

A Systematic Review of Challenges Experienced by Cross Border Investments in Developing Countries. A Case of Multinational Companies Expanding into The African Region

Tatenda Katoma, Dr. Abubaker Qutieshat

PhD Business and Management, University of Zambia, Graduate School of Business, Great East Road Campus, Lusaka, Zambia, Email : tk.tate24@gmail.com

Associate Professor & Research Lead, ODC, Oman, Associate Member of Staff & Honorary Researcher, University of Dundee, UK, Email address: aqutieshat@dundee.ac.uk. ORCID: <https://orcid.org/0000-0002-3569-6576> (Links to an external site.)

Abstracts: This paper provides a systematic review of challenges faced by multinational companies in developing countries, in particular the African region. This paper review relevant literature aimed at addressing the research question: "What are the challenges faced by cross border investments as they expand into Africa? The paper discusses the findings and proposes various recommendations to the challenges with the aim of improving the investment environment in developing countries to boost economic activity. Major challenges identified to be impacting cross border investments in developing countries are Political environment, regulatory environment, diversity and multicultural challenges, Leadership, Governance and Economic environment. For the purposes of literature review, the term cross border investments may be interchanged with Multinational Companies. The paper concludes by highlighting areas for future research.

Keywords: Multinational Companies, Challenges, Developing Countries, Cross Border Investments.

1. INTRODUCTION

Many companies are diversifying their businesses by expanding into foreign markets. This has resulted in significant increase in capital flow across borders and uplift in regional and international trade. Multinationals and regional companies face an array of challenges when they want to expand into other territories. This is negatively impacting the potential investments in most developing countries and also resulted in very high cost of capital charges in the event that capital is deployed. The aim of this research paper is to focus on the challenges being faced by these companies and also having deep insight into those companies that have failed or lost capital through regional expansion. The intention of this paper is to have a clear understanding of the African investment environment and be able to come up with a model that positions Africa as a safe investment destination.

In recent decades, cross-border money flows have significantly increased in size and significance. Foreign investment is a substantial source of funding for emerging economies and accounts for a sizeable share of the global GDP in many nations (Lane and Milesi-Ferretti, 2007). Numerous researchers have examined various drivers of bilateral capital flows, ranging from macroeconomic conditions and geographic proximity to institutional quality.

While all investments are exposed to political uncertainty, foreign investment is burdened with additional layers of rules and regulations associated with national boundaries such as capital controls and differential tax treatments. Furthermore, foreign investments are subject to expropriation risk, culture shocks and governance challenges.

1.1 Methodology of The Systematic Review

The perusal of papers used for this systematic review was done between January 2023 and March 2023. The following sources were used to select papers and examine the relevant references that are consistent with the problem statement, namely: Science Direct, Economic Literature (Econlit), Google Scholar, Research Papers in Economics (RePEc) and the mainstream search engine of Google.

2. LITERATURE REVIEW

2.1 Political Challenges

In terms of conflict, courts in destination countries may be biased in favour of native companies and investors (Bhattacharya et al., 2007). Since the foreign investor has little protection from the legal and political institutions of the host nation, Dixit (2011) emphasizes that cross-border investment is more vulnerable to the political climate than domestic investment. FDI is thought to be the form of cross-border capital flow that is most susceptible to political instability and institutional changes. According to Stokey (2016), businesses adopt a wait-and-see strategy when tax policy is in flux but is expected to be clarified soon. Businesses postpone irreversible investment until the ambiguity is cleared up, and then they proceed with the postponed initiatives, sparking a brief increase in investment.

Rodrik (1991) simulates the decisions made by private foreign investors in the context of political unpredictability, whereby foreign investors delay making investments until a significant level of ambiguity over the outcome of political reform is cleared up. Political leaders' choices can have an impact on a variety of issues, including taxation, labour regulations, raw material costs, transportation infrastructure, educational systems, and many more.

2.2 Diversity and Multicultural Challenges

Other equally significant obstacles to cross-border investment include the capacity to adapt to cultural variations, standards, and practices, Sauvart, et al (2009).

