

1 Building Strategic Capabilities in Emerging Economies

*Alvaro Cuervo-Cazurra, William Newburry,
and Seung Ho Park*

Emerging market firms are becoming an increasingly influential component of the global economy, impressing managers and academics alike. Many are becoming large multinationals dominating their industries and creating new competition against long-time incumbents from advanced economies. Several studies have examined the phenomenon of emerging market multinationals, praising their virtues and competitive capabilities and describing their internationalization processes (Cuervo-Cazurra & Ramamurti, 2014; Demirbag & Yaprak, 2015; Guillén & García-Canal, 2012; Park, Zhou & Ungson, 2013; Peng, 2002; Ramamurti & Singh, 2009; Sauvart, 2009). Others have identified the challenges these firms face in their internationalization (e.g. Cuervo-Cazurra, Newburry & Park, 2016).

However, before these firms became multinationals, they needed to upgrade their capabilities to become internationally competitive at home and abroad. Surprisingly little attention has been devoted to the way this happens across multiple countries (an exception being Williamson et al., 2013). Most studies have instead focused on single-company cases of leading firms, such as the Chinese platform Alibaba (Clark, 2016; Erisman, 2015); the Brazilian airplane manufacturer Embraer (Rodegen, 2009); the Chinese software firms Alibaba, Xiaomi, and Tencent (Tse, 2015); the Chinese white goods firm Haier (Fischer & Lago, 2013; Hu & Hao, 2017; Yi & Ye, 2013); the Mexican cement producer Cemex (Fuentes-Berain, 2007; Lessard & Lucea, 2009); and the Chinese telecommunication equipment manufacturer Huawei (Yang, 2015; Tian & Wu, 2015).

In this book, we complement these studies by providing a better understanding of how firms manage the twin challenges of upgrading capabilities to international levels while operating in the challenging conditions of emerging economies. Much of the competitive advantage of a multinational comes not from supportive factors in the home country but from the ability to learn from multiple countries (Bartlett & Ghoshal, 1989; Doz, Santos & Williamson, 2001), obtain technology from advanced countries (Luo & Tung, 2007), to arbitrage differences across countries (Kogut, 1985;

Ghemawat, 2001), and to benefit from the economies of scale that global operations facilitate (Yip, 2000). However, before firms become multinationals, they need to achieve the level of competitiveness that enables them to compete across countries and the resources to deal with the costs of doing business abroad (Hymer, 1960/1976). Emerging market firms must also deal with the challenges of operating in emerging economies (Grosse & Meyer, 2019), such as those in which a large proportion of the population has low income (Prahalad, 2004) and in which there are underdeveloped institutions with limited promarket infrastructure (Khanna & Palepu, 2010).

Thus conditions in the country of operation become central to our understanding of the processes by which emerging market firms upgrade their capabilities. Instead of discussing one type of capability and how firms from a variety of countries deal with that capability (as in Williamson et al., 2013), we focus on analyzing how firms from various emerging markets have dealt with some of the challenges of succeeding in their own countries and managed to upgrade their capabilities both at home and in their international operations. The book's focus is on providing contextually relevant analyses and recommendations based on studies of multiple companies across a wide range of emerging markets.

The overarching message of the book is that the development of capabilities to international levels can best be understood by examining the conditions present in the countries in which firms operate. Our approach extends the traditional structure–conduct–performance paradigm of industrial economics (Bain, 1956), in which the structure of competition in the industry determines the strategies of firms and the level of their success. We expand this model by including the context of the country in the causality chain, so that it becomes context–structure–conduct–performance. We explain how conditions in the country influence the competitive strategies that firms use to upgrade their capabilities and thus, eventually improve their performance.

The context and conditions present in a country include many dimensions. In this book we group them into two broad categories: institutions, which comprise the set of rules and norms that facilitate interactions and transactions among economic actors (North, 1991); and endowments, which are the factors and resources that can become inputs for the productive systems of companies (Penrose, 1959). Emerging economies are typically characterized by the underdevelopment of institutions (Khanna & Palepu, 2010), in the form of relatively less supportive and sophisticated laws and regulations and weaker judicial systems that result in lower protection of contracts and intellectual property. These factors discourage investment in the development of advanced capabilities. Such countries are also characterized by the underdevelopment of endowments,

populations with relatively low levels of education and income, and unsophisticated innovation systems and weak capital markets. These factors tend to limit investment in capability development.

