

Volume 15, Number 2

Print ISSN: 1544-0222

Online ISSN: 1544-0230

Journal of International Business Research

Editor

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PREPARING GRADUATES FOR ENTERING THE GLOBAL BUSINESS ARENA: A GROUP MENTORING APPROACH

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ABSTRACT

Mentoring is traditionally thought of as a relationship where a more experienced, older individual (the mentor) provides advice and guidance to a less experienced, younger individual (the protégé). Group mentoring is a new approach to traditional mentoring in that it provides protégés with multiple mentors. It is especially suited for providing graduating students with invaluable expertise on how to succeed in an international arena, as mentoring advice can be collected by leaders from all over the world.

In this study, we provide an initial demonstration of how group mentoring can benefit and augment international education by providing insights on how new graduates can develop their international careers. An electronic survey was administered to members of the European Foundation for Management Development (EFMD). Approximately 2,000 subjects were asked to make recommendations on a variety of topics to help new graduates succeed as global managers.

Subjects were asked to provide career-related advice by recommending books, magazines, and journals that new graduates should read as well as blogs and twitter feeds graduates should follow to be successful internationally. Subjects were also asked to recommend courses and skill sets that should be developed. Finally, subjects were asked to provide psychosocial advice by recommending life experiences graduates should embrace or avoid and to describe their own significant life experiences they felt shaped their success.

Advice to women that may be different than advice provided to men was also solicited. The recommendations provided by respondents were qualitatively analyzed, categorized, and synthesized. This article provides a summary of these recommendations to inform readers and assist new graduates develop their international savvy as they begin their business careers.

INTRODUCTION

Mentoring is traditionally described as the relationship between a younger, less experienced individual (i.e. the mentee or protégé) and an older, more experienced individual (i.e. the mentor), where the more experienced person advises and guides the younger individual. Kram's (1983, 1985) formative research on mentoring identified that mentors provide two forms of support. The first is career-related support to help the mentee advance in the organization. This includes functions such as sponsorship, providing exposure and visibility, coaching, protection and providing challenging assignments. The second is psychosocial support and includes functions such as role modelling, acceptance and confirmation, emotional support and counselling.

Research has reported many benefits associated with being mentored such as higher salaries, more promotions, improved work performance, increased preparedness to handle new

career roles, greater career mobility and enhanced ability to develop new skills (Burke, Mckeen & Mckenna, 1994; Day & Allen, 2004; Douglas, 1997; Dreher & Cox, 1996; Ehrich & Hansford, 1999; Emmerik, Baugh & Euwema, 2005; Ensher & Murphy, 2011; Fagenson, 1989; Ragins & Cotton, 1999). Meta-analyses examining the career benefits resulting from mentoring found that workers who have been mentored advance more quickly than workers who have not (Allen et al., 2004; Eby et al., 2008).

Over the past few decades, several approaches to mentoring have been developed, including formal mentoring (a formally administered program where a mentor is matched with a mentee), reciprocal mentoring (younger workers mentoring older workers), peer-to-peer mentoring, and e-mentoring (mentoring virtually or electronically with limited face-to-face contact).

A relatively new approach to mentoring is *Group Mentoring*, which we believe could be invaluable in our increasingly global economy. Group Mentoring involves matching multiple experts, considered mentors, with multiple learners, considered mentees (Carvin, 2011). Participants choose topics of relevance, assemble either face-to-face, through electronic conferencing or other means, and discuss and learn about the topics, often with the help of a group facilitator (Emelo, 2011). Mentors can be peers, or individuals at any level of the organization who are experts with respect to the topic of discussion. Group Mentoring offers a relatively quick, inexpensive and effective mentoring experience for members from different backgrounds, genders, ethnicities, countries and cultures.

Given growing globalization, more and more universities incorporate globalized views and diversity training into their curriculum and many business schools are seeking accreditations from societies (e.g., European Quality Improvement System - EQUIS, Association of Master of Business Administration - AMBA, Association to Advance Collegiate Schools of Business - AACSB) that encourage the acquisition of internationalisation perspectives. Training industry leaders does not end at graduation, however, it continues well beyond formal schooling. It takes years to acquire the skills, knowledge and understanding of the international 'know how' via access to the advice, guidance and coaching of others who already operate in this complex and multi-faceted environment. Understanding and conveying 'know how' is especially suited to Group Mentoring, as it requires pooling the advice and input of many experienced executives from all over the world.

One way Group Mentoring can function is to have a facilitator solicit advice from a diverse pool of experts and then share that advice with new graduates. In this study we asked an international pool of experts to advise new graduates on what they should do to prepare themselves to be successful in the global arena. We identified topics that could benefit the mentees and compiled the responses to provide a comprehensive resource that combines career-related advice (e.g. courses to take, books to read, etc.) as well as psychosocial advice, such as the intangible factors that shaped the path of leaders from various countries (e.g. experiences that should be avoided/embraced, formative junctions in mentors' life).

The primary objective of this study is to demonstrate how group mentoring can benefit the education of new graduates entering the global arena. The secondary objective of the current study is to synthesize the advice of an international pool of educational experts to provide guidance to those seeking international perspectives.

METHODOLOGY

Procedure

Surveys were forwarded to approximately 2000 senior officials listed in the European Foundation for Management Development (EFMD) membership directory. The EFMD is an international forum where leading academic, businesspeople, public servants and consultants from 81 countries exchange information and ideas regarding best practices in management development and promote a fine balance between high academic quality, professional relevance and internationalism in institutions dedicated to management education. The surveys were administered using Fluid Survey. An invitation as well as a one week delayed reminder were sent via email.

Sample

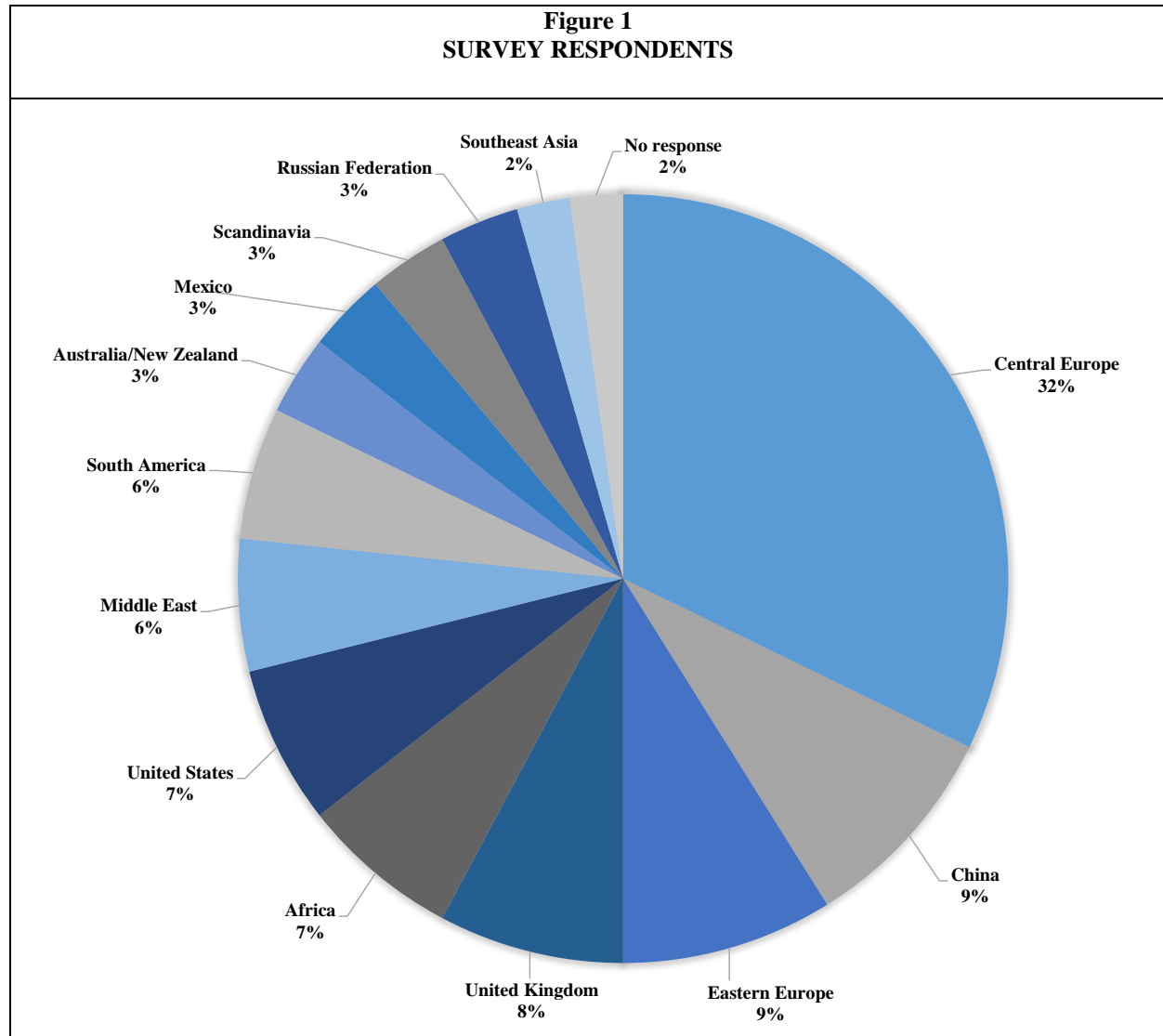
Ninety completed surveys were obtained. Of the 90 participants, 31% were female and 67% were male, with 2% choosing not to disclose their gender. About 71% of the subjects had completed a PhD degree, 27% completed a graduate degree other than a PhD, 1% completed an undergraduate degree and 1% chose not to disclose their academic standing. The ages of the participants varied significantly, ranging from 30 to 80 years of age with an average of 53 years. Given the goals of this study, it was important that the sample include an international array of respondents. Figure 1. Illustrates the location of respondents.

Survey

The questionnaire was divided into three categories. First, respondents were asked to recommend what books, magazines, journal articles, blogs and twitter feeds business graduates should read to prepare themselves for an international career. They were also asked to recommend avenues for future education and what skill sets graduates should develop. Note that this section corresponds to the career-related advice component of mentoring. Second, advice was solicited regarding life experiences that should be avoided or embraced. Respondents were then asked what single life experience had shaped them the most. This section corresponds to the psycho-social component of mentoring. The third section consisted of a single question to probe what advice would be given over and above the previous advice for aspiring female graduates.

Analysis

Responses were downloaded into a Microsoft EXCEL spreadsheet and analysed qualitatively. First similar answers were combined. When appropriate, responses were subsequently categorized. The frequencies reported in each category reflects the total number of times responses fitting that category were provided. Note that because some subjects provided more than one response per question, the total number of responses may be greater than the number of subjects.



RESULTS

Which Academic Journal(S) Would You Suggest Graduates Read?

Academic journals were grouped into seven categories (see Table 1). By far the most commonly recommended journal was the Harvard Business Review (recommended 21 times). The frequencies corresponding to other journals can be found in the table; if no frequency is provided, it was cited only one time. Twenty-one subjects did not reply.

Which Book(S) Would You Recommend Graduates Read?

Books were grouped into nine categories: Popular management/self-help (n=39); Management textbooks (n=11); History (n=10); Classics (n=5); Biography/Memoire (n=3); Religion (n=3); Finance/Economy (n=3) and Novels (1). Eleven respondents provided only general answers (e.g., “whatever is of interest”) and four subjects did not respond.

Roughly 43% of all subjects recommended books in the popular management/self-help category (see Table 2. for an alphabetical list of books and their authors). The two books that were most commonly recommended in this category were “The Seven Habits of Highly Effective People” by Stephen R. Covey (n=5), and “The World is Flat” by Thomas L. Friedman (n=4).

Table 1
RECOMMENDED JOURNALS

Category	Recommendations
Business and Management (n=41)	Harvard Business Review (n=21), Academy of Management Journal (n=6), Journal of Management, Strategic Management Journal (n=3), Journal of Management (n=2), California Management Review (n=2), Journal of Applied Management, , Journal of Business Research, Journal of Management Science, Interfaces, Knowledge Management Research & Practice, Innovation
International (n=17)	Journal of International Business Studies (n=4), International Journal of Purchasing and Material Management, International Marketing Review, Journal of International Economics, Journal of International Business Ethics, International Journal of Management Review, International Journal of Business and Management, Journal of World Business, China Quarterly, Journal of Economics and International Finance, International Business Review
Finance and Economics (n=9)	Journal of Economics (n=2), Applied Corporate Finance, Financial Management, Journal of Finance, Journal of Finance and Banking, Journal of Economic Literature, Journal of Economic Perspectives
Marketing (n=7)	Journal of Marketing (n=4), Journal of Consumer Research, Journal of Media & Communication, Marketing Research
Organizational Behavior and Human Resource Management (n=5)	The Leadership Quarterly, Journal of Behavior, Human Relations, Industrial and Corporate Change, Education + Training
Ethics (n=5)	Business Ethics Quarterly (n=2), Journal of Business Ethics (n=2), Corporate Social Responsibility
Entrepreneurship/Small Business (n=4)	Journal of Small Business Management, Journal of Business Venturing, Entrepreneurship Theory and Practice, Entrepreneurship and Regional Development

Which Blog(S) Would You Suggest Graduates Follow?

Fifty-two respondents chose either not to answer this question, reported that they do not read blogs or said that they have no idea which blog to recommend, (e.g. “don't know”, “anyone who is a thought leader”) and 11 responded that they have no specific recommendation (e.g. “Any relating to their field of specialism”). Recommendations were grouped into five categories (see Table 3. for the Blog names and URLs). The blogs of specific individuals was the most frequently cited (n=10), followed by news organizations (n=8) and business blogs (n=6). The most frequently cited business blog was the Harvard Business Review (n=3). The frequencies corresponding to the other blogs can be found in the table; if no frequency is provided, it was cited only one time.

Table 2	
RECOMMENDED BOOKS IN THE POPULAR MANAGEMENT AND SELF-HELP CATEGORY	
Book Title	Author(S)
Blink	Malcolm Gladwell
Built to Last	James C. Collins and Jerry I. Porras
First Break all the Rules	Curt Coffman and Marcus Buckingham
From Good to Great	James C. Collins
Getting to Maybe	Frances Westley and Brenda Zimmerman
How do you Measure your Life?	Clayton M. Christensen, James Allworth and Karen Dillon
How to Change the World	David Bornstein
Images of Organization	Gareth Morgan
Leadership without Easy Answers	Ronald A. Heifetz
Leading Quietly	Joseph L. Badaracco
Managers not MBAs	Henry Mintzberg
Maslow on Management	Abraham Maslow
On Competition	Michael E. Porter
Running Lean	Ash Maurya
Strategy Safari	Henry Mintzberg and Joseph Lampel
The 7 Habits of Highly Effective People (n=5)	Stephen Covey
The Art of War	Sun Tzu
The China Strategy	Edward Tse
The Effective Executive	Peter Drucker
The Essential Drucker	Peter Drucker
The Realities of Work	Mike Noon and Paul Blyton
The Talent Masters	Bill Conaty and Ram Charan
The Tipping Point	Malcolm Gladwell
The World Business Cultures how to Unlock them	Barry Tomalin and Mike Nicks
The World is Flat (n=4)	Thomas L. Friedman
Thinking, Fast and Slow	Daniel Kahneman
Topgrading	Bradford Smart
What Color is my Parachute	Richard Nelson Bolles
Why Should Anyone Be Led by You?	Gareth R. Jones and Robert Goffee
Winning (n=2)	Jack Welch and Suzy Welch

Which Twitter User(S) Would You Recommend Graduates Follow?