Varied Demographics

MNCs frequently make the serious error of assuming that African consumers are uniformly homogeneous, Cui (1999). Regional differences in consumer preferences exist even within the same nation. Local expertise is necessary for cross-border investments to succeed in the market, but it can be difficult to acquire, particularly if the company is run by an expat.

It can be difficult for an MNC to open offices all over the region Sungmala & Verawat (2021). In order to prevent offense and promote harmonious teamwork, they must strike a balance between allowing employees to express their opinions and educating everyone about cultural diversity.

Localizing company culture

French employees were perplexed by Google's emphasis on positive comments when the business first opened headquarters in France Meyer (2015). That was because Google's "American" organizational culture emphasizes providing positive feedback quite regularly, in contrast to the French culture, which values criticism more than acknowledgment. In most cases, the terms "localization" and "globalization" are used to describe the process of tailoring a product to the market in which it is sold, respectively. These ideas also apply to organizational culture, Meyer (2015). Leaders should be encouraged to localize that culture where appropriate, even while multinationals have a broad global culture that embraces their principles.

Language Barriers

The languages used in the nations you want to expand into while conducting business internationally are crucial to take into account, Zander et al (2012). Does the messaging for your product translate well into another language? This can be a major setback for a company as it tries to position its products in the market. One example of a product that was "lost in translation" is Mercedes-Benz, a high-end automobile manufacturer, Chiang & Mi, (2009). The business picked the moniker Bensi, which is Mandarin Chinese for "Benz," when it entered the Chinese market. Mandarin Chinese translation of the moniker is "rush to death," which was not the image

Mercedes-Benz wanted to make on its new audience. The business swiftly changed its name to Benchi, which means "run quickly, speed, or gallop," in Chinese, Catherine Cote (2020).

2.3 Financial and Economic Challenges

Price Centric Customers

According to Cant & Scheers (2012) Africans have a special, price-focused mentality that is frequently cited as one of the issues cross border investments encounters. Statistics show that Africans are more price conscious than brand loyal. Balancing cost and quality; recognizing the importance of institutions including the legal, political, and educational systems; and blending traditional local culture with contemporary global culture (Zainulbhai, 2005).

Emerging markets are characterized by high price sensitivity, regional demands, and low purchasing power Prahalad & Lieberthal, (1998). Transactional risks, income risks from operations, income risks from financing, and accounting risks resulting from changes in the rate of exchange of the local currency are additional risks for MNCs. They also face inflation threats, bank instability, and legal exposures, Prahalad & Lieberthal, (1998). Currencies are different from one country to the other and exchange rates also do differ from one nation to another.

2.4 Leadership and Human Capital Challenges

Given Africa's talent pool and the resources accessible to cross border investments, Meyer & Xin (2018) one would think hiring new employees would be simple, but in fact, hiring new employees remains one of the difficulties foreign businesses in Africa confront. First of all, the major global corporations are competing with one another to hire the best candidates. Secondly, the crème of Africa's best institutes is no longer satisfied with working for a brand, they want to develop their own. Research has shown that national values and conventions typically take precedence over organizational procedures when analyzing the relationship between a company's culture and those of its country markets, Meyer & Xin (2018). This has a big impact on how motivated individuals are at work, and as a result, leaders encounter opposition when implementing company-wide initiatives rather than obtaining local support.

Managing Global Teams

Managing personnel who are located all over the world is another difficulty faced by multinational corporations, Zander (2012). It can be challenging to take into consideration time zones, language difficulties, cultural variations, and various levels of technology access and dependency while attempting to work as a team.

In terms of organisation structure, for example, Asian managers may be more directive to their subordinates, with the latter possessing a lower degree of expectation when it comes to flexibility to pursue directions on their own volition, Cote (2020). Conversely, in the West, employees are entrusted with greater flexibility to make independent choices but may tend to be more focused on personal achievement than devotion to their bosses. The way one's message is received by international co-workers may also vary when it comes to communication. In order to ensure that the content is understood as intended while presenting across cultures, it is crucial to modify the delivery style, Cote (2020).

