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Friends or Foes? Bilateral Relationships and Ownership Choice in Cross-border Acquisitions by Emerging Market Firms

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Emerging market firms (EMFs) are increasingly recognized as a heterogeneous group of business enterprises, providing a unique context for examining the predictive power of existing theories. Drawing on real options and internalization theories, this paper predicts the contrasting effect of bilateral relationships on EMFs' ownership choice in cross-border acquisitions. The conflicting conjectures are tested using data consisting of almost 1,000 cross-border acquisition deals. Our results show that weak economic, political and military relationships between acquiring and target countries induce EMFs to opt for full acquisitions. The findings support the view of internalization theory, highlighting that EMFs prefer full ownership over partial ownership by coping with the political risk derived from weak bilateral relationships.

Introduction

Recent studies suggest that consideration of bilateral relationships between nations is crucial for the success of cross-border acquisitions (Bertrand, Betschinger and Settles, 2016; Hasija, Liou and Ellstrand, 2019; Li *et al.*, 2019). Unfavourable or weak bilateral relationships between acquirer and target country provide challenges in cross-border acquisitions, especially for emerging market firms (EMFs) as acquirers. As cross-border acquisition helps EMFs to rapidly catch up with their competitors in target countries by securing critical resources, acquiring advanced technology and managerial expertise (Chari and Chang, 2009; Kohli and Mann, 2012; Luo and Tung, 2007), it often invokes fear and anxiety amongst the local population and creates institutional barriers in host countries (Hope, Thomas and Vyas, 2011; Kim, 2007; Riad and Vaara, 2011; Shenkar, Luo and Yeheskel, 2008).

For example, Chinese firms faced harsh reactions on their ownership decision from Australia's Foreign Investment Review Board (FIRB) in 2009. The Foreign Acquisitions & Takeovers Act (FATA) states that individual foreign buyers need approval to acquire more than 15% of an Australian company – or 40% if there is more than one buyer – and the application to acquire a company may be refused if it is deemed to be against the national interest (Economist Intelligence Unit, 2010). This evidence shows that bilateral relationships entail a great deal of complexity (e.g. antitrust laws, merger and acquisition (M&A) regulations) for EMFs' ownership choice in cross-border acquisitions (Duanmu, 2014; Li and Vashchilko, 2010; Zhang, Zhou and Ebbers, 2011).

Despite the relevance of bilateral relationships to EMFs' ownership choice in cross-border acquisitions, this has received relatively little attention (Li and Vashchilko, 2010, p. 765). Prior studies examine the effects of firm, deal and country-specific factors on the ownership choice of acquiring firms (Contractor *et al.*, 2014; Malhotra and Gaur, 2014; Malhotra, Lin and Farrell, 2016). Among the country-level factors, most research

focuses on the influence of cultural, geographic and institutional distances between a home and a host country rather than addressing the special (bilateral) relationship between a home and a host country as a potential driver of ownership decisions in cross-border acquisitions. While the role of distance or difference between countries in international business may have diminished with advancements in telecommunication and transportation (Friedman, 2007), bilateral relationships are recognized as powerful and attractive forces to achieve economic aims in an increasingly globalized world (Balabanis *et al*., 2001; Ramamurti, 2001).

Seeking to address these issues, the purpose of this paper is to theorize and examine the effect of bilateral relationships between acquirer and target nations on the ownership choices of EMFs as acquirers in cross-border acquisitions. It adopts a parsimonious approach, contrasting real option theory, which predicts that weak bilateral relations will result in partial acquisitions or a lower equity share in target firms by EMFs with internalization theory, which predicts that EMFs will choose full acquisitions or seek a higher equity share in target firms when bilateral relationships between acquiring and target countries are weak. The empirical data on cross-border acquisitions during 2000–2013 by EMFs from Brazil, China, India, Mexico and Russia is analysed. Our analysis to explain the ownership choice of EMFs supports the view of internalization theory.

Our contributions are twofold. First, combining insights from real options and internalization theory, it advances our understanding of how affinity (or animosity) between countries, reflected in their economic, political and military affairs, influences EMFs' ownership choice in cross-border acquisitions (Balabanis *et al*., 2001; Ramamurti, 2001). This complements prior work that has primarily considered Western multinational firms' tendency towards balancing the need for control and the need to contain the cost of ownership (Malhotra, Lin and Farrell, 2016; Xu and Shenkar, 2002). Our analysis of EMFs shows that they have an overwhelming concern for control and much less sensitivity to issues of ownership cost. This finding reminds us that economic rationales based on Western experience may not be universally applicable, emphasizing the need to examine the predictive power of existing theories in a new context (Peng, 2003).

Second, we contribute more broadly to an emerging body of international business literature drawing on the perspective of international relations scholarship and political risk (Arikan, Arikan and Shenkar, 2020; Duanmu, 2014; Gao, Wang and Che, 2018; Li and Vashchilko, 2010; Makino and Tsang, 2011) that emphasizes the need to extend the country-dyadic lens from distance to friction (Shenkar, Luo and Yeheskel, 2008). While many studies have shown that distance or difference leads to discordance in cross-border acquisition, affecting its completion and value creation, unfavourable or weak bilateral relationship as a source of discordance was overlooked (Li *et al*., 2019). We show that weak bilateral political, economic and military relationships between acquiring and target countries entail a higher political risk for foreign acquiring firms (Doh, Teegen and Mudambi, 2004), thereby affecting their ownership strategies. In this sense, we contribute to a growing body of research (Arikan and Shenkar, 2013; Bertrand, Betschinger and Settles, 2016; Gao, Wang and Che, 2018; Hasija, Liou and Ellstrand, 2019; Li and Vashchilko, 2010; Li *et al*., 2018; Peillex, Yoon and Rouine, 2019; Zhang and He, 2014) that has begun to capture a dyadic view of institutional factors in the context of cross-border acquisitions.

Literature review

The international business literature examining the role of institutional factors has focused on location-specific immobile attributes that are found independently in certain countries (Makino and Tsang, 2011). Accordingly, prior studies mainly consider the distance and difference (cultural, geographic, language, legal, political, regulatory) between countries (Buckley *et al*., 2016, 2017; Cuypers, Ertug and Hennart, 2015; Ellis *et al*., 2018; Morosini, Shane and Singh, 1998; Wu and Salomon, 2017). The basic premise is that the various kinds of distance between countries make international exchange and transactions difficult and costly (Makino and Tsang, 2011).

Despite the contributions made by the prior studies, the role of distance or difference between countries in contemporary international business may be less relevant than the strength of ties. This is mainly because distance or difference between countries does not capture the strength of

bilateral relationships that have become a powerful tool in doing international business in an increasingly polarized world (Binnendijk, 2016). In fact, even though the cultural and geographic distance between China and Japan is lower than that between China and the UK, Chinese firms may prefer or be more welcomed[1] to invest in the UK than in Japan due to the favourable and friendly bilateral relationships (meaning less conflicts in economic, political and military agenda) formed between China and the UK.

This prompts the need to examine the role of bilateral relationships that have evolved over time between countries (Balabanis *et al*., 2001; Ramamurti, 2001). In response to this, we use time-variant measures of bilateral relationships to explain EMFs' cross-border acquisitions. In this sense, the approach used in our current study extends the country-dyadic lens of existing institutional-level determinants from (static) distance to (time-variant) relationships between home and host countries (Shenkar, Luo and Yeheskel, 2008).