Sixty-seven participants chose not to answer this question, six recommended “nothing specific” while two respondents recommended avoiding this media all together (e.g. “avoid media like these”). The fifteen subjects remaining recommended: Business (Harvard Business Review and Smallbiztrends); News Organizations (ThinkBig, Business Week, Wall Street); Individuals (three professors, two businessmen and one TV journalist); Sina Weibo (note that this was also recommended in the blog section); and general recommendations (well-known economists, their own CEO).

Table 3 RECOMMENDED BLOGS	
Blog Name	Blog Url
Business Blogs (n=6) Harvard Business Review (n=3) Young Entrepreneurs 50 plus 20 Banka Magazine	https://hbr.org/ https://www.entrepreneur.com/topic/young-entrepreneurs http://50plus20.org/ http://www.banka.hr/
News Organizations (n=8) CNN (n=2) The Financial Times (n=2) The Guardian Wall Street Journal The Economist ESPN	http://business.blogs.cnn.com/ http://www.ft.com/comment/blogs http://www.theguardian.com http://www.wsj.com/news/us http://www.economist.com/blogs http://espn.go.com/
Individuals (n=10) Jeff Sachs Paul Krugman Michael Czinkota Subroto Bachi Richard Branson Seth Godin Steve Blank Stephen Covey David Gurteen Ted Talks	http://jeffsachs.org/ http://www.krugmanonline.com/ http://michaelczinkota.com/ http://subrotobagchi.mindtree.com/ https://www.virgin.com/richard-branson http://sethgodin.typepad.com/ https://steveblank.com/ http://www.stephencovey.com/blog/ http://www.gurteen.com/ http://www.ted.com
Social Media (n=2) Sina Weibo (n=2)	http://www.weibo.com/signup/mobile.php?lang=en-us
General (n=2) Blogs of 10 top business schools Blogs of Chambers of Commerce	

Which Print Magazine(S) Would You Advise Graduates To Read Regularly?

The Economist was the most widely recommended print magazine (n=39), followed by Harvard Business Review (n=11), Financial Times (n=9), BusinessWeek (n=6), Time Magazine (n=5), Forbes (n=2), Newsweek (n=2) and The New Yorker (n=2). Seven respondents recommended local magazines (e.g., New China Digest, Lebanon Opportunities), four respondents provided non-specific recommendations (e.g., “all of them” or “professional/academic journals”) and five subjects did not respond.

What Educational Course(S) Should Graduates Take?

Recommended courses were grouped into six categories (see Table 4). The largest category of recommendations corresponded to core MBA curriculum and eight respondents simply recommended pursuing an MBA. Subjects also promoted courses that provided breadth (n=26). Developing people (n=15), analytical (n=11) and career advancement (n=6) skills were also frequently recommended. Finally, courses to develop accountability (n=8) were also recommended. Thirteen respondents recommended taking courses according to ‘personal

interest’ or gave a non-specific recommendation (e.g. “anything that furthers them in maturity,” “the ones they feel useful”) and six subjects did not respond.

Category	Courses
Core Management (n=30)	Marketing, OB, Strategy, International Business, Entrepreneurship, Accounting, Finance, Economics
Breadth (n=16)	History, Philosophy, Psychology, Law, Humanities, Physical Sciences, Anthropology, Sociology, Politics
People Skills (n=15)	Leadership, Cross-cultural Management, Languages, Coaching, Mentoring, Negotiation
Analytical Skills (n=11)	Creativity, Research Methods, Statistics, Critical Thinking
Accountability (n=8)	Ethics, Corporate Governance, Sustainability, Social Impact
Career Advancement Skills (n=6)	Public Speaking, Executive Presence, Self-Awareness, Emotional Intelligence

What Skill(S) Should Graduates Develop?

The response rate to this question was the highest in the survey, with 89 of the 90 subjects responding. Recommended skills were grouped into eight categories (see Table 5.). Developing ‘soft skills’ such as Communication Skills (n=37) and People Skills (n=27) were the most frequently recommended. Developing skills that are critical for leadership roles were also frequently recommended (Leadership Skills, n=27; Emotional Skills, n=11; Ethical Skills, n=4). Finally, developing skills that would make the graduate a better ‘international manager’ were also frequently recommended (Thinking Skills, n=19; Managerial Skills, n=10; Cross-Cultural Skills, n=8).

Skills	Recommendations
Communication Skills (n=37)	Develop oral, written, listening and presentation Skills. Use proper grammar and spelling. Develop the use of rhetoric.
People Skills (n=27)	Be respectful, empathetic, open-minded and patient. Develop interpersonal, team, networking and coaching skills.
Leadership Skills (n=27)	Develop dynamism, perseverance, adaptability, agility, confidence, creativity and entrepreneurship. Embrace continuous learning.
Thinking Skills (n=19)	Develop critical, analytical, abstract and strategic thinking. Develop enquiring, research and decision making skills.
Emotional Skills (n=11)	Develop self-awareness, emotional intelligence, self-reflection and coping skills. Learn how to manage stress.
Managerial Skills (n=10)	Develop time management and project management skills. Learn to prioritize. Learn various computer applications. Be efficient and effective.
Cross-Cultural Skills (n=8)	Develop cultural awareness and a global mindset. Learn languages and how to manage diversity.
Ethical Skills (n=4)	Develop accountability and transparency.

What Life Experience(S) Should They Try or Embrace?

The recommendations were grouped into seven categories (see Table 6.). The recommendations suggest subjects value International Exposure (n=38), both in terms of traveling to other countries but also in preparing oneself to adapt to international life (International Preparedness, n=5). Other life experiences recommended were to be exposed to challenging situations (n=13) and to engage in service activities (n=13). Working on life skills such as developing composure (n=9) and resilience (n=8) were also recommended. Six subjects did not respond.

Life Experience	Recommendations
International Exposure (n=38)	Travel, study abroad, international internships, work abroad, live abroad
Exposure to Challenging Situations (n=13)	Get a demanding job, Work for a start-up, Become an entrepreneur, Find something new, Find competition, Become a leader, Work hard, Develop lateral thinking, Engage in consulting
Service (n=13)	Be socially responsible, Charity work, Military service, Government service, Community involvement, Teach, Volunteer
Exposure to Differences (n=12)	Exposure to diversity, Exposure to rural life in developing countries, Exposure to poverty, Exposure to the 'base of the pyramid,' Travel to remote places
Developing Composure (n=9)	Meditate, Be honest/sincere/patient, Engage in journaling, Be introspective, Focus on work/life balance
Developing Resilience (n=8)	Fail at something, Survive a near-death experience, Deal with setbacks, Go camping, Don't fear the unknown, Travel with a low budget, Keep a sense of humour, Look forward and live in the present
International Preparedness (n=5)	Be coached/mentored, Buy online, Learn English, Learn about other cultures

What Life Experience(S) Should Graduates Avoid?

Life experiences to be avoided were grouped into ten categories (see Table 7.). Avoiding illegal and unethical behaviors were the most frequently cited recommendations (n=17 and 5 respectively). Many recommended avoiding staying in one's comfort zone (n=20) while conversely others recommended avoiding risky situations (n=6). Recommendations also focused on ensuring emotional and psychological well-being by avoiding people and jobs that may lead to unhappiness (n=10 and 4 respectively) as well as harbouring negative attitudes and behaviour, such as hatred (n=4). Finally, subjects recommended to avoid being lazy (n=8), but also to avoid working too hard and focusing too much on money (n=7). Five respondents believed that all experiences are meaningful and thus provided responses that were categorized as non-specific (e.g. "probably there is something to learn from all experiences") and twelve subjects did not respond.

Table 7
LIFE EXPERIENCES TO AVOID

Experiences To Avoid	Recommendations
Staying in one's Comfort Zone (n=20)	Do <u>not</u> be alone, stay home, stay in one place or one job, do nothing, be inflexible, be narrow in focus or stop pushing forward after a first success. Travel, take risks and open your networks.
Illegal Behaviors (n=17)	Do not take drugs or engage in illegal behaviors such as fraud, domestic abuse, murder, corruption.
Interpersonal Unhappiness (n=10)	Avoid people who make you uncomfortable and who are selfish and take advantage of you. Avoid destructive conflicts. Be happy, satisfied and self-confident.
Laziness (n=8)	Do not be lazy, take shortcuts, and adopt an 'employee mentality.' Continue to develop competencies.
Risky Behaviours (n=6)	Avoid risky activities such as bungee-jumping, gambling, going to nightclubs, going to the extremes in any pursuit and visiting dangerous places.
Focus on Money (n=7)	Do not be materialistic, greedy, self-indulgent and only focused on one's career.
Unethical Behaviors (n=5)	Avoid unethical behaviour and practices, cheating, and using tricks to manipulate others.
Negative Behaviors/Attitudes (n=4)	Do not be hateful, conceited, arrogant and judgemental.
Unhappiness at Work (n=4)	Do not work in a toxic workplace, let yourself be a victim, engage in politics or accept a job that others think is good for you

What Single Life Experience Has Shaped You the Most?

The examples of formative single life experiences were grouped into seven categories (see Table 8). International Experience was cited as one of the most formative life experiences (n=19). The remaining examples can be further grouped into two broad categories: positive experiences such as single work/life experiences which were significant (n=19), family (n=15), achieving a major accomplishment (n=14) and knowing oneself (n=9). These formative positive life experiences frequently appeared in childhood or young adulthood (n=11). Positive experiences with family were primarily related to having children (n=9). Negative experiences, such as having to deal with death and illness (n=6) and significant unpleasant work/life experiences (n=5) were also cited as formative life events. Four subjects did not respond.

What Advice Would You Provide Women in International Management That is Over and Above Your Previous Recommendations?

These recommendations were grouped into eight categories (see Table 9). The most frequently recommended advice was to take on characteristics typically associated with men (n=22) and one respondent bluntly recommended "be a man." Conversely, many others recommended the opposite (n=20) with half in this category recommending "don't forget that you're a woman." Others recommended that women in international management should 'forget' that they are women (n=5) or work harder to be better than men (n=5). Many offered psycho-social advice on how to cope (n=18) and get help (n=7). Some recommended career-related advice such as taking risks (n=6) and investing in one's human capital (n=3). Nine subjects did not respond, some indicating that they did not feel qualified to provide advice because they were men.

Shaping Life Experience	Examples
International Exposure (n=19)	Travel, international assignments, working abroad, living abroad
Significant Work/Life Experiences (n=19)	Working in public administration, volunteering, teaching, changing company, joining the military, a great job, outdoor adventures, sports, team competitions, attending university, summer camps, theatre production
Family (n=15)	Marriage, children, fatherhood, motherhood, talks with one's father
Major Accomplishments (n=14)	Starting up a company, a successful business ventures, running a marathon, dealing with a difficult job, defeating adversity, obtaining a scholarship, reading at an early age, achieving independence
Knowing Oneself (n=9)	Faith, patience, taking a sabbatical, self-approval, finding a mentor
Death/Illness (n=6)	Near death experience, death in the family, family member illness, recovering from an illness, near death of a child
Negative Job/Life Experience (n=5)	Major fight, being ignored, failure at work, not being promoted

Category	Recommendations
Be Male (n=22)	Be assertive, ambitious, tenacious, persistent, self-confident, passionate and proud. Be as strong a man at work. Forget you are a woman. Don't take 'no' for an answer. Speak freely.
Be Female (n=20)	Be a woman. Stay in gendered roles. Accept that in some cultures women are less likely to be in management positions. Stay calm. Be an active listener. Don't be too friendly towards men. Be patient and careful. Don't try to change others.
Cope (n=18)	Ignore negative views. Be strategic and focused. Stick to your values and ambitions. Be resilient and keep a sense of humour. Love yourself and maintain a work/life balance.
Get Help (n=7)	Network and find a mentor. Let men help you.
Seek Risks (n=6)	Take chances, risks and opportunities. Accept challenges. Apply for stretch jobs (i.e., jobs you think you can do, not know you can do).
Forget that you're a Woman (n=5)	Act like you are equal, treat men equally, do not expect preferential treatment, be inclusive with staff
Be Better than Men (n=5)	Act like a Queen, work harder than men, you are better than men, aim high
Invest in your Human Capital (n=3)	Get an MBA, CMB, CFA, ACCA. Gain international experience.

DISCUSSION

This study provided a rare opportunity to gather invaluable information from an international group of leaders who are dedicated to promoting the quality in management education worldwide. Their expert responses offered students with a preliminary understanding of 'what do I need to know to be successful as a global leader?' The main goal of the study was to synthesize the advice of an international pool of educational experts to assist business schools students to prepare for successful careers as international leaders. To that end, we were indeed able to gather, synthesize and analyze valuable advice regarding the tangible and intangible factors that promote a successful path. However, we should also keep in mind the shortcomings of the current study.

First, although the survey was initially distributed to a directory of approximately 2000 members, it generated only 90 completed surveys, an overall response rate of 4.5%. It is possible that the low response rates can be attributed to language issues arising from the international nature of the sample. Perhaps translating the existing questionnaire to accommodate for the multiple languages spoken by EFMD members would increase the response rate.

Second, our sample consisted of respondents from 44 different countries, which aligns well with the purpose of this study and represents the international diversity in the current workforce. However, we must keep in mind that cultural background can potentially affect respondents' perspectives and hence individual advice provided in the survey might reflect culturally specific perspectives rather than broader international trends. Future research should aim to obtain a larger sample from individual countries to allow controlling for cultural differences.

Group mentoring is still in its infancy and this is an initial attempt towards achieving the goal of creating a global group mentoring platform that would help aspiring business students worldwide. Ultimately, an international group-mentoring program could be a joint initiative undertaken by academia, businesses, governments and accreditation societies with the objective of providing guidance to students envisioning international careers.

CONCLUSION

As we get closer to the end of the second decade of the twenty-first century the attention being paid to, if not the emphasis for managers is on mastering technology and the quantitative nature of business decisions. From apps, analytics, and predictive modelling, to drones, artificial intelligence, 3D printing, and robotics, the signals to aspiring managers is on understanding consumers, employees, and stakeholders from the zero through nine perspective rather than from an A to Z one.

Before acquiescing to a wholesale shift in perspective however, it is worth noting while the ascendance of technology and quantitative approaches to decision-making and managing is undeniable, managers can still benefit from development of an older and well-documented approach - mentoring.

A visit to the business / career self-help section of any local or online bookstore reveals no lack of titles offering to educate people on the merits of soft skills and seeking out one or more key individuals for mentoring relationships. Somewhat ironically, a good many of these titles are at least to some degree derivative from earlier works.

The *Art of War* attributed to the writings of Sun Tzu, believed to have been written approximately 2500 years ago, has been called into service as a text on business strategy and spawned numerous military-oriented strategy books. More recently, *How to Win Friends and Influence People* by Dale Carnegie, originally published in the 1930s in the aftermath of the U.S.' Great Depression has given way to a vast number of books on interpersonal influence – both for use in business as well as in society at large.

It seems at the same time both intuitive and counterintuitive that in an era of rising importance of the quantitative and technology, managers need to recognize the renewed importance of people, and how to deal with them, in developing and carrying out the aftermath of all that analysis and data.

