

Relationship between Internationalisation of Firms and Economic Performance: A Case Study Selected Banks in Nigeria.

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Abstract

Despite the growing internationalisation of firms from the developing economies, study examining the effect of internationalisation on their economic performance remain elusive, as evidence from prior studies are based on firms from the developed and the emerging economies. This study examines the relationship between the internationalisation, measured by percentage of foreign assets over total assets and performance, measured by return on assets of Nigerian banks. By using a cross sectional panel data covering the period of 2008 – 2010, Ordinary Least Square (OLS) result showed a positive relationship while the ANOVA result showed a significant relationship between internationalisation and the economic performance of the banks. The study concluded that international expansion can bring better economic performance to firms from developing economies. However, internationalising firms must be wary of the potential challenge of over-internationalisation which may negate the expected economic benefit.

Keywords: Internationalisation; Firm; Economic performance; Developing economies

1. Introduction

The unprecedented competitive transformation witness in the global market is no more a mirage. Driven by impulses from technological changes, lower costs of international transport, reduction in trade barriers and homogenisation and convergence of consumer spending (Konya and Ohashiz, 2004), firms are more aware than ever before the continuous need to weigh corporate strategies as against their performance. Often, they are to implement such strategies as quickly as possible or learn from competitors or other industry to respond to these impulses. Of such response to these impulses is firm internationalisation strategy and its implication on performance. That is, as these impulses drive firms to look beyond national borders for market opportunities, what then is the implication of this on the firm economic performance?

As globalisation and its evolving drivers enable firms around the world to co-ordinate their operations more effectively and efficiently than ever before, one begins to assume that internationalisation offers more benefits than the associated costs. This assumption is built around evidence from contemporary studies of internationalisation and firm economic performance relationship (IP-relationship) which are largely based on western countries. But for firms from the developing economies, study explaining the relationship between their internationalisation and performance has been extremely few (Nachum, 2004). And for those few ones (Fleury, Beroni, Fleury and Junior, 2007; Contractor, Kumar and Kundu, 2007), they are largely based on firms from emerging economies like the BRICS (Brazil, Russia, India, China and South Africa) countries. Hardly can one find research on this phenomena that relates to developing economies from Africa for example. Yet, firms from these countries are finding their way to set up operations in other countries, even in the developed economies. For example, United Bank of Africa of Nigeria (UBA) has, other than Nigeria, over 15 wholly-owned subsidiaries in other countries including Paris, New York and London. Also, the Guaranty Trust Bank of Nigeria Plc became the first African bank to be listed on the London Stock Exchange (LSE) in March of 2007 when it won the approval of the United Kingdom Financial Service Authority (FSA) to begin corporate and retail banking services in the United Kingdom. Other banks like the First Bank of Nigeria Plc and Zenith Bank of Nigeria Plc have also won the approval of the FSA not only to trade their stocks in the LSE but also to operate corporate and retail banking services in the United Kingdom.

Doubtlessly, the growing regional integration among the developing economies is providing a veritable platform for firms in these economies to explore the inherent benefits of internationalisation. Yet, grasping this complex phenomena (IP-relationship) in the context of these firms seems relatively unknown. This challenge was noted when Nachum (2004) consented that despite the growing influential position of firms from the developing economies in their domestic and the global economy, literatures on their international diversification and performance have been neglected. The fact is that these firms are finding their way to set up operations in other national markets, but study of their internationalisation and performance is seemingly lacking. Based on the

foregoing, this study provides insight into the relationship between internationalisation the performance of firms in developing economies.

2. REVIEW OF LITERATURE

Literature has continuously, conceptually, argued for the benefits inherent in firms' internationalisation. The resource-based view (RBV) for example contended that such internationalisation allows firms to leverage excess firm-specific resources into new markets creating economies of scope (Wiersema and Bowen, 2011) and accentuation of existing core competencies, and access to substantial growth opportunities in the product markets of foreign countries (Hitt, Tihanyi, Miller and Connelly, 2006). Others further argued that internationalisation gives firms the opportunity to gain competitive advantage through economies of scale – spreading fixed cost across larger markets. The organisational learning theory on the other hand, argued for the internationalisation of firms as such expansion gives a concomitant learning curve effect – increasing firms' knowledge diffusion and innovation. And as firms learn from their new environments in which they operate, such knowledge is transferred internally to its subsidiaries within the same country or from country to country which enhances firms' innovative performance (Letto-Gilles, 2009).

