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**An empirical investigation into the effect of international trading strategy choice on financial performance**

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The University of Nebraska - Lincoln, 1988



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AN EMPIRICAL INVESTIGATION
INTO THE EFFECT OF INTERNATIONAL
TRADING STRATEGY CHOICE ON
FINANCIAL PERFORMANCE

by

Patricia Manley Feltes

A DISSERTATION

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For the Degree of Doctor of Philosophy

Major: Interdepartmental Area of Business

Under the Supervision of Professor Lester A. Digman

Lincoln, Nebraska

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## TITLE

AN EMPIRICAL INVESTIGATION INTO THE EFFECT OF INTERNATIONAL TRADING STRATEGY CHOICE ON FINANCIAL PERFORMANCE

**BY**

PATRICIA MANLEY FELTES

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AN EMPIRICAL INVESTIGATION
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Advisor: Lester A. Digman

Firms may choose among three strategies related to international trading: Domestic; Export; and, Foreign Direct Investment. This study hypothesized that firms in high-technology industries which follow pro-international trading strategies (Export or Foreign Direct Investment) financially outperform firms in the same industries which follow a Domestic strategy.

In addition, it was suggested that that relationship would vary significantly based on two environmental factors -- one external (industry characteristics) and one internal (firm size). With respect to size, it was expected that smaller firms, using an Exporting strategy would be more successful than those that used a Domestic or Foreign Direct

Investment strategy, while among the large firms, the most successful would use a Foreign Direct Investment strategy.

The relationship between international trading strategy choice and financial performance could also be differentially affected by external factors (industry characteristics). The level of seller concentration was used as a surrogate measure of barriers to entry to classify the two related industries in the study.

The results of the research did not support the hypotheses. The international trading strategy used by a firm was not significantly related to higher rates of financial performance, nor did those findings vary when the interaction of size or industry concentration was considered.

According to the study, participation in the international marketplace will not necessarily result in either positive or negative effects on a firm's financial returns. Therefore, the decision to become involved in international trading must rest on other perceived benefits rather than on the assumption of the receipt of short-term financial benefits.

## DEDICATION

with love to

Estelle Manly

John Manly

Paula Halbmaier

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for all occasions, and for being an example of how to make the difficult seem easy.

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Thank you all.

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# Overview of Research

## Introduction

Organizations created to generate profits from their activities are interested in the maximization of those profits (Venkatraman & Ramanujam 1986; Caves 1977 p. 5; Kirchhoff 1977) either directly through the profit margin or indirectly through growth (Caves 1977 p. 4). The improvement of organization performance is at the heart of strategic management (Venkatraman & Ramanujam 1986; Steers 1975) and the test of its success (Schendel & Hofer 1979).

To accomplish this, strategies are chosen to mesh the internal resources of the organization with identifiable opportunities in the environment. Firms attempt to find some competitive advantage in relation to their industry and environment. "Strategy is generally viewed as a pattern of important decisions that 1) guides the organization in its relationships with its environment, 2) affects the internal structure and processes of the organization, and 3) centrally affects the organization's performance." (Hambrick 1980)

One of the primary aims of strategic management research is to develop prescriptive theories which will aid firms in their choice of high performance strategies (Porter 1980; Barney 1986). In order to develop these theories, researchers have attempted to identify linkages among environmental conditions, strategic decisions, and economic performance (Fahey & Christensen 1986).

An area of research which has received limited attention but has potential effect on corporate performance is the international trading strategy chosen by the firm. This study conducted an empirical investigation of that issue. In addition, it suggested that financial performance within an industry varies as a result of the interaction of firm size and the chosen international strategy.

Questions of interest in this study can be stated as follows:

1.) What is the relationship between a firm's international trading strategy and its financial performance?

2.) Does the size of the firm interact with the international trading strategy to vary the relationship?

3.) Does the international trading strategy and firm financial performance relationship vary because of seller concentration level differences between industries?

## Background

### Organization Performance

The relative success of a firm seldom can be traced to a single factor (Lenz 1980). Researchers have investigated a number of variables in attempts to explain the different performance results among companies.

A few of the studies and their variables of interest include: size of firm (Child 1974, 1975); size of market share (Prescott, Kohli & Venkatraman 1986; Buzzell, Gale and Sultan 1978); formal planning (Rhyne 1986; Schoeffler, Buzzell & Heany 1974); diversification (Rumelt 1982); investment intensity and product quality (Hambrick, MacMillan & Day 1982); divestment (Duhaime & Grant 1975); environment (Porter 1980; Harrigan 1980); age of organization (Freeman, Carroll & Hannan 1983); and choice of strategy (Hatten, Schendel & Cooper 1978).

Dalton, Todor, Spendolini, Fielding and Porter (1980) in a review of the literature, found a limited number of organization structure studies that used performance as a dependent variable. Of the five studies relating corporate performance to total organization size, only two used "hard criteria" ie. sales, growth, profit etc.

Performance Improvement

Full utilization of assets, including intangibles, is one approach to increase performance (Teece 1984). Intangible assets can include unique process knowledge (employee know-how in production, research and development, marketing; management characteristics or structure; perceived differentiation of product or service) and/or a specific property (trademarks, brandnames, patents; unused credit capability) (Caves 1982).

As long as performance is satisfactory and a firm can fully employ its assets in its present market, it has no incentive to look beyond that market's boundaries. When that market can no longer profitably utilize those assets, the firm looks outside the

market for opportunities. These opportunities may consist of: 1) increased penetration of the existing market by the existing product line through price or advertising competition ie. taking share away from the competition, 2) the development of new products for the existing market, 3) the expansion of the served market for the present product; and 4) the diversification into new products and markets (Kotler 1976; Ansoff 1965).

Growth-minded organizations will consider increasing the market served from a local focus to a regional, national, or international one (Thompson & Strickland 1981 p. 53). International geographic expansion of the market for the products presently produced is, therefore, one of the strategic options available (Pugel 1980).

International Strategy and Performance

Limited study has been done to investigate the relationship of the choice of international strategy and the financial performance of the corporation. In particular there have been few studies which have compared the effect of the particular forms of international trading strategy.