It is into this world that the general importance of mentoring is reaffirmed. The current research focuses on group mentoring as an extension of the more familiar one-on-one type. The recommendations of managers concerning everything from information sources to monitor and

experiences to both have and avoid represents a virtual mentoring experience from a large collection of individuals who have made the professional journey that many businessmen and businesswomen aspire to. It would be wise to listen to what they have to say.

ACKNOWLEDGEMENT

The authors would like to extend their thanks to Shlomit Jacobson, University of Ottawa graduate student, for her contributions on an early draft of this manuscript002E

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GEOGRAPHIC DIVERSIFICATION AND RISK REDUCTION FOR THE PRIVATELY HELD COMPANY: FROM HERE TO WHERE?

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ABSTRACT

Previous literature on diversification strategies has focused primarily on motivation and value creation from the perspective of publicly traded companies. For publicly traded companies, using diversification – whether into different product markets, industries, or countries – solely for risk reduction purposes and lowering volatility in returns is generally considered not to be in the best interests of shareholders who can accomplish this more efficiently themselves by holding a diversified portfolio of stocks. Far less research has examined rational motivations for diversification from the perspective of a privately held company. Here there is no separation of ownership and control and owners are unable to diversify away unsystematic risk by holding a portfolio of stocks. This paper focuses on country-level factors important for privately held holding companies to consider when making geographic diversification decisions for risk reduction purposes. Using a sample of 8 countries, including Germany, and their annual GDP growth rates from 2003 to 2013, this study found evidence that there are indeed risk reduction benefits connected to international diversification into certain countries, under the premise that the annual GDP growth rate is a representative indicator for a country's economic situation. The results from the conducted quantitative analysis support the theoretical findings based on previous literature on international diversification that under certain circumstances international diversification is a valid means to reduce the volatility in returns and thereby the risk of bankruptcy in the long run.

INTRODUCTION

According to portfolio theory (Markowitz, 1952), lowering the variance of returns means lowering risk. Therefore, economic data can be analyzed to assist firm owners in their international diversification decisions by demonstrating the risk reduction benefits of expansion into particular new countries. The motivation of this paper is to investigate potential merits and drawbacks to a privately held holding company taking an international investment approach. In other words, is bringing diversification from the corporate to the international level an effective way to reduce the risk of bankruptcy for a privately held holding company? The aim of this paper is to investigate the potential risk reduction benefits of international diversification in the case of a privately held holding company. Would it be rational to diversify in an international context with regard to risk reduction purposes and, if so, under which circumstances would it create value?

This paper examines the case of a holding company that is already diversified on a corporate level, but tied solely to one economy on a country level. The overall performance of the company is good and there are no current profit issues that need to be solved. However, regarding the company's strategic plans in the long run, there is a potential risk given the fact

that all of the company's current investments are tied to the German economy. What would happen if the German economy were to fall into a recession while the entire portfolio is comprised of only German companies? It might result in poor performance of the companies in the holding company's portfolio and thus to a declining profit and a higher risk of bankruptcy.

In this case, the privately held holding company exerts little active management in terms of resource transfers (money or managers) across its subsidiaries. Instead, the holding company manages them through financial goals. This is of course a diversified organization, but given that they do not attempt to integrate the subsidiaries, it is basically a portfolio.

RELEVANT LITERATURE

In general, a diversification strategy is described as entering new markets in which a firm is not currently operating. Two major distinctions when it comes to diversification strategies are corporate diversification, where the organization is expanding into different product markets and international diversification, where the organization is expanding into different geographic locations.

Firms may diversify into different geographic markets in order to reap the benefits of the use of an excess in resources and capabilities in different geographic locations. Firms may also diversify internationally in an attempt to reduce risk by investing in more than one geographic location. By diversifying across different geographic markets whose economic cycles are not perfectly correlated, investors can typically reduce the variability of their returns. The value creation premise that can be identified with regard to international diversification is that it is possible to use differences in business cycles of different countries to reduce the volatility in returns or realize growth options.

A number of studies have investigated the effects of international diversification on firm performance. Bühner (1987) investigated the effects that international diversification of firms in Western Germany has on market performance. Based on the argument that economic activity in different countries is less than perfectly correlated, diversification across international boundaries should improve investors' risk-return opportunities. Results showed significant positive relationships between geographic diversification and both market and accounting performance and significant negative relationships between product diversification and performance measures. As a conclusion, domestic product diversity appears to be motivated by internal 'push' stimuli such as risk reduction and poor profitability in traditional lines of business while internationalization appears to be 'pulled' by external stimuli of prospective market opportunities.

Shaked (1986) focused on risk reduction via corporate international diversification, by calculating the failure probabilities of a sample of multinational corporations and comparing them with those of a control group of domestic corporations. Aspects of international diversification are for instance risk reduction and the potential reduction in the probability of bankruptcy. Key findings of this study were that the mean insolvency-probability is significantly higher for domestic corporations than it is for multinational corporations and the average systematic risk of multinational corporations is significantly lower than that of domestic corporations.

Lu and Beamish (2004) investigated the benefits and costs of geographic expansion over different phases of internationalization. Data on 1,489 Japanese firms over 12 years show a consistent S-shaped relationship between multi-nationality and performance. The findings resulted in a horizontal S-curve, which at first showed a performance decline with increasing

internationalization, followed by a positive relationship between increasing geographic diversification and firm performance, which then declined at very high levels of multinationality. These findings imply that the relationship between internationalization and performance is dynamic, that is it varies with the phase of internationalization. A key takeaway for managers is that they need to take a long-term view of internationalization, in order to look beyond the initial stage decline in profits.

Makino, Isobe and Chan (2004) focused on the extent to which country effects explain the variation in the performance of foreign affiliates of multinational corporations. Their findings showed that country effects are as strong as industry effects, following affiliate effects and corporate effects, and that industry and country effects jointly rather than independently influence foreign affiliates' performance. A comprehensive database, which consists of a panel of over 5,183 foreign affiliates, established by 616 Japanese MNC's in 159 businesses (industries), in 79 host countries, over a 6 year period (1996-2001), was used in their study. Foreign affiliates' performance varied not only between parent firms and between industries, but also between host countries that have different comparative and competitive advantages and provide different institutional environments to foreign affiliates.

Nachum and Song (2011) viewed the multi-national enterprise (MNE) as a portfolio of interdependent sub-units and elaborated on its growth trajectory in relation to its existing portfolio. The distinctive source of value creation of an MNE is the management of the interactions among its sub-units. Their study focused on the question of why companies that are similar in regard to size and client orientation and are originated in the same home country, take different paths when it comes to internationalization. They used a dataset comprised of all the international location moves of US legal services MNEs during 1949-2006. The findings showed that MNEs have a preference for countries that resemble their portfolios, which means that firms have a tendency to evolve in directions that follow from their past, rather than break away from it. Existing portfolios exercised stronger impact on entry than on exit; this suggests that path dependent processes affect MNEs' expansion more strongly than their contraction. Entry moves are strongly related to the past, whereas exit moves are driven primarily by firm specific characteristics.

Ke, Ng and Wang (2010) analyzed the US equity holdings of more than 3000 non-US based mutual funds from 22 countries and found robust evidence that fund managers strongly preferred to invest in stocks of US firms that have presence in their home country. Plausible explanations for investors' strong preference for domestic equities include the existence of cross-border boundaries that give rise to exchange rate risk, variation in regulation, taxation, accounting standards, corporate governance, transaction costs, information asymmetries, and biased expectations. However, these factors did not fully account for investors' international asset allocation decisions. Their key findings were that mutual fund managers favor US firms that have presence in their home country, even after controlling for various characteristics of both the firms and fund managers. This bias suggests that the potential benefits of international diversification derived from cross-border holdings are not being fully realized. Implications for practice are that firms could raise equity financing in the foreign markets by establishing a physical presence in those markets, and policy makers could attract foreign investments in their domestic equity markets by encouraging domestic firms to expand internationally.

Goetzmann, Li and Rouwenhorst (2005) collected information from 150 years of global equity market history in order to evaluate how stationary the equity correlation matrix is through time. They found that the structure of global correlations shifts considerably through time and

that roughly half the benefits of diversification available today to the international investor are due to the increasing number of world markets available and half to a lower average correlation among the available markets.

Lee and Hooy (2013) focused on the role of common, country and industry effects on international diversification potential in ASEAN stock markets. They found that despite the increasing integration of economic and financial markets, country effects dominate industry effects.

Rowland and Tesar (2004) also examined the gains from international diversification and found that multinational corporations may have provided diversification benefits for investors in Germany and the United States and that the addition of foreign market indices to a domestic portfolio provided substantial diversification benefits to all countries in the 1984-1995 period.

All of the reviewed literature supports a positive relationship between international diversification and risk reduction benefits and some even state that country effects dominate industry effects (Lee & Hooy, 2013; Serra, 2000). However, all previous work that has been reviewed for this paper has either had a truly financial perspective or investigated the risk reduction benefits of international diversification for the publicly-traded corporation.

THEORETICAL PERSPECTIVES ON DIVERSIFICATION

Resource Based View

The resource based view sees the firm as a bundle of valuable tangible or intangible resources that provide a basis for the competitive advantage of the firm (Wernerfelt, 1984, 1995; Penrose, 1959). The resource based perspective argues that the portfolio of resources a firm controls reflects the portfolio of product market positions that a firm takes. Hence, competition among product market positions held by firms can also be described as competition among resource positions held by firms (Barney & Clark, 2007).

With regard to corporate diversification, the focus is merely on the importance of shared tangible assets across the multiple businesses a diversified firm is operating in (Rumelt, 1974; Montgomery, 1982). One of the most cited explanations of corporate diversification is consistent with the resource based view of the firm: firms diversify in order to exploit their core competencies (Prahalad & Bettis, 1986; Prahalad & Hamel, 1990).

Kor and Leblebici (2005) concluded that success in growth and diversification strategies requires attention to the availability, experience and knowledge of firms' managerial and expert human resources. Even more important than the kind of resources a firm possesses is how they manage them. Strategies related to management and development of human assets at the business level affects the success of diversification strategies. Their purpose was to develop and test a theory of how firms can successfully deploy and develop their strategic human assets while recognizing and managing the tradeoffs in their diversification strategies. Their sample consisted of 105 large US law firms, all private companies, in the years 1995, 1997 and 1999. Their key findings were that human capital leveraging and geographical diversification individually improved profitability, but pursuing both strategies simultaneously at high levels produced negative interaction effects on financial performance. Lateral hiring can help firms build new knowledge bases and take timely advantage of growth opportunities, high levels of both partner leveraging and lateral hiring of associates results in lower profitability. Firms achieve superior returns when there is a strategic fit between diversification strategies and human capital deployment strategy. Service diversification increases firms' profitability by promoting efficient

utilization of knowledge based resources. At high levels of leveraging, law firms are better off with internal development of associate human capital. When a firm diversifies at a faster rate than its bundle of resources can handle, its financial performance suffers.

Depending on the level of strategy (business versus corporate), strategic goals can range from the achievement of a sustained competitive advantage to exploiting synergies by taking advantage of economies of scope. However, the motive for diversification has the same origin. Diversification often results from the excess of resources and capabilities. However, the value creation potential for the firm depends on the specificity of those resources and capabilities and if not even more important on the management of those resources.

Agency View

The agency view of the firm divides the firm into two major groups that are dependent on each other: top managers, referred to as agents, and owners, referred to as shareholders or principals. Given that the two groups might have different interests at certain points in time, there are two major concerns connected to the relationship between them: asymmetric information and moral hazard. So, not only might the interests of the groups differ at some point, they might also have different information regarding a certain matter. When that is the case, it is called asymmetric information. Principal-agent analysis focuses on problems of contracting with asymmetric information which models a widely applicable case where a principal (e.g., a shareholder) cannot monitor how an agent (e.g., a manager) is behaving without any costs connected to the monitoring. This may arise either because the agent has greater expertise or knowledge than the principal, or because the principal cannot directly observe the agent's actions. It is exactly this asymmetric information which leads to a problem of moral hazard. This means that to an extent managers can pursue their own interests. Traditional managerial models typically assume that managers, instead of maximizing profit, maximize a simple objective utility function which is subject to an arbitrarily given profit constraint. This utility function might include for instance salary, security, power and prestige (Berle & Means, 1991).

Taking this into account it might be highly likely that whenever a principal-agent situation arises and there are no appropriate governance mechanisms in place to ensure that the agent is not solely following his or her own agenda, that the actions taken by the agent might not be aligned with the interests of the principal and therefore might not be in the best interest of the firm. Moreover, the manager could even harm the firm value by putting his or her short term utility first, for instance bonus payments because of earlier return rates from an investment, above the interest of the firm to ensure long term profitability. Because of this, the agency view of diversification predicts a negative relationship between diversification and firm value (Montgomery, 1994).

Hoskisson and Hitt (1990) used agency theory, where the crucial contract is between top managers (agents) and owners (shareholders or principals), as the context for their study to argue that there are three theoretical perspectives on diversification. The first perspective assumes market perfection and focuses on firm resource heterogeneity. The second perspective assumes market and firm imperfection and focuses on external and internal incentives for diversification. The third perspective assumes market and firm imperfection and focuses on managerial motives for diversification. Under the assumption of relative market perfection, industry structure is the dominant force affecting firm performance, therefore firm level actions have minimal impact on performance. Diversification is not likely to create any value for the firm, leading to the conclusion that there would be few, if any, significant incentives to diversify. Under the

assumption of market and firm imperfection, firm diversification is more important because managers have much more discretion and choice. From this perspective, higher relative performance is derived from better strategic fit with external and internal conditions. Under the assumptions of imperfection and managerial motives to diversify, the central motives for diversification include managerial employment risk reduction and increased executive compensation. The governance structures in place to prevent managerial abuse are also imperfect and, under certain conditions, may even induce increased diversification.

According to Miller, Le Breton-Miller and Lester (2010), it is generally believed that a concentrated ownership structure reduces the ability of managers to engage in opportunistic acquisitions, due to the superior monitoring capabilities and influence of large owners. Agency theory states that due to better ability to monitor managers, concentrated ownership discourages investment that rewards managers through compensation and status but penalizes shareholders through increased risk and underperformance. They argued that it is not ownership concentration per se, but rather who the owners are and their priorities and preferences that most influence corporate conduct. Their results show an inverse relationship between family ownership and the number and value of acquisitions and, as family ownership increases, so does the tendency to make diversifying acquisitions.

Depending on the environment managers are operating in, they might put their own interests above the interest of their firms. Hence, without the right governance mechanisms in place to ensure that managers act in the best interest of the firm, diversification is not expected to create much value to the firm. Regarding the value creation or value destroying aspect of diversification for the firm from an agency perspective, it is important that the interests between principals and agents are aligned. If managers are only acting in their own best interests, without taking the strategic fit of the diversification strategy into account, it is highly likely that it rather results in value destruction than in value creation for the firm. If the firm can ensure that the managers are acting in the firm's best interest, it will increase the chances that the chosen diversification strategy will result in value creation for the firm.

Portfolio Theory

The foundation of modern portfolio theory is a portfolio selection theory developed by Harry M. Markowitz in 1952. Markowitz sought to scientifically demonstrate the fundamentals of diversification decisions of investors and, second, he wanted to find out what kind and how many shares are necessary in order to build the optimal portfolio. He was the first one who investigated the positive effect of diversification on the risk and expected return of the collective portfolio (Watson & Head, 2007).

The cornerstone of Markowitz's seminal theory is that investors have the ability to diversify away unsystematic risk by holding portfolios consisting of a number of different assets. Markowitz's starting point is to construct what is known as the envelope curve. This represents the set of portfolio choices available to investors when investing in different combinations of risky assets (Markowitz, 1952).