Despite these benefits, internationalisation has some attendant costs. As firms expand their operations beyond national borders, there are correlative operational challenges like increasing costs of co-ordination and control, liability of foreignness and other risks connected to foreign activities. For example, Lu and Beamish (2004) Oesterle, Richta, and Stratmann (2008) argued that internationalisation is usually associated with disadvantage of risk of discrimination by host country customers or government which may erode the relative gain from internationalisation.

But while these conceptual arguments for the benefits and costs of internationalisation seemingly looked settled, empirical researches however have showed mixed relationships. One of the few studies of firm IP-relationship in the developing country was carried out by Nachum (2004) and it revealed a significant and positive association between industrial and geographic diversification and performance, and considerable variation of these relationships across developing regions and diversification strategies. That is, as firms geographically expand their operation, there seems to be a correlative improvement in their economic performance. Other studies like Baek (2004), Contractor et al. (2007), Pangarkar (2008), and Hagemeyer and Kolasa (2011) have all found a positive/linear relationship (U-shaped curve) between firm IP-relationship. For example, Contractor et al. (2007), claimed that prior studies have been on the advanced countries and decided to investigate IP-relationship in one of the emerging economies (India) between service and manufacturing firms. They found a U-Shaped curve depicting the IP-relationship of Indian firms.

Scholars like Gerpott and Jokopin (2005) and Hennart (2007) have also claimed that there is zero/non-linear I-P relationship from their findings. Hennart (2007), relying on the transaction cost/internalisation theory of internationalisation argued against the benefits of international expansion (the economies of scale and scope, resource efficiency access, and organisational learning). The finding (Hennart, 2007) showed that there is no direct and general relationship between international expansion and performance.

However, scholars like Tallman and Li (1996), Riahi-Belkaoui (1998) and Lu and Beamish (2004) have all found a different kind of relationship – The Sigmoid or the S-curve based on the three stage theory (Contractor, 2007). That is, firm's performance declines, then increases, and finally decreases as the firm international expansion increases (Riahi-Belkaoui, 1998). For example, Lu and Beamish's (2004) longitudinal study of 1,489 Japanese firms found that returns from the international expansion relates to costs and benefits which varied with the extent of firm's internationalisation. This association was manifested in a horizontal S-curve, which at first showed a performance decline with increasing internationalisation, followed by a positive relationship between increasing international expansion and firm performance, which then declined at very high levels of internationalisation.

To bridge these contradictions and reconciled the variations, Contractor's (2007) studies of empirical research on IP-relationship for over thirty years (30 years) found that while international expansion of a firm will not necessarily always improve performance (during the initial international expansion stage or in cases where a firm may have over internationalised, for the most part, over a considerable range of expansion – international expansion does indeed result in net positive benefits to a firm. These conflicting findings have necessitated the need for further understanding of this relationship, especially, by drawing inference from firms developing economies like Nigeria.

3. METHODOLOGY

3.1 Population and Sample

The target population was all the commercial banks in Nigeria with an entire strength of about twenty-two (22) banks. A total of five (5) banks were purposively selected for this study. The selected banks were those that owned wholly subsidiaries in other countries and also have their stock been traded on the London Stock Exchange. This constitute about 23% of the entire population. The selected banks include - First Bank of Nigeria Plc, Zenith Bank of Nigeria Plc, Guarantee Trust Bank of Nigeria Plc, United Bank of Africa Plc and Access Bank of Nigeria Plc.

3.2 Data Source

Like prior research (Ruigrok and Wagner, 2003; Fluery et al., 2007; and Hagemeyer and Kolasa, 2011), secondary data was used. The data relevant for the purpose of the research were available on the case banks' website – Consolidated Annual financial report (CAFR) from 2008 to 2012. The attractiveness of the CAFR is that, apart from being accounting-based as well as being prepared in accordance with internationally acceptable financial reporting standards – International Financial Reporting Standards (IFRS), the geographical segmentation of their activities made it easy to extract valuable data needed for the research.