Thus we tackle the challenge of explaining how companies in emerging economies manage to develop competitive capabilities to international levels despite the underdevelopment of systems and resources in the home countries in which they operate. To do so, we conduct a country-by-country analysis in which we study a variety of companies in terms of the type of industry in which they function (low-tech, high-tech, or service) and also in terms of their internationalization (purely domestic, exporter, or multinational). This provides insights into processes of capability development that have broad applicability and can be easily generalized to firms in other countries. Our research methodology is explained in the next section. In the chapter's final section, we summarize our process for accomplishing our research aims and explain the structure of the book.

1.1 Research Methodology

In this project, we systematically examine the various strategic capabilities that are likely to help emerging market firms achieve success. This includes identifying capabilities that will be most beneficial to these firms in their future advancement, revealing actions and processes that facilitate the development and honing of sophisticated capabilities, and uncovering strategies that enable firms to reduce disadvantages. To accomplish this, we pursued the following steps.

First, we realized that the complexities of studying a phenomenon that requires in-depth local knowledge demanded a team of researchers from around the globe. We believe that this necessity for local knowledge is a major reason why so many emerging market studies are based on a single country or very few countries. To enable global comparisons, we developed a network of research partners from some of the top universities in twelve emerging markets that were part of the global research network of Nanyang Business School's Centre for Emerging Markets. Our selected team included researchers from Asia (China, India and Kazakhstan), Africa (South Africa), Europe (Russia, and Poland), and Latin America (Argentina, Brazil, Chile, Colombia, Mexico, and Peru). These researchers brought with them knowledge along with significant local contacts, either known to them individually or facilitated on the basis of the prestige of their universities. This enabled access to CEOs and top company managers whose input we needed in order to truly understand our study phenomenon.

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Table 1.1 *Data collection matrix*

		Firm category		
		Purely domestic	Exporter	Multinational
Industry type	High-tech			
	Low-tech			
	Service			

Second, we asked research partners in the twelve countries to identify and collect information on company cases, each corresponding to a different cell out of the nine total cells within our data collection matrix, shown in Table 1.1. This matrix records both the industry in which a company operates (low-tech, high-tech, or service) and the degree of internationalization of a firm (purely domestic, exports, or multinational). From preliminary discussions, we realized that firms representing all nine cells might not be available in all markets due to industry differences and other variations in the local economies. Additionally, in many cases, purely domestic firms might not yet have developed the capacity to adequately evaluate the strategic nature of their capabilities at an international level. Our goal was, nonetheless, to collect enough data across these two dimensions to obtain a good cross-section of firms to compare.

Third, while we expected the case study examinations to be exploratory in nature given the widely varying conditions across the emerging markets and our nascent understanding of the phenomena, we also aimed to achieve some degree of comparability across the cases. To aid in this regard, we identified several potential capabilities, listed in Table 1.2, that were shown by prior research to be associated with firm success. This list was not meant to be exhaustive, as different capabilities may be needed in different markets, but rather to provide a starting point for our examinations and to allow comparison among firms and countries.

Fourth, we also developed a series of general questions to guide researchers in their interviews. We did not necessarily advocate that the researchers pose the questions in a standard manner, but rather that they engage the interviewees in a conversation, first asking them to describe their business and what capabilities they felt had best aided them in achieving success. The questions were then used to guide the interview as topics naturally came up, or to fill in gaps not covered by the interviewee. These questions were sent to the interviewees in advance, along with a cover letter describing the project, so that they could be adequately prepared for the interviews. These were conducted in person and

Table 1.2 *Potential strategic capabilities*

Major capability category	Subcategories
Obtaining resources	Resource identification Ability to purchase inputs Ability to develop resources internally
Product/service capabilities	Product manufacture Research and development Local product adaptation
Operations and management	Production management Supply chain management Hard skills Soft skills Entrepreneurship Cross-cultural management
Marketing	General sales capabilities Understanding local customer needs
Managing the external environment	Political capabilities Relationship capabilities Adjusting to poor infrastructure

generally lasted from sixty to ninety minutes. The questions investigated the following aspects of various potential capabilities and resources.

- 1) To what extent are these resources critical to the company when operating in its home market? In other emerging countries? In advanced economies?
- 2) To what degree does the company possess this particular capability in comparison to its domestic, host country, or global competitors?
- 3) If a company lacks a critical strategic capability, how can it obtain that capability in the home and host countries?
- 4) To what extent is each capability important across different stages of the internationalization process: the entry stage (e.g., during country selection, entry mode selection, or establishment of a foreign subsidiary) or the operations stage (e.g., during local operations, integration of a subsidiary with the broader multinational, or expansion of operations)?
- 5) How does the firm’s degree of internationalization impact the importance of particular strategic capabilities?
- 6) To what extent does the firm’s industry impact the importance of particular strategic capabilities?
- 7) How does the firm’s target customer base impact the importance of particular strategic capabilities?