Cognitive bias

Although avoiding biases when working with, managing, or selling in foreign nations may be particularly challenging, it is crucial to be aware of these tendencies and steer clear of them wherever feasible, Cote (2020). Also, when entering Asian markets, miscommunication and other difficulties can result from the East and Anglo-Saxon cultures' various cognitive orientations, Cote (2020). Although these differences may result in more serious disputes, they also give rise to a wider range of options and viewpoints.

2.5 Governance Challenges

Globalization may be a reality, but it is still extremely unstable, one of the most significant difficulties faced by governments and corporate leaders alike is bridging the gaps in global governance frameworks and integrating global market forces into common ideals and institutionalized practices Kell & Ruggie, (1999). Industrial infrastructure is ineffective, there is no protection for intellectual property rights, there are high tariffs, expensive bureaucracy, ambiguous rules and regulations, monopolistic practices, control over distribution systems, unreliable and subpar suppliers, and there is general industrial manipulation, Gutierrez, Spencer & Zhu, (2012).

The business climate in emerging nations is fraught with hazards of various kinds, including bribery, corruption, facilitation fees, improper gratuities, and gift-giving. In the case of emerging markets, other behaviours such as commercial bribery, vendor collusion, conflicts of interest, asset misappropriation, and fake financial reporting have been recorded, Boets, (2008).

2.6 Regulatory Challenges

Other significant problems in the emerging markets include the lack of specialized intermediaries, a regulatory framework, and means for enforcing contracts. Khanna, Palepu & Sinha, (2005). Even though this model significantly expands the pool of possible clients, it also necessitates that businesses are familiar with local customs and regulatory obligations. Various countries have differing rules regarding competitiveness, environmental resources, and human rights, which could result in either more profits or bigger problems, Backer (2015).

Repatriation of capital, income, and dividends is another issue for MNCs, assert Moosa and Kardak (2006). Around 50% of IMF members have implemented limitations during the past ten years, blocking remittances from multinational corporations. These limitations sometimes take the form of temporarily preventing subsidiaries from sending royalties, fees, and/or profit back to their parent company's headquarters. Survey results and actual evidence point to how these constraints impact cross border investments. One of the top three variables influencing decisions to make direct investments is repatriation limits, according to Moosa and Kardak's (2006) study of 300 MNCs.

2.7 Market Entry and Positioning Strategy

According to Zainulbhai (2005), other significant challenges MNCs in developing countries face include appropriate market segmentation, dealing with the low purchasing power of the majority of the market, and establishing successful marketing techniques to use in various segments of the changing society.

Guarino (2010) argues that military coups, hyperinflation, and debilitating foreign debt were all fairly typical in emerging countries not too long ago. When emerging markets develop, common hazards include contract non-compliance, intellectual property theft, violation of rules and regulations, product counterfeiting, and gray marketing of high-margin or high-value goods, Boets (2008).

3. FINDINGS AND DISCUSSION

Good ideas fail at times, as history has demonstrated, so firms must exercise extra caution when venturing into uncharted seas.

Political and regulatory challenges

In recent years, multinational companies have been criticized. Over Years They have begun to participate with the internal political relations of the countries in which they work in order to protect their rights. Multinational businesses are willing to invest every amount, Stokey (2016) and pay for the bribe to preserve their rights. These allegations have resulted in stringent laws and regulations being enforced on cross border investments.

Regulation is also tightened on cross border investments as these companies are generally accused for avoidance of taxation. In countries with the lowest tax rate, several multinationals set up businesses. They funnel benefit into the countries with the lowest tax rates for companies.

Multinational corporations are usually vertically integrated, and they have been accused of transfer pricing challenges. Companies set prices arbitrarily to have to pay fewer taxes in host country, Barker (2015). To reflect smaller profits made in Africa, they intentionally raise the transfer prices for intermediate products (i.e., components) manufactured in their parent country or by their foreign affiliates. They are successful in avoiding paying corporate income tax as a result.