The geographical segmentation in financial report segmented the activities of the banks into domestic and foreign activities. The global activities represents the summation of both the domestic and foreign activities. For example, our independent variable, internationalisation, measured by the banks' Foreign Assets to Total Assets (FATA) was computed by dividing the total/global asset by Foreign Assets. On the other hand, our dependent variable, performance, was measure using the Return on Assets (ROA). The ROA is usually stated in the CAFR. And where the CAFR is not stated, the accounting-based method were used in calculating the ROA, the involve dividing the banks' annual global net income by annual global assets of the banks for the study periods. The measurement index is similar to Daniel and Brack (1989), Riugrok and Wagner (2003); Lu and Beamish (2004) and Contractor (2007).

3.3 Method of Data Analysis.

Frequently used analytical techniques to reveal the IP-relationship include ANOVA techniques (Sullivan, 1994; Fluery et al, 2007), Ordinary Least Squares Method – OLS (Lee, Chan, Yeh and Chan, 2010) and correlation (Lu and Beamish, 2004; Gerpott and Jakopin, 2005; Fluery et al, 2007). The use of multiple statistical techniques strengthen the validity of the research result.

In our study, we made use of the OLS and the Analysis of Variance (ANOVA) techniques. This allowed us to summarise the point estimate that calculate the average effect of internationalisation on the average effect on performance of the firms (Lee et al., 2010). With the Anova technique, we were able to determine whether the differences in the mean performance of the banks are significant and it is not due to chance alone.

Table 1: Pooled Ordinary Least Square (OLS), using 25 observations

<u>Included 5 cross-sectional units</u>					
<u>Time-series length = 5</u>					
<u>Dependent variable: Performance</u>					
	<i>Coefficient</i>	<i>Std. Error</i>	<i>t-ratio</i>	<i>p-value</i>	
constant	3.39906	0.647549	5.2491	0.00003	***
Internationalisation	-0.107699	0.0508596	-2.1176	0.04524	**
Mean dependent var	2.144800	S.D. dependent var		1.400268	
Sum squared resid	39.38040	S.E. of regression		1.308507	
R-squared	0.163152	Adjusted R-squared		0.126768	
F(1, 23)	4.484094	P-value(F)		0.045235	
Log-likelihood	-41.15337	Akaike criterion		86.30674	
Schwarz criterion	88.74449	Hannan-Quinn		86.98286	
Rho	0.325345	Durbin-Watson		1.093337	

Table 2: ANOVA - Internationalisation and Performance

	Sum of squares	df	Mean square
Regression	7.67763	1	7.67763
Residual	39.3804	23	1.71219
Total	47.058	24	

$R^2 = 7.67763 / 47.058 = 0.163152$
 $F(1, 23) = 7.67763 / 1.71219 = 4.48409$ [p-value 0.0452]

