitors. The Chinese firms are numerous but they are still at an early stage. Therefore, they do not have the experience and competency of the Swedish firms in these industries. However, the Chinese firms are growing quickly, and it is a question of some years before they will level up their gap.

Moreover, the Swedish subsidiaries are distinguished by their product/service quality and their knowledge about their industry. Most of them are worldwide leaders in their business. One subsidiary said that their product differentiation is their level of product adaptation.

### **6.1.6 Organizational structure**

Organizational structure is composed of two factors, the management style choice and the percentage of Chinese employees (questions n° 18 & 19). The subsidiary that has chosen a management style with western practice training, gains 0 point; the subsidiary that has chosen a mixed style, gains 1 point; and the subsidiary with the Chinese style, gains 2 points. Furthermore, the subsidiary that has a percentage of Chinese employees over 80% in the subsidiaries gains 1 point, otherwise, just 0 point.

From the table 6 (i.e. appendix), we have found an interesting phenomenon, which is that all the Swedish subsidiaries have a very high percentage of Chinese employees. In terms of the organizational structure, three have chosen to adapt their management to the Chinese style with local managers. Five have very little adaptation. They have

increased their communication and used a mixed management style. Two subsidiaries did not adapt their management style due to the strong corporate culture. The reason obviously is related to the headquarters' global strategy. One interviewee said that they know in which way to act and are not allowed to do things differently than the headquarters.

In conclusion, 80% of the subsidiaries have adapted their management to the new environment. The high percentage of local employees shows the Swedish subsidiaries willingness of adaptation and recognition.

## **6.1.7 Degree of local responsiveness**

The table below represents a summary of the overall degree of local responsiveness of each subsidiary according to the dimensions studied.

N°	Company Name	Customization	Distribution channels	GOV DEMANDS	Business practices & culture	Organizational structure	Competitors	TOTAL
1	IKEA	1	0	3	3	1	3	11
2	L&W	0	1	3	3	1	1	9
3	Exir	2	0	3	3	2	2	12
4	Haganas	0	0	2	2	2	3	10
5	Nolato	3	0	0	3	1	2	9
6	Sandvik	0	1	0	2	3	3	9
7	Storaenso	2	3	3	3	2	2	15
8	Thule	1	2,5	0	3	3	1	10,5
9	Intentia	2	2	3	3	2	3	15
10	SCA	1	1	3	2	3	3	13
	Total	12	10,5	20	27	20	23	113,5

Table 6.1: Degree of Local Responsiveness of the Swedish subsidiaries sample

This table reveals that two principal dimensions generated a need for local adaptation. They are the business practices and the competition intensity. The theories about local responsiveness mention that the number of competitors increases the need of adaptation, especially the local competitors. In the case of China, the assumption does not fit the environment. All the main competitors are western companies and only few Chinese firms compete at the same level of the Swedish subsidiaries. This is due to the gap between the two markets. Chinese firms are still at an early stage of their development.

Therefore, the Swedish subsidiaries do not need to increase their level of adaptation, yet because of the lack of local competitors. However, in the future it will change as the Chinese firms are developing quickly. One company also talks about the copying problem.

The figure below represents the total degree of the local responsiveness of each subsidiary investigated. There are two companies with a high degree of adaptation (15 points on a total of 18 points). The reason, for these subsidiaries, is that they have a low need of responsiveness in the product customisation, distribution channels. There are no subsidiaries with less then the average (9 points over maximum points of 18) and four are on the average. The average of the degree of local adaptation of the investigated subsidiaries is 11.3.

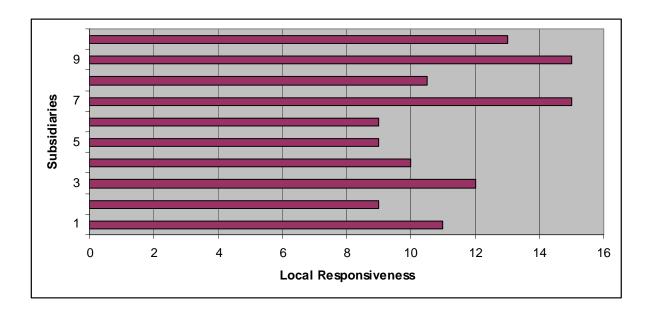


Figure 6.1: Degree of local responsiveness subsidiaries 1 to 10

#### 6.1.8 Conclusion

In this part, we have carefully analysed the interview answers of the investigated subsidiaries. According to the companies, the degree of adaptation differs. The product customization is the dimension that needed the lowest degree of responsiveness. This is due to the type of the Swedish subsidiaries industry and the global strategy adopted by some of them. Most of the subsidiaries are in high technology industries; therefore, it is difficult to adapt this kind of products. The adaptation to the distribution channels is also low. One can explain this phenomenon with the type of industry and the production

established in China. Moreover, the Swedish subsidiaries sell in business to business. Their main customers are the other western companies established in China. The Swedish subsidiaries came to China mainly in order to follow those customers. Most of the subsidiaries have adapted to the local market in order to succeed, especially in these two dimensions: government demands and business practices. The government demands dimension shows a very strong need for adaptation. The Chinese market is not yet a real free market. The government still plays an important role. In other words, the government is the maker of the game rules. These needs for adaptation sometimes involve some difficulties because of the different understanding of the market and the business practices.

## 6.2/ Analysis of the hypotheses & models

Based on the analysis of the interviews, we will test our eight hypotheses in this section. These hypotheses are founded on the models that we want to apply (Hill, 2005; Doz & Prahalad, 1989; Y.Luo, 2002).