Recently, although there have been a small but growing number of studies that address the role of bilateral relationships in international alliance formation (Arikan and Shenkar, 2013), foreign direct investment (FDI) location choice and performance (Gao, Wang and Che, 2018; Li *et al*., 2018), acquisition deal completion (Zhang and He, 2014; Zhang, Zhou and Ebbers, 2011) and FDI flows (Li and Vashchilko, 2010), we need to pay closer attention to at least two issues in the internationalization of EMFs. First, since EMFs are known to focus on securing critical resources or strategic assets mainly through acquisitions (Anderson, Sutherland and Severe, 2015; Luo and Tung, 2007; McCarthy and Aalbers, 2016), understanding their ownership decisions (full vs. partial) in cross-border acquisitions is important. In fact, there is often no other way to secure the resources than through acquisitions, because such critical resources are not available as free-standing assets on the open market.

Second, it is known that bilateral relationships influence nation-states to reduce conflict and improve cooperation, as they bring fewer disagreements and pose less of a threat to each other's interests. Despite their significance, there are only a few studies investigating the role of bilateral relationships in the internationalization of EMFs. Prior studies (Economist Intelligence Unit, 2010; Zhang and He, 2014; Zhang, Zhou and Ebbers, 2011) have highlighted the fact that EMFs' acquisitions encounter economic nationalism in host countries derived from weak bilateral relationships. Under these circumstance, cross-border acquisitions led by EMFs are not always preferred or viewed as favourable by stakeholders in host countries, thereby triggering host-country government interference[2] (Hope, Thomas and Vyas, 2011).

To address the above issues, we craft our hypotheses to explain the effect of bilateral relationships on EMFs' ownership choice in cross-border acquisitions.

Theoretical foundation and hypothesis development

We build our two contrasting predictions by drawing on real options and internalization theories to explain the choice of ownership by EMFs in the context of cross-border acquisitions. Our analysis draws on these two theories to formulate contrasting hypotheses, as the contextual conditions for utilizing both theories is met in the case of acquisitions which have a firm versus market and a timing dimension.

Real options theory mainly addresses two types of options (Buckley, Casson and Gulamhussen, 2004, p. 57). First, non-contractual options allow firms to vary the size, location, timing and utilization of an investment project once the initial phase is complete. Second, contractual options allow firms to acquire or divest assets owned or partly controlled by other firms. The inclusion of these two types of options – non-contractual (especially location issues) and contractual (ownership) options – advanced the modern economic theory of international business. Our study focuses on contractual options in cross-border acquisitions. From a real option perspective, partial

[1]For example, whereas the Japanese government banned China's Huawei and ZTE from official contracts, the British government decided to let Huawei build its 5G network (New York Times, 2020).

[2]Although government interference can take explicit (e.g. *de jure*) or implicit (e.g. *de facto*) forms, it is known that many countries rarely have *de jure* power to block any acquisitions based on the acquirer's nationality (Dinc and Erel, 2013).

ownership or acquisitions[3] gives EMFs the flexibility to cope with political risks by making their investment in target firms more easily reversible (e.g. selling a minority stake is easier than selling the whole firm) and more easily extendable (e.g. by increasing the ownership share) (Chi *et al*., 2019).

Whereas real option theory is more bounded in its applicability, as it is focused upon the ability to defer decisions, and thus to attain flexibility with the possibility of acquiring more information and avoiding mistakes (Buckley and Casson, 2010), internalization theory addressing full ownership is a general theory focusing on the conditions under which organization of activities within a firm is superior to market transactions (contracts) (Buckley and Casson, 1976). Internalization theory emphasizes that cross-border acquisitions provide learning opportunities for acquiring firms to appropriate the rent generated by internalizing activities with high up-front investment via full ownership (Buckley and Casson, 1976). Overall, cross-border acquisitions fall within the normal boundary conditions of both theories.

By using these two theoretical lenses, we are able to probe deeper into the effect of bilateral relationships[4] on EMFs' ownership choice. The basic assumption is that acquisitions by EMFs originating from countries with strong or favourable bilateral relationships are less likely to be perceived as a threat and cause unfavourable interferences by the host country (Ellis *et al*., 2018). In other words, host-country government agents are less likely to be concerned about cross-border acquisitions if economic transactions involve foreign firms from countries with similar national interests (Hasija, Liou and Ellstrand, 2019). However, acquiring firms – especially originating from a country with an unfavourable bilateral relationship – can be viewed as conquerors that carry a threatening aura of dominance (Salk and Shenkar, 2001). Subsequently, a weak or unfavourable bilateral relationship implies higher transaction costs and information asymmetries for acquiring firms, raising the additional cost of doing business in the host market (Meyer, 2001).

Collectively, weak or unfavourable bilateral relationships increase the likelihood of host-country government interference, because the host country considers the transaction to pose a relatively higher threat to its economic well-being and other national interests (Bertrand, Betschinger and Settles, 2016; Eden and Miller, 2004). Accordingly, the overarching reasoning in our predictions relies on political risk, which is conceived of host government interference (Kobrin, 1979). Specifically, we adopt Simon's (1984) framework, which categorizes political risk according to the flow of risk including direct-internal, direct-external, indirect-internal and indirect-external. Since our analysis focuses on changes in relations between the host and home countries, we focus on indirect-external political risks, which we operationalize as bilateral relationships. Given the political risk derived from the bilateral relationships, EMFs can either opt for a lower equity position by balancing the need for control and cost from a real options perspective, or fully acquire the target firm by having more concerns over control than cost from an internalization view.

First, according to real options theory, higher investment risk increases the value of adopting lower equity investments while waiting for the resolution of potential risks (McDonald and Siegel, 1986; Rivoli and Salorio, 1996). Although the real options reasoning has thus far been advanced to explain foreign market entry through joint ventures (Kogut, 1991), as in the case of entry into emerging technology markets (Folta, 1998), a growing number of studies (Ahammad *et al*., 2017; Chari and Chang, 2009; Cuypers and Martin, 2010; Malhotra and Gaur, 2014) argue and show that entry through the cross-border acquisition of partial equity in target firms can also serve the same purpose of economizing on the cost of resource commitment. This flexible approach of partial acquisitions gives managers the capability to respond to unknown waters (Ahammad *et al*., 2017; Wooster, Blanco and Sawyer, 2016).

In the context of EMFs' cross-border acquisitions, a weak bilateral relationship entails higher political risk and information asymmetry for EMFs that may limit their access to information about target firms, about the industry in which those targets operate and about the host country

[3]While selling a full stake is more flexible (ease of decision-making), the net loss is likely to be lower for partial ownership than for full ownership if the acquirer must exit (Malhotra and Gaur, 2014). Thus, firms' partial ownership decision is consistent with real options theory.
[4]We focus on the bilateral relationships formed around economic, political and military arenas and between home and host countries (Buckley *et al.*, 2017; Oneal and Russett, 1997).

(Shimizu *et al*., 2004). The costs of acquiring credible, reliable information in foreign countries also increase with greater information asymmetry derived from a weak bilateral relationship (Portes and Rey, 2005). In a similar vein, Ragozzino (2009) found that investors choose to acquire a larger stake in a target based in a neighbouring market than in a more remote market. Thus, by opting for a lower equity position in the target firm, EMFs can overcome the challenges associated with information asymmetry derived from weak bilateral relationships (Chi *et al*., 2019; Malhotra and Gaur, 2014).