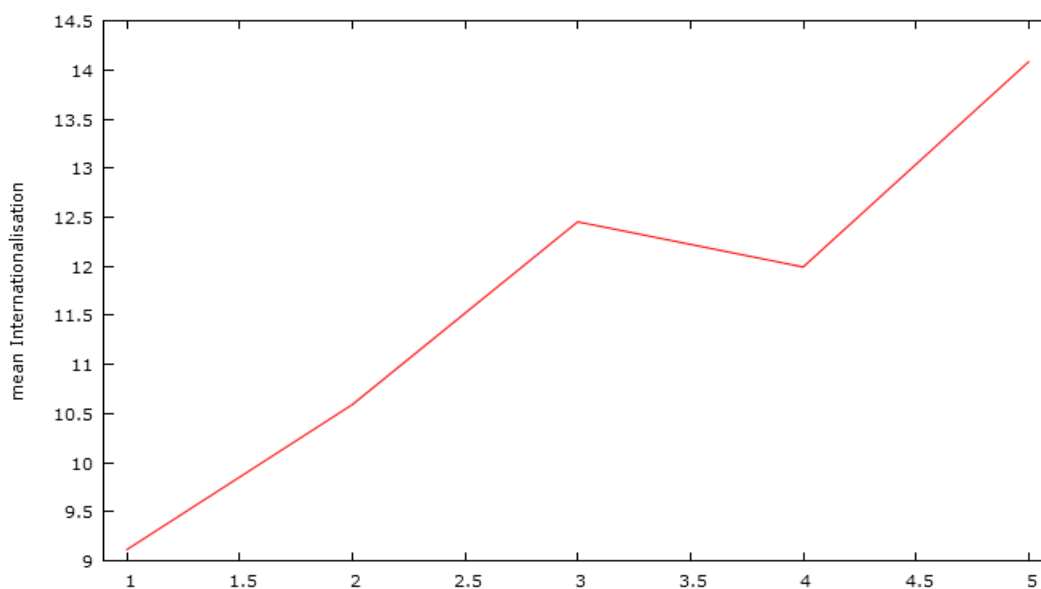


Figure 1: Mean Internationalisation of Five Nigerian Banks.

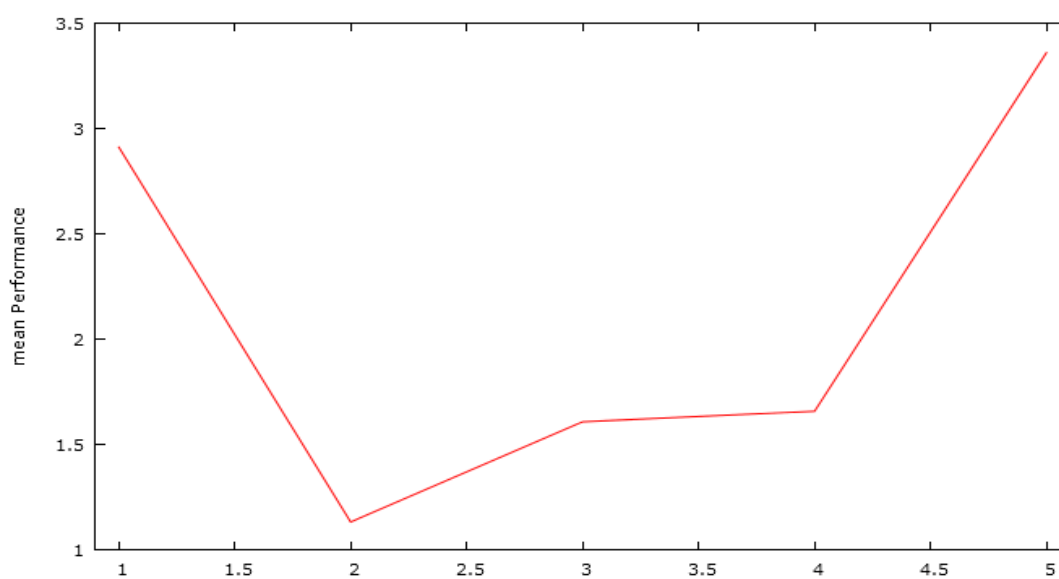


Figure 2: Mean Performance of Five Nigerian banks

3.4 Results

Table 1 shows the main Ordinary Least Square (OLS) result of analysis of the relationship between performance, measured by the Return on Assets ratio (ROA) and the internationalisation, as measured by firm's Foreign Assets to Total Assets ratio (FATA) of five Nigerian Banks. The ordinary least square regression shows "R-Square" as equal to 16% (Table 1). This is a very weak relationship but negligible as it indicates a positive relationship between the variables -internationalisation and performance. It is worthy of note that this weak relationship may be explain by the size of the variables. Importantly, the more internationalised and larger the firm, the better the performance, meaning that for banks within Nigeria, internationalisation may guarantee an improved performance compare to banks that do not internationalised.

The ANOVA test (Table 2) shows a significant difference in the means of internationalisation and performance of the banks. The statistical level of significant at $P < 0.0452$ as against $P < 0.05$ and F-statistics of 4.484094 corroborate the R-Square outcome that there is a relationship between the variables. With $P < 0.0452$ at 95% significant level, we are confident that the risk of falsely inferring that there is a relationship between the variable is 4.5 out of 100 as against 5 of 100 and it due to chance. Therefore, the ANOVA test shows a strong evidence that there is a significant relationship between performance and internationalisation of the banks.