#### **6.2.1** Analysis of the hypotheses

H1: Having a previous experience in emerging markets is positively associated with LR According to this assumption, a company's experience and knowledge about emerging markets will increase its level of adaptation in China. To test this hypothesis, we compared the numbers of experience in other markets of each MNE and the years operated in China with the degree of LR calculated in the interview analysis.

The table H1 (i.e. appendix) shows that the companies with fewer experiences in other markets and with few years of activity in China have a lower degree of local responsiveness. For instance, company n° 5 is established in five other countries and has six years of experience, its degree of local responsiveness is lower than that company n°9 which has nine years of experience and is established in 40 countries (respectively 9 and 15). Another example is company n° 2 which is established in 35 markets and in China since two years. Its degree of LR is only 5 points. Company n°1 is also established in 35 countries but has more knowledge of the Chinese market since they have established there for 17 years. Therefore, its degree of LR is 11 points. However, company n°10 is established in China since only four years and has a high degree of

adaptation (13 points). We can explain its local adaptation by its local management. Therefore, the first hypothesis is not rejected to some extent.

#### *H2: An established network facilitates the LR.*

According to the theory, the need of a network is really important in China to deal with the government. To test this hypothesis we have compared the degree of LR with the government demands and business practices dimensions and the mode of entry. The mode of entry in a new market (FDI) has impact on the need of a network. A WOS will require less degree of network, as the company does not have local partners to enter the new market (i.e. appendix table H2).

On ten subsidiaries interviewed, eight mentioned the need of a good network in business. The network is also needed to deal with the government. The three companies (n°5, 6 & 8) without specific demands have the lowest degree of adaptation. Moreover, the two companies (3 & 7) that have established a JV need a high degree of responsiveness (respectively 12 & 15 points). The set up of JV means that you have a network as you have a local partner. Therefore we do not reject this hypothesis.

#### *H3: The cultural distance between Sweden and China has a high impact on LR.*

According to the Hofstede theory, Swedish culture and Chinese culture differ in the five dimensions. These differences will be embodied in business practices and management styles. All the interviewees think that the cultural distance plays an important role in their business. Four companies highlighted that good relationships with the government and the customers are very important. Two other ones said that it is important to know the Chinese history and language in business. This shows the importance of the culture and the tradition for the Chinese people. Two subsidiaries pointed out the difference in business practices and the situation in China. The customers life is very different from western countries; therefore, the subsidiary needs a higher understanding of their way of life to know how, when, where and to whom to position the products. One subsidiary mentioned the importance of adapting their management, especially in the decision-making process because of the cultural differences. For instance, in Sweden the rule is the person closer to the problem solves it. While in China, you have to go all the way to the top. Another example is the difference in staff initiative. Chinese staffs tend to show less initiative than the Swedish ones. The Chinese society values hierarchy while

Swedish society values equality. This is reflected in the Chinese and Swedish organizational structures. Swedish firms have a flatter structure than Chinese companies. Concerning the initiative aspect, the Chinese society does not encourage people to have individual achievements. Sweden is a more individualistic culture where personal initiatives are more appreciated. All the interviewees need to increase their knowledge about the culture differences and integrate this into their business practice. Therefore, we do not reject this hypothesis.

#### *H4: The type of industry influences the degree of local adaptation.*

According to the model 3 from Daniel & al. (2004) the type of industry has an impact on the local responsiveness. To test this hypothesis we have applied this model to our studied subsidiaries. We placed the companies into the I-R grid focus on the type of industry. Then, we compared their position in the I-R grid with their total degree of LR (graph 6.1.7). We can observe some differentiations.

HIGH  I N T G R	Sandvik Hoganas Thu	Nolato Exir Stora Enso L&W SCA	Standardization and central control are imperative across international operation
T I C N	Intentia IKEA	No studied companies in this category.	Standardization and central control are useful but not necessary across international business

*Figure 6.2: adaptation of I-R grid, types of industries (Daniels & al, 2004)* 

This hypothesis is true for Stora Enso, SCA and Exir if we looked at their LR degree. These three subsidiaries have total scores of LR of 15, 13 and 12 points respectively. This is reflected in the application of the I-R grid above. For the seven other companies, the type of industry is not the main reason of LR. We did not find link between the

industry and the total degree of LR in this I-R grid. We conclude that the type of industry is not the main reason for local adaptation. Therefore we compared the type of industry with the degree of product customization. We did not find links between them either. Hence, we presume that other factors have to be taken into account, such as the government demands, the organizational structure and the like. Thus, we reject this hypothesis.

## H5: The more the market is segmented, the higher is the need for LR.

We know from the theories that China is a highly segmented market. The demand is heterogeneous. Firms have to adapt to different customer needs and preferences. Only one company (Nolato) said that they have to adapt their product depending on the customers because the market of this industry is segmented. For the other subsidiaries the market is less segmented as they operate in a specific industry demanding few product adaptations and segmentation. Therefore, H5 is rejected.

#### *H6: The higher the competition is the higher is the need for LR.*

According to the theories, if a company has more domestic and international competitors, its need for adaptation will be higher in order to keep local customers and business (i.e. appendix table H6)

The international competitors are numerous in China, as all the main MNEs are established there. Therefore, the international competition is intense and the need for product adaptation should be high. However, some Swedish subsidiaries have a global company strategy involving the standardization of their products all around the world (n°1 & 6). Others have to follow international requirements (standards) like the safety and protection of the environment (n°2). Some companies have customized their products to reduce the cost with cheaper materials (n°3 & 7). Thus, the firms are adaptive to the price sensitive Chinese market and are more competitive.