In addition, when the bilateral relationship is weak, EMFs may be exposed to moral hazards by target firms. In order to cope with the issue, acquirers can create a hostage effect by opting for partial or lower equity ownership. Acceptance of partial ownership by target firms signals their confidence in the future prospects of their firm, which reduces the acquirer's risk of ex-post moral hazards (Chen and Hennart, 2004). As the partner from a target country has a stake in the merged entity, it also has an incentive to ensure that the new entity succeeds by restraining its opportunistic behaviour. Furthermore, when the bilateral relationship between acquirer and target countries is weak, the potential negative attitudes accompanying acquisitions become aggravated, as targets view the acquisition as posing a danger to their national identity and pride (Riad and Vaara, 2011; Shenkar, Luo and Yeheskel, 2008). Subsequently, it can lead to host-country government interference and pronounced resistance by the target firms, and in turn will induce acquiring firms to be hesitant to have full control over the target firms (Bertrand, Betschinger and Settles, 2016; Malhotra and Gaur, 2014). Thus, partial ownership will be favoured by EMFs, which helps them test unknown waters, because they are concerned with the costs of making choices on deploying fewer resources due to the increase in political risk.

In light of all these arguments, from the perspective of real options theory, we posit:

> *H1a*: EMFs will choose partial acquisitions or seek a lower share of equity in target firms when the bilateral relationships between acquiring and target countries are weak.

While our expectation on real options theory would highlight the risk derived from weak bilateral relationships that limits acquiring firms' commitment (Beugelsdijk, Ambos and Nell, 2018; Nell, Kappen and Laamanen, 2017), internalization theory emphasizes that doing business in a country with weak bilateral relationships can provide learning opportunities (Stahl and Tung, 2015). Such an internalization advantage applies to firms that fully exploit their ownership advantage internally, thereby minimizing the transaction costs associated with the inter-firm transfer of proprietary knowledge and capabilities (Buckley and Casson, 2020; Buckley and Hashai, 2009). Despite the high level of political risk associated with cross-border acquisitions, foreign firms can commit a significant amount of up-front resource investment and transfer costs to internalize business activities and control risks (Buckley and Hashai, 2005; Contractor *et al*., 2014; Hashai, 2009; Malhotra and Gaur, 2014; Malhotra, Lin and Farrell, 2016). By committing financial resources to the target firms, acquiring firms benefit from a variety of synergies, albeit together with the increased transaction costs deriving from full ownership (Ahammad *et al*., 2018).

In the context of EMFs' cross-border acquisitions, weak bilateral relationships can induce pronounced resistance by the target firms (Bertrand, Betschinger and Settles, 2016). As weak bilateral relationships increase the likelihood of government intervention in favour of the domestic target firm, the bargaining power of the domestic target firm can be strengthened, triggering target firms' opportunistic behaviour (Dinc and Erel, 2013; Enderwick, 2011). In other words, partial ownership in the context of weak bilateral relationships can overlook partner-related opportunism and create more tensions between acquiring and target firms, making negotiation and integration processes difficult (Chari and Chang, 2009). However, with greater levels of ownership and hierarchical control, EMFs can reduce opportunism on the part of target firm managers (Williamson, 1985) or facilitate the transfer of uncodifiable assets (Kogut, 1988; Kogut and Zander, 1993). Although full acquisitions entail higher investments in human, physical and intangible assets, and greater overall commitment (e.g. acquisition premium), especially when the bilateral relationship is weak (Ahammad *et al*., 2017; Bertrand, Betschinger and Settles, 2016), EMFs may prefer full ownership to reduce tensions with business partners and as a way of circumventing problems arising from a lack of strategic fit (Cui and Jiang, 2009). The

greater level of control associated with full ownership can make it easier to obtain cooperation from the management and employees of the target firm originating from hostile countries. As such, greater internalized control allows EMFs to achieve more efficient learning. Thus, full ownership can be favoured by EMFs as it facilitates faster, more efficient decision-making, reduces the chances of conflict and boosts their learning (Malhotra and Gaur, 2014).

In light of all these arguments, from the perspective of internalization theory, we posit:

> *H1b*: EMFs will choose full acquisitions or seek a higher share of equity in target firms when the bilateral relationships between acquiring and target countries are weak.

Methods

Data and sample

Cross-border acquisition deals led by EMFs that occurred between 2000 and 2013 were collected from the Securities Data Corporation (SDC) Platinum database. Our empirical analyses focus on the firms originating from five large scalable emerging economies – Brazil, China, India, Mexico and Russia – that are characterized by a high degree of internationalization (see Luo and Tung, 2007). Our sample only includes the cross-border acquisitions originating from these five emerging countries, as suggested by Luo and Tung (2007), because in recent decades their national economies have grown rapidly, their industries have undergone dramatic structural changes and their markets hold promise despite volatile domestic institutions.

In constructing our sample, we followed the procedures of Chakrabarti, Gupta-Mukherjee and Jayaraman (2009) and kept the acquisition deals: (1) that are fully completed; (2) where the acquirer and target are from different countries; and (3) where the acquiring company is publicly traded (among 10,861 observations from our initial dataset, 331 cross-border acquisition deals were made by non-publicly traded acquiring firms). We drop the observations if the acquiring firms were originating from Hong Kong or Macao; or the target firms were from tax havens such as Bermuda, the Bahamas, the British Virgin Islands, the Cayman Islands and Puerto Rico (Chakrabarti, Gupta-Mukherjee and Jayaraman, 2009; Li *et al*., 2018; Yoon and Lee, 2016). The first screening process allowed us to secure 10,530 observations. We then used Thomson Reuters DataStream to collect firm-level data. Among our 10,530 observations, only 3,199 firms had a Datastream code. After merging all our data from multiple sources (see Table 1) to construct variables at deal, firm and country level, and removing missing values, our sample consists of 1,001 cross-border acquisitions. Moreover, in accordance with the approach of Luo and Tung (2007) on EMFs, we exclude state-owned enterprises (SOEs) from our sample. Thus, our final sample consists of 997 cross-border acquisitions led by the acquiring firms from Brazil, Russia, China, India and Mexico.

As shown in Table 1, the majority of cross-border acquisitions were led by Indian firms (408 out of 997). The remainder of the transactions were led by Russian (17.05%), Chinese (14.64%) and Brazilian and Mexican firms (around 13%). Regarding the target countries, 26% were in the USA and 6% in the UK. The number of different combinations of countries in our sample is 166. The most common country pairs are India–USA (124 deals), Mexico–USA (53 deals), India–UK (45 deals), China–USA (44 deals) and Brazil–Argentina (35 deals).

Variables

Dependent variable. Following Lahiri, Elango and Kundu (2014), we consider that if the acquiring firm obtains less than 100% of the target firm, the acquisition is partial. By contrast, the acquisition is considered full if the acquiring firm bought 100% of the target firm. Accordingly, we constructed a dummy variable *Ownership Choice* that equals 1 if the acquisition is full, and 0 if the acquisition is partial (Lahiri, Elango and Kundu, 2014; Malhotra, Lin and Farrell, 2016). In our sample, we observe a moderately balanced distribution between the number of partial acquisitions (433) and the number of full acquisitions (564).

