Chapter 18

Wholly-Owned Subsidiaries, Greenfield Investments and Mergers & Acquisitions

Wholly-owned subsidiaries afford an MNC increased control over its international business operations. This Chapter discusses the advantages and disadvantages of the main methods for acquiring wholly-owned subsidiaries, building new facilities (greenfield investments) and buying existing assets (acquisitions).

Foreign Direct Investment and Wholly-Owned Subsidiaries

FDI is an *internationalisation strategy* involving the transfer of equity funds to other nations to gain (whole or partial) ownership and control of foreign assets. *Partial ownership* relates to international collaborative ventures, i.e. international joint ventures or international strategic alliances (see Chapter 17). *Wholly-owned subsidiaries*, in contrast, represent full ownership (100%) and full control over foreign business entities. By establishing wholly-owned subsidiaries, companies can achieve ownership, location and internalisation advantages, as proposed in the OLI Paradigm (see Chapter 6).

International Portfolio Investment

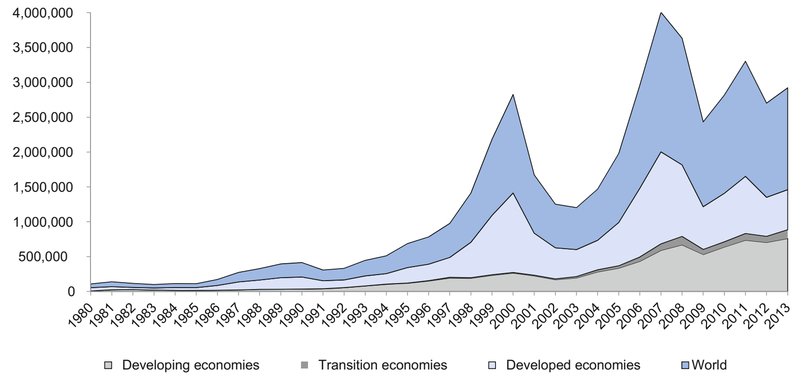
In contrast to FDI, *international portfolio investment* involves passive ownership of foreign securities such as bonds or stocks. The main purpose of portfolio investment is to generate *financial returns*. In contrast, FDI seeks control of business units abroad and represents a long-term commitment (Cavusgil/Knight/Riesenberger 2014, p. 423). In order to qualify as FDI, the investment must afford the parent enterprise control over its foreign affiliate. To define *control*, the United Nations uses a benchmark of 10% or more of the ordinary shares or voting power of an incorporated firm or its equivalent for an unincorporated firm (UNCTAD 2013).

Foreign direct investment inflows are very important for the world economy. They have continued to rise over recent years (see Figure 18.1), thus highlighting the importance of this internationalisation strategy. However, roles have changed between developed and developing countries with regard to FDI. In 2012, for the first time ever, developing countries accounted for more than 50% of global FDI inflows, and thus absorbed more FDI than developed countries. Developing countries have emerged as an important source of FDI

D. Morschett, H. Schramm-Klein, J. Zentes, *Strategic International Management*, DOI 10.1007/978-3-658-07884-3_18

flows and account for almost one third of global FDI outflows (UNCTAD 2013).

Figure 18.1 Global FDI Inflows (in billion USD)



Source: UNCTAD 2014.

Characteristics of Wholly-Owned Subsidiaries

This Chapter focuses on wholly-owned subsidiaries as a specific form of FDI. They are characterised by several key features (Cavusgil/Knight/Riesenberger 2014, pp. 423-425):

- *Greater resource commitment*: Establishing wholly-owned subsidiaries involves the highest commitment in terms of a firm's resources and capabilities.
- *Local presence and operations*: By establishing subsidiaries in the host countries, the MNC chooses to have a local presence and establish direct contact with local actors such as customers, intermediaries, suppliers or governmental institutions.
- *Global scale efficiencies*: By launching wholly-owned subsidiaries in different countries, MNCs can enhance their global performance if each location is chosen on the basis of competitive advantages. For example, R&D activities can be located in the most knowledge-intensive countries, or production facilities can be built at locations that provide the best ratio of productivity to labour cost.
- *Substantial risk and uncertainty*: Wholly-owned subsidiaries represent the highest level of risk because this strategy involves substantial local investment in the form of a permanent and fixed presence in the host coun-

try and thus exposes the MNC to local risk such as government inventions or inflation. It also reduces the company's flexibility.

- *Greater importance of cultural or social variables of the host markets*: Because of the high commitment to the host country markets, MNCs must deal more closely with particular social and cultural variables in order to minimise potential problems.

Table 18.1 shows the main advantages and disadvantages of wholly-owned subsidiaries.