According to Markowitz (1952) the process of selecting a portfolio can be divided into two stages. The first stage starts off with observation and experience and concludes with beliefs about the future performance of available securities. At the second stage the conclusion from the first stage marks the starting point and the second stage ends with the choice of a portfolio. Furthermore, he showed that the variance of the rate of return was a meaningful measure of portfolio risk.

Overall risk can be separated into systematic and unsystematic risk. Systematic risk is also known as non-diversifiable, non-specific, unavoidable or market risk and it represents the effects on a share's return by systematic factors such as business cycles, government policy and changes in interest rates. Unsystematic risk is also known as diversifiable, specific, avoidable or non-market risk, and is the risk specific to a particular share, for instance, the risk of the individual company to perform badly or go into bankruptcy. An investor can progressively reduce unsystematic risk by spreading investments over a larger number of different securities. It is this opportunity to reduce unsystematic risk through holding a diversified portfolio of shares that is the basis of Markowitz's portfolio theory (Watson & Head, 2007).

While attitudes towards risk may differ, it is expected that investors act rationally and do not expose themselves to higher risk without the possibility of higher returns (Watson & Head, 2007). Even though in general investors' preferences in regard to risk might differ, portfolio theory assumes that investors are basically risk averse, meaning that when they are given a choice between two assets with equal rates of return they will select the one with the lower level of risk (Reilly & Brown, 2003).

Like every theory, portfolio theory is based on a few assumptions. The theory assumes that investors are making their investment decisions based on expected cash flows and with the goal to increase their wealth. Investors collect information and make their decisions based on this information by balancing out the advantages and disadvantages of a possible investment. This implies that investors act rationally and in order to increase their own utility. Another assumption, in order to make the analysis as easy as possible, is that capital markets are efficient (Watson & Head, 2007).

Markowitz (1952) concluded that it is not possible to eliminate all variance by using diversification and that the portfolio with maximum expected return is not necessarily the one with minimum variance. However, since the patterns of returns of single capital investments differ from one another, it is possible to use investments with risks that are negatively correlated to balance each other out. Furthermore, the important factor to consider when adding an investment to a portfolio is not the investment's own variance but its average covariance with all the other investments in the portfolio.

Lubatkin and Chatterje (1994) investigated the linkage between relationships of a firm's unsystematic and systematic risk. Whereas portfolio theory is based on the premise of passive management, that cash flows can be combined but not altered, corporate diversification theory assumes that managers can actively intervene to lower corporate risk in a manner not available to shareholders. Contrary to what modern portfolio theory suggests, and in alliance with corporate diversification theory, their results suggest that firms can best minimize unsystematic risk by diversifying into similar businesses. Furthermore, the highest levels of unsystematic risk were associated with both the least diversified and the most diversified strategies. The lowest level of risk was associated with midrange strategies which implies that there is an optimal level of diversification for firms. Unrelated diversifiers showed high levels of unsystematic risk, in spite of an offsetting portfolio effect; systematic risk has a diversifiable component. Firms that diversify in a constrained manner appear able to realize synergies that other diversification types cannot, and these synergies help to protect the firm from macro-economic uncertainties. Building competitive advantage is best accomplished through a constrained diversification strategy.

Regardless of the basis of classification, both unrelated and related acquisition strategies have been shown to create significant synergies (Seth, 1990). The strategy literature states that firms following related diversification strategies should outperform unrelated diversifiers (Salter

& Weinhold, 1979; Rumelt, 1974). However, this previous literature mainly focuses on firms that either produce goods or offer services. With regard to acquisitions, value creation depends on the combination of characteristics of the two firms, rather than those of each of the firms considered alone. Previous literature on international diversification for risk reduction purposes has focused on diversification decisions for a portfolio of stocks or has analyzed publicly traded companies and the correlation of stock market returns has been the variable of choice. No prior studies have examined how international diversification strategies affect the performance of privately-held companies.

Different Motives for Privately-Held Firms

Management scholars maintain that, for publicly traded companies, risk reduction purposes shouldn't be the primary motivation for diversification or an acquisition. The underlying reasoning is that while the diversification might be able to reduce risk, this might be at the expense of returns. So when financial figures go public at the end of the year, stockholders, who are in general risk neutral, might complain that they could have reduced the risk on their own simply by investing in different stocks or they already might have broadly invested in different types of companies.

The rationale of using diversification to lower earnings volatility is not sufficient, because of the fact that when trying to reduce risk by adding new businesses, managers try to achieve something that shareholders could do more efficiently themselves. In general, stockholders decrease their portfolio risk by owning shares in companies whose returns are less than perfectly positively correlated. Given the fact that the cost of business diversification would be much larger than the costs of adjusting a stock portfolio, it seems obvious that using diversification in order to lower the corporation's financial risk is a poor use of resources (Amihud and Lev, 1981; Lane, Canella and Lubatkin, 1998).

Bringing businesses which are imperfectly correlated together under common ownership also reduces the variance of the combined cash flows. Since shareholders can diversify risk by holding a diversified portfolio, the risk reduction benefits from diversification appeal more to managers than to owners. In theory, a possible advantage for companies would be if they were able to use diversification at lower cost than the individual investor. In reality quite the opposite is true: The transaction costs to companies which diversify through acquisitions are far higher than to shareholders which diversify their portfolios. Moreover, in addition to the costs of using investment banks and legal advisers, they also face costs for an acquisition premium to gain control of an independent company (Grant, 2013).

Taking this into account, it can be said that diversifying for pure risk reduction purposes should be subordinated to trying to improve returns in each business unit, which can only be achieved when the corporation builds strong ventures or develops ventures that strengthen current businesses (Walker, 2009).

According to the capital asset pricing model the risk that is relevant in order to determine the price of a security is not the overall risk (variance) of the security's return but the systematic risk, which is the part of the variance of the return that is correlated with overall market returns. This certain part of the variance is measured by the beta coefficient, which can't be reduced by corporate diversification. If several companies are brought together under common ownership, in the absence of any other changes, the beta coefficient would simply be the weighted average of the companies. Hence, an increase in shareholder value through risk reduction can't be achieved by simply putting different businesses together under common ownership (Brealey, Myers and

Allen, 2006). Most scholars are supportive of this (Levy and Sarnat, 1970; Mason and Goudzwaard, 1976; Weston, Smith and Shrieves, 1972). Moreover, unrelated diversification might even fail to lower unsystematic risk (Lubatkin and Chatterjee, 1994).

Nevertheless, if we are considering the risk of bankruptcy, diversification can help a marginally profitable firm to avoid cyclical fluctuations of returns, which could lead to bankruptcy in the long run. However, this argument holds rather for bondholders and other creditors than for shareholders (Lee, 1977). Moreover, if the firm can realize economies from financing investments internally rather than using external capital markets, the stability in the firm's cash flow that results from diversification may reinforce independence from external capital markets (Grant, 2013).

Taking all of the just mentioned arguments into account, diversification for purely risk reduction purposes is not considered to be rational for the publicly traded firm. However, in the case of a privately held company with no separation of ownership and control and a non diffused ownership structure it might be rational to diversify after all. The argument related to the fact that there is no separation of ownership and control alone is not strong enough to justify the rationality of a risk diversification decision, but it shouldn't be neglected at all.

The Holding Company

The holding company is a financial structure created by a parent company acquiring controlling equity stakes in a number of subsidiary companies. The management structure is built by the parent company appointing the board of directors of the subsidiaries and receiving dividends. Otherwise the management structure is characterized by little integration or managerial control. The holding company structure allows entrepreneurs to control large business empires without the need for either the capital or the management structure an integrated corporation would require (Grant, 2013).

In general, the holding company structure is appropriate when the individual businesses in a corporation's portfolio do not have much in common; hence, the potential for synergies is limited. The organizational form can be described as a variation of the divisional organizational structure - where products, projects, or product markets are grouped internally - in which the divisions have a high degree of autonomy both from other divisions and from corporate headquarters (Dess, Lumpkin, Eisner and McNamara, 2012)

In addition to the already mentioned possible reasons which could motivate firms under different theoretical perspectives to diversify, holding companies are highly likely to have different motivations to diversify. For holding companies, where diversification or acquisitions could be either related or unrelated and there is no coordination mechanisms between the acquisitions, motivation for diversification or acquisitions may result from fundamental analysis and the identification of undervalued companies or assets. In a conglomerate, where diversification or acquisition is unrelated but there is a financial coordination mechanism, a diversification or acquisition motivation may also include the desire to establish internal capital markets (Grant, 2013; Seth, 1990).

In many instances one could argue that for simple risk reduction purposes, the holding company or conglomerate could level out the patterns in ups and downs by buying stock in another country. So instead of acquiring a company in a different country, a simple investment in foreign stock could be a feasible alternative. Moreover, Errunza, Hogan & Mao-Wei Hung (1999) found evidence that in the time period of 1976 to 1993 U.S. investors could effectively mimic foreign market returns with domestically traded securities.

Management scholars maintain that, for publicly traded companies, risk reduction purposes shouldn't be the primary motivation for diversification or an acquisition. However, in the case of privately held holding companies, these reservations do not hold. In comparison to privately held companies, publicly traded companies show a more diffused ownership structure, which means that people of means might already have broadly invested. In theory, the owners of privately held companies of course also have the possibility to reducing the risk by investing broadly. In reality, however, and especially with regards to family owned firms, they often keep all of their eggs in one basket.

Some scholars even argue that it would be indeed possible to achieve the benefits from international diversification for risk reduction purposes without investing abroad. They argue that by investing in national stocks that mimic the volatility of returns of international stocks, the same benefits with regards to lowering risk could be achieved (Errunza, Hogan & Hung, 1999). In theory, this might be a valid option to consider. In practice, however, the capital needed to execute such a large investment might be difficult for some firms to obtain.

METHODOLOGY

The case study reported here involves a privately held holding company that at the time had investments in only one country, Germany. The question addressed was whether a reduction of risk could be demonstrated by analyzing potential portfolios of investments including acquisitions in other countries. Ownership of the holding company was concerned that if problems occurred with the German economy, it would negatively affect its profits. Seven countries were chosen for analysis: Poland, Turkey, the United Kingdom, Sweden, Spain, France, and the Czech Republic. As noted earlier, the holding company exercised little active management over its subsidiaries in terms of resource transfers, instead managing them through financial goals. At the time, the overall performance of the company was good and there were no current profit issues that needed to be solved. The company was interested in adding another country to their current portfolio by taking an international instead of a domestic investment approach in the future.

According to Markowitz's portfolio theory, an investor is able to reduce unsystematic risk by holding shares in his or her portfolio which are not perfectly positively correlated. In the case of this paper all of the company's revenue flows are tied to the German economy, in other words, the level of unsystematic risk connected to the portfolio of companies is fully determined by the German economy. Presently, the subject company consists of seven firms.

With regard to risk reduction being the major concern of the holding company in this paper and according to portfolio theory (Markowitz, 1952) the company is looking to minimize the variance or standard deviation of their portfolio of companies. So the question is *from which country should the holding company add an acquisition to their current portfolio of companies in order to reduce the overall variance of the portfolio?*

Measures

As reviewed above, past research in this area has often focused on corporate diversification of portfolios, whereas this paper focuses on international diversification. This past research has utilized measures of risk from the area of financial theory, namely stocks or stock market indices. In his seminal work about portfolio selection, Markowitz (1952) used the return rates of investments to determine the risk reduction benefits for the investor if those

investments would be combined a portfolio. Since Markowitz's work originated in the field of financial theory, previous work on the risk reduction benefits for the international investor has focused on holding a diversified portfolio of stocks or used stock market indices as a variable to measure the level of correlation between global markets (Bekaert, Hodrick and Zhang, 2009; Serra, 2000; Rowland & Tesar, 2004). However, for a privately held holding company, there is no direct connection to the stock or equity market.

One argument for the choice of an appropriate measure could be that since previous literature (Bekaert, Hodrick and Zhang, 2009; Serra, 2000; Rowland & Tesar, 2004; Goetzmann, Li and Rouwenhorst, 2005; Lee & Hooy, 2013) measured the development of the stock market or equity market by using stock or equity returns, a parallel approach could be to measure the development of an economy by the annual growth or decline in economic value. This supported the idea that the variable used to explore the research question should not be either stock market or equity market returns. However, the connection between the economic situation of a country and the resulting volatility in returns suggested the idea to use an economic measure as the variable for the present study. The aim was to select a variable that reliably represents the development of a country's economy. Therefore, the chosen variable is the annual GDP growth rate. According to the World Bank the GDP growth rate is defined as the

“Annual percentage growth rate of GDP at market prices based on constant local currency. Aggregates are based on constant 2005 U.S. dollars. GDP is the sum of gross value added by all resident producers in the economy plus any product taxes and minus any subsidies not included in the value of the products. It is calculated without making deductions for depreciation of fabricated assets or for depletion and degradation of natural resources” (World Bank, 2015).

Sample

The countries chosen for this study reflected the interests of the holding company in this case study. In order to separate business cycles and possibly economic shocks from long term growth, and, since more recent developments are more important, the time horizon for the analysis in this paper was the 2003-2013 time period, representing one full business cycle. Thus, the final sample consists of the annual GDP growth rates of Germany, Poland, Turkey, United Kingdom, Sweden, Spain, France and the Czech Republic from 2003-2013. The data were obtained from the World Bank national accounts database and the OECD National Accounts data files through the World Bank's development indicators catalogue.

For all of the calculations in this chapter it is assumed that as a first step of international diversification the company would be interested in adding only one other country to its current portfolio. Also, since there is no current specific international investment target, the magnitude of the international investment could not be specified. Therefore, in each pair of countries investigated, both countries were weighted equally in the portfolio.

RESULTS

Markowitz (1952) showed that portfolio risk is meaningfully measured by the variance in returns. The company's current portfolio consists of seven companies, nevertheless, on a country level it only consists of one country. Hence, in the following and as a first step the variance of the current portfolio is calculated by using the GDP growth rates of Germany and the variance formula stated below. Furthermore, following Markowitz (1952), the percentage growth rates

have been converted into decimal numbers for all calculations. A table with the annual GDP growth rates in percent and the decimal numbers can be found in the Appendices.

$$\text{VAR}(x) = s_x^2 = \frac{1}{n} \sum_{i=1}^n (x_i - \bar{x})^2 \quad (1)$$

Where in the case of this paper n denotes the number of years of the chosen time horizon, x_i denotes the country's GDP Growth rate in a certain year and \bar{x} denotes the mean of one country's GDP growth rate across the chosen time horizon. The calculated variance for Germany is 0.0007. As a next step, the variance of the other countries in the sample is first calculated on an individual basis and furthermore on the basis that each country would be in a portfolio with Germany. Table 1 shows the results of these calculations.

Table 1 VARIANCE		
Country	Individual Variance	Average Variance Together with Germany
Germany	0.0007	0.0007
Poland	0.0003	0.0005
Turkey	0.0017	0.0012
United Kingdom	0.0005	0.0006
Sweden	0.0009	0.0008
Spain	0.0007	0.0007
France	0.0002	0.0005
Czech Republic	0.0011	0.0009

Source: Own work, data used for calculations obtained from the World Bank database.