We realized that organizing such a large network of researchers in twelve countries required special attention to ensure consistency, even with the common tools guiding the data collection described above. To help ensure this, we held a forum for all the authors to attend at the China-Europe International Business School in Shanghai, China, early in the process of collecting data to discuss preliminary data collection efforts in order to identify specific issues that might have developed. This was useful in ensuring a common methodology. We supplemented this in-person meeting with multiple videoconferencing calls to address ongoing issues.

At the meeting in Shanghai, we also established a common format for the chapters along with shared elements that we planned to include in each chapter, including a presentation of the breakout for each country based on the Table 1.1 framework and a similar breakout of which capabilities were described as strategic for each company, building on Table 1.2. We did not dictate a rigid chapter format given the unique nature of each of the country environments we were examining, but we focused on achieving enough commonality in essential elements to ensure comparability across the countries. The book's three editors reviewed each chapter and provided feedback to the authors several times to ensure the best possible consistency of presentation throughout the book.

Information was collected from seventy-two companies in our twelve study countries. They are listed by country, along with their industry types and levels of multinationality, in Table 1.3.

1.2 Organization of the Book

The next chapter (Chapter 2) provides a theoretical overview of the academic literature related to the development of strategic capabilities among emerging market firms. It presents a four-I framework of mechanisms that emerging market firms have used in their capability development: imitation, integration, incorporation, and internal development. The chapter highlights how the relative usage of these four mechanisms varies depending on the development stages of both emerging market firms and their host countries.

Each of the next twelve chapters (Chapters 3 through 14) examines how firms upgrade capabilities in each individual country. The chapters are organized by region and written by local experts.

Among emerging Asian countries we have included chapters on China, by Mohan Song, William Newburry, and Seung Ho Park; India, by Subhashish Gupta, P. D. Jose, and Ashok Thampy; and Kazakhstan, by Venkat Subramanian and Almira Abilova.

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Table 1.3 *Companies studied*

Country	Company	Industry type	Multinationality
Argentina	Grupo Mirgor	high-tech	domestic
	Bodega Lagarde	low-tech	exporter
	Arcor	low-tech	multinational
	San Miguel	low-tech	multinational
	Grupo Bagó	high-tech	multinational
	Grupo ASSA	service	multinational
Brazil	Globant	service	multinational
	Dr.Consulta	service	domestic
	Grendene	low-tech	exporter
	WEG	high-tech	multinational
	Fanem	high-tech	multinational
	Stefanini	service	multinational
Chile	Integration	service	multinational
	BeitGroup	low-tech	domestic
	Kunstmann	low-tech	exporter
	Casas del Toqui	low-tech	exporter
	ALTO	high-tech	multinational
	Forus	high-tech/service	multinational
China	Derco	service	multinational
	eClass	service	multinational
	AVIC	high-tech	multinational
	Advantech	high-tech	multinational
	ShangGong Group	high-tech	multinational
	Higer	high-tech	exporter
Colombia	Chervon	low-tech	multinational
	Siwei-Johnson	low-tech	multinational
	Baby First	low-tech	exporter
	Sanpower	service	multinational
	Grupo Bios	high-tech	domestic
	Mattelsa	low-tech	domestic
India	Haceb	high-tech	exporter
	Sempertex	low-tech	exporter
	New Stetic	low-tech	exporter
	Brainz	service	exporter
	Colcafé	low-tech	multinational
	Gokaldas Exports	low-tech	exporter
Kazakhstan	Tata Consultancy Services	service	multinational
	Biocon	high-tech	multinational
	Titan Company Ltd.	low-tech	multinational
	Air Astana	service	domestic
	Tsesna	low-tech	exporter
	Kamaz	high-tech	multinational
Sportmaster	Sportmaster	service	multinational
	Sberbank	service	multinational

Table 1.3 (cont.)