Advantages and Disadvantages of Wholly-owned Subsidiaries

Table 18.1

Advantages	Disadvantages
• direct and independent presence • independent marketing activities • pushing of own strategies, easy alignment of own structures • uniformity of market appearance • influence- and supervision options • bundling and deployment of company know-how (supervision of inflow and outflow) • increasing market power towards buyers, suppliers and competitors • frequent settlement sponsorships by host countries	• investment requirements and barriers • high risks especially in insecure countries • build up of considerably resources • cost intensive acquisitions and time consuming start up • decision for investment much less reversible than other transaction forms ▪ disadvantages in terms of flexibility because of capital commitment but advantages through decision superiority

Source: Adapted from Kutschker/Schmid 2011, pp. 908-909.

Types of Wholly-Owned Subsidiaries

Establishing wholly-owned subsidiaries can be done in several ways. The main routes are *greenfield ventures* and *M&As*. *Greenfield investments* involve the establishment of new facilities in foreign markets, as opposed to *acquisition strategies*, i.e., purchasing existing facilities or existing companies in the host country.

Greenfield Investment

The *greenfield strategy* involves starting operations in the host country "from scratch" (Griffin/Pustay 2013, p. 363). As the term "greenfield" implies, companies typically invest in empty plots of land and build new facilities such as production plants, logistics subsidiaries, or other facilities for their own use (Cavusgil/Knight/Riesenberger 2014, p. 428).

This strategy gives the firm a much greater ability to build the kind of subsidiary company needed to efficiently pursue its *international strategy*. Firms can, for example, select the site that best meets their needs and construct modern or contemporary facilities (Griffin/Pustay 2013, p. 363). Unlike acquisitions, firms that follow the *greenfield strategy* start their activities in the host country with a clean record and do not need to deal with existing debts or problems resulting from the past activities of existing firms.

Government Incentives

Host countries often prefer MNCs to undertake greenfield investments because in many cases they create new jobs, new production capacity, and contribute to enhanced transfer of expertise to locals. Many governments therefore offer *incentives* such as flat tax or construction subsidies to encourage greenfield investments (Cavusgil/Knight/Riesenberger 2014, p. 428).

Tacit Knowledge

Greenfield investments may be also favoured by companies that operate in businesses where transferring competencies, skills, and expertise is difficult; *tacit knowledge* often plays an important role. By establishing new ventures, companies can build an organisation culture from scratch, which is much easier than changing the existing culture of an acquired unit. Also, it is easier to establish processes and procedural methods in a new venture than to convert existing operating routines of acquired units (Hill 2013, p. 498).

However, greenfield ventures are slower to establish. They are often riskier because of a higher degree of uncertainty, both in terms of future revenue and profit prospects (Hill 2013, p. 499).

Other *drawbacks* can be associated with specific types of subsidiaries. For example, when firms establish new production plants, it is important that land in the desired location is available. Additionally, firms must comply with various local regulations, recruit staff from the local workforce and train them to meet the MNC's performance standards (Griffin/Pustay 2013, p. 364). This can be a very *time consuming* process.

Mergers & Acquisitions

Brownfield Strategy

The second strategy to establish wholly-owned subsidiaries is the acquisition of existing facilities or existing firms in the host country. This strategy is also called the "*brownfield strategy*" of international expansion.

Merger

In a *merger,* two (or more) firms join to form a new, larger entity. The corporations combine and share their resources and often the shareholders of the combining firms remain as joint owners of the combined company. In an *acquisition,* the acquired firm becomes a part of the acquirer. In a merger a new entity is formed, subsuming the merging firms (Sudarsanam 2010, p. 3).

Horizontal Vertical and Conglomerate M&As

Cross-border M&As can be accomplished across different types of industries. In *horizontal M&As*, firms that operate in the same business, i.e. firms selling the same products or a similar range of products, are acquired or come together in a merger. These firms share certain commonalities such as inputs, technology, knowledge base, marketing or sales and distribution. In a horizontal M&A, the firms operate on the same level of the value chain.

In contrast, a *vertical M&A* is a combination of firms that produce goods or services that represent the output of successive stages of the same vertical chain, i.e. downstream or upstream activities in the flow of the production and distribution process. These forms of M&As represent a specific type of *vertical integration* (Barney/Hesterly 2012, pp. 164-166).

In horizontal and vertical M&As, firms that operate in the same industry are combined. *Conglomerate M&As* differ, because the firms that come together operate in unrelated businesses. Conglomerate M&As thus represent the *diversification* of business activities for the acquiring firm or the merging firms.

M&As may take many forms. Table 18.2 gives an overview of a selection of M&A strategies.