The local competitors are also various depending on the industry. Nevertheless, they are still behind the Swedish firms due to the gap between the two markets. For example, L&W mentions that Chinese companies are 50 years behind in the paper industry. However, Chinese firms are growing quickly. We can expect that in few years the local competitors will catch up the Western companies. Therefore, the need of customization

will increase because the Chinese standards will not be the same. Moreover Chinese companies will know more about the needs of the final customers as they share the same culture. As a result, they will have a competitive advantage over the western companies. Another cause of competitive advantage may be due to the copying problem.

As the subsidiaries did not yet adapt their products to the competitive environment, we reject this hypothesis.

H7: Component localization policy is one of the most important government demands that determine the degree of LR.

We assume that local policy drives up subsidiaries adaptation. To test this hypothesis we compared the questions about the government demands in each industry. (i.e. appendix table 7)

Except three subsidiaries, all the companies face specific demands from the local authorities. The three companies (n°5, 6 & 8) without specific demands have a lower degree of LR. Therefore we do not reject this hypothesis.

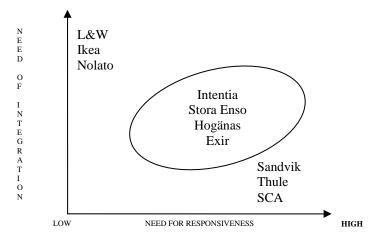
H8: Environment complexity increases the requirement for LR

The interview result shows that most of the subsidiaries encountered some difficulties to face the complex environment. This complex environment is characterized by the corruption, the unclear legal system, the market size, the fast and risky growing environment, as well as, the different level of the market comprehension. Consequently, among ten companies, six think that the environmental complexity is a real challenge while doing business in China. As a result, they have to understand and adapt to it. This indicates that the environmental complexity increases the need for LR in China. Thus, we do not reject this hypothesis.

## **6.2.2** Adaptation of the models to the Chinese market

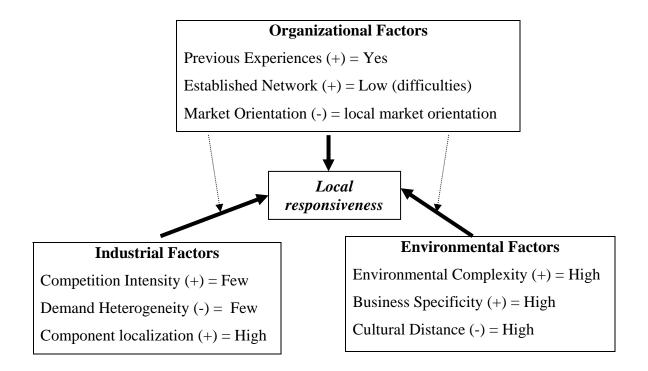
Model 1: I-R Grid: strategic focus and organizational adaptation (Doz & Prahalad, 1986)

As we find that the organizational structure is an important aspect, we applied this I-R grid.



This grid shows the organizational structure adaptation of the investigated subsidiaries. We can see that four subsidiaries out of ten have a middle degree of adaptation. L&W, Ikea and Nolato are more integrated. The most adapted subsidiaries are Sandvik, Thule and SCA. To sum up, according to our investigation the Swedish subsidiaries are aware of the need for organizational structure adaptation. This grid helps to understand the importance of this dimension as we mentioned in the interview analysis.

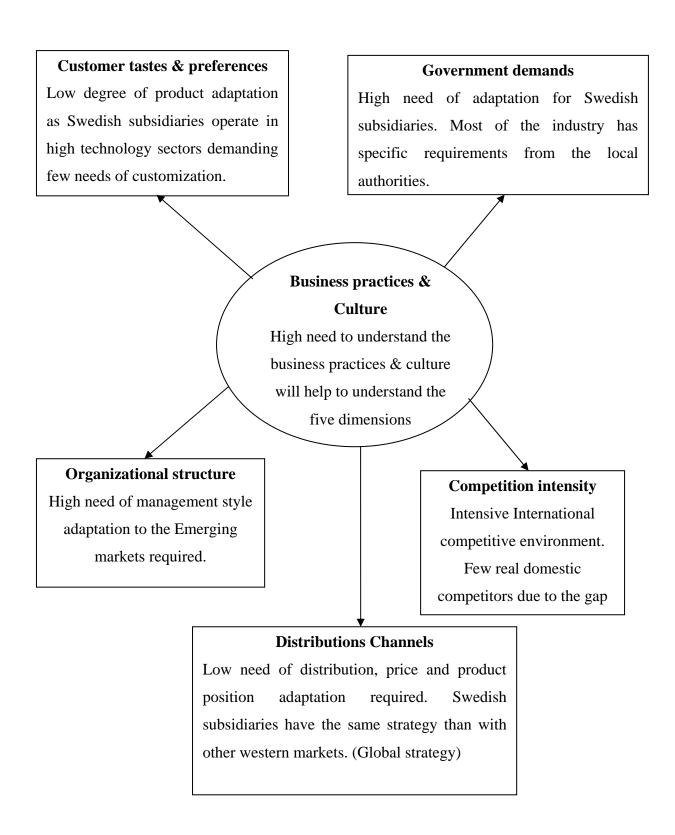
Model 2: Determinants of local responsiveness in emerging markets (Y. Luo, 2002)



This figure above shows the level of the LR determinants of the Swedish subsidiaries. The factors have been explained in the theoretical part ( $n^{\circ}3.2.1.5$ ). We have also tested these factors in our hypotheses. Regarding the organizational factors, the investigated Swedish subsidiaries need to be more responsive concerning the establishment of the network, and therefore, increase their business practices knowledge. Concerning the environmental factors, the subsidiaries try to be more responsive. They are aware of the environment complexity, the business specificity and the cultural distance, as the culture issue is very important for them. Finally, the infrastructure factors show that the Swedish subsidiaries have to be more responsive concerning the component localization. The two other categories do not seem to subject to adaptation concerning our findings.