4. Discussion

The main purpose of this study is to examine one of the contentious issue in international business: Does internationalisation affects firm's performance? As showed in the Table 1 (R-Square = 16%), we found that there is a positive relationship between the internationalisation and performance of Nigerian banks, though a modest relationship. This means that as the banks expand their operations beyond national border, there is a modest corresponding growth in the performance of the banks. This supports the earlier conceptualization that internationalisation brings better performance. Also, the analysis of the mean internationalisation and performance of the banks for the five years period of 2008 and 2012 (Figure 1 and 2) showed that at a point there was a rise in the mean internationalisation and performance with a corresponding fall in the both internationalisation and performance of the banks. This was followed by a parallel mean internationalisation and performance and finally an increase in the both the mean internationalisation and performance. One explanation for this relationship can be found in the Uppsala model of firm internationalisation. According to the model, at the start of the internationalisation process, firms tends to face the difficulties of cultural challenges (Psychic Distance). This means firms will undergo a learning process which leads to increase operation costs of internationalisation. But with time (understanding of the new markets through appropriate strategy) internationalisation cost efficiency increase. This interplay explained the modest positive relationship between the internationalisation and performance of the banks. Thus, we consent that internationalisation may bring about better performance despite the modest positive relationship (R-Square = 16%).

5. Conclusion

OLS and ANOVA results confirmed, as with earlier research that for Nigeria banks there is a positive IP-relationship - internationalisation can bring better economic performance to the banks. This result lend strength to other developing economies' firms weighing the option of internationalisation. For managers, internationalisation tends to have a modest positive effect on firms performance. Generally, managerial challenges is often the translation of firm strategies into sustainable and positive economic performance. Understanding the positive impact of internationalisation on firm performance, means managers can begin to explore international markets to enhance the performance of the firm. Importantly, managers must recognized the growing patterns of globalisation and its drivers which tends to support the need for firms to look beyond national borders for market opportunities. With this positive relationship however, managers must be wary of the potential challenge of over-internationalisation. They must design strategies that ensure optimising internationalisation in terms of when, where and how to expand (setting internationalisation threshold). This can save the firm from the complexities encountered in the international expansion process that may overwhelm the capabilities of managing complexities in international business (Lu and Beamish, 2004).

Despite this new insight, there are considerable limitations of inherent in the research, yet they do not compromise the importance of the findings from the research. Rather, it presents new grounds for future research. One of the limitations is the size of the research samples and time-series used is relatively small. Future research can expand the sample size as well as the timeline to strengthen the research findings. The choice of variables and method of analysis also limit the generalisation of this research. Future research can employ variables other than common indicators of performance measurement that are largely accounting-based or market-based. Rather, the motive of internationalisation should be allow to determine performance indicators. For example, one of the motive of banks' internationalisation is the concept of "Follow-the-Client" – the bank

internationalised because its major client move or operate in another country. Thus we suggest that future research can measure firm performance with the motive behind firm internationalisation like - "Follow-the-Client". With this one can understand IP-relationship beyond the usual measure variables. Also, future understanding of the IP-relationship can use qualitative methods rather the common quantitative approach. This can open new ground for qualitative empirical research in IP-relationship.

Another limitation of this research is the drawing generalisation for developing economies from Nigerian banks. This is country-specific and it raised the question of whether such findings can be apply to financial institutions in other developing economies like Ghana, Bolivia and Kenya. Though the methodology used are found in earlier research and are globally acceptable - gave credence to the research and its finding. Even so, there is a need for further research that can examine IP-relationship in a different industrial as well as nationality context. This, no doubt, will widen our understanding of IP-relationship across industries and nationalities which are rare.

Conclusively, our research provided valuable insight into area of international business that is lacking empirical study in the context of firms from the developing economies. Importantly, it provided positive ground for future research in IP-relationship and especially international business in the developing economies. It must also be recognised that with globalisation and its consequences - the increasing multinational and bilateral trade agreements among countries, new market opportunities are being opened around the world. Thus our research provides answer to one of the contentious issue in international business - does internationalisation affects firm's performance? And with the evidence from this research, we support firm strategies that are directed at increasing internationalisation of a firm as this enhance better performance.

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