Types of M&A Strategies

Table 18.2

Strategy	Method
Merger of Equals	Companies of equal size come together. Often, one of the merging companies is considered the “primus inter pares” once the merger has taken place.
Friendly Takeover	The management of the takeover target has a positive attitude towards the takeover.
Tender Offer	Public, open offer by an acquirer to all shareholders. The bidder contacts the shareholders directly, inviting them to sell their shares to the offer price.
Unfriendly/Hostile Takeover	The takeover target is unwilling to be acquired or the target’s management has no prior knowledge of the offer.
Proxy Contest	Specific type of a hostile takeover in which the acquiring company attempts to convince the existing shareholders to use their proxy votes to install a new management that is open for the takeover.
Builder Acquisition	The objective of the acquisition is to integrate the takeover target into the network of the MNC, e.g. to realise synergies, economies of scale, etc.
Raider Acquisition	Acquisitions that are conducted with the purpose of post-acquisition asset stripping.
Leveraged Buyout (LBO)	Acquisition of a company with cash that is raised with a preponderance of debt raised by the acquirer. Several different types of LBO exist, depending on the acquiring party, for example investor buyout, management buyout, or employee buyout can be distinguished.

Empirically, cross-border M&As are the most relevant strategy. Table 18.3 gives an overview of worldwide cross-border M&A activity by home country of both selling and purchasing companies.

Table 18.3 *Cross-border M&As by Region of Purchaser and Seller in 2012*

Value of cross-border M&As by region/economy of seller, 2012 (in million of USD)		Value of cross-border M&As by region/economy of purchaser, 2012 (in million of USD)	
United States	66,113	United States	79,885
United Kingdom	35,852	Canada	39,474
Canada	29,325	China	37,111
Australia	23,087	Japan	35,666
Netherlands	17,051	Switzerland	16,254
Brazil	16,359	Germany	15,453
Ireland	12,096	Chile	9,764
France	11,985	Malaysia	9,292
China	9,995	Hong Kong/China	8,016
Switzerland	8,635	Russian Federation	7,807

Source: UNCTAD 2013.

Motives and Barriers of Cross-border M&As

M&As often take place in industries that are in the mature or declining stages of the product life cycle. These industries are characterised by low overall growth, excess capacity and a small number of large competitors. The main *motives* for cross-border M&As are revenue enhancement and cost savings (see Sudarsanam 2010, pp. 123-140):

- *Revenue enhancement*: (Horizontal) M&As lead to an increase in the market share of the merging firms, conferring enhanced market power. Additionally, the merging firms may be able to exploit each other's marketing resources, such as brands or general marketing expertise. The distribution channels established by each firm in the diverse countries may be used to sell the joint firm's products and thus the global presence of the new entity can be created expeditiously.
- *Cost savings*: A consolidating M&A is associated with opportunities for economies of scale, scope and learning in various functional activities such as production, marketing, distribution, logistics or R&D. However, the merging firms or the acquirer may also rationalise production and remove excess capacity from the new entity or the MNC's network. Additionally, redundancies in other functions such as marketing or distribution may be reduced, thereby reducing the fixed costs of the joint entity.

Nevertheless, cross-border M&As face a variety of *obstacles*. In the diverse economic and legal frameworks of different countries, there are barriers that can complicate M&As and hinder the attainment of objectives. The main *barriers* to M&As in different countries are described in Table 18.4.

Barriers to Cross-border M&As

Table 18.4

Structural Barriers	
Statutory	• strong powers for supervisory boards to block mergers; unions and workers' councils have say on takeovers and strong redundancy rights • issue of bearer shares, double voting or non-voting shares; absence of one share, one vote (OSOV) principle • discriminatory tax laws against foreign acquirers, e.g. withholding taxes on dividends
Regulatory	• antitrust regulation, foreign investment review, rules of stock exchange and professional self-regulatory bodies • absence of statutory or voluntary bodies to regulate takeovers
Infrastructure	• absence of M&A services, e.g. legal, accounting, investment banking services
Technical Barriers	
Management	• two-tier boards which cannot be removed or changed quickly • families dominate shareholding • powers to issue shares with differential voting rights or to friendly persons • powers to limit maximum voting rights; powers to override shareholders in company's interest
Information Barriers	
Accounting	• accounting statements not available, quality of information poor • low compliance with international generally accepted accounting principles; accounting practice biased to avoid tax liability, or conservative, hence accounting statements opaque
Shareholders	• due to issue of bearer shares, shareholding structure not known
Regulation	• regulatory procedures not known or unpredictable
Culture and Tradition	
Attitude	• "to sell is to admit failure" syndrome; dislike of hostile bids; dislike of institutional constraints on dividends or short-term profits • unwillingness to disclose information
Value system	• high premium on trust and confidence in negotiations rather than formal contracts

Source: Adapted from Sudarsanam 2010, p. 231.