#### Model 3:

The theory of Hill (2005) emphasizes four aspects of LR. The research findings reveal that for the Swedish subsidiaries established in China the main aspect generating a higher degree of LR is culture & the business practices. Another important aspect, not clearly interpreted by Hill, is the organizational structure. These two dimensions are the results of the culture distance between the two markets. Indeed, the higher is the understanding of the cultural differences and business practices, the more the firm will increase its responsiveness. Without these understandings, the firm cannot be properly responsive to the four other dimensions. It cannot catch the customer's attention, establish a good relationship with the government, set up a distribution channels and understand the infrastructures differences. Therefore, we have developed his model to our investigated subsidiaries by adding these two dimensions. To develop this model, we also based our findings according to the LR determinant of emerging markets model n°2. We put the culture and business practices in the middle, as it is the central dimension influencing the need for responsiveness in the other dimensions. All the dimensions interactively influence each other. The model 3 below represents our findings.



Model 3: New model of Swedish subsidiaries' Local Responsiveness in China

# 6.3/ Summary

In this chapter, we analyzed the dimensions and the degree of local adaptation of the investigated subsidiaries based on the chosen theories and interview results. We know from the theory that local adaptation covers six dimensions. In our findings, we confirmed that these dimensions did influence the overall degree of LR. Among them, we found out that two dimensions were very important to the degree of LR within our sample. These two dimensions are business practices and organizational structure. Furthermore, we tested our eight hypotheses based on the interview results in order to confirm or reject them. As a result, we confirmed that the degree of local adaptation is influenced by the previous experiences in other emerging markets, the need for a strong network and need to respond to the specific requirement of the authorities. The cultural distance and the complex environment of China have also influenced the degree of LR. In the next step, we developed a new model by applying the models of Luo and Hill's theory. We have emphasized the impact of the culture & business practices on the other dimensions. As we explained, without understanding of the culture & business practices, it is difficult to respond to the customers' needs and the government requirements. It is also difficult to adapt the distribution channels and organizational structure. It is also difficult to know the local competitors as well.

# **Chapter VII: Conclusion**

In this chapter, we will conclude the dissertation. A summary will be given first, and then the modification of the models will be presented. Further research suggestions will be introduced, as well. Finally, the practical implications for this research will be put forward.

# 7.1/ Summary of dissertation

The first step of this dissertation is to have an overview of the LR phenomenon. MNEs have two strategic choices when they establish in a new market. The first one is to adopt a global strategy due to a pressure for costs reduction. The second one is the multidomestic strategy because of a pressure for local responsiveness. There are debates between various authors concerning this choice. Authors such as Dickens and Dunning talked about the pressure for global integration. Hill, De Witt & Meyer and some other scholars talked about the pressure for local responsiveness. There are different dimensions influencing the degree of LR which are: customer tastes and preferences, host government demands, distribution channels, infrastructure, the business practices & culture, the organizational structure, and the competition intensity.

The choice between more adaptation and more integration will be more important to MNEs when they consider entering an emerging market. Therefore here, we have answered our first research question which is about the overview of the phenomenon of LR.

An emerging market is a special market characterized by its early stage of development. Emerging markets are open to foreign direct investments and they have an important liquidity and size. (Alberta Finance, Heritage Fund Glossary, [http://...1]). According to Y. Luo (2002), the emerging markets possess four attributes. The first one is the weak and incomplete legal infrastructure, which is impeded by political, social, historical, and cultural factors. The second one is the weakness in the market and institutional support needed for economic development and business growth. The third one is the

uncertainties and volatilities of the fast economic growth of emerging markets. The fourth one is the appearance of a middle-class consumer (e.g. in China and India). An MNE whishing to open a subsidiary there needs to be responsive in order to fulfil the specific requirements of those markets.

One says that the main difficulty encountered by a MNE entering a new market is its ability to understand the new environment and to react accordingly. Furthermore, it is more difficult for Western companies to understand the environment of an emerging market. For the reason, that the differences between both markets are huge. The question is, who has to adapt, the MNE or the host country? The answer will depend on the company's strategy and the market it entered.

The Chinese market is one of the emerging markets, which possesses the commonalities of other emerging markets, as well as, some special attributes. The first attribute characterizing China is its old and strong culture and tradition. The second one is that China has a political, legal, economical and social environment embedded by a communist party. China is at a stage of dynamic changes and deepening reforms. The last but not least characteristic of this market is its big size and largest population (1.3 billion). Moreover, 25% of its population has an increasing purchase power. These characteristics will have some effects on companies that desire to establish their business there, for instance Swedish firms.

In order to test the theories, we designed an interview to know the degree and the dimensions subject to adaptation of the ten interviewed Swedish subsidiaries. Based on their answers, we ranked the degree of responsiveness. From the analysis and the test of our hypothesis, we can answer our last three research questions.

What are the main dimensions subject to adaptation in China and their reasons?

The most important dimension subject to adaptation is the culture and business practices. China is a country with a long history and a strong culture. In addition, the immaturity and the underdevelopment of the market cause some special business practices.

The second dimension for adaptation is competition intensity. Nowadays, the main competitors for the studied Swedish subsidiaries are from other western MNEs due to the early stage of the domestic competitors. However, with the development of those domestic competitors, they will face more intense competition from domestic and international sides.

The next dimension for adaptation is the government demands. As China is still not a real free market, the government plays an important role in the MNES' business. Therefore, the subsidiaries have to build their own network in order to respond to the specific government requirements.