Independent variables. We test the effect of the bilateral relationships on ownership choice by considering economic, political and military arenas between acquiring and target countries (Buckley *et al*., 2017; Oneal and Russett, 1997). Our independent variables are universal and cover the vast majority of nations in the global economy. First, *Economic Relations* measures the degree of

Table 1. Number of cross-border acquisitions by country

Acquirer countries	N	%
Brazil	136	14.00
China	146	15.00
India	408	41.00
Mexico	137	14.00
Russia	170	17.00
Total	**997**	**100**

Target countries	N	Target countries	N	Target countries	N
Argentina	47	Indonesia	10	Peru	18
Australia	48	Ireland-Rep	4	Philippines	3
Austria	6	Italy	24	Poland	3
Bahamas	1	Japan	11	Portugal	10
Bangladesh	1	Kazakhstan	16	Qatar	1
Belgium	13	Kenya	1	Romania	7
Bolivia	3	Laos	1	Senegal	1
Brazil	36	Latvia	2	Singapore	15
Bulgaria	5	Liberia	2	South Korea	7
Cambodia	1	Libya	1	Spain	20
Canada	39	Lithuania	1	Sri Lanka	8
Chile	13	Luxembourg	6	Sudan	1
China	7	Malaysia	4	Sweden	5
Colombia	20	Mauritius	8	Switzerland	10
Czech Republic	13	Mexico	17	Tajikistan	2
Denmark	5	Mongolia	6	Thailand	5
El Salvador	3	Mozambique	1	Turkey	8
Estonia	5	Namibia	2	Turkmenistan	2
Finland	7	Nepal	2	United Kingdom	61
France	20	Netherlands	22	United States	262
Gabon	4	New Zealand	6	Uruguay	11
Germany	34	Nicaragua	3	United Arab Emirates	10
Greece	1	Norway	4	Uzbekistan	7
Honduras	1	Oman	6	Venezuela	3
Hungary	6	Paraguay	5	Vietnam	4
India	9			**Total**	**997**

bilateral trade openness between the target and the acquirer nation. This variable is the summation of export and import flows between the host and the home country divided by the gross domestic product (GDP) of the target country (Chakrabarti, Gupta-Mukherjee and Jayaraman, 2009; Oneal and Russet, 1997).

Economic relations between countries are formed through international trade activities (Buckley and Munjal, 2017). A strong economic connection via international trade between acquiring and host nations helps EMFs encounter less resistance to deal-making in cross-border acquisitions. This accounts for economic interdependencies in the dyad that could influence the ability of host governments to intervene. Some studies have shown that countries with similar national interests trade more with each other, and vice versa (Dixon and Moon, 1993). Dixon and Moon (1993) explain that although countries that share similar views on global political issues are not guaranteed to have friendly economic relations with each other, those countries are far less likely to experience hostile economic actions (i.e. trade protectionism) than countries characterized by a higher divergence in opinion on economic affairs. In our research context, a strong economic bilateral relationship could signal to the EMFs that it is less risky and easier to collaborate with the host-country firm and to entrust their local operations to the host-country counterparts.

Second, *Political Relations* measures the level of political affinity between the home and the host country, which is based on the annual voting decisions of the acquiring and the target country made in the United Nations (UN) General

Table 2. Overview of variables

Variables	Measurement
Dependent variable	
Ownership Choice (Lahiri *et al.*, 2014; Malhotra *et al.*, 2016)	Dummy variable coded as 1 if the acquisition is full and 0 if the acquisition is partial. *Source*: SDC Platinum
Independent variables	
Economic Relations (Oneal and Russet, 1997; Chakrabarti *et al.*, 2009)	Degree of bilateral trade openness between the target and the acquirer nation. Measured by the summation of export and import flows between the host and the home country divided by the GDP of the target country. *Source*: World Bank
Political Relations (Gartzke, 2000)	Level of political affinity between the home and the host country. Estimated from the annual voting decisions of the acquiring and the target country made in the UN General Assembly. *Source*: Correlates of War project
Military Relations (Vergne, 2012; Vergne and Depeyre, 2016)	Measured by the summation of arms export and import flows between the host and the home country divided by the GDP of the target country. *Source*: SIPRI Arms Transfers
Control variables	
Cultural Distance (Chari and Chang, 2009; Malhotra and Gaur, 2014)	Distance between the host and the home country across the four cultural dimensions of Hofstede (1980). *Source*: Hofstede
Institutional Distance (Gaur and Lu, 2007; Kaufmann *et al.*, 2009; Malhotra and Gaur, 2014)	Difference in governance infrastructure quality between host and home country by aggregating the national scores for control of corruption, government effectiveness, political stability, regulatory quality, rule of law and voice and accountability. *Source*: World Bank
Expropriation (Duanmu, 2014)	Expropriation risk of the host country extracted from the Index of Economic Freedom. *Source*: Heritage Foundation
Colony (Cuervo-Cazurra and Genc, 2008)	Dummy variable coded as 1 if the target and the acquirer nation had a colonial link and as 0 otherwise. *Source*: CEPII
Common Language (Buckley *et al.*, 2017)	Dummy variable coded as 1 if the target and the acquirer country share a common official language and 0 otherwise. *Source*: CEPII
Geographic Distance (Ellis *et al.*, 2018; Malhotra *et al.*, 2011)	Logarithm of geographic distance between capitals of the target and acquirer nations (in kilometres). *Source*: CEPII
Developed Country (Buckley *et al.*, 2007; Gubbi *et al.*, 2010)	Dummy variable coded as 1 if the host firm is from an OECD member country and 0 otherwise. *Source*: OECD
GDP Growth Target Crisis Target (Chung *et al.*, 2013)	GDP growth rate in the host country. Dummy variable coded as 1 if the target country experienced four consecutive quarterly declines in GDP before the deal and 0 otherwise. *Source*: World Bank
Private Target (Kedia and Bilgili, 2015; Malhotra *et al.*, 2011)	Dummy variable coded as 1 if the target firm is private and 0 otherwise. *Source*: SDC Platinum
Industry Relatedness (Contractor *et al.*, 2014)	Dummy variable coded as 1 if the target and the acquiring firm have the same three-digit SIC code and 0 otherwise. *Source*: SDC Platinum
Cash Payment (Lim *et al.*, 2016; Malhotra *et al.*, 2016)	Dummy variable coded as 1 if more than 50% of the deal value is paid with cash, and zero otherwise. *Source*: SDC Platinum
Acquirer Size (Chari and Chang, 2009; Kogut and Singh, 1988)	Logarithm of total assets of the acquirer firm. *Source*: Thomson Reuters DataStream
Acquirer Profitability (Bertrand *et al.*, 2016; Lim *et al.*, 2016)	ROA of the acquirer firm. *Source*: Thomson Reuters DataStream
Acquirer Leverage (Peillex and Ureche-Rangau, 2016)	Debt-to-equity ratio of the acquirer firm. *Source*: Thomson Reuters DataStream
Acquisition Experience (Malhotra *et al.*, 2016)	Dummy variable coded as 1 if the acquirer firm has a prior CBA in the target country and 0 otherwise. *Source*: SDC Platinum

Assembly (Gartzke, 2000). The variable represents the degree of closeness of votes at UN General Assemblies between states and so reveals their bilateral national interests (Bertrand, Betschinger and Settles, 2016). From an empirical perspective, political affinity approximates the similarity degree of the bilateral national interests in year t from the votes V_t^i and V_t^j of country i and country j, calculated as follows:

$$Political\ Affinity_t^{i,j} = 2\frac{D_t\left(V_t^i;\ V_t^j\right)}{D_t^{max}}$$

where D_t is the sum of metric distance (in absolute value) between V_t^i and V_t^j and D_t^{max} denotes the largest distance between those votes. In the UN General Assembly, countries have a choice between three voting options, namely, approve an issue, disapprove an issue or abstain. The variable $Political\ Affinity_t^{i,j}$ is between −1 and +1. While the value −1 indicates that the country dyads made completely opposite votes in year t, the value +1 indicates that they have an identical voting pattern in year t.