The important factor that needs to be taken into consideration when an investment is added to a portfolio is not just the investment's own variance, but its average covariance with the other investments in the portfolio (Markowitz, 1952; Reilly & Brown, 2003). As a next step the covariance between the German annual growth rates and the annual GDP growth rates of the other countries in the data sample is calculated by using the following formula:

$$\text{COV}(xy) = s_{xy} = \frac{1}{n} \sum_{i=1}^n (x_i - \bar{x}) * (y_i - \bar{y}) \quad (2)$$

where x_i denotes Germany's annual GDP Growth rate in a certain year, \bar{x} denotes the mean of Germany's GDP growth rate across the chosen time horizon, y_i denotes the annual GDP growth rate of the other possible country in the portfolio and \bar{y} denotes the mean of the other country's annual GDP growth rate. Table 2 shows the results of the calculations.

Countries	Covariance
Germany-Germany	0.0007
Germany-Poland	0.0003
Germany-Turkey	0.0009
Germany-United Kingdom	0.0004
Germany-Sweden	0.0007
Germany-Spain	0.0003
Germany-France	0.0004
Germany-Czech Republic	0.0006

Source: Own work, data used for calculations obtained from the World Bank database.

As previously mentioned, the important factor that needs to be considered when adding an investment to a portfolio is not the investment's own variance, but its average covariance with all the other investments in the portfolio (Markowitz, 1952; Reilly & Brown, 2003). Therefore Markowitz (1952) derived a formula that takes both the weighted variance of the single investment in the portfolio and the covariance between the investments into account. By using this formula the standard deviation of returns for a portfolio of assets is computed, which is considered the measure of risk for a portfolio (Markowitz, 1952).

Using Markowitz's formula, as a last and final step the standard deviations for an international portfolio are computed:

$$\sigma_{portfolio} = \sqrt{\sum_{i=1}^n w_i^2 \sigma_i^2 + \sum_{i=1}^n \sum_{\substack{j=1 \\ i \neq j}}^n w_i w_j Cov_{ij}} \quad (3)$$

where $\sigma_{portfolio}$ denotes the standard deviation of the portfolio, w_i denotes the weights of the individual countries in the portfolio, where in the case of the paper the countries are equally weighted, σ_i^2 denotes the variance of annual GDP growth rates for the single countries in the portfolio and Cov_{ij} denotes the covariance between the annual GDP growth rates for Germany and another country in the portfolio. Table 3 shows the results of the calculations.

Countries	Standard Deviation of Portfolio
Germany-Germany	0.0264
Germany-Poland	0.0192
Germany-Turkey	0.0321
Germany-United Kingdom	0.0219
Germany-Sweden	0.0269
Germany-Spain	0.0227
Germany-France	0.0204
Germany-Czech Republic	0.0277

Source: Own work, data used for calculations obtained from the World Bank database.

The results show that the greatest risk reduction benefit would be achieved by adding Poland to the subject company's current portfolio, since it would reduce the standard deviation

of the portfolio from 0.0264 to 0.0192. This means that the standard deviation of the portfolio would decline by 27.27%. This leads to a reduction in the variation of GDP growth rates from their mean value. Since the level of risk has been defined as the volatility in returns, by reducing the volatility, the risk is reduced.

The results also show that adding the United Kingdom, Spain or France to the company's current portfolio would still provide risk reduction benefits, but not to the same degree as adding Poland. The argument for the risk reduction benefit still holds, but with a different magnitude. On the other hand, adding Turkey, Sweden, or the Czech Republic would increase the standard deviation of the portfolio and hence would cause an increase in risk.

DISCUSSION AND CONCLUSIONS

The aim of this paper was to investigate the potential risk reduction benefits of international diversification in the case of a privately held holding company. The research question raised at the beginning of this paper asked whether it would be rational for such a firm to diversify in an international context with regard to risk reduction purposes and, if so, under which circumstances it would create value.

Three different theoretical perspectives on diversification were identified and analyzed with regard to their motives and value creation premises for diversification. In connection to the holding company structure and their primary concern being risk reduction, the justification of the use of portfolio theory for this study has been made. In the case of a privately held holding company and with regard to the chosen theoretical lens in this paper the primary motive for diversification has been identified as leveling out the volatility in returns by diversifying across different industries or across different geographic locations that are less than perfectly positively correlated with each other.

Previous work on international diversification from a portfolio theory perspective, which has been mainly from the perspective of a publicly traded company or an international investor that is seeking to select a diversified portfolio of stocks or bonds for risk reduction purposes, suggests that diversifying into different industries or across different geographical locations which are less than perfectly positively correlated with each other is a useful means in order to reduce the volatility in returns. The argument maintained by many Management and Finance scholars that diversification solely for risk reduction purposes is not considered to be rational for publicly traded firms has been acknowledged and discussed for the case of a privately held company. It has been concluded that the argument does not hold in this case.

Prior research on international diversification suggests that in the case of a privately held holding company which is already diversified on a corporate level, international diversification for risk reduction purposes is considered rational and the value creation premise would be to identify and select a country that shows characteristics that would enable the company to reduce the volatility in returns.

Having identified the motive and value creation premise in the case of a privately held holding company, a quantitative analysis was conducted for a particular firm with seven subsidiaries in Germany in order to identify a potential country that shows those characteristics. Following Harry Markowitz's method for portfolio selection, the economic data of seven countries has been analyzed in terms of their risk reduction benefits when adding one of them to the company's current portfolio. The results of this analysis suggest that the greatest risk reduction benefit in this particular situation and given the countries selected would be provided by adding Poland to the subject firm's current portfolio. Furthermore, adding Spain, France or

the United Kingdom would also provide risk reduction benefits, but to a lesser extent. On the other hand, adding Turkey, Sweden or the Czech Republic, would result in increased risk. Referring back to the research question and with regard to the assumptions and constraints made in this paper, it can be concluded that it would be rational to diversify internationally. The circumstances that need to be given to result in value creation is the identification and selection of a country which, when combined in a portfolio with Germany, would result in a lower volatility in returns and hence reduce the risk.

As for the implementation of the strategy and with regard to the analysis conducted in this paper it is advised to search for potential investment targets internationally. Once a potential target in an appropriate economy has been identified, it is advised to conduct further analyses that go beyond the scope of this paper.

The calculations reported above are based on several assumptions. First, within pairs, countries in the portfolio were weighted equally. In practice it would be highly unlikely to be appropriate, as the weighting should be based on the magnitude of a potential investment and the size of the existing portfolio. Further, since in this study the countries were equally weighted, it magnifies the risk reduction benefit and adjusting the weightings in accordance to the magnitude of the investment would allow a more precise measurement risk reduction benefit. Also, since the magnitude of the investment cannot be taken into account, it is not possible to measure the risk reduction benefit by means of a certain Euro amount or any other currency. Second, a further assumption was made that a ten-year time period was appropriate to explore risk return in this context. The choice of different time horizons may influence the results obtained.

The present study also assumes that Markowitz's (1952) formula can be extended from its original purpose - to calculate the standard deviation of return rates for assets in a portfolio – to the context of international diversification. The connection between the assets in a portfolio and their return rates is direct, where in the case of the economies it is highly unlikely that the growth of the entire economy of a country is also reflected in a certain company in that country.

Another limitation of this paper is the focus solely on the risk reduction benefit from international diversification. Investing in countries with characteristics that result in a decrease in the volatility of returns certainly decreases the risk, but at the same time, it also limits the growth potential. Leveling out the ups and downs in returns makes the future more predictable and hence less risky, but since it limits the bandwidth of the returns, it also limits the growth potential. Future research could focus on a combination of risk level and growth potential of certain economies.

Furthermore the definition of risk in this study also provides a limitation. Risk is defined as the volatility in returns affected by annual economic growth of countries. Future research could focus on other risk factors which might be important to take into account when investing abroad, for instance political risk or legal risk.

Future research might also analyze the effects with regard to risk reduction, if not only one, but more countries are added to the current portfolio. Especially for this purpose it might be advisable to extend the list of pre-selected countries to analyze. Also, this study focused on country level factors; further research could include industry effects as well. In other words, how much of the economic growth or decline of a country's economy originates in which industries.

In conclusion, this study extends the international diversification literature to include the case of the privately-held holding company, provides analysis of value to a particular privately-held holding company in Germany, and provides several opportunities for future research.

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APPENDICES

Appendix 1											
ANNUAL GDP GROWTH RATES (IN %) 2003 – 2013											
Country	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Germany	-0.7	1.2	0.7	3.7	3.3	1.1	-5.6	4.1	3.6	0.4	0.1
Poland	3.6	5.1	3.5	6.2	7.2	3.9	2.6	3.7	4.8	1.8	1.7
Turkey	5.3	9.4	8.4	6.9	4.7	0.7	-4.8	9.2	8.8	2.1	4.1
United Kingdom	4.3	2.5	2.8	3.0	2.6	-0.3	-4.3	1.9	1.6	0.7	1.7
Sweden	2.4	4.3	2.8	4.7	3.4	-0.6	-5.2	6.0	2.7	-0.3	1.5
Spain	3.2	3.2	3.7	4.2	3.8	1.1	-3.6	0	-0.6	-2.1	-1.2
France	0.8	2.8	1.6	2.4	2.4	0.2	-2.9	2.0	2.1	0.3	0.3
Czech Republic	3.6	4.9	6.4	6.9	5.5	2.7	-4.8	2.3	2.0	-0.8	-0.7

Source: World Bank's development indicators catalogue, own illustration

Appendix 2											
ANNUAL GDP GROWTH RATES (IN DECIMAL FORM) 2003 – 2013											
Country	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Germany	-0.007	0.012	0.007	0.037	0.033	0.011	-0.056	0.041	0.036	0.004	0.001
Poland	0.036	0.051	0.035	0.062	0.072	0.039	0.026	0.037	0.048	0.018	0.017
Turkey	0.053	0.094	0.084	0.069	0.047	0.007	-0.048	0.092	0.088	0.021	0.041
United Kingdom	0.043	0.025	0.028	0.030	0.026	-0.003	-0.043	0.019	0.016	0.007	0.017
Sweden	0.024	0.043	0.028	0.047	0.034	-0.006	-0.052	0.060	0.027	-0.003	0.015
Spain	0.032	0.032	0.037	0.042	0.038	0.011	-0.036	0	-0.006	-0.021	-0.012
France	0.008	0.028	0.016	0.024	0.024	0.002	-0.029	0.020	0.021	0.003	0.003
Czech Republic	0.036	0.049	0.064	0.069	0.055	0.027	-0.048	0.023	0.020	-0.008	-0.007

Source: World Bank's development indicators catalogue, own calculation and illustration

THE MODEL OF GRADED SALARY INCREASE A SOLUTION TO THE PROBLEM OF SALARY COMPRESSION AND INVERSION IN FACULTY SALARIES

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ABSTRACT

This study tested a model of graded salary increase (MGSI) as a solution to the problem of salary compression and inversion in faculty salaries. The model ties salary increase rates with tenure of faculty members. Based on the faculty salary data collected by College and University Professional Association for Human Resources (CUPA-HR) between 2005 and 2014, we found that MGSI solves the problem of salary compression and inversion.

Keywords: *equity, salary compression, salary inversion, faculty salaries.*

INTRODUCTION

Equity is an important issue in pay determination. John Adams' Equity Theory (1963) posits that employees constantly compare how much they gain from a job with how much effort, time and experience they input in the job. A perception of over-input and under-payment will lead to negative feelings and such behavioral consequences as reduction of work effort, expression of grievance, making requests for higher pay or simply resigning from the job. A major component of job input is employee's work experience. People with more work experience tend to perform better than those without work experience. Since work experience is largely related to employee's tenure on a job within an organization, it is a common thought that tenure should be compensated. However, rewarding employees' tenure is not easy to practice in spite of its obvious benefits for employee motivation. In reality, senior employees often find themselves getting paid similar to new employees. Moreover in some organizations and occupations, new employees get paid more than senior employees. The former phenomenon is termed as salary compression and the latter is termed as salary inversion.

Various studies reported the problems of salary compression and salary inversion in faculty salaries (e.g. Brown & Woodbury, 1998; Duncan, Krall, Maxcy, & Prus, 2004; Finch, Allen & Weeks, 2010; Jacobs & Herring, III, 1987; Lillydahl & Singell, 1992; Martinello, 2009). Brown & Woodbury (1998) discovered a negative relationship between faculty job tenure and their financial return based on personnel data between 1981 and 1990 at Michigan State University. Data from a national survey to AACSB-accredited business schools showed replacement hires for vacant positions of assistant professors and associate professors require an average salary increase between \$10,000 and \$30,000 (Finch, et al, 2010). The salary compression and inversion problems are usually more serious during the first several years of faculty tenure. Jacobs & Herring, III (1987) found a strong negative relationship between experience and pay for assistant professors but a positive relationship between experience and

Pay for associate professors and full professors. It seems that productivity of professors becomes a more dominant factor in pay determination as professors' academic tenure grows (Jacobs & Herring, III, 1987). Ransom (1993) observed a u-shaped relationship between faculty seniority and their pay. Specifically, pay is negatively related to faculty seniority for new assistant professors and assistant professors. However, the relationship between the two becomes positive for associate and full professors. This u-shaped pattern was also observed by other studies (e.g. Duncan, et. al., 2004; Martinello, 2009).

Faculty salary compression and inversion are believed to result from higher growth rate of entry salaries and lower salary increase rate of long term employees (Gomez-Mejia & Balkin, 1987). Entry salaries are tied to the market rates. Market rates are largely determined by the balance between supply and demand of faculty. Academic disciplines experiencing the biggest imbalance between faculty demand and supply (e.g. business and engineering) usually suffer the most from the salary compression and inversion. On the other hand, salary increases for employed faculty are mostly adjustments of cost of living, which are limited by the annual budgets of the universities. Because of a short supply and a rising demand for faculty and other priorities of annual budgets, entry salaries for faculty grow much faster than salaries of employed faculty (Finch, et. al., 2010; Gomez-Mejia & Balkin, 1987).

As suggested by the Equity theory (Adams, 1963), salary compression and inversion could lead to negative attitudinal and behavioral consequences. It is no exception for faculty members. Previous studies revealed that faculty with compressed pay tend to exert less work effort, pay less attention to work quality, request higher pay, engage in unionization activities, spend more time on profitable work outside the employment (e.g. consulting job), create difficulties in work for more highly paid junior faculty members, demonstrate unwillingness to serve on committees or leave the university for a better paid position in another university or in private industry (Daniels, Shane, & Wall, 1984; Huseman, McHone, Rungeling, 1996).

Various approaches have been created to cope with the problem of salary compression and inversion. Most of them focus on periodical salary adjustment. The amount of salary adjustment is usually determined by one's pay deviance from the national level. Many experts in employee compensation suggest extracting faculty performance level from faculty pay while calculating pay deviance (Duncan, et. al., 2004). Huseman, et al. (1996) presented a model of salary adjustment, which was built on four basic blocks: college-based model, inclusion of national salary standards in calculation, and incorporation of employee performance and tenure. In spite of its wide practice, salary adjustment is obviously an aftermath solution to salary compression and inversion. It requires enormous time and effort to complete the whole administration process periodically. One IOMA's report on salary survey claimed such process could require at least 2 years (IOMA, 2002). For that reason, it is necessary to explore approaches aimed to prevent salary compression/inversion from happening.