Culture and diversity

Depending on complexity of the job and specialty knowledge required, companies should give preference to local leadership instead of expats in order to align company culture and host country culture. These individuals are more knowledgeable about what it takes to be successful in their market and are familiar with both the market dynamics and the cultural makeup of the nation.

Leadership and Human resources

Soft skill development is very essential in the success of cross border investments. Leaders should spend more time aligning the company culture and the cultures of their personnel. Most companies in Africa that have seconded expats to lead their new foreign investments have, in some instances, struggled to instil a winning culture within these companies.

The respect and emotional intelligence required to conduct business successfully can be projected by demonstrating that you have taken the time to understand their cultures when managing teams in foreign offices.

Financial and economic challenges

At times cross border companies do not give themselves time to learn about the currency exchange rates between their home nation and the countries with which they intend to conduct business. On pricing, some MNCs adopt their home nation pricing strategy which may result in them being uncompetitive in host countries.

It's also critical to keep an eye on inflation rates, which can be volatile and catastrophic to the companies' international investments. The cost of materials and labour can be affected by the inflation rates that differ between nations and may result in the business becoming unsustainable.

Understanding and keeping an eye on these two variables might help businesses gain important information about the future market worth of the products they sell.

4. RECOMMENDATIONS

Given the variety and complexity of the risks faced by cross border investments in emerging markets, Boets (2008) contends that establishing a risk culture, properly aligning organizational structure and risk management procedures, and improving communications can build a solid foundation for better risk management in any market. MNCs have the following options for managing risks:

providing host customers with excellent products and services at fair prices; investing in regional markets, collaborating with the local government, advocacy organizations, and corporate players.

Management Challenge: It can be challenging to run a business successfully in a developing market for a number of reasons. According to Boets (2008) the general management challenges faced by cross border investments fall into three categories:

- The management principles that the MNCs has adopted, such as choosing to hire managers from one's own nation rather than the host nation or other countries.
- An organizational structure with mechanisms for operational control, such as how the parent company and its subsidiaries are related and how decision-making authority is distributed.
- Controlling corporate culture (i.e., home country versus host country management techniques, styles, and work culture). It involves either imposing one's own culture on that of the host country, accepting local culture, or fusing the two together. It's also quite important to look at the languages that the team members of your organization who work in overseas offices speak. Again, using interpreters can help make sure that your business continues to run smoothly.

To build and maintain a strong working relationship, encourage regular check-ins with your international staff, preferably via video conferencing software so you can speak in real time. According to Gallup research, employees who routinely check in with their superiors are three times more likely to be engaged at work than those who don't.

Overall, cross border investments should invest in feasibility studies to fully understand their targeted territories. They should engage local consultancies who have full understanding of the macro-economic environment and the targeted industry.

For future studies, I recommend employing primary research data collection to gather feedback from those companies that have gone regional. This data gathering will bring a better understanding on the market entry and positioning strategies, challenges encountered and how they were resolved.

CONCLUSION

This paper examines challenges that are faced by cross border investments in developing countries. The results from the systematic literature review shows that there are various challenges, ranging from macro-economic challenges, industry challenges and firm specific challenges. It is of paramount importance for these firms to embark on thorough market research to have a deep understanding of the targeted market before deploying resources. More success stories of cross border investments will result in more companies pursuing regional and international investments resulting in more capital flow, increased economic activity and improved livelihood.