Political affinity reflects the political bilateral relations between countries that is an underlying driver of 'special relationships' between countries. It influences the decision-making process in cross-border acquisitions through political interference by host-country governments. This is because the interests of a host country are strongly affected when foreign firms take possession of domestic (host-country) firms and the resources embedded in them. Once the assets of the domestic target firm are under the control of the foreign firms, the host country could expect its external dependence to increase, leading to political and economic vulnerability (Bertrand, Betschinger and Settles, 2016). In sum, when political relations (affinity) are stronger (higher), countries pose a lower threat to each other's interests (Dixon and Moon, 1993; Gartzke, 2000), which reduces the potential conflict in cross-border acquisitions (Bertrand, Betschinger and Settles, 2016; Li *et al*., 2019; Peillex, Yoon and Rouine, 2019).

Third, *Military Relations* is measured by arms transfers between the host and the home country. With the data collected from SIPRI (Stockholm International Peace Research Institute) Arms Transfers, we measure the variable by the summation of arms export and import flows (aircraft, air defence systems, anti-submarine warfare weapons, armoured vehicles, artillery, engines, missiles, sensors, satellite and ships) between the home and the host country divided by the GDP of the target country (Vergne, 2012; Vergne and Depeyre, 2016). The flows are based on the known unit production costs of weapons and thus represent the transfer of military resources rather than the financial value of the transfer.

From the perspective of security and the balance of power, Waltz (1979) proposed that countries will form military ties to counter other nations and groups of nations seeking to achieve a dominant position. In particular, once the arms-importing countries become familiarized with sophisticated weapons, they lead to learning by doing or adaptation to domestic uses (Leuenberger and Weinstein, 2012). In other words, the higher the arms transfer, the less the exporting countries are concerned with the recipient countries' appropriation of military weapons and technology. In addition, the presence of strong military relations means that there is mutual respect and trust between home and host countries. It also shows that they have a common or similar interest in their national security issues. Thus, an EMF is less likely to experience hostile sanctions or actions from the host-country regime when there is a strong military relationship formed between home and host country.

Control variables. To account for any idiosyncratic differences, we used acquirer country, industry and year dummies throughout all our models. Moreover, we include a number of deal, firm and country-specific variables as used in prior studies (e.g. Chari and Chang, 2009; Contractor *et al*., 2014; Lahiri, Elango and Kundu, 2014; Malhotra, Lin and Farrell, 2016).

Following Kedia and Bilgili (2015) and Malhotra, Sivakumar and Zhu (2011), we control for the target firm status by creating a dummy variable *Private Target*, coded as 1 if the target firm is a private entity, and 0 otherwise. Since private firms are generally smaller than public firms, it is easier for acquiring firms to finance the full acquisition of private firms than public firms (Malhotra, Lin and Farrell, 2016; Malhotra, Sivakumar and Zhu, 2011). We control for *Industry Relatedness*, which is coded as 1 if the two firms have the same three-digit SIC code, and 0 otherwise (Contractor *et al*., 2014). The variable captures the '(dis-)similarity in the knowledge-base, business practices, routines, norms, and general competitive environment that exists between the target firm's industry and the acquirer's industry' (Ahammad *et al*., 2018). Previous studies observe that full ownership is preferred when two firms are from the same industry (Contractor *et al*., 2014; Ellis *et al*., 2018; Lahiri, Elango and Kundu, 2014).

In addition, we take into account the effect of payment method on the ownership choice, because prior studies have documented that cash-based acquisitions tend to amplify information asymmetry and thus the acquiring firm is likely to invest less resources in the target firm's acquisition (Malhotra and Gaur, 2014). In line with Lim, Makhija

and Shenkar (2016) and Malhotra, Lin and Farrell (2016), the payment method (*Cash Payment*) is a binary variable, coded as 1 if more than 50% of the deal value is paid with cash, and 0 otherwise.

As for the firm-level control variables, we include *Acquirer Size*, as previous works have shown that larger acquirers have greater resources available for full acquisitions than smaller firms (Chari and Chang, 2009; Kogut and Singh, 1988). We measure the acquirer size as the logarithm of total assets. We also control for *Acquirer Profitability*, because higher profitability increases the manager's confidence to undertake riskier projects and therefore choose the complete acquisition even when it does not seem the best entry mode choice (Barkema and Vermeulen, 1998). In accordance with Bertrand, Betschinger and Settles (2016) and Lim, Makhija and Shenkar (2016), we measure *Acquirer Profitability* with the return on assets (ROA), which is used as a control variable. We also control for *Acquirer Leverage*, because it can be argued that a firm's debt level influences its financial flexibility (Peillex and Ureche-Rangau, 2016) and therefore inhibits its ability to mobilize resources to engage in full acquisitions. We measure *Acquirer Leverage* with debt-to-equity ratio, which is used as a control variable. Finally, we control for *Acquirer Experience* as we expect that firms with greater experience in the target country may better manage the risks related to internationalization, and in turn develop a preference for a full acquisition (Gaur and Lu, 2007; Kogut and Singh, 1988). *Acquirer Experience* takes the value 1 if the acquiring firm has a prior cross-border acquisition in the target country, and 0 otherwise (Malhotra, Lin and Farrell, 2016).

Regarding country-specific control variables, we include eight variables: *Cultural Distance*, *Institutional Distance*, *Expropriation*, *Colony*, *Common Language*, *Geographic Distance*, *Developed Country*, *GDP Growth Target* and *Crisis Target*. Previous studies have documented that a greater *Cultural Distance* increases uncertainty and thus affects the firm's entry mode choice (Chari and Chang, 2009; Malhotra and Gaur, 2014). In line with Lahiri, Elango and Kundu (2014), Malhotra and Gaur (2014) and Malhotra, Sivakumar and Zhu (2011), *Cultural Distance* is estimated using Hofstede's (1980) data on four cultural dimensions. These four dimensions are power distance, individualism, masculinity and uncertainty avoidance. To aggregate these dimensions, we apply the formula from Kogut and Singh (1988):

$$Cultural\ Distance_{t}^{i,j} = \sum_{t=1}^{4} \frac{\left(H_{i,t} - H_{j,t}\right)^2}{4 * V_t}$$

where $H_{i,t}$ is the score for country i on the cultural dimension t, and $H_{j,t}$ is the score for country j on the cultural dimension t. V_t is the variance of the index score of cultural dimension t.

Moreover, we control for *Institutional Distance*, which measures the difference in governance quality between host and home country, increasing uncertainty and thus exerting a significant effect on ownership choice (Gaur and Lu, 2007; Malhotra and Gaur, 2014). It is based on the scores of the World Bank's six Governance Indicators (Kaufmann, Kraay and Mastruzzi, 2009), including control of corruption, government effectiveness, political stability, regulatory quality, rule of law and voice/accountability. These indicators are commonly mobilized to capture institutional distance (Contractor *et al*., 2014; Malhotra and Gaur, 2014; Malhotra, Lin and Farrell, 2016). In accordance with Kogut and Singh (1988), the institutional distance is computed as follows:

$$Institutional\ Distance_{t}^{i,j} = \sum_{t=1}^{6} \frac{\left(G_{i,t} - G_{j,t}\right)^2}{4 * V_t}$$

where $G_{i,t}$ is the governance score t for country i and $G_{i,t}$ is the governance score t for country j. V_t is the variance of the index score of governance indicator t.

Beyond the institutional distance, a foreign firm's ownership choice may be affected by host-country institutional environment. In particular, foreign firms are concerned about being expropriated when they are acquiring firms in host countries with poor institutional environment. Thus, our analysis includes the variable *Expropriation*, which is extracted from the Index of Economic Freedom provided by the Heritage Foundation (Duanmu, 2014).