We also found out an important dimension, which is not detailed by the theories. All the interviewed subsidiaries have more than 80% of local employees. As a result, the Swedish managers have to adapt their management style in the long run. We categorized this aspect as the organization structure dimension and used it to develop our model.

From the stated hypotheses new factors were identified. These factors improve the degree of adaptation of the subsidiaries.

The more a subsidiary has an experience in other emerging market and the more it has experience in China, the more it will have good understanding of the particularities of the emerging market environment. Therefore, the subsidiary will be more responsive. With a strong established network, the subsidiary will be more ready to adapt itself as it will have local partners, which will help them understand the environment and practices.

What will be the new model if there are new factors concerning local adaptation?

We have created a model specific to the Chinese market. This new model shows the importance of the knowledge of the Chinese culture and business practices in order to succeed on this market. This understanding will help the Swedish MNE establishes in China to attract the local customers, respond quickly to the government demands, be aware of the competition intensity, set up an efficient distribution channels and have an adapted organizational structure.

What would be the trend of adaptation for Swedish subsidiaries in China?

To answer this research question, we need to look from two perspectives, which are the environmental changes in China and the prediction of the trend of local responsiveness of the interviewees.

Concerning the environmental changes in China, it is hard to predict in detail. However, China will be more and more involved in the global economy. Since 1979, China has been changing and it will continue to respond to all the requirements of the WTO. Meanwhile, it will maintain its particularities as the country has very strong tradition. FDI will still be an important force for economical and technological development. The consequence will be the rise of local enterprises and the growth of their internationalization.

The mean degree of local adaptation of the interviewed subsidiaries in China is 11.3 on 18 points, according to our ranking. Therefore, the subsidiaries have a middle degree of responsiveness. We ask them how they will see the future about their need of responsiveness. 50% predicted the need for adaptation would be higher; 30% predicted it to be lower, 10% predicted it to be the same and another 10% were not sure.

With these facts, we analyse that the trend of local adaptation for Swedish MNEs will be more adaptive under the background of being more open.

## 7.2/ Modification of the models

In the theoretical framework, we presented three models. The last model presented was developed from the theories about LR, the model of Luo and the empirical data findings According to our research findings; we think Hill's theory did not take into account the culture & business practices, organizational structures, and competition intensity factors. Thus, we added these dimensions to develop our model in our study.

The empirical data shown, that the main business practice difference is the need of a strong network. The Chinese market is uncertain and volatile. Therefore, Swedish subsidiaries have to be flexible and have to have a good partner in order to react in a good way for their business. Managing a subsidiary in another country demands an

adaptation in the organizational structure. The most reasonable way seems to be the mix of both Swedish and Chinese managing styles. The Swedish managers have to be clearer and control the tasks and missions, as the Chinese structure is more hierarchical. Another adaptation phenomenon is that all the Swedish subsidiaries interviewed have a high numbers of Chinese employees. It shows their willingness to adapt their organizational structure. However this aspect could be also a requirement from the host government.

Concerning the competition intensity, which faces high pressure for adaptation, we did not find a need for higher local adaptation caused by this dimension. The main Swedish competitors are from western countries or Japan. However the Chinese learn quickly and there is the phenomenon of copying. The state starts to establish some rules to avoid this problem. Nevertheless the legislations in general are still not clear but are in the process of improvement.

In order to apply the model of LR determinants of emerging markets (Luo, 2002) we tested our hypotheses. The application of this model shows in which studied dimensions the Swedish subsidiaries have to improve their local responsiveness. We found out that the Swedish subsidiaries have difficulties to establish a good network and understand the legislation. Even though the competition is intense, the subsidiaries do not face a great need of adaptation in this dimension.

At the same time, we have put the studied subsidiaries into the Integration-Responsive grid to locate them with strategy focus and organizational adaptation. Thus we compare the reality with the theory.

This model shows that on ten investigated subsidiaries, four have a middle degree of adaptation. The companies' strategy is a mix of responsiveness and integration. Most the Swedish subsidiaries need to improve it. This need will be higher when Chinese competitors will become more important and more involved in business.

## 7.3/ Methodological Improvements

We conducted our research with interviews. The telephone or the Internet interviews lack face-to-face communication and observation, which can generate more information than the words. Moreover, we had to control the length of time for the phone interview to China because of the price and the availability of the participants. So, we think it will be better if we could have done a field trip to the studied subsidiaries. We could have also gone deeper in this research by interviewing Chinese managers working in Swedish subsidiaries.

On the other hand, we think the research findings could be different if we have done a quantitative study. The qualitative method provides higher in-depth information. However with a survey, we can obtain different types of information that could be more representative of the studied topic. Therefore, it would have been possible to generalize our findings to all Swedish subsidiaries.

#### 7.4/ Further research

Within the constraints of time, resources, finance, and access to available interviewees, we limited our dissertation to ten Swedish subsidiaries established in China. Most of them are in the technologically intense industries. In the future, we think it will be meaningful to do the further researches on:

- First step on a long research process. We could also reiterate this investigation in few years in order to see the evolution of the studied subsidiaries in their process of local adaptation
- 2. More Swedish subsidiaries in these industries. We used case studies for this research, but we still think if the interviewed subsidiaries can amount to a statistical numeric size, it would have been good to have quantitative study of this topic. Because there are more than 200 Swedish companies established in China. Ten subsidiaries are not enough to represent all the situation of their local adaptation.
- 3. Swedish subsidiaries in a specific industry (e.g. service industry). We think it would have been interesting to focus our research in this industry, as it seems to have more

adaptation dimensions than the high technology industry.