Advantages and Disadvantages of M&As

The high relevance of cross-border M&As is a result of the major advantages associated with this strategy. By acquiring existing ventures or merging with partner firms, a company can obtain *quick access* to new markets and rapidly build their presence in the host country. In acquisitions, for example, the acquiring firm can use this strategy to rapidly build a sizable presence in the target market, because it gains control over the acquired firm's facilities, employees, technology, brands or distribution networks. It is important to notice that M&As add no new capacity to the industry. This is an obvious benefit in mature markets or if markets are characterised by *overcapacity* (Griffin/Pustay 2013, p. 364).

Entering foreign markets via M&A can also be a strategy to *pre-empt* an MNC's *competitors*. This is of major importance in highly globalised industries with intense competition (Cavusgil/Knight/Riesenberger 2014, p. 429). Cross-border M&As in this context can be used to rapidly obtain global scale and improve *competitive strength* compared with the MNC's global competitors (Hill 2013, p. 501).

Even though *acquisition strategies* are associated with large sums that have to be paid to acquire the takeover candidate, usually shortly after the deal is closed, acquisition strategies are often regarded as less risky than *greenfield investments*. The main argument is that the acquisition provides the MNC with an immediate stream of revenue and profits. Additionally, the firm acquires a set of tangible assets (e.g. factories, logistics systems) and intangible assets (e.g. local brands, local management expertise) that can reduce the risk of *mistakes* or *failure* in foreign markets (Hill 2013, pp. 501-503).

In *mergers*, the companies pool tangible and intangible resources and capabilities of the partner firms in the new entity. This is associated with economies of scale and scope. If these resources are complementary, the competitive advantage of the new venture may be enhanced.

Hidden Liabilities

However, cross-border M&As are associated with several disadvantages and often produce disappointing results. One of the main reasons for failures or problems in international acquisitions is that as well as purchasing all the valuable assets of the acquisition candidate, the acquiring firm is also confronted with all its *liabilities* (e.g. managerial or financial liabilities).

Often, the MNC cannot anticipate all the liabilities and buys "a pig in a poke". The acquired firm may, for example, reveal *hidden liabilities* such as poor labour relations or unfunded financial obligations once the acquisition process is finished (Griffin/Pustay 2013, p. 364).

Advantages and Disadvantages of Cross-border M&As

Table 18.5

Advantages	Disadvantages

• access to customers, distribution channels, materials, HR
• rapid market development
  ▪ time savings/synergy effects
  ▪ if applicable fast market entry in numerous geographic regions
  ▪ positive cash-flow
• scale effects
• gain of know-how
  ▪ complementary effects
• gain of market position/image
• fastest mode of diversification
• no increasing competition intensity in host
• country
  ▪ little danger of overcapacity
	• massive risk
	• huge capital availability as requirement
	  ▪ best case scenario: financial markets as balancing instrument
	  ▪ in reality: limited range of alternatives for SME
	• high information and search costs
	  ▪ adequate target company as basic requirement
	  ▪ negotiation problem (Information asymmetries)
	• necessity of coordination and integration of heterogeneous structures, systems, cultures
	• adaptation of market appearance required
	• provisos/resistances of local management
	  ▪ possibly brain drain
	• provisos/resistances of host country government (foreign infiltration)
	• growing management complexity

Source: Adapted from Zentes/Swoboda/Morschett 2004, p. 658.

In this connection, another problem in acquisition strategies relates to the calculation of an adequate price for the takeover candidate. It is difficult for acquiring firms to estimate the appropriate takeover sum and they often *overpay* for the assets of the firm acquired. This is often the case if more than one firm bids for the target firm (Hill 2013, p. 503). The main general advantages and disadvantages associated with cross-border M&As are summarised in Table 18.5.

Causes of Failure and Success in Cross-border M&As

Table 18.6

Cause of Failure	Cause of Success
• target management attitudes	• detailed post-acquisition integration plans
• cultural differences	• speed of implementation
• no post-acquisition integration planning	• clarity of acquisition purpose
• lack of knowledge of industry or target	• good cultural fit
• poor management of target	• high degree of target management cooperation
• no prior acquisition experience	• knowledge of target and its industry

Source: Adapted from Sudarsanam 2010, p. 726.

The disadvantages of M&As frequently lead to *integration failures*. Particularly in cross-border M&As, empirical evidence shows that in many M&A transactions the companies are not able to achieve the expected outcomes, e.g. in terms of economies of scale, market performance or synergy effects (see Table 18.6).