When salary compression/inversion occurs, new faculty members are overpaid whereas senior faculty members are underpaid. A general HR practice to cope with the overpaying and underpaying issues is to reduce the salary increase rate of those who are overpaid and improve the salary increase rate of those who are underpaid (Dessler, 2012; IOMA, 2008). Along the same line of this thought, applying lower rates of salary increase to junior faculty members and higher rates of salary increase to senior faculty members will likely solve the problem of salary compression/inversion. This paper proposes a model of graded salary increase (MGSI), which is aimed to tie salary increase rates with tenure of faculty members. As previous section mentions, faculty salary compression and inversion most likely occur during the first several years of

employment and among assistant professors (Duncan, et. al., 2004; Martinello, 2009; Ransom, 1993). Since the standard period for an assistant professor to be promoted to associate professor is 6 years, the proposed model merely covers the first six years of employment, which includes five processes of salary increase.

The Model of Graded Salary Increase

Traditionally, employees' salaries increase by following the following formula:

$$\text{Salary} = (1 + \text{Salary Increase Rate}) * \text{Salary of the Previous Year}$$

Unlike traditional model of salary increase, the Model of Graded Salary Increase ties salary increase rate to employees' tenure. To achieve this goal, tenure-based constants can be used for creation of graded salary increase rates. The median point of 5 years of salary increase is the third year (which is the fourth year of the employment). By assigning constant "1" to the median point, constants for salary increase rates from Year 1 to Year 5 should be 0, 0.5, 1, 1.5 and 2. Here is the mathematic formula for this model:

$$\text{Salary} = (1 + \text{Salary Increase Rate} * \text{Tenure Constant}) * \text{Salary of the Previous Year}$$

The model proposed in this paper focuses on tenure only. Other factors such as performance level can be built into the model by creating an overall product of the constants of different factors, such as tenure and performance level.

METHODOLOGY

Data

The salary data are gathered from the annual executive reports of "Faculty in Higher Education Salary Survey" by College and University Professional Association for Human Resources (CUPA-HR) from 2005 to 2014 (CUPA-HR, 2014). The average annual salaries of full professor, associate professor, assistant professor and new assistant professor are reported in the following disciplines:

1. Agriculture, Agriculture Operations, and Related Sciences
2. Natural Resources and Conservation
3. Architecture and Related Services
4. Area, Ethnic, Cultural, Gender and Group Studies
5. Communication, Journalism and Related Programs
6. Communications Technologies/Technicians and Support Services
7. Computer and Information Sciences and Support Services
8. Education
9. Engineering
10. Engineering Technologies and Engineering Related Fields
11. Foreign Languages, Literatures, and Linguistics
12. Family and Consumer Sciences/Human Sciences
13. Legal Professions and Studies
14. English Language and Literature/Letters
15. Liberal Arts and Sciences, General Studies and Humanities

16. Library Sciences
17. Biological and Biomedical Sciences
18. Mathematics and Statistics
19. Multi/Interdisciplinary studies
20. Parks, Recreation, Leisure and Fitness Studies
21. Philosophy and Religious Studies
22. Theology and Religious Vocations
23. Physical Sciences
24. Psychology
25. Homeland Security, Law Enforcement, Firefighting and Related Protc Servs
26. Public Administration and Social Service Professions
27. Social Science
28. Visual and Performing Arts
29. Health Professions and Related Programs
30. Business, Management, Marketing, and Related Support Services
31. History General

Statistical Methods

ANOVA tests will be used to compare the means of the salaries of new assistant professors with those of full professors, associate professors and assistant professors in each year from 2005-2014. If the means of the salaries of new assistant professors are not significantly different from those of professors of other ranks, then salary compression exists.

To demonstrate how the Model of Graded Salary Increase solves the problem of salary compression and inversion, two steps will be taken. First, the salaries of new assistant professors hired in different years from 2005 to 2013 will be calculated for each of the years following their employment. Two formulas will be used for calculation: one follows the Model of Graded Salary Increase and the other one follows the traditional model of straight forward salary increase. 2.36%, the average of the median salary increase rates for assistant professors from the year 2006 to 2014 (CUPA-HR, 2015), will be used for calculation as the salary increase rate for those years. Appendix A is an example of calculation of salary increases using two methods with the salary data of assistant professors in the area of agriculture/agricultural operations/the related sciences. Second, salaries of assistant professors in their last year of the tenure track (6th year) will be compared to salaries of junior assistant professors in the same year. The model of graded salary increase is effective if senior assistant professors have higher salaries than junior assistant professors by the end of their tenure track. Independent-samples t test will be used to test the mean differences of salaries of assistant professors in their 6th year and the salaries of assistant Professors in their 1st, 2nd, 3rd, 4th, and 5th year.

RESULTS

The ANOVA tests of mean salaries of professors of different ranks showed that the mean salaries of new assistant professors in 31 disciplines are significantly lower than those of full professors and those of associate professors (See Table 1). The mean salaries of new assistant professors are not significantly different from those of assistant professors in all nine years (2005-2014). This result demonstrated existence of salary compression among assistant professors. In six of the nine years, the entry salaries of new assistant professors are higher than the average salaries of assistant professors, which implied existence of salary inversion during the years in study.

Table 1			
MEAN DIFFERENCES BETWEEN NEW ASSISTANT PROFESSOR (NASTP) AND ASSISTANT PROFESSOR (ASTP), ASSOCIATE PROFESSOR (ASOP) AND FULL PROFESSOR (FP).			
Year	Mean Differences NASTP – ASTP	Mean Differences NASTP – ASOP	Mean Differences NASTP – FP
2005-2006	-\$286	-\$10,058**	-\$27,492**
2006-2007	\$160	-\$9,916**	-\$27,955**
2007-2008	-\$456	-\$11,297**	-\$30,392**
2008-2009	-\$379	-\$11,463**	-\$31,599**
2009-2010	\$438	-\$10,462**	-\$30,555**
2010-2011	\$667	-\$11,094**	-\$31,673**
2011-2012	\$1,100	-\$10,041**	-\$30,716**
2012-2013	\$717	-\$10,023**	-\$30,692**
2013-2014	\$759	-\$10,130*	-\$31,551**

Note: * p<.05; ** p<.01

Table 2 & 3 display the first six years' salaries of new assistant professors hired in different years from 2005 to 2013. Table 2 displays the results obtained through calculations following the traditional model. Table 3 displays the results obtained through calculations following the Model of Graded Salary Increase. The results of the independent-samples t tests showed that the mean difference of the salaries of assistant professors in their 6th year and those of assistant professors in their 1st, 2nd, 3rd, 4th, and 5th year under the traditional model was -\$622.25 ($t=-.92$, $p>.05$); the mean difference of the salaries calculated following the Model of Graded Salary Increase was \$773.80 ($t=1.12$, $p>.05$) (See Table 4). Although not statistically significant, the results indicated that under the traditional model, salaries of senior assistant professors could not catch up to the salaries of junior assistant professors by the end of their tenure track; under the Model of Graded of Salary Increase, salaries of senior assistant professors did catch up and surpass the salaries of junior assistant professors by the end of their tenure track.

Table 2
ANNUAL MEAN SALARIES OF NEW ASSISTANT PROFESSORS (NASTP) HIRED IN YEAR 2005, 2006, 2007, 2008, 2009, 2010, 2011, 2012 AND 2013 CALCULATED BY FOLLOWING THE TRADITIONAL MODEL OF SALARY INCREASE.

Year	NASTPs Hired in 2005	NASTPs Hired in 2006	NASTPs Hired in 2007	NASTPs Hired in 2008	NASTPs Hired in 2009	NASTPs Hired in 2010	NASTPs Hired in 2011	NASTPs Hired in 2012	NASTPs Hired in 2013
2005	Y1 \$52,209								
2006	Y2 \$53,441	Y1 \$54,278							
2007	Y3 \$54,702	Y2 \$55,559	Y1 \$55,909						
2008	Y4 \$55,993	Y3 \$56,870	Y2 \$57,229	Y1 \$57,969					
2009	Y5 \$57,314	Y4 \$58,212	Y3 \$58,580	Y2 \$59,337	Y1 \$59,325				
2010	Y6 \$58,667	Y5 \$59,586	Y4 \$59,963	Y3 \$60,737	Y2 \$60,725	Y1 \$60,049			
2011		Y6 \$60,992	Y5 \$61,378	Y4 \$62,170	Y3 \$62,158	Y2 \$61,466	Y1 \$61,721		
2012			Y6 \$62,827	Y5 \$63,637	Y4 \$63,625	Y3 \$62,917	Y2 \$63,178	Y1 \$63,311	
2013				Y6 \$65,139	Y5 \$65,127	Y4 \$64,401	Y3 \$64,669	Y2 \$64,805	Y1 \$64,944

Table 3
ANNUAL MEAN SALARIES OF NEW ASSISTANT PROFESSORS (NASTP) HIRED IN YEAR 2005, 2006, 2007, 2008, 2009, 2010, 2011, 2012 AND 2013 CALCULATED BY FOLLOWING THE MODEL OF GRADED SALARY INCREASE.

Year	NASTPs Hired in 2005	NASTPs Hired in 2006	NASTPs Hired in 2007	NASTPs Hired in 2008	NASTPs Hired in 2009	NASTPs Hired in 2010	NASTPs Hired in 2011	NASTPs Hired in 2012	NASTPs Hired in 2013
2005	Y1 \$52,209								
2006	Y2 \$52,209	Y1 \$54,278							
2007	Y3 \$52,825	Y2 \$54,278	Y1 \$55,909						
2008	Y4 \$54,072	Y3 \$54,919	Y2 \$55,909	Y1 \$57,969					
2009	Y5 \$55,986	Y4 \$56,215	Y3 \$56,569	Y2 \$57,969	Y1 \$59,325				
2010	Y6 \$58,629	Y5 \$58,205	Y4 \$57,904	Y3 \$58,653	Y2 \$59,325	Y1 \$60,049			
2011		Y6 \$60,952	Y5 \$59,954	Y4 \$60,037	Y3 \$60,025	Y2 \$60,049	Y1 \$61,721		
2012			Y6 \$62,784	Y5 \$62,162	Y4 \$61,442	Y3 \$60,758	Y2 \$61,721	Y1 \$63,311	
2013				Y6 \$65,096	Y5 \$63,617	Y4 \$62,192	Y3 \$62,449	Y2 \$63,311	Y1 \$64,944

Year	Salaries Calculated Based on the Traditional Model of Salary Increase				Salaries Calculated Based on the Graded Model of Salary Increase			
2010	AP (6 th Y)	\$58,667	AP (5 th Y)	\$59,586	AP (6 th Y)	\$58,629	AP (5 th Y)	\$58,205
		\$58,667	AP (4 th Y)	\$59,963		\$58,629	AP (4 th Y)	\$57,904
		\$58,667	AP (3 rd Y)	\$60,737		\$58,629	AP (3 rd Y)	\$58,653
		\$58,667	AP (2 nd Y)	\$60,725		\$58,629	AP (2 nd Y)	\$59,325
		\$58,667	AP (1 st Y)	\$60,049		\$58,629	AP (1 st Y)	\$60,049
2011	AP (6 th Y)	\$60,992	AP (5 th Y)	\$61,378	AP (6 th Y)	\$60,952	AP (5 th Y)	\$59,954
		\$60,992	AP (4 th Y)	\$62,173		\$60,952	AP (4 th Y)	\$60,037
		\$60,992	AP (3 rd Y)	\$62,158		\$60,952	AP (3 rd Y)	\$60,025
		\$60,992	AP (2 nd Y)	\$61,466		\$60,952	AP (2 nd Y)	\$60,049
		\$60,992	AP (1 st Y)	\$61,721		\$60,952	AP (1 st Y)	\$61,721
2012	AP (6 th Y)	\$62,827	AP (5 th Y)	\$63,637	AP (6 th Y)	\$62,784	AP (5 th Y)	\$62,162
		\$62,827	AP (4 th Y)	\$63,625		\$62,784	AP (4 th Y)	\$61,442
		\$62,827	AP (3 rd Y)	\$62,917		\$62,784	AP (3 rd Y)	\$60,758
		\$62,827	AP (2 nd Y)	\$63,178		\$62,784	AP (2 nd Y)	\$61,721
		\$62,827	AP (1 st Y)	\$63,311		\$62,784	AP (1 st Y)	\$63,311
2013	AP (6 th Y)	\$65,139	AP (5 th Y)	\$65,127	AP (6 th Y)	\$65,096	AP (5 th Y)	\$63,617
		\$65,139	AP (4 th Y)	\$64,401		\$65,096	AP (4 th Y)	\$62,192
		\$65,139	AP (3 rd Y)	\$64,669		\$65,096	AP (3 rd Y)	\$62,449
		\$65,139	AP (2 nd Y)	\$64,805		\$65,096	AP (2 nd Y)	\$63,311
		\$65,139	AP (1 st Y)	\$64,944		\$65,096	AP (1 st Y)	\$64,944
Independent – Samples T Test	Mean Difference= -\$622.25 t= -.92 df=38 Sig. (2-tailed)=.36				Mean Difference=\$773.80 t=1.12 df=38 Sig.(2-tailed)=.27			

Note: AP=Assistant Professor; Y = Year

For an exploratory purpose, we compared the total amount of salaries paid to an assistant professor in the full tenure track under the traditional model of salary increase versus the Model of Graded Salary Increase. The results showed that universities could save over \$6,000 in one assistant professor's salary in 6 years of tenure track under the Model of Graded Salary Increase in comparison to the amount under the traditional model of salary increase. (See Table 5).

Year	Pay Difference Using TSIM versus MGS New Assistant Professors Hired in 2005	Pay Difference Using TSIM versus MGS New Assistant Professors Hired in 2006	Pay Difference Using TSIM versus MGS New Assistant Professors Hired in 2007	Pay Difference Using TSIM versus MGS New Assistant Professors Hired in 2008
2005-2006	1 st Year: \$0			
2006-2007	2 nd Year: \$1,232	1 st Year: \$0		
2007-2008	3 rd Year: \$1,877	2 nd Year: \$1,281	1 st Year: \$0	
2008-2009	4 th Year: \$1,921	3 rd Year: \$1,951	2 nd Year: \$1,320	1 st Year: \$0
2009-2010	5 th Year: \$1,328	4 th Year: \$1,997	3 rd Year: \$2,011	2 nd Year: \$1,368
2010-2011	6 th Year: \$38	5 th Year: \$1,381	4 th Year: \$2,059	3 rd Year: \$1,684
2011-2012		6 th Year: \$40	5 th Year: \$1,424	4 th Year: \$2,133
2012-2013			6 th Year: \$43	5 th Year: \$1,475
2013-2014				6 th Year: \$43
Total	\$6,396	\$6,650	\$6,857	\$6,703

DISCUSSION

This paper tested the Model of Graded of Salary Increase as a possible solution to the problem of salary compression and inversion. Faculty salary data collected by the CUPA-HR in the years from 2005 to 2014 were used to test the model in comparison to the traditional straight salary increase model. The results showed that the proposed model overall solved the problems of salary compression and salary inversion. One condition, however, must be met for this model to work: a consistent salary increase rate over the years. This model is aimed to reward assistant professors' tenure by putting increasing weight on the salary increase rate toward the end of their tenure track. If the salary increase rates fluctuate downward, then increasing weight of salary increase rates will be evened out. In order to maintain a consistent salary increase rate over the years, a university needs to create a reserve fund for salary. In years of high salary budget, the university should put aside certain amount in the reserve fund so as to maintain a consistent salary increase rate in years of low salary budget.