Furthermore, since prior studies found that colonial ties, as a measure of informal institutional distance, affect the ownership decision (e.g. Ellis *et al*., 2018), we control for the colonial link between the acquiring and the target country. In accordance with Cuervo-Cazurra and Genc (2008), *Colony* is a dummy variable coded as 1 if the acquiring and the target country had a colonial link,

and 0 otherwise. *Common Language* is also a binary variable that equals 1 if the acquiring and the target country share a common official language, and 0 otherwise (Buckley *et al*., 2017). Using the same language reduces the communication barrier for international capital flows and increases the propensity to opt for a full acquisition as entry mode. In line with Malhotra, Sivakumar and Zhu (2011) and Ellis *et al*. (2018), *Geographic Distance* is measured by the logarithm of geographic distance between capitals of the target and acquirer nations (in kilometres). Since greater *Geographic Distance* amplifies the cost of transportation and information during and after cross-border acquisitions, acquirers may prefer partial acquisitions when countries are geographically distant (Malhotra, Sivakumar and Zhu, 2011). We consider the learning intention of acquiring firms in cross-border acquisitions by including *Developed Country*, which equals 1 if the target firm is from an OECD member country, and 0 otherwise (Buckley *et al*., 2007; Gubbi *et al*., 2010). As foreign firms' ownership choice may be influenced by the economic growth potentials in host countries, we control for the GDP growth rate of the host country by including *GDP Growth Target*. In order to further take into account the host-country specific risk, we also include a dummy variable *Crisis Target*, following Chung *et al*. (2013), that takes the value 1 when the target country experienced four consecutive quarterly declines in GDP before the deal, and 0 otherwise.

Results

Regarding the correlation matrix (see Table 3), most of the bivariate correlations are moderate. It shows that *Economic Relations*, *Political Relations* and *Military Relations* are negatively related to the full ownership choice (−0.16, −0.21 and −0.08, respectively). To check whether multicollinearity is a concern, we calculated the variance inflation factors (VIFs). On average, the VIF is 1.80, which is far below the recommended tolerance level of 10.

Since the dependent variable is a dummy variable, we use logistic regressions (see Table 4). In all estimations, we included acquirer country, industry and year dummies to control for unobserved effects derived from sample heterogeneity and time-varying conditions. We observe consistent effects of the control variables across all the models. Based on the results of Model 1, *Developed Country* and *Acquirer Profitability* significantly increase the propensity for EMFs to opt for full ownership. The significant effect of *Developed Country* ($\beta = 0.76$, $p < 0.01$) shows the strategic asset-seeking behaviour of EMFs in cross-border acquisitions by opting for full acquisition. *Acquirer Profitability* is significant and positive ($\beta = 0.01$, $p < 0.01$), as profitable firms tend to have sufficient financial resources to afford full acquisitions.

In contrast, *Institutional Distance*, *Expropriation*, *Cash Financed* and *Acquirer Size* significantly increase the propensity for EMFs to opt for partial ownership. Since partial acquisitions offer greater flexibility to EMFs, the significant effects of *Institutional Distance* ($\beta = -1.35$, $p < 0.05$) and *Expropriation* ($\beta = -0.02$, $p < 0.01$) can be explained by their desire to reduce the risk derived from uncertain institutional environment. *Cash Financed* shows a significant and negative sign ($\beta = -0.53$, $p < 0.01$), because it is not easy for firms to finance full acquisitions with cash. Finally, *Acquirer Size* is negatively associated with the dependent variable ($\beta = -0.39$, $p < 0.01$), as large firms tend to diversify their business by exploiting target firms through partial ownership.

Main analyses

As shown in Table 4, Model 2 estimates the effect of *Economic Relations* on *Ownership Choice*. As expected, there is a negative relationship between *Economic Relations* and *Ownership Choice* ($\beta = -6.23$, $p < 0.01$). Model 3 reveals the effect of *Political Relations* on *Ownership Choice*. It shows that *Political Relations* has a negative and significant effect on the propensity for EMFs to opt for full ownership ($\beta = -0.55$, $p < 0.05$). Model 4 shows the effect of *Military Relations* on *Ownership Choice*. The corresponding coefficient is also negative and statically significant ($\beta = -15.55$, $p < 0.05$), which indicates that EMFs opt for full ownership to overcome the weak *Military Relations* between their home country and host country. In Model 5, we include all our main independent variables to explain the ownership choice. The results are qualitatively consistent with the estimates of previous models. Indeed, Model 5 shows negative and significant effects of *Economic Relations* ($\beta = -6.34$, $p < 0.01$), *Political Relations*

Table 3. Summary statistics and correlations

Variables	Mean	S.D.	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19
1. Ownership Choice	0.56	0.50	1																		
2. Economic Relations	0.03	0.05	−0.16*	1																	
3. Political Relations	0.24	0.54	−0.21*	0.33*	1																
4. Military Relations	0.002	0.01	−0.08*	0.13*	0.14*	1															
5. Cultural Distance	1.54	0.25	−0.02	0.19*	−0.17*	0.16*	1														
6. Institutional Distance	0.56	0.25	0.08*	−0.21*	−0.51*	−0.13*	0.35*	1													
7. Expropriation	29.26	23.86	−0.18*	0.34*	0.67*	0.19*	−0.16*	−0.83*	1												
8. Colony	0.10	0.31	−0.02	0.28*	0.12*	0.26*	0.14*	−0.01	0.06*	1											
9. Common Language	0.31	0.46	0.09*	−0.09*	−0.21*	0.04	−0.16*	0.02	−0.14*	0.29*	1										
10. Geographic Distance	8.63	0.02	0.08*	−0.49*	−0.43*	−0.11*	−0.11*	0.19*	−0.32*	−0.21*	0.30*	1									
11. Developed Country	0.65	0.48	0.21*	−0.34*	−0.63*	−0.18*	0.15*	0.58*	−0.70*	0.02	0.03	0.22*	1								
12. GDP Growth Target	2.72	3.79	−0.06	0.25*	0.29*	0.18*	−0.09*	−0.30*	0.33*	0.06	0.03	−0.12*	−0.34*	1							
13. Crisis Target	0.15	0.35	0.05	−0.09*	−0.13*	−0.05	0.07*	0.12*	−0.12*	−0.01	−0.01	0.07*	0.13*	−0.56*	1						
14. Private Target	0.44	0.50	0.03	0.03	−0.01	0.01	−0.07*	−0.02	0.00	0.02	0.13*	0.04	0.02	0.05	−0.08*	1					
15. Industry Relatedness	0.35	0.48	−0.06	0.01	0.08*	0.06	−0.02	−0.14*	0.14*	0.01	0.03	−0.01	−0.10*	0.06	−0.02	−0.10*	1				
16. Cash Financed	0.52	0.50	−0.13*	−0.03	−0.01	−0.01	−0.03	0.00	−0.01	−0.03	−0.04	0.07*	−0.04	0.06	−0.02	−0.13*	0.02	1			
17. Acquirer Size	6.16	1.01	−0.17*	0.07*	0.23*	0.07*	0.10*	−0.12*	0.19*	0.02	−0.23*	−0.23*	−0.14*	−0.02	0.04	−0.27*	0.02	0.12*	1		
18. Acquirer Profitability	55.00	1485	0.03	0.00	−0.05	−0.01	0.01	0.03	−0.02	−0.01	−0.02	0.03	0.02	0.00	−0.01	−0.03	−0.03	−0.03	−0.10*	1	
19. Acquirer Leverage	90.00	106	−0.04	−0.02	0.06	0.03	−0.05	−0.03	0.00	0.06	−0.04	−0.05	0.03	−0.01	0.01	−0.02	−0.05	−0.01	0.15*	−0.05	1
20. Acquisition Experience	0.38	0.49	−0.02	−0.04	0.02	−0.04	−0.14*	−0.05	−0.01	−0.02	0.05	0.15*	−0.02	0.01	0.01	0.00	−0.04	0.02	0.00	0.04	0.06*

N = 997.
*p < 0.05.