Conclusion and Outlook

Foreign direct investment is a hierarchical mode of international market entry. The establishment of wholly-owned subsidiaries, either by greenfield operations or by cross-border M&As, represents an *internalisation* strategy.

Despite high investment costs and a time-consuming process of entry into new markets, the main advantage of *greenfield investments* is that companies are able to establish *"optimal" facilities* that fit with the interests of the firm. Greenfield strategies offer the possibility to integrate *state-of-the art* technology (e.g. production facilities) and thus can result in increased operation efficiency.

Post-Merger Integration

Cross-border M&As also represent entry strategies that are usually associated with high investment costs. Additionally, they are characterised by high *costs of integration* of the diverse companies with diverse organisational (and national) cultures. While M&As provide opportunities for *rapid entry* into new markets and quick access to distribution channels, existing management experience, local knowledge, contacts with local markets, suppliers and governments and established brand names or company reputation, there also are high risks. For example, taking over companies that are regarded as a *country's heritage* can raise national resentments in the host country. Also, a lack of integration with the acquiring company's existing operations, between the merging firms or *communication* problems between the companies can produce unfavourable outcomes (Hollensen 2014, p. 413).

Further Reading

DUNNING, J.; LUNDAN, S. (2008): Multinational Enterprises and the Global Economy, 2nd ed., Cheltenham, Edward Elgar Publishing, pp. 116-144.

GHEMAWAT, P.; GHADAR, F. (2000): The Dubious Logic of Global Megamergers, in: Harvard Business Review, Vol. 78, No. 4, pp. 65-72.

HARZING, A. (2002): Acquisitions versus Greenfield Investments: International Strategy and Management of Entry Modes, in: Strategic Management Journal, Vol. 23, No. 3, pp. 211-227.

Case Study: ThyssenKrupp*

Profile History and Status Quo

This case study concerns the German company *ThyssenKrupp* and several of its business operations in international markets. More precisely, this case study provides insights into the company's activities with regard to wholly-owned subsidiaries, especially greenfield investments and mergers & acquisitions.

Today, *ThyssenKrupp* is the largest steel producer in Germany and one of the largest steel producing companies in the world. The multinational conglomerate is based in Germany and consists of 630 companies in 77 countries and has about 160,000 employees worldwide. As well as steel production, the company also provides components and systems for the automotive industry, elevators, escalators and industrial services.

The company is the result of the merger between *Thyssen AG* and *Krupp*, and now has its operational headquarters in Essen. The negotiations for the merger started in the early 1980s. The two companies then cooperated closely in several business areas and the proposed alliance was finalised in 1983. In 1997, the two companies combined their activities in the flat steel business and formed *Thyssen Krupp Stahl AG*. In the same year, *Krupp* and *Thyssen* further negotiated on expanding their cooperation into other business areas. During these talks, both companies identified a great potential for strategic development and operating synergies through a full merger, which took place in 1999.

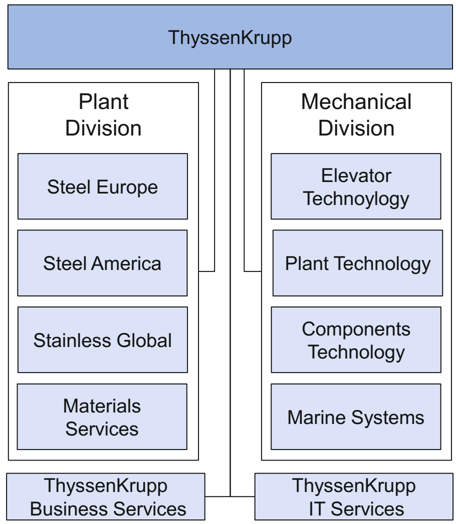
In 2009, the company was reorganised into eight business areas, which fall under the Materials and Technology divisions. After a further reorganisation, the Technology division was divided into Plant and Mechanical divisions. Today, the Mechanical division designs and manufactures high-quality components for the automotive, machinery, energy and construction industries. Furthermore, as a part of this division, the company also produces innovative technological goods such as modern elevator systems.

The Plant division extends from the engineering and construction of complete industrial complexes to a global service network and advanced naval technology. Last but not least, the Material division includes custom material solution, efficient materials manufacturing and processing with a focus on stainless steel and carbon steel, and materials services. The portfolio is fur-

* Sources used for this case study include the website http://www.thyssenkrupp.com as well as information from press releases and annual reports from ThyssenKrupp.

ther supplemented by *ThyssenKrupp Business Services* and *ThyssenKrupp IT Services* (see Figure 18.2).