Our test results also showed that the proposed model considerably lower the total amount of salary the university pays to an assistant professor in 6 years of tenure track. The amount saved can be used to reward professors based on their performance level independent of their tenure. As we mentioned earlier, this proposed model only focuses on the tenure factor. However, performance factor can be incorporate in the model too. In addition to constants for tenure, other constants can be created to reflect different levels of performance. Assistant professors' salaries can be determined by both tenure and performance level by following the formula below:

$$\text{Salary} = \text{Previous Year's Salary} * (1 + \text{Average Salary Increase Rate} * \text{Tenure Constant} * \text{Performance Constant}).$$

One more merit for the graded salary increase model proposed by this paper is that it is easy to administer, which wins over the contest against aftermath salary adjustment.

Salary compression and salary inversion are serious compensation problems. It is closely related employees' motivation and turnover intent. Our proposed model appeared to solve both problems from the mathematical perspective. The next step is to test the model in a real work setting on its practicality.

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APPENDIX A

An Example of Calculation of Salary Increases

Using the Traditional Salary Increase Model and the Graded Salary Increase Model

I. The Model of the Traditional Salary Increases

1st Year: The mean salary of new assistant professors in Agriculture/Agriculture Operations/Related Science in 2005: \$55,911 (CUPA-HR Faculty Salary Survey)

2nd Year: The mean salary of the professors in 2006: $\$55,911 * (1+2.36\%) = \$57,231$

3rd Year: The mean salary of the professors in 2007: $\$57,231 * (1+2.36\%) = \$58,582$

4th Year: The mean salary of the professors in 2008: $\$58,582 * (1+2.36\%) = \$59,965$

5th Year: The mean salary of the professors in 2009: $\$59,965 * (1+2.36\%) = \$61,380$

6th Year: The mean salary of the professors in 2010: $\$61,380 * (1+2.36\%) = \$62,829$

II. The Model of the Graded Salary Increases

1st Year: The mean salary of new professors in Agriculture/Agriculture Operations/Related Science in 2005: \$55,911

2nd Year: The mean salary of the professors in 2006: $\$55,911 * (1+2.36\%*0) = \$55,911$

3rd Year: The mean salary of the professors in 2007: $\$55,911 * (1+2.36\%*.5) = \$56,571$

4th Year: The mean salary of the professors in 2008: $\$56,571 * (1+2.36\%*1) = \$57,906$

5th Year: The mean salary of those professors in 2009: $\$57,906 * (1+2.36\%*1.5) = \$59,956$

6th Year: The mean salary of those professors in 2010: $\$59,956 * (1+2.36\%*2) = \$62,786$

WALMART-BHARTI JOINT VENTURE: FORMATION, BREAKUP, & STRATEGIES

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ABSTRACT

This case study article discusses the following subjects as they relate to the formation and breakup of Bharti-Walmart joint venture in India: (a) The Indian legal, economic, and social environment (b) Formation of Bharti Walmart joint venture, (c) Breakup of Bharti Walmart Joint Venture, (d) Walmart's contributions, (e) Walmart's criticisms, (f) Walmart's strategies after joint venture breakup, and (g) India's foreign direct investment strategy in retailing. The article also proposes several hypotheses for future research.

Keywords: *Bharti-Walmart joint venture formation and terms; Bharti-Walmart joint venture breakup and reasons; Walmart's contributions; Walmart's criticism; India's foreign direct investment laws; Walmart strategies in India; and suggestions for India's foreign direct investment policy.*

INTRODUCTION AND PURPOSE

The Bharti Enterprises of India, a premier business conglomerate in India, and Walmart of U.S.A., the largest retailer in the world, made a historic partnership agreement to operate wholesale cash and carry stores in India. The joint venture, however, lasted only for a few years before they cancelled it.

The objectives of this case study article are to discuss the following topics:

1. The Indian legal, economic, and social environment related to this joint venture
2. Formation of Bharti Walmart joint venture
3. Breakup of Bharti Walmart Joint Venture,
4. Walmart's contributions,
5. Walmart's criticisms
6. Walmart's strategies after joint venture breakup
7. India's foreign direct investment strategy in retailing

An important related objective of this research is to propose—based on the multitude of facts and data used in this article—several hypotheses which have been presented in this article for future research.

INDIAN LEGAL, ECONOMIC AND SOCIAL ENVIRONMENT

Indian Economy and Society

India, with its more than 1.2 billion people, is the largest democracy and the second most populous country in the world. However, it is also one of the poorest nations on this planet. According to the World Bank, India, with its 2013 per capita nominal gross domestic product (GDP) of \$1,499, ranked #148 in the world. According to the same source, here is how some other countries stood in terms of their per capita nominal GDP and ranking in the world: Monaco with \$163,026 ranked #1; U.S. with \$53,143 ranked #13; China with \$6,807 ranked #84;

Thailand with \$5,779 ranked #93; Bhutan with \$2,498 ranked #132; and Pakistan with \$1,299 ranked #152. (Wikipedia contributors. "List of countries by GDP (nominal) per capita." Wikipedia, The Free Encyclopedia.)

India had an estimated unemployment rate of 8% in 2013. The corresponding numbers for China were 4.1% (December 2013); for Pakistan, 6.6 % (2014), for Thailand, 0.9% (May 2014), and for U.S., 5.6% (December 2014). (Wikipedia contributors. "List of countries by unemployment rate." Wikipedia, The Free Encyclopedia.)

The cumulative value of foreign direct investment (FDI) received by India as of December 31, 2013 stood at \$310 million; with a world rank of 20. The corresponding figures for the U.S. were \$2,815 million (#1); China \$1,344 million (#4), Thailand, \$193.7 million (#29); and Pakistan, \$22.73 million (#68). The world has a whole received a total of \$16,360 million in FDI. (Wikipedia contributors. "List of countries by received FDI." Wikipedia, The Free Encyclopedia.)

India had a current account trade deficit of \$91.47 billion in 2012; it ranked 190 in the world. The corresponding numbers for U.S. were \$440 billion in 2012 (# 192). On the other hand, China had a current account surplus of \$213.8 billion (#1); Pakistan had a current account surplus of \$0.268 billion, and Thailand had a current account surplus of \$11.9 billion (#25). (Wikipedia contributors. "List of sovereign states by current account balance." Wikipedia, The Free Encyclopedia.)

A number of Indians are highly educated; a number of them live in the U.S. and other countries, a number of them regularly travel abroad, and a number of them are millionaires and billionaires. All the same, however, Indians cannot forget that their country was invaded and ruled by the British for about 200 years; and that it was repeatedly invaded and ruled by the Arabs for hundreds of more years before the British.

Based on these data and information, the following hypothesis is presented:

H1 India is way behind countries such as China to attract much needed foreign direct investment to help grow its "overall economy" due to its laws, bureaucracy, and corruption.

The State of Retailing Industry in India

India's retailing industry mainly consists of small, sometimes very small, shops owned and operated by their owners and their family members. They include the grocery stores, kirana stores, vegetable and fruit stands, paan shops, convenience stores, hand carts, street vendors, and the like.

In the case of vegetables and fruits, shoppers often have a chance to touch and feel the products. They can also examine various types of grains, nuts, and spices. If the shopkeepers know you, you can also take the items such as fabrics home for family approval. Bargaining for prices is a norm; although some stores follow the fixed prices policy. Packaged products are legally required to display their maximum price. Once purchased, the items are non-returnable, especially the perishable items. Since a large part of the shopping is for essential items, returning items is an exception rather than a rule. Most purchases are small in value and paid for in cash.

Each shop generally specializes in selling a limited number of related items. The shopper has to go to different shops to purchase different categories of household items. Often items lack information about their origin, maker, ingredients, and composition. Using technology is almost absent. Overall, the unorganized small shop retailing industry lack the convenience, quality, and cost-advantage that organized large scale retail industry can offer the shoppers.

There are several middlemen between the farmers, producers, and retailers. Each intermediary in the chain adds its own costs of doing business to the produce and the product before they reach the retailer and finally to the consumer. According to some estimates, small Indian farmers and manufacturers get only about one-third of what the consumers pay. Intermediaries keep the two-thirds. The small shops also cannot take advantage of large scale buying from wholesalers.

A good portion of all kinds of perishable items is regularly spoiled due to poor or non-existent cold storage facilities at different stages between the farmers and the consumers.

India's retail and logistics industry employs about 40 million Indians, 3.3% of Indian population. (Wikipedia contributors. "Retailing in India." Wikipedia, The Free Encyclopedia.)

Based on these data and information, the following hypothesis is presented:

H2 On the one hand, India's retail industry is very positive for keeping and creating millions of jobs in this industry. On the other hand, however, it is very negative for its millions of customers in the matters of cost, convenience, health, and safety.

India's FDI Retailing Laws

The above facts show that, on the one hand, India is one of the poorest countries in the world and it can clearly use billions of dollars in FDI in its retail industry year after year for its economic growth. On the other hand, however, it is also difficult for India to place a blind trust in its foreign partners. As such, India wants to receive those investments in a way that is generally satisfactory to its various stakeholders who often have divergent or opposing views. It is a very difficult task to accomplish to say the least. Its laws related to the FDI in retail industry such as those narrated below are a result of these multidimensional backgrounds and views.

India has separate laws for FDI in single-brand stores and multi-brand stores. It allows 100% foreign ownership in single brand retail stores such as Nike and IKEA. However, with 51% or more ownership in such stores, the foreign investor has to source 30% or more of their goods locally from small and medium size firms. (Government of India, "FDI Policy in Multi Brand Retail," 28 November 2011.)

Beginning September 2012, Indian laws also allow foreign companies to own up to 51% of multi-brand retail stores, such as Walmart. These foreign investments are also subject to sourcing 30% of their requirements from local small and medium size firms (Government of India, "FDI Policy in Multi Brand Retail," 28 November 2011.)

Indian laws permit 100% foreign ownership in wholesale businesses. Such whole sellers, however, can only sell to retailers, not to the general public. (Government of India, "FDI Policy in Multi Brand Retail," 28 November 2011.)

FDI should be of \$100 million or more spread over a three year period. Half of this should be invested in the back-end infrastructure, and the other half in the front-end operations. (Government of India, "FDI Policy in Multi Brand Retail," 28 November 2011.)

India's FDI Retailing Laws: Central vs State Governments

The FDI laws have been enacted by India's central government. However, it is up to its individual states to decide where FDI in wholesale or retail industry should be located. This is further limited by the requirement that the city in which FDIs can be located should have a

population of a million or more. (Government of India, "FDI Policy in Multi Brand Retail," 28 November 2011.)

Arvind Kejriwal, whose Aam Aadmi Party came to power in the State of Delhi in December 2013, told the central government that while it is not closed to FDI in other sectors, it cannot permit foreign multi-brand supermarkets to operate in the State because doing so would wipe out thousands of small shop owners and neighbourhood stores (Ghosh, 2014). The Aam Aadmi Party thus rescinded the earlier permission that was given by the Congress Party in power at the time, for allowing FDI to establish such retail stores in Delhi.

Similarly, the new Bhartiya Janata Party government, which came back to power in December 2013 in the State of Rajasthan, told the central government that it will not allow FDI in multi-brand retail industry in Rajasthan because of its adverse consequences for the state's various stakeholders. The FDI permission was earlier given by the state government then led by the Congress Party. (Mathew, 2014.)

The central Commerce Minister Anand Sharma expressed his frustration telling reporters that states which had given their nod to the new FDI policy could not throw it out of the window. We are not a banana republic, he said (Ghosh 2014). Such reversals have raised alarms both in India and abroad. The central government is seeking expert legal advice whether a once opted-in state could opt-out.

Based on these data and information, the following hypothesis is presented:

H3 Indian federal and state laws as they relate to the FDI in retail industry in India significantly discourage such investments.

FORMATION OF BHARTI-WALMART JOINT VENTURE

Walmart and Bharti Enterprises: An Introduction

Walmart is a mega retailer with headquarters in Arkansas, U.S.A., was established in 1962. On January 31, 2015, Walmart had 4,516 stores in the U.S., 647 Sam's Club, and 6,290 stores internationally; making a total of 11,453 units worldwide. (Walmart website, "Walmart Corporate Locations," 2015) It has 20 wholesale stores in India, which operate under the brand name Best Modern Price Wholesale. (Walmart website, Walmart India, 2015). It had net sales of more than \$473 billion in its fiscal year 2014.

Bharti Enterprises, an Indian conglomerate headquartered in New Delhi, was founded in 1976. It had revenues of US\$ 16.5 billion in 2014. It had 30,000 employees in 2010. Its subsidiaries include Bharti Airtel, Bharti AXA General Insurance, Bharti Realty, Bharti Retail, and Field Fresh Foods, among others. It presently has 220 retail stores operating under the Easyday name in various states of India. (Wikipedia contributors "Bharti Enterprises," Wikipedia, The Free Encyclopedia.)

India's Growing Retail Industry

According to the Investment Commission of India, the Indian retail sector is expected to grow almost three times its current levels to \$660 billion by 2015 (Muthukumar and Subasri 2014-2015). According to another projection, cash-and-carry business is expected to grow to about \$22 billion business in India by 2017 (Baily, 2013). Similarly, a study by McKinsey &

Company shows that India will climb from its position as the twelfth-largest consumer market in the world today, to the world's fifth-largest consumer market by 2025 (Ablett, et al., 2007).

Then there is the problem of lost opportunity. The retail industry in India is flooding with some major name national and international competitors. These include Marks & Spencer, Reliance Industries, the Tata Group, the RPG Group, the Aditya Birla Group, TESCO, Carrefour, Pantaloons, Mahindra Retail, and more. It is to Walmart's advantage to get into the Indian retail game sooner than later. It could not afford to miss the opportunity. If other competitors can live and deal with India's laws and labor, Walmart can do it too.

Joint Venture Agreement

In spite of all the legal restrictions and uncertainties at the central and state levels mentioned above, Walmart saw a huge growth potential in India as mentioned above. It, therefore, signed an agreement with Bharti Enterprises on November 27, 2006 to establish a 50-50 joint venture to do wholesale business there. The partnership called Bharti Walmart Private Ltd, would operate stores called Best Price Modern Wholesale.

Both parties brought their own strengths to the joint venture. Walmart came with its financial strength and support, its globally recognized brand name, and its expertise in national and international retail management. It is also known for its expertise in just-in-time inventory management, retail information management, and retail transportation management.

Bharti Enterprises brought to the table its familiarity with the Indian laws, culture, economy, and labor. It is also involved in agribusiness, food processing, retailing, insurance, and telecom industries nationally and internationally.

Walmart also did not want to go alone in India with all its challenges and uncertainties. Even in Germany, a west European country, it had to incur heavy losses before withdrawing from there entirely.

Joint Venture Terms

The historic joint venture included the following terms.

Walmart invested \$103 million in the venture (Rana, 2014.)

The retail shops will be owned by Bharti Enterprises under the Wal-Mart franchise. Bharti is expected to pay royalty for the cash and carry operations. It is also expected to pay various kinds of fees to Walmart such as, franchises fee, software license fee, administrative support fee, design fee, technical training fee, and documentation fee (The Economic Times, 2007).

Walmart would manage Bharti's multi brand retail convenience stores and supermarkets called EasyDay. It was believed that this arrangement would help Walmart to introduce its own brand in India later on. (Banjo, Shelly and R. Jai Krishna, 2013).

The whole sale cash and carry partnership would sell a variety of products ranging from grocery to apparel and consumer electronics to retailers, offices, and organizations.