- 4. Subsidiaries from other cultures in specific industry. We think it would have been more comparative if we have studied the similarity and dissimilarity of the degree of local adaptation dimensions within different cultural contexts. Actually, in the interview process we started to interview German and French companies. With more time, it would have been possible to conduct more interviews in order to make a comparison between different European MNEs.
- 5. Chinese views on local adaptation. In this dissertation, we only interviewed Swedish managers about their views on local adaptation, instead of the Chinese managers or employees. Since MNEs are established in China, we think the Chinese shall have a say on this topic.

# 7.5/ Empirical Implications

Throughout this research, we keep in mind the target groups that we think the study may help.

Firstly, our findings could help those Swedish subsidiaries, already established, to position themselves on the Chinese market. The findings can be used as parameters for the Swedish subsidiaries in similar industries. Thus, they can position their local adaptations and adjust them accordingly.

Secondly, our findings could also be useful to some extent to European MNEs or small and middle-sized enterprises. Because most of the big multinationals have entered China, what left are those small and middle-sized ones? Although cultures vary from country to country in Europe, the differences are not as big as those between China and Sweden. Moreover, the trade between China and EU is increasing, as does the conflicts. Therefore, our findings could be parameters for these mentioned enterprises.

Thirdly, our findings could help the relevant institutions or government departments to know the updated information, and make policies according to the new situation.

According to our knowledge, there is only one government department doing this research.

Fourthly, our findings could help the Chinese enterprises that will compete with the established subsidiaries in the market to know their competitors. As the ancient military strategist said, you would never lose if you know yourself and your rivals well.

Finally, our findings could help those Chinese enterprises that will go abroad. The contents of adaptation will be different, but the thinking is similar; when, where, how to enter a foreign market and how to adapt to the environment there.

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# **APPENDICES**

# Tables of the interview analysis

Table 1: Product customization

Product modification:

No = 0 points; Minor = 1 point; Some = 2 points; High = 3 points

N°	Company	Product customizations	Customization
	Name		Grade
1	IKEA	Almost the same in other market of the	
		world. (but adaptation is not company's	
		strategy)	1
2	L&W	No International standard	0
3	Exir	Yes and the reasons are Cheaper materials.	
		Good infrastructure and supplier systems	2
4	Hoganas	No, the same as in Europe, USA and Japan.	
		Most customers have learned our products	
		abroad	0
5	Nolato	The products are customized depending on	
		the customers.	3
6	Sandvik	No customization of the product. Same	-
		products all over the world.	0
7	Storaenso	To some extent yes. Due tot the cheaper	•
		local material and chemicals. Customers are	
		used to local grades.	2
8	Thule	Yes and still in the process of customization.	-
		They are actually investigated to lower the	
		price to attempt the Chinese customers and	
		adapt the product to Chinese cars.	1
9	Intentia	Customization to be adjusted to the Chinese	
		system and to meet the requirements of the	
		Chinese government.	2
10	SCA	No exactly the same in term of packaging,	
		only logo change	1

Table 2: Distribution Channels

No adaptation on those 3 categories = O points If there is adaptation in one category = 1 point If there is adaptation in two categories = 2 points If adaptation in 3 categories = 3 points

No	Different Product Position	Rank	Distribution channels Adaptation	Rank	Price Difference	Rank	Distribution channels Grade
1	Same as in Europe	no	No.	No	No	no	0
2	Different. Due to the lag of techniques of the Chinese companies in this industry.	yes	No	No	we did not have different price strategy. No price ( cheaper salary will increase fast) difference – successful in long run	no	1
3	Same	no	No	No	Same	no	0
4	No answer	no	No	No	We don't sell hardly all products in Sweden	no	0
5	Same	no	No main adaptation. Product shipping to Europe.	No	No real difference	no	0
6	Same	no	No specific adaptation of the distribution channels. Is the same in the principle some changes due to the new environment but they are not major.	Yes	No	no	1
7	Higher position due to the Swedish high quality product	yes	Yes by using local merchants	Yes	China is very costs/price sensitive market. Quality is no yet that important neither are so called sustainability and environmental issues	yes	3
8	Higher position due to the recognition of the Swedish products	yes	Yes. Have to create the distribution channels because it doesn't exist for this kind of product. It is a daily work to get to the distribution channel.	Yes	Basically the same but try to adapt it. Lower the price to attempt Chinese customers by lowering the costs.	middle	2,5
9	Higher Level	yes	NO	No	The price strategy in China is different than in Sweden.	yes	2

No	Different Product Position	Rank	Distribution channels Adaptation	Rank	Price Difference	Rank	Distribution channels Grade
10	No as the customers are global companies	no	Yes, DC needs to be closer to the customers and have higher flexibility	Yes	No because the customers have a global strategy	No	1

Table 3: Government Demands

Specific demands from the government = 1 point If the subsidiary do not obey = 0 points If the subsidiary tries to find a compromise = 1 point If the subsidiary obey = 2 points

No	<b>Government Demands</b>	Rank	Incoherence between host government and subsidiaries	Rank	GOV DEMANDS Grade
1	Many government demands depending on the products. For instance the electric products have different requirements	1	Obey. In fact, we rarely had this problem	2	3
2	Specific demands from the government. Difficulties in the export of products abroad. Need of complex documents	1	Have not yet had this problem. I think we shall give what they need if things happen.	2	3
3	Yeah. Handling wave standards – combine two channels into one line.  Demand how to be done	1	Obey the law otherwise bring trouble to the mother company	2	3
4	yes for trade and import-export.	1	Discuss with local officials and authorities	1	2
5	There is no important demand in the telecommunication industry from the government. The government is interested to this industry and wants to promote foreign companies to increase their activity. Some exporting restrictions in the telecommunication industry. B	0	In general in this industry the government condition are good. Telecommunication is the major export market, the condition of the political demands are better then textile industry for example.	0	0
6	No specific demands from the government in this industry	0	No	0	0
7	Yes, New environmental regulation which are closer and closer to the European ones.	1	Local players have not yet full understanding of what all the regulations mean whereas we have used to operate according to very strict rules	2	3