REFERENCES

- [1]. Backer LC. Regulating multinational corporations: Trends, challenges, and opportunities. *Brown J. World Aff.*. 2015;22:153.
- [2]. Bass AE, Chakrabarty S. Resource security: Competition for global resources, strategic intent, and governments as owners. *J Int Bus Stud.* 2014 Oct 1;45:961-79.
- [3]. Cant M, Scheers LV. Identifying the correlation between the gender and knowledge of the South African consumer in the selection of grocery products. 2nd International Conference on Economics, Trade and Development. 2012 Jan 2 (Vol. 36).
- [4]. Cahen FR. Internationalization of state-owned enterprises through foreign direct investment. *Rev de Adm Empresas.* 2015 Nov;55:645-59.
- [5]. Chiang SY, Mi H. Glocalization through Global Brand Transposition. *Imagining Globalization: Language, Identities, and Boundaries.* 2009:45-59.
- [6]. Choudhury P, Khanna T. *Toward resource independence—Why state-owned entities become multinationals: An empirical study of India's public R&D laboratories.* Springer International Publishing; 2018.
- [7]. Christiansen H, Kim Y. State-invested enterprises in the global marketplace: Implications for a level playing field.
- [8]. Cote C. 5 Common challenges of international business you should consider. Harvard Business School Online, available at: <https://online.hbs.edu/blog/post/challenges-of-internationalbusiness> (accessed 17th March 2022). 2020.
- [9]. Cuervo-Cazurra A, Inkpen A, Musacchio A, Ramaswamy K. Governments as owners: State-owned multinational companies. *J Int bus stud.* 2014 Oct 1;45:919-42.
- [10]. Cui G. Segmenting China's consumer market: A hybrid approach. *In Consumer Behavior in Asia 2014 Jun 23 (pp. 55-76).* Routledge.
- [11]. Duanmu JL. State-owned MNCs and host country expropriation risk: The role of home state soft power and economic gunboat diplomacy. *J Int Bus Stud.* 2014 Oct 1;45:1044-60.
- [12]. Estrin S, Meyer K, Nielsen B, Nielsen S. The internationalization of state owned enterprises: The impact of political economy and institutions. London Business School. 2012 Oct 31.
- [13]. Goldstein A. New multinationals from emerging Asia: the case of national oil companies. *Asian Dev Rev.* 2009 Jul 1;26(2):26.
- [14]. Gouri G. Privatisation and public sector enterprises in India: Analysis of impact of a non-policy. *Econ Polit Wkly.* 1996 Nov 30:M63-74.

- [15]. Gupta N. Partial privatization and firm performance. *J Finance*. 2005 Apr;60(2):987-1015.
- [16]. Lane PR, Milesi-Ferretti GM. The external wealth of nations mark II: Revised and extended estimates of foreign assets and liabilities, 1970–2004. *J Int Econ*. 2007 Nov 1;73(2):223-50.
- [17]. Li MH, Cui L, Lu J. Varieties in state capitalism: Outward FDI strategies of central and local state-owned enterprises from emerging economy countries. *State-Owned Multinationals: Governments in Global Business*. 2018:175-210.
- [18]. Meyer E. When culture doesn't translate. *Harvard Business Review*. 2015 Oct 1;93(10):66-72.
- [19]. Meyer KE, Xin KR. Managing talent in emerging economy multinationals: Integrating strategic management and human resource management. *Int J Hum Resour Manag*. 2018 Jun 17;29(11):1827-55.
- [20]. Moosa IA, Cardak BA. The determinants of foreign direct investment: An extreme bounds analysis. *J Multinatl Financ Manag*. 2006 Apr 1;16(2):199-211.
- [21]. Ramamurti R. State-owned enterprises in high technology industries: Studies in India and Brazil. (No Title). 1987 Jan.
- [22]. Sungmala N, Verawat A. The impact of socio-demographic factors on employee engagement at multinational companies in Thailand. *J Multidiscip Humanit Soc Sci*. 2021 May 10;4(2):694-711.
- [23]. Vernon R. The international aspects of state-owned enterprises. *J Int Bus Stud*. 1979 Sep 1;10:7-14.
- [24]. Zander L, Mockaitis AI, Butler CL. Leading global teams. *J World Bus*. 2012 Oct 1;47(4):592-603.

DOI: <https://doi.org/10.15379/ijmst.v10i1.3058>

This is an open access article licensed under the terms of the Creative Commons Attribution Non-Commercial License (<http://creativecommons.org/licenses/by-nc/3.0/>), which permits unrestricted, non-commercial use, distribution and reproduction in any medium, provided the work is properly cited.