Figure 18.2 *ThyssenKrupp Group Structure*



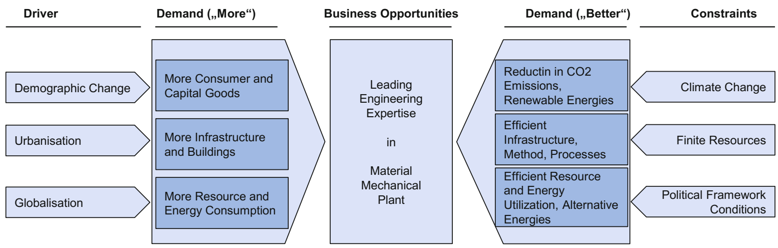
Source: ThyssenKrupp AG 2010.

The company's strategy focuses on the development of innovative products, high quality materials and intelligent industrial processes and services for a sustainable infrastructure and resource efficiency, providing several challenges and business opportunities (see Figure 18.3).

To achieve these strategic aims, *ThyssenKrupp* has to combine its traditional competitive advantage in materials with its engineering expertise and broad technology expertise to deal with a worldwide demographic change, the globalisation of goods flows and the rapid growth of mega cities, meaning that global demand still will continue to rise.

Figure 18.3

Business Opportunities for ThyssenKrupp



Source: ThyssenKrupp AG 2013, p. 31.

ThyssenKrupp has made several investments and previous attempts to deal with the aforementioned challenges and to realise future business opportunities in international markets. Throughout the company's history, an integral part of the company's business strategy for expansion and international growth has involved wholly-owned subsidiaries and mergers and acquisitions in emerging markets and international markets with a suitable infrastructure and a stable demand for the company's products. After a brief overview of activities in the company's early history, the following provides some detailed examples of greenfield investments and mergers and acquisitions made by *ThyssenKrupp*.

The Company's International Expansion

Mergers and Acquisitions

In the early 1970s, *Thyssen* was already considering ideas to strengthen the group's international focus. Plans to produce steel in different locations around the world and process it in Duisburg were abandoned after the 1973 oil crisis. To expand their business base and to reduce the company's dependency on steel demand, the *Budd Company* (USA) was acquired in 1978. With the acquisition of *Budd's* automotive operations in 1978, *ThyssenKrupp* entered the North American automotive industry. *Budd Company* became the automotive division of *Thyssen* and was operated in North America as *Budd Thyssen*, later *ThyssenKrupp Budd Co.* In October 2006, *ThyssenKrupp* sold *ThyssenKrupp Budd's* North American body and chassis operations to *Martinrea International Inc.*

During the 1990s, further international expansion was based on a concentration on selected fields of business with good market and earnings potential. In this context, it is worth highlighting the acquisitions of the machine tool manufacturer *Giddings & Lewis Inc.* (USA) and *Copper and Brass Sales Inc.*

(USA), a leading trading and service centre for nonferrous metals in North America, in 1997, and of *Dover Elevators* (USA), market leader in hydraulic elevators in North America, in 1998.

Four years later, *ThyssenKrupp* acquired the Korean-based *Dongyang Elevator*. These latter acquisitions can be considered the starting point of the company's tremendous success in the international elevator market. After that, *ThyssenKrupp Elevator* pressed ahead with acquisitions of established small and medium-size elevator companies in the USA in the following years. In 2013, *ThyssenKrupp* acquired all the assets of Ohio-based *Edmonds Elevator, Inc.* With this acquisition, *ThyssenKrupp* continued its international growth strategy and strengthened the company's service business in the North American market.

Investment in North America

In 2007, as a part of their forward strategies for profitable and sustainable growth, *ThyssenKrupp* started to plan a new plant in the USA at a cost of 2.3 billion EUR. After a phase of extensive preliminary investigations, the site selection process focussed on Alabama and Louisiana. The investigations revealed several positive factors in these states in terms of energy costs, logistical advantages and geological conditions.

This greenfield venture was mainly intended to considerably strengthen *ThyssenKrupp's* position in North America. The NAFTA (North American Free Trade Agreement) is one of the biggest volume markets for high-quality flat carbon steel, and *ThyssenKrupp* thought that the company would be able to leverage the strengths of its broad range of high-quality products in this sector. Another reason for setting up a new production facility was that at this point in time *ThyssenKrupp* was already an established producer on the NAFTA market thanks to its cold rolling mill in Mexico and sales/distribution bases in the USA. Hence, the new plant was intended to produce for the fast-growing US market, while the production facility in Mexico focused more on the Mexican market. The central element of the new plant was a hot strip mill, which would be used primarily to process slabs from the new *ThyssenKrupp* steel mill in Brazil. In addition, the plans for the new plant included cold rolling and hot-dip coating capacities for high-quality flat carbon steel end products.