Table 4. Effects of economic, political and military relations on ownership choice

	Model 1	Model 2	Model 3	Model 4	Model 5
Economic Relations		−6.23***			−6.34***
		(0.01)			(0.00)
Political Relations			−0.55**		−0.52**
			(0.01)		(0.01)
Military Relations				−15.55**	−14.32*
				(0.04)	(0.06)
Cultural Distance	0.02	0.30	−0.06	0.19	0.21
	(0.95)	(0.36)	(0.85)	(0.56)	(0.54)
Institutional Distance	−1.35**	−1.80***	−1.19**	−1.44**	−1.67***
	(0.02)	(0.00)	(0.04)	(0.02)	(0.01)
Expropriation	−0.02***	−0.02***	−0.01*	−0.02**	−0.02**
	(0.01)	(0.00)	(0.09)	(0.01)	(0.04)
Colony	−0.09	0.01	0.01	0.01	0.20
	(0.72)	(0.98)	(0.96)	(0.99)	(0.50)
Common Language	−0.06	0.16	−0.18	−0.12	0.09
	(0.77)	(0.38)	(0.38)	(0.55)	(0.65)
Geographic Distance	0.18	−0.21	0.02	0.11	−0.28**
	(0.16)	(0.10)	(0.84)	(0.39)	(0.03)
Developed Country	0.76***	0.65***	0.55**	0.74***	0.43*
	(0.00)	(0.01)	(0.01)	(0.00)	(0.06)
GDP Growth Target	0.04	0.05	0.04	0.04	0.06
	(0.20)	(0.14)	(0.18)	(0.16)	(0.08)
Crisis Target	0.44	0.45	0.42	0.46	0.43
	(0.12)	(0.12)	(0.14)	(0.11)	(0.13)
Private Target	−0.11	−0.07	−0.09	0.04	−0.06
	(0.46)	(0.63)	(0.50)	(0.49)	(0.71)
Industry Relatedness	−0.24	−0.22	−0.25*	−0.25*	−0.21
	(0.1)	(0.12)	(0.08)	(0.08)	(0.14)
Cash Financed	−0.53***	−0.54***	−0.56***	−0.56***	−0.56***
	(0.00)	(0.00)	(0.00)	(0.00)	(0.00)
Acquirer Size	−0.39***	−0.30***	−0.27***	−0.28***	−0.28***
	(0.00)	(0.00)	(0.00)	(0.00)	(0.00)
Acquirer Profitability	0.01***	0.01***	0.01***	0.01***	0.01***
	(0.01)	(0.00)	(0.00)	(0.00)	(0.00)
Acquirer Leverage	−0.01	−0.01	−0.01	−0.01	−0.01
	(0.36)	(0.34)	(0.31)	(0.29)	(0.39)
Acquisition Experience	0.01	−0.11	−0.07	−0.10	−0.10
	(0.94)	(0.48)	(0.66)	(0.54)	(0.51)
Constant	2.82**	5.21***	3.37**	2.36	5.89***
	(0.06)	(0.00)	(0.02)	(0.11)	(0.00)
Observations	997	997	997	997	997
Pseudo R-squared	0.10	0.11	0.11	0.11	0.12

Note: This table presents the results of logit models predicting full versus partial ownership. In all estimations, we included acquirer country, industry and year dummies. We estimate the models with robust standard errors. The p-values are presented in parentheses.
***$p < 0.01$.
**$p < 0.05$.
*$p < 0.1$.

($\beta = -0.52$, $p < 0.05$) and *Military Relations* ($\beta = -14.32$, $p < 0.1$) on EMFs' propensity to opt for full ownership entry mode.

In sum, these results suggest that when EMFs acquire target firms originating from countries with weak economic relationship with their home country, they opt for full ownership supporting the view of internalization theory, which supports H1b.

Robustness checks

In order to ensure the robustness of our findings, we performed several additional analyses by using

Table 5. Sensitivity checks

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Economic Relations	−6.00***	−5.61**	−6.62***	−3.81***	−0.74***	−4.86**
	(0.01)	(0.01)	(0.00)	(0.00)	(0.01)	(0.02)
Political Relations	−0.45***	−0.53***	−0.47***	−0.31***	−0.06**	−0.54**
	(0.00)	(0.01)	(0.02)	(0.01)	(0.04)	(0.02)
Military Relations	−16.18**	−16.25**	−13.74*	−8.91*	−0.79	12.39
	(0.04)	(0.04)	(0.07)	(0.07)	(0.57)	(0.55)
Cultural Distance	0.09	−0.06	0.18	0.11	0.08*	0.99**
	(0.79)	(0.90)	(0.59)	(0.58)	(0.08)	(0.02)
Institutional Distance	−1.92***	−1.92***	−1.70***	−1.08***	−0.14	−0.92**
	(0.00)	(0.00)	(0.00)	(0.01)	(0.22)	(0.21)
Expropriation	−0.02**	−0.02**	−0.02**	−0.01***	−0.01	−0.01
	(0.03)	(0.02)	(0.02)	(0.03)	(0.31)	(0.39)
Colony	0.20	0.17	0.19	0.12	0.01	0.10
	(0.50)	(0.56)	(0.49)	(0.50)	(0.74)	(0.76)
Common Language	0.05	0.06	0.08	0.04	−0.02	−0.21
	(0.79)	(0.74)	(0.65)	(0.75)	(0.49)	(0.39)
Geographic Distance	−0.25*	−0.23	−0.26**	−0.18**	−0.04*	−0.24
	(0.07)	(0.11)	(0.03)	(0.02)	(0.08)	(0.13)
Developed Country	0.42*	0.43*	0.40*	0.27*	−0.02	−0.16
	(0.06)	(0.06)	(0.07)	(0.05)	(0.95)	(0.52)
GDP Growth Target	0.06*	0.06*	0.06*	0.04*	0.01*	0.04*
	(0.09)	(0.08)	(0.06)	(0.08)	(0.07)	(0.08)
Crisis Target	0.41	0.42	0.47*	0.26	0.05	0.26
	(0.15)	(0.15)	(0.06)	(0.13)	(0.20)	(0.39)
Private Target	−0.06	−0.07	−0.08	−0.05	−0.03	−0.10
	(0.67)	(0.64)	(0.58)	(0.61)	(0.14)	(0.56)
Industry Relatedness	−0.21	−0.22	−0.21	−0.13	−0.01	0.03
	(0.14)	(0.14)	(0.13)	(0.14)	(0.85)	(0.87)
Cash Financed	−0.54***	−0.54***	−0.53***	−0.34***	−0.05**	−0.21
	(0.00)	(0.00)	(0.00)	(0.00)	(0.01)	(0.20)
Acquirer Size	−0.29***	−0.29***	−0.27***	−0.17***	−0.04***	−0.33***
	(0.00)	(0.00)	(0.00)	(0.00)	(0.00)	(0.00)
Acquirer Profitability	0.01***	0.01***	0.01***	0.01***	0.01**	0.01***
	(0.00)	(0.00)	(0.01)	(0.00)	(0.03)	(0.00)
Acquirer Leverage	−0.01	−0.01	−0.01	−0.01	−0.01	−0.01
	(0.45)	(0.42)	(0.31)	(0.38)	(0.26)	(0.43)
Acquisition Experience	−0.05	−0.05	−0.08	−0.04	−0.02	0.27
	(0.77)	(0.74)	(0.58)	(0.68)	(0.45)	(0.14)
Constant	6.06***	6.06**	5.62***	3.69***	1.41***	5.30***
	(0.00)	(0.00)	(0.00)	(0.00)	(0.00)	(0.00)
Observations	997	997	997	997	997	997
Pseudo R-squared	0.12	0.12	0.09	0.12	0.12	0.11

Note: We estimate the models with robust standard errors. The p-values are presented in parentheses.
***p < 0.01.
**p < 0.05.
*p < 0.1.

alternative measures and changing some specifications, as shown in Table 5. First, in the previous analysis, *Political Relations* was calculated considering three voting options, namely, approval for an issue, disapproval for an issue or abstain. We include an alternative measure of *Political Relations* in Model 1 that only considers the two voting options: approval for an issue and disapproval for it. Second, we include an alternative measure of *Cultural Distance* in Model 2 that also considers two additional Hofstede's cultural dimensions (i.e. long-term orientation vs. short-term orientation and indulgence vs. restraint).