Country	Company	Industry type	Multinationality
Mexico	Interlub	high-tech	exporter
	Belticos	low-tech	exporter
	Vidanta	service	exporter
	Neoris	high-tech	multinational
	Farmacias Similares	service	multinational
	KidZania	service	multinational
	Elektra	service	multinational
Peru	Deltron	low-tech	domestic
	Cantol	low-tech	exporter
	Resemin Group	high-tech	multinational
	Alicorp	low-tech	multinational
	Yobel	low-tech	multinational
Poland	Lolimsa	service	multinational
	Kooptech	high-tech	exporter
	Granna	low-tech	exporter
	Prochem	service	exporter
	Aplisens	high-tech	multinational
	Nowy Styl Group	low-tech	multinational
Russia	Audioteka	service	multinational
	SIBUR	high-tech	domestic
	Gazprom M&T	high-tech	domestic
	ByTerg	high-tech	domestic
	Ecolab	high-tech	multinational
South Africa	Swilar	service	multinational
	Standard Bank Group	service	multinational
	Nedbank Group	service	multinational
	Clover Industries	low-tech	multinational
	Tiger Brands	low-tech	multinational

Our chapter on South Africa was prepared by Helena Barnard and Christian Nedu Osakwe.

The chapters on emerging Europe cover Russia, written by Natalia Guseva; and Poland, by Mariola Ciszewska-Mlinarič and Krzysztof Oblój.

We covered six countries in the emerging Americas: Argentina, written by Michel Hermans and Diego Finchelstein; Brazil, by Maria Tereza Leme Fleury, Cyntia Vilasboas Calixto, Cláudia Sofia Frias Pinto, and Afonso Fleury; Chile, by Santiago Mingo and Francisca Sinn; Colombia, by Maria Alejandra Gonzalez-Perez, Ana Maria Gomez-Trujillo, Eva Cristina Manotas, Camilo Pérez-Restrepo, Maria Teresa Uribe-Jaramillo, Juan Velez-Ocampo, and Verónica Duque-Ruiz; Mexico, by Miguel

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A. Montoya and Gerard Velasco; and Peru, by Armando Borda and Carlos Cordova Chea.

Each of these chapters provides insights into the ways in which the specific characteristics of the particular country have influenced the development of companies and their strategic capabilities, while also examining the common elements we have already mentioned to enable us to make comparisons within each country, across industries, and across multiple countries.

Stemming from the evidence gathered through the seventy-two interviews conducted in the twelve study countries, the final chapter (Chapter 15) integrates the findings of the cases. It first presents a summary of which capabilities were identified by the most companies as being strategic in their development. It then breaks down which companies were most prominent based on industry (low-tech, high-tech, and service), degree of firm internationalization (purely domestic, exporter, and multinational), and country of evaluation. The chapter integrates examples from the various chapters to illustrate the capabilities that were found to be most strategic and proposes some reasons why this is the case.

Looking at some of our most prominent results, understanding local customer needs was the strategic capability that was most strongly identified by the emerging market firm leaders in our study. It was perceived as highly important across industries and levels of multinationality, although there was some interesting variation across countries. In particular, this capability was universally identified as important across all of the six Latin American countries in the study. The second most strongly identified strategic capability, relationship capabilities, was also shown to be commonly identified across industries and levels of multinationality. However, an unusually low score in China was notable, and seemed contrary to findings presented in prior literature. The result may reflect the rising level of development of Chinese firms, leading the country to focus on the internal development of technical capabilities, such that relationships may be less important.

Beyond these first two capabilities, we begin to see much more variation in capability identification. For example, we found that general sales capabilities were more highly identified as important in low-tech and service industries and among multinationals. Similarly, local product/service adaptation was identified by these same two industries and by both multinationals and exporters. By contrast, research and development capabilities were highly associated with high-tech industries, where competition may be based on differentiation as opposed to low cost. Supply chain management was identified more frequently among low-

tech firms and purely domestic firms. These results and many more are presented throughout the book.

Overall, the book makes significant contributions that will be useful both to academic researchers and to practitioners. Most research by academics on emerging markets in general, and on emerging market strategic capabilities in particular, focuses on only one country, often China, or a small set of countries, to draw conclusions about emerging markets in general. By examining a varied set of emerging market countries across five continents, we are able to add needed depth to the study of emerging market multinationals. We present information on both consistent patterns and significant differences across these markets, along with variations at the industry level and across levels of multinationality. Thus we are able to provide a more nuanced understanding of these firms than is contained in much of the existing academic literature.

For practitioners, the research is particularly valuable in presenting practical advice on the development of strategic capabilities – advice that can be tailored to their country, their industry, and their firm’s level of multinationality. This should be useful to companies operating in their home countries but also to multinationals operating across different host countries in terms of understanding the capabilities that drive local competitive dynamics.