No	Government Demands	Rank	Incoherence between host government and subsidiaries	Rank	GOV DEMANDS Grade
8	There is no law about their products but only an arbitrary judgment of the local police. It is difficult for the company to know what they can do and what they cannot.	0	No national law about this industry. The rules changes according the different judgement in local. The company try day to day to be aware of the new rules and ask often to the authorities but their demands are always block in the government.	0	1
9	Yes. Need to adapt one product to the government demands.	1	No incoherent interest with the government. The government is not including to the various project. Only one or two customers are owned by the government and these clients know they have a lot of power so they do as they wish	2	3
10	yes for the safety and health issue	1	They have a local management so it is easier. Some problem with unclear legislation	2	3

Table 4: Business practices and culture

No adaptation = 0 points; Adaptation = 1 point Culture is not important = 0 points; culture is important = 1 point; culture is very important = 2 points.

<b>N</b> °	Company Name	Business practice differences	Rank	Level of importance of culture and tradition when doing business in China	Rank	Grade
1	IKEA	Size, distance and culture	1	Very important.	2	3
2	L&W	Relationship - network	1	Very Important	2	3
3	Exir	Guanxi, changing situation	1	Very important.	2	3
4	Hoganas	Guanxi	1	important	1	2
5	Nolato	Price value, guanxi, relationship, network & hierarchy. T	1	Very important.	2	3
6	Sandvik	Guanxi, culture, state policy.	1	important	1	2
7	Storaenso	Network, price sensitiveness and low cost attitude, tradition.	1	Very important.	2	3
8	Thule	Business practice, immature market, low business risk, language issue, difficult to keep Chinese manager, culture and habits, less initiative and expect recognition.	1	Very important,	2	3
9	Intentia	Chinese more denouncing, authoritative, directive; unclear contract; short term; immature market	1	Very important	2	3
10	SCA	Need of trust and network, flexible to the fast environment	1	important	1	2

Table 5: Competition intensity

No competitors = 0 points; less then 5 competitors = 1 points; between 5 & 10 competitors = 2 points; over ten competitors = 3 points

N°	Company Name	Direct Competitors	Product Differentiation	Grade
1	IKEA	Many: Different competitors in different product areas	Range	3
2	L&W	4 foreign competitors. Many Chinese small workshops lagged 50 years behind ( not real competitors)	All products are very unique, The company have been market leader for many years and they valued research development	1
3	Exir	10 International and Domestic very competitive competitors	Longest experience in China to compare with foreign competitors (8 years in China and 10 years in this industry), The product is a newer and fashionable	2
4	Hoganas	More than 20 (International & Domestic?)	Stability of the quality	3
5	Nolato	Huge competitors in general. 3 Chinese competitors (???), 2 Singapore and 5-6 western companies.	Business ethics, portfolio, the way of doing business and working	2
6	Sandvik	The numbers depend on the product branches. In general around 10-15 direct competitors according to the product area. Less then 5 are Chinese firms.	Quality and customer services	3
7	Storaenso	5-10 serious ones in China and Europe	Good quality and good services/reliability	2
8	Thule	2-3 competitors and some Chinese competitors who only exports their products (actively).	Internationalization of their product. Product adapted in kind of cars. The only brand known worldwide.	1
9	Intentia	10 foreign competitors and 10 domestic competitors. The Chinese competitors are smaller companies with less background and experience.	Competitive edge. Good knowledge about the local customers. Quality of the service with a good knowledge of the industry and the customers.	3
10	SCA	Few international competitors, 99% of domestic competitors (2500)	Higher competitiveness in certain category of product. Portfolio (higher range of product), higher quality & service	3

Table 6: Organizational structure

Western management style = 0 points; mix management style = 1 point; Chinese management style = 2 points

Over 80% of local employees = 1 point

N°	Company Name	Ways to deal with management issues	Rank	Percentage of Chinese employees	Rank	Organizatio nal Grade
1	IKEA	Training. But still much needs to do.	0	> 95%	1	1
2	L&W	Strong company culture. We prefer to do things in our way and we have clear way to do things; We are not allowed to do things different from headquarters	0	87.5%	1	1
3	Exir	Communication and a lot of communication	1	95%	1	2
4	Hoganas	Not yet serious problems. Training to some extent	1	>90%	1	2
5	Nolato	Soft Swedish management. They have to be clearer in the communication, with the expectations, tasks and orders, more authoritative. Failure with the politic tradition.	1	98%	1	1
6	Sandvik	No particular staff conflicts in the management	2	98.4%	1	3
7	Storaenso	Combination of the Western management with local skills. It is not different from Russia or Latvia.	1	99.7%	1	2
8	Thule	Asian manager who speaks well English and help for the international network.  There is some misunderstood between the 2 business cultures.	2	96%	1	3

N°	Company Name	Ways to deal with management issues	Rank	Percentage of Chinese employees	Rank	Organizatio nal Grade
9	Intentia	There are some difficulties with the Chinese staff and managers from Sweden. You have to understand it.	1	95%	1	2
10	SCA	Local management, only 7 European managers at the international level and 25 managers from other Asian countries who can speak English on 3 500 employers	2	99%	1	3

# Tables of the hypotheses

Table H1: Having a previous experience in emerging markets is positively associated with LR