In addition, we used alternative empirical specifications by (a) running logistic regressions after excluding acquirer country, industry and year

dummies as shown in Model 3; and (b) using probit regressions as shown in Model 4. Moreover, instead of employing a dummy variable as our dependent variable (1 if the acquisition is full and 0 if the acquisition is partial), we used a censored continuous variable to measure the ownership choice of EMFs in Model 5. Since this variable is the percentage of ownership by the acquiring company after the transaction, which ranges from 0.1% to 100%, we use a Tobit model.

Finally, we have coded our dependent variable using the 50% threshold to estimate the results as presented in Model 6 of Table 5. The variable takes the value 1 if the firms acquired more than 50% of the target company (full acquisition) and 0 if the firm acquired less than 50% of the target company (partial acquisition). The results obtained from these additional analyses remain qualitatively similar to our main finding, thereby supporting H1b.

Discussion and conclusion

Theoretical contributions and managerial implications

By theorizing and testing the effect of bilateral relationships on EMFs' ownership choice, our study first contributes to prior research on multinational corporations' cross-border acquisitions. Specifically, by developing conflicting hypotheses grounded in real options theory and internalization theory, it advances our understanding of how affinity (or animosity) between countries – reflected in their bilateral relationships – shapes international business transactions between firms. Given the political risks derived from weak bilateral relationships, internalization theory would emphasize the potential for learning opportunities (Stahl and Tung, 2015), while real options theory would highlight the potential for misunderstanding (Beugelsdijk, Ambos and Nell, 2018; Nell, Kappen and Laamanen, 2017). In line with the internalization predictions, our analysis shows that when bilateral relationships between home and host countries are weak, entailing higher transaction and coordination costs, EMFs opt for full ownership. Despite the costs and complexities of operating in unfavourable host-country environments, derived from their weak bilateral institutional relationships, we show that EMFs prefer full acquisitions to achieve more efficient learning via greater internalized control.

Second, and more broadly, our study intends to make a connection between international business and international relations literature. It is well known that bilateral relationships between home country and host country play an influential role in gaining or losing a competitive edge for multinational corporations (Hymer, 1960). This is because the nature of multinational corporations as entities operating under multiple national jurisdictions pinpoints the relevance of interstate political relations to international business (Li and Vashchilko, 2010). Yet, prior international business research, drawing on institutional perspective and political risk, has provided little insight into the institutional impact associated with the broader international relations by considering bilateral or dyadic networks (Demirbag, McGuinness and Altay, 2010). Drawing on an international relations perspective to explain the ownership choice implications of economic, political and military relationships in a comprehensive manner, our analysis not only shifts the country-dyadic lens of existing country-level determinants from distance to contact/friction (Li *et al*., 2019; Shenkar, Luo and Yeheskel, 2008), but also from differences to discordance (Lee, Shenkar and Li, 2008; Miller and Parkhe, 2002).

Third, our study advances understanding of EMFs' internationalization behaviour by highlighting the underlying factors that cause ownership variances among EMFs. Although recent research has recognized EMFs' strong heterogeneity, the explanatory power of existing theories to explain EMFs' ownership choice remained ambiguous. Specifically, we endeavoured to apply both real options theory and internalization theory to explain the ownership implications of bilateral relationships in the context of EMFs. Apart from the results of our main hypotheses, our analysis further shows that EMFs prefer full acquisitions when they enter developed countries (Hennart, 2009). Such risk-taking behaviours by EMFs are often intended to overcome their latecomer disadvantages, which are characterized by the acquisition of critical assets from target firms to compensate for weaknesses (Luo and Tung, 2007). The findings – along with our main results – enable us to disentangle the ambivalence in ownership choice research and answer a growing body of research calling for examining the predictive power of existing theories across different contexts (Peng, 2003).

The current study also provides managerial implications. It is known that one effective way to deal with risks is to opt for partial ownership in order to benefit from the existing legitimacy of the local firm (Xu and Shenkar, 2002). This conventional wisdom is based on the evidence from traditional multinational corporations (mainly from the developed world). According to our findings, EMFs choose full ownership even when there are weak bilateral relationships. This is because EMFs usually originate from countries where the presence of institutional voids and political hazards is evident. As their political capabilities developed over time can handle such constraints in their home (emerging) countries, they are inoculated against the potential disadvantages that are driven by weak institutional relationships when they internationalize (Guillén and García-Canal, 2009; Luo and Tung, 2007). Notably, one of the key features of EMFs' internationalization is their tolerance for host-country institutional risk (Buckley *et al*., 2018). Therefore, instead of viewing the institutional environment as an exogenous element, MNEs need to proactively and systematically exploit and internalize institutional advantages by carefully incorporating political actors into their governance structure and strategic planning (Doh, Lawton and Rajwani, 2012; Mellahi *et al*., 2016).

Opportunities for future work

This study is not without limitations. Ownership strategies as an entry mode cover a wider range of possibilities (e.g. foreign subsidiaries, international joint venture, etc.) than just cross-border acquisitions, so we must be cautious in extrapolating the findings to other contexts (Sun, Hu and Hillman, 2016). Despite the contextual limitation, our study focused on the ownership choice in the context of cross-border acquisitions, as cross-border acquisitions have particular relevance for EMFs (Luo and Tung, 2007, p. 485). This is mainly because the strategic assets required by EMFs are not available as free-standing assets on the open market, other than through international acquisitions. Future studies can test the predictive power of real options and internalization theories in other international business contexts by considering the ownership decisions related to foreign subsidiaries and international joint ventures. Moreover, our analysis excludes state-owned enterprises (SOEs) following Luo and Tung's (2007, p. 482) approach on operationalizing EMFs. However, it would be interesting to extend our study to empirically examine the role of bilateral relationships in SOEs' ownership decisions.

Finally, it is important to note that our theory development is based on three premises on EMFs. First, EMFs often intend to overcome their latecomer disadvantages through learning characterized by the acquisition of critical capabilities from target firms in order to compensate for weaknesses (Luo and Tung, 2007). Second, EMFs are less vulnerable to institutional challenges and government interference, as their country of origin includes institutional voids and political hazards that give them strong political capabilities (Guillén and García-Canal, 2009; Luo and Tung, 2007). Third, EMFs are in need of greater legitimacy in host countries to cope with the risks derived from weak bilateral relationships. Given the elements embedded in our research, the generalizability of our findings might be limited due to our sample comprising EMFs, which are known to have special forms of internationalization strategy (Buckley *et al*., 2018; Luo and Tung, 2007). Nonetheless, our research provides a context for advancing the understanding of the predictive power of existing theories (Peng, 2003).

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