Overall, the estimated annual capacity of the new production facility was about 4.5 million metric tons of end products and the planned costs of the investment were about 1.8 billion EUR. The new plant opened in December 2010. It was ultimately one of the largest foreign investments in the history of *ThyssenKrupp*. Contrary to expectations, the overall costs of the new production facility were about 3.7 billion EUR.

Greenfield Investment in Brazil

In 2005, *ThyssenKrupp* started planning the construction of a new facility to produce steel in Brazil for the global market. The initial estimated costs for the establishment of the new production facility were about 1.3 billion EUR. But, when construction was finished in 2010, the final costs for this greenfield investment proved to be much higher (about 5.3 billion EUR). The reasons for this tremendous increase in costs were the strict constraints put in place by the Brazilian government regarding environmental protection, especially concerning prevention of atmospheric pollution. The new plant was intended to produce five billion tons of steel, which would be refined in Germany and in North America for the automotive industry in Europe, North America and China.

In 2014, *ThyssenKrupp* started the construction of a new automotive supply plant for the production of assembled cylinder-head modules in Brazil (Pocos de Caldas, Minas Gerais). The company has invested about 40 million EUR in the construction of the plant, which is expected to be completed by the end of 2014 and will create about 170 jobs. The production is planned to start in early 2015. With this greenfield investment, *ThyssenKrupp* will be able to produce more than one million modules a year. The finished products will mainly be supplied to car producers in Brazil.

The new Brazilian plant is the fourth such plant being built or put into operation around the world by *ThyssenKrupp* since 2013, and it is an important part of the company's global growth strategy as a supplier of high-performance components for the automotive industry. As a result of extraordinary efforts in the development of innovative and high-quality components for the automotive industry, *ThyssenKrupp* now has a substantial competitive advantage compared to its competitors in the global market. For example, *ThyssenKrupp's* products allow car producers to reduce weight by up to 30%. This will considerably lower fuel consumption and hence reduce carbonate dioxide emissions.

But ultimately the greenfield investments in the North and South American market strategy were not a success. With the beginning of the worldwide recession starting in 2008 and the associated cutbacks, *ThyssenKrupp* lost about 8 billion EUR on its two new plants in North America and Brazil, which sold steel below the cost of production. Hence, the two steel production facilities were offered for sale as a consequence of continuous losses. *ThyssenKrupp's* stainless steel division, including the stainless portion of the US plant, was sold to Finnish stainless steel company *Outokumpu* in 2012. In 2013, *ThyssenKrupp* offered the remaining portion of the plant for sale at less than 4 billion USD. Finally, *ThyssenKrupp's* Clavert carbon steel production facility was sold to *ArcelorMittal* and *NipponSteel* in 2014.

Overall, the greenfield investments of *ThyssenKrupp* in North America and

Brazil and the related losses have caused serious problems for the whole company. While this strategy has allowed *ThyssenKrupp* to protect their tacit knowledge from competitors in the new market to a certain degree, these investments show the associated high risks of this kind of internationalisation strategy for the overall business success of a company, due to the high investments and long time required to establish new production facilities and create a business in a foreign country.

International Expansion into the Chinese Market

For *ThyssenKrupp*, China is the world's most important growth market. In the last two fiscal years the company has invested about 250 million EUR in new supply plants for the Chinese automotive industry and now has seven Chinese production facilities in this technology sector.

In 2013, *ThyssenKrupp* opened a new automotive supply plant in China (Chengdu, Sichuan Province). Thanks to the opening of this new production facility, the company now produces springs and stabilisers for the Chinese automotive market. Springs and stabilisers are important comfort and safety related components in cars. They ensure even grip, while absorbing and cushioning shocks from the road surface and centrifugal forces during cornering. *ThyssenKrupp* has invested around 20 million EUR in the new plant and has created about 200 new jobs. The strategic expansion of automotive supply plants in one of the world's fastest growing regions is a key component of *ThyssenKrupp's* transformation into a diversified technology group.

Overall, since 2010 the company has invested around one billion EUR in the global expansion of its auto components business. Another production facility for cylinder head modules is currently under construction. The components produced there support the company in its ability to meet the still rising demand for greater personal mobility in the Asian market, by meeting the need for lighter, more comfortable, more economical and safer vehicles.

A new production line for cylinder-head modules in Dalian and a new crankshaft plant in Nanjing were opened in 2013. In Shanghai, a new production line for steering systems also started operation. The company has invested around 350 million EUR in these projects.