No	Company	Experience in other markets	Length in China	TOTAL
1	IKEA	35	17 Years	11
2	L&W	35	2 years (15 years of agent)	9
3	Exir	Sweden, China & Hungary	8 years	12
4	Hoganas	India and Brazil. Present on the main continent of the world	13 years	9
5	Nolato	Eastern Europe: Estonia and Hungary 5	6 years	9
6	Sandvik	India, China, other Asian countries 130	15 years	9
7	Storaenso	Russia and Latin America pretty well. India to some extend 40	8 years in Beijing	15
8	Thule	North America, Europe, East Europe, South America, South Africa, Dubai.	6 years	10.5
9	Intentia	Sri Lanka, Indonesia, Mexico, East Europe. 40	9 years	15
10	SCA	50 countries, South America, Asia, Pakistan, India	4 years	13

 $Table \ H2: \textit{The network established facilitates the LR}.$ 

N°	Company Name	Business differences	GOV DEMANDS	FDI	TOTAL
1	IKEA	1	3	acquisition	11
2	L&W	1	3	WOS	9
3	Exir	1	3	JV	12
4	Hoganas	1	2	both JV &WOS	9
5	Nolato	1	0	WOS	9
6	Sandvik	1	0	WOS	9
7	Storaenso	1	3	JV (contractual)	15
8	Thule	1	0	WOS	10.5
9	Intentia	1	3	Merger with American group	15
10	SCA	1	3	WOS	13

Table H6: The More the competition is intense the more the need for LR is high.

N°	Company Name	Competitors	TOTAL
1	IKEA	3	11
2	L&W	1	9
3	Exir	2	12
4	Hoganas	3	10
5	Nolato	2	9
6	Sandvik	3	9
7	Storaenso	2	15
8	Thule	1	10.5
9	Intentia	3	15
10	SCA	3	13

Table H7: Component localization policy is one of the most important government demands that determine the degree of LR.

N°	Company Name	GOV DEMANDS	TOTAL
1	IKEA	3	11
2	L&W	3	9
3	Exir	3	12
4	Hoganas	2	10
5	Nolato	0	9
6	Sandvik	0	9
7	Storaenso	3	15
8	Thule	0	10.5
9	Intentia	3	15
10	SCA	3	13

# Interview questions of Swedish subsidiaries in China

- 1) How long has your company been established in China? ...... Years
- 2) What kind of Foreign Direct Investment has your company established (Wholly owned subsidiaries, Joint-Venture...)?
- 3) Why your company chose to establish a subsidiary in China? What are the advantages?
- 4) Do you sell your products (or services) in China or outside? If you sell in China what is your target customer (Business to Business or Business to Customer)?
- 5) Are you familiar with emerging market?

Customer taste & preferences: if the company sells its product or service in China

- 6) Have you customized the product to target customers? If yes, what were the main modifications to compare with the product sell in Europe?
- 7) What were the reasons of these changes?

#### Distribution channels:

8) Did you have to adapt the distribution channels to the new environment? If there were some changes how you manage them and if no changes what are the reasons?

If you sell your product in China:

- 9) Is there a different price strategy to compare with the Swedish market?
- 10) What is the product position? Is it the same as in Sweden?

#### Availability of substitutes:

11) How many direct competitors implanted in China do you have (domestic and/or foreign firms)?

12) Is there something unique in your product that makes it different compared to competitors?

#### Host government demands:

- 13) Does the government ask for specific demands in your industry?
- 14) If yes, what are the specific demands?
- 15) How do you handle company interests and governmental demands when they are incoherent?

### Business practices:

- 16) What are the 3 major differences in terms of business practices between China and Sweden? (e.g. Culture, Tradition, Guanxi, Government, Management)
- 17) Do you think the business culture and tradition are important when doing business in China? If so, then in which way are they?
- 18) What is the percentage of Swedish and Chinese employees in your subsidiary?
- 19) How does your firm deal with and solve the conflicts of staff and management styles due to different cultures, values etc.
- 20) Are there other factors (not mentioned in the questions above) that your business needs to adapt to Chinese environment?
- 21) According to your personal opinion, do you think the local adaptation in China will be lower due to the wide openness to the world or higher due to the strong cultural tradition?
- 22) In conclusion, what is your general view of doing business in China? Could you define the challenge for a Swedish company to enter the Chinese market?

Interview cover letter

Kristianstad University

Department of Business Studies

Anne Barbaroux: 0046 7 33 86 28 92

Li Miao: 0046 7 36 64 16 80

Dear Miss or Mister,

We are Exchange Students at the University of Kristianstad (Sweden) doing our master degree in International Business. We are now working on the final dissertation about the Local Responsiveness of Swedish enterprises in the Chinese Market. We want to research the degree of adaptation of these firms and what are the factors influencing their Local Responsiveness in China. Local Responsiveness (LR) is defined as the ability to react in an appropriate timescale to events, opportunities and threats in order to be or maintain the competitive advantage

(Barcley et al. 1996). There are four types of LR in this dissertation, which are:

product adaptation to the differences in consumer taste and preferences

adaptation to the national distribution channels

adaptation to the differences in the infrastructure

adaptation to the traditional business practices and to host government demands.

We based our interview questions on the above four categories. We think the questions in these categories will reveal the present situation, the development and the future of Swedish

companies in China.

The interview will take around 30 minutes. It will not only be of great help to our research, but will also enable us to cast some lights on the strategy of the LR of firms in China. Moreover the interview analysis will help those small & medium size companies to get ready to enter China.

In our research we guarantee you an integral confidentiality. We will not mention information that you feel inappropriate for the anominity of your company and yourself. If you wish to read the results of this research, an electronic copy will be available in December 2006.

You can ask us to send it to you.

Sincerely yours,

Anne Barbaroux & Li Miao

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