Overall, *ThyssenKrupp's* range of automotive products in China now ranges from crankshafts, camshafts, cylinder head modules and steering systems to springs and stabilisers. In total, *ThyssenKrupp* employs around 3,800 people at ten production facilities in the components sector for the Chinese auto, truck and building machinery and wind power industries. In the 2012/2013 fiscal year, the company generated sales of around 750 million EUR in this segment in China, with the automotive sector accounting for about two thirds of this result.

Summary and Outlook

The company's strategy of global growth through greenfield investments and mergers and acquisitions is an integral part of *ThyssenKrupp's* business strategy and has considerably strengthened the company's position in the international markets. Today, *ThyssenKrupp* generates about 69% of its consolidated sales in international markets, while customers in the German domestic market account for the remaining 31%. Overall, the member countries of the European Union (24%) and North America (21%) are the key foreign markets for the company's business activities.

ThyssenKrupp companies hold leading positions with their products in numerous international markets and the degree of internationalisation of the whole group is still rising. *ThyssenKrupp* is already the world market leader in assembled camshafts and is continuously optimising this established technology in line with the latest findings and requirements. The company is able to meet car manufacturers' demands for lightweight components and the associated reduction in fuel consumption. Furthermore, *ThyssenKrupp* is one of the world's leading elevator manufacturers (sales: 5.7 billion EUR in the 2011/2012 fiscal year). Their portfolio consists of passenger boarding bridges, stair and platform lifts, as well as tailored services for all components.

Questions

1. List the potential advantages and disadvantages of greenfield investments and M&As and evaluate *ThyssenKrupp's* current situation.
2. Does the sequence of *ThyssenKrupp's* strategy of international expansion follow the theoretical concept of psychic distance?
3. Which processes and organisational structures are important for creating new subsidiaries in foreign countries?

Hints

1. See Gaughan 2002.
2. See Chapter 14 as well as Sousa/Bradley 2004 for an explanation of the concept of psychic distance.
3. See Collis 2014.

References

BARNEY, J.; HESTERLY, W. (2012): Strategic Management and Competitive Advantage: Concepts, 4th ed., Upper Saddle River, New Jersey, Pearson.

CAVUSGIL, S.T.; KNIGHT, G.; RIESENBERGER, J.R. (2013): International Business: The New Realities, 3rd ed., Boston, Pearson.

COLLIS, D. (2014): International Strategy and Competition, New York, Wiley & Sons.

DUNNING, J.; LUNDAN, S. (2008): Multinational Enterprises and the Global Economy, 2nd ed., Cheltenham, Edward Elgar Publishing.

GAUGHAN, P. (2002): Mergers, Acquisitions, and Corporate Restructurings, 3rd ed., New York, Wiley & Sons.

GHEMAWAT, P.; GHADAR, F. (2000): The Dubious Logic of Global Megamergers, in: Harvard Business Review, Vol. 78, No. 4, pp. 65-72.

GRIFFIN, R.; PUSTAY, M. (2013): International Business: A Managerial Perspective, 7th ed., Upper Saddle River, New Jersey, Pearson.

HARZING, A. (2002): Acquisitions versus Greenfield Investments: International Strategy and Management of Entry Modes, in: Strategic Management Journal, Vol. 23, No. 3, pp. 211-227.

HILL, C.W.L. (2013): Global Business Today, 8th ed., Boston, McGraw-Hill.

HOLLENSEN, S. (2014): Global Marketing, 6th ed., Harlow, Pearson, pp. 471-648.

KUTSCHKER, M.; SCHMID, S. (2011): Internationales Management, 7th ed., Munich, Oldenbourg.

SOUSA, C.M.; BRADLEY, F. (2006): Cultural Distance and Psychic Distance: Two Peas in a Pod?, in: Journal of International Marketing, Vol. 14, No. 1, pp. 49-70.

SUDARSANAM, S. (2010): Creating Value from Mergers and Acquisitions: The Challenges, 2nd ed., Harlow, Financial Times Prentice Hall.

THYSSENKRUPP AG (2010): 11th General Stockholders' Meeting ThyssenKrupp AG, Bochum.

THYSSENKRUPP AG (2013): Annual Report 2012/2013, Essen.

UNCTAD (2013): World Investment Report 2013: Global Value Chains: Investment and Trade for Development, Geneva.

UNCTAD (2014): World Investment Report 2014: Investing in the SDGs: An Action Plan, Geneva.

ZENTES, J.; SWOBODA, B.; MORSCHETT, D. (2004): Internationales Wertschöpfungsmanagement, Munich, Vahlen.