Since the Indian laws allow FDI in retail industry only in cities with a population of a million or more, it is not easy to find suitable real estate in these large urban areas. The partnership, therefore, planned to establish relatively small size stores compared to their larger counterparts in other countries.

Based on these data and information, the following hypothesis is presented:

H4 The Indian economy, in spite of its federal and state laws which are not friendly to FDI in retail industry, is large and growing enough to attract some FDI in this industry.

BREAKUP OF BHARTI-WALMART JOINT VENTURE

A successful functioning of a joint venture requires that the partners clearly define its goals, clearly spell out their respective responsibilities to accomplish these goals, and carry out those responsibilities. A joint venture's success or failure depends not only upon the partners accomplishing these goals and carrying out these responsibilities, but also on the socio-economic and political variables beyond their control.

So when on October 9, 2012 the Walmart and Bharti announced the breakup of their dream team and decided to go separate ways in both retail and wholesale ventures, people wondered why? There are several reasons behind this widely celebrated Indo-American partnership.

Corruption and Politics

Some primary reasons for the low and slow flow of FDI in India are the Indian legal and political factors. Indian laws are considered unclear and uncertain; and their implementation is routinely marred by bureaucracy, hurdles, delays, corruption, and grafts. It is not uncommon to be first charged for taking a bribe and then let go by giving another bribe. An editorial in the *The Economic Times* said it like this: "No company can operate without greasing a palm here or shelling out unaccounted amounts there." (ETRetail.com., 2013).

In September 2012, the Congress Party led Indian government stated that it would allow foreign supermarket chains to take majority ownership in multi-brand retailing in India. The current BJP led government, however, opposes it. It, however, would not cancel such applications already approved. However, no global supermarket chain has been rushing to apply.

Sourcing Requirement Laws

The requirement that those interested in making FDI in India's wholesale or multi-brand retail industry should source at least 30% of their products from local small and medium size industries is problematic for them. While this condition may be met in sourcing textiles and handicrafts items, it may not be easy to comply with it in sourcing some other products such as electronics.

Scott Price, Wal-Mart's chief executive called it as "critical stumbling block" to establish its consumer stores in India. He also said that these small and medium size companies don't have the ability to meet the large scale requirements of large retailer. He also said that because the Indian retailers are not bound by this condition, it makes it an uneven playing field (Harris, 2013).

Foreign investors also find the requirement to invest 50% of the FDI in back-end infrastructure difficult.

Bharatiya Janata Party (BJP) leader Rajnath Singh is opposed to FDI in retail because multinational companies like Walmart are buying 80 per cent of their goods from countries like China. "India will become a dumping ground for Chinese goods." (Mookerji, 2012)

However, Rajan Bharti Mittal, vice- chairman and managing director of Bharti Enterprises, said that the Bharti-Walmart venture plans to source 90 to 95 per cent of the

products locally. The only foreign stuff that could be sold at Walmart India would include some toys, appliances, olive oil etc. As for food items, around 98 per cent of the total is likely to be sourced from India. (Mookerji, 2012).

Questionable Investment in Cedar Support Services

In March 2010, Walmart invested \$100 million in compulsory convertible debentures of Cedar Support Services (CSS). The CSS is both the parent company of Bharti Retail and the operator of the latter's front-end retail stores. These compulsory convertible (into equity) debentures in effect amounted to Bharti Retail ceding its control and management to Walmart. However, Indian laws don't permit FDI in front-end retail (multi-brand) stores.

In September 2012, P. Achuthan, a CPI (Communist Party of India) member of Rajya Sabha (India's upper house of parliament) asked the government of India about the legality of this Walmart investment. The Enforcement Directorate for alleged FEMA (Foreign Exchange Management Act) violations is investigating the issue. (Hindustan Times. "Wal-mart, Bharti deal: diary of a troubled marriage," October 10, 2013.)

Allegations of Corruption and Impropriety By Walmart

Concerned by its alleged corruption and other improper practices in Mexico, Brazil, China, India and elsewhere, Walmart began a global review of its operations to assure that they are in compliance with both the U.S. Foreign Corrupt Practices Act and also the host country laws. "Its lawyers flagged India among the countries with the highest corruption risk." (Hindustan Times. "Wal-mart, Bharti deal: diary of a troubled marriage," October 10, 2013.)

As a consequence of this inquiry, Bharti-Walmart suspended its five top executives in November 2012. Walmart India CEO Raj Jain resigned in June 2013; he was replaced by Ramnik Narsey. At Bharti Retail, Chief Operating Officer Mitch Slape, an old Walmart hand, was sent back to Walmart USA. These executives, however, were not charged for any wrong doing. (Hindustan Times. "Wal-mart, Bharti deal: diary of a troubled marriage," October 10, 2013.)

While lobbying is legal in the U.S., it is illegal in India. So when Walmart disclosed to the U.S. Senate and House of Representatives that it spent about \$25 million since 2008 on its lobbying activities in India that included enhanced market access for investment in India, there was a huge uproar in the Indian Parliament which led to the Indian government starting an investigation against Walmart. (Hindustan Times. "Wal-mart, Bharti deal: diary of a troubled marriage," October 10, 2013.)

With all these allegations and challenges facing Walmart internationally, especially in India, its breaking up with Bharti Enterprises and taking complete control of its Indian operations appeared to be a logical thing to do.

Wal-Mart has invested more than \$200 million on overhauling its worldwide operations in order to assure that these are in compliance with both the U.S. and the host country anti-corruption laws (Banjo, Shelly and R. Jai Krishna, 2013).

Bharti Enterprise's Reasons

Bharti Enterprises seemed to have its own reasons to call it quits.

Bharti Retail is interested in growing its own retail business involving various formats. With its 212 Easy Day stores, it already has a strong foothold in the industry. (Bose, 2013.)

The Bharti Enterprises is disappointed with the lack of growth in the number of the Best Price Modern Wholesale stores, which was growing but has now been stuck at 20 units. It is also concerned with these units' losses of Rs 372 crore as of December 2012. (Mookerji, Nivedita. 2013.)

Bharti Airtel, with billions in debt, is financially strained after buying some telecom firms in the developing world, including its purchase of Zain of Middle East and North Africa.

Terms and Costs of Joint Venture Breakup

Here are some of the main terms of the Bharti Walmart joint venture breakup.

Wal-Mart will acquire Bharti Enterprises' 50% stake in the 20 Best Price Modern Wholesale cash-and-carry stores that had been run by the Bharti Walmart joint venture. It would thus own it 100%, which is allowed under the India laws. (Banjo, Shelly and R. Jai Krishna, 2013.)

Bharti Enterprises would acquire the compulsory convertible debentures (CCDs) worth \$100 million that Walmart had invested in Cedar Support Services, the parent company of Bharti Retail that operates its EasyDay stores. Bharti Enterprises would run them by itself now. (Bailay and Malviya, 2014.)

In monetary terms, Walmart spent \$334 million to end its partnership with Bharti Enterprises. It paid \$100 million to buy Bharti Enterprises 50% share in the partnership; and it took a \$234 million loss for waiving the debt and other investments it had made in the Bharti Enterprises. (Bailay and Malviya, 2014.)

It may be noted here that Walmart also incurred costs and losses associated with the closure of its about 50 underperforming units in Brazil and China (NDTV 2014)

Other Joint Venture Breakups in India

The Walmart and Bharti is not the first international partnership breakup in India. Some other major names which have broken up their relationships or having problems working together include Procter & Gamble (USA) and Godrej; Telenor (Norway) and Unitech; Fiat (Italy) and Tata Motors Ltd.; Ford (U.S.A.) and Mahindra & Mahindra; McDonald's (U.S.A.) and Connaught Plaza Restaurants; Di Bella Coffee (Australia) and Sachin Sabharwal; and Honda (Japan) and Munjals; among others.

Based on these data and information, the following hypothesis is presented:

H5 The foreign companies in India, in its retail or other industries, should remain clear of any misbehavior in India, in their home country, or elsewhere in order to establish, stabilize, and grow their business in India.

WALMART'S CONTRIBUTIONS

Walmart, through its Bharti-Walmart joint venture, and through its other associations with India, has made some important contributions to the country such as follows.

Benefits of Best Price Modern Wholesale Store

According to a Walmart website, the Best Price Modern Wholesale Stores offers the following benefits.

“Best Price Modern Wholesale stores are a one-stop-shop that offers best prices with unmatched convenience, choice, quality and hygiene. The stores meets day-to-day needs of business members namely restaurant owners, hoteliers, caterers, fruit and vegetable resellers, kiranas, other retail stores, offices and institutions. Around 5,000 items, including food and non-food items, are available at competitive wholesale prices by lowering cost of operations. Over 95% of these items are being sourced locally, which in turn reduces the costs and eventually, the prices” (Walmart Website)

“A typical cash-and-carry store stands between 50,000 and 100,000 square feet and sells a wide range of fresh, frozen and chilled foods, fruits and vegetables, dry groceries, personal and home care, hotel and restaurant supplies, clothing, office supplies and other general merchandise items” (Walmart Website)

“Best Price Modern Wholesale stores have introduced several education programs for its members with customized modules for different target segments. A model ‘Mera Kirana’ has been created in each store that shares best practices with both, small and medium retailers. It also promotes usage of low cost modern techniques and processes such as assortment planning, layout and fixtures, displays, backroom, licenses, safe food handling, customer retention and value added services. Further, different educational programs for members on Taxation, Food Preparation, Food Safety and Category workshops are organized on a regular basis” (Walmart Website)

Best Price stores provide safe, clean, healthy, and hygienic food. Vegetarian products, Dairy, Meat & Fish departments are physically separated from each other to respect the religious sentiments of its members. All food equipment are sanitized every four hours. (Walmart website.)

Walmart plans to continue to improve India’s infrastructure. It also plans to duplicate its no-questions-asked ‘return policy’ in India that it uses in other countries.

Corporate Social Responsibility

Bharti Wal-Mart has been involved in helping community and environment right from the beginning. It has provided pushcarts to the poor to help them build their business, it partnered with Coca-Cola India to plant trees in Amritsar, it partnered with Amritsar Municipal Corporation, to adopt and manage certain roads, it partnered with the Punjab government to launch skills training and centers, and it has supported schools and their underprivileged children there (Business Standard 2009).

Bharti Walmart joint venture has also sponsored a Women’s Economic Empowerment Initiative to enhance economic opportunities for women in India (Bharti website).

Based on these data and information, the following hypothesis is presented:

H6 Walmart’s continued presence and growth in India would be good for the Indian economy.

WALMART’S CRITICISMS

Walmart continues to be opposed primarily for one major reason: It destroys jobs most anywhere it goes. Let us look at it from the Indian perspective.

Destroying Jobs

Anand Sharma, India's then Commerce and Industry Minister, said that he expects new FDI in retail to create 10 million new jobs over three years, about five to six million of which would be in logistics. (Dhume, 2011).

However, that optimistic opinion does not present the entire scenario. This may be true if one looks only at the jobs created by FDI (Walmart and other international investments) in the new stores and infrastructure it helps develop. Actually, as many people argue, the FDI really destroy many more millions of jobs which are currently performed by the small kirana merchants, the small farmers, and the small intermediaries all over the country.

According to a study by Neumark et al, opening of Walmart stores clearly reduces local employment and payroll (Neumark et al., 2005).

However, according to a study by the Indian Council of Research in International Economic Relations (ICRIER), large corporate and FDI money in the retail sector would not harm the small retailer in the long run. The FDI in organized retailing would help overall consumer spending to increase and help improve the purchasing power of all income groups. Lower income consumers would benefit the most. (Joseph et al., 2008).

Right from the beginning, the Bharti-Walmart joint venture has raised concerns and protests by small shop owners, traders, hawkers, farmers, and trade unions who fear substantial job losses due to FDI entry in India's retail industry.

For example, several hundred shopkeepers in Delhi and elsewhere in the country protested the partnership on August 9, 2007. They chanted "Quit retail," echoing the famous "Quit India" slogan that Gandhi successfully used to gain independence from Britain 60 years ago this month. (Gentleman 2007). This time, however, Walmart does not appear to pull out of the growing Indian retail market.

Similarly, in November 2011 when India announced its policy to allow 51% foreign ownership in multi-brand retail, millions of small shop keepers, traders and others demonstrated against the policy throughout the country. (Chen, 2012).

Several hawkers and vendors protested outside the Walmart's head office in Gurgaon, on November 19, 2014 to bring attention to the damage it is causing them, the low wages it pays to its employees and the poor working conditions in its stores. (Chatterjee, November 20, 2014).

Likewise, as Walmart was about to open its 21st store near the Taj Mahal in Agra, India, the street vendors who sell similar goods as Walmart does protested the move saying it will take away their business and jobs. (Upadhyaya, 2015).

Retailing in the Disguise of Wholesaling

Under Indian laws, FDI partnered wholesale stores are allowed to sell only to "retail businesses" like shops, restaurants, vendors, hotels, and offices. Customers are required to have a photo ID to enter these stores. There is also a minimum purchase requirement so that individuals will not take advantage of the cards.

However, according to an undercover investigation by web portal Cobrapost.com, the international retailers, Wal-Mart, Metro Cash & Carry and Carrefour, do routinely sell their merchandise to individuals too. (Rajendran, 2014).

This violation of law by these companies hurts the poor small shops owners who are dependent on these individual buyers.

Based on these data and information, the following hypothesis is presented:

H7 Walmart would continue to face serious opposition from small local Indian merchants for their current and future unemployment.

WALMART'S STRATEGIES AFTER JOINT VENTURE BREAKUP

Walmart has several strategic alternatives to choose from after its breakup with Bharti Enterprises. Its decision would affect both its own future in Indian retail industry; as well as the overall flow of FDI in India. It can stay in India, first, by continuing and growing its wholesale business there; and, then, it can enter India's multi-brand retail business as and when it seems appropriate. Alternatively, it can pull out of India completely, as the French mega retailer Carrefour decided to do in July 2014.

Walmart's Strategy to Continue Wholesale Operations in India

Indian retail industry is expanding all over the country, both in the highly populated large cities and the less populated smaller towns. According to the Indian Brand Equity Foundation, the local retail market, with a value of about \$518 billion, should grow to about \$866 billion in 2015. For a comparison, the U.S. market would be about \$424 billion in 2010. The organized retail sector in India, currently about 10% of the overall market, would grow up to about 20% by 2020. (Octogona, 2014).

According to Rachna Nath, a retail analyst for PricewaterhouseCoopers, the Indian retail market is estimated to expand to more than \$1.3 trillion by 2020. It already racks up more than \$400 billion in sales each year, but is dominated by traditional markets and mom and pop shops. (Banjo, Shelly and R. Jai Krishna, 2013)

Walmart, logically, has chosen to continue and expand its Wholesale Best Price cash-and-carry operations in India. It also plans to continue to make important contributions toward India's socio-economic environment. According to Walmart's international president, David Cheesewright, India is a long-term commitment for Walmart (Mookerji, 2014).

In April, Walmart announced plans to open 50 wholesale stores in the next four to five years to expand its footprint in the country (Indian Express, 2014). It recently acquired a wholesale store in Agra from its rival Carrefour, the French mega retailer who losing money on it and who has decided to exit India due to several reasons.

For a general comparison, Walmart opened under 40 stores annually in China since 2008. In Mexico, its neighboring country, however, it opened an average of 266 stores every year since 2008. While this comparison may not be totally objective, it does throw some light on what India offers in terms of both the opportunities and the challenges. (The Telegraph, 2013.)

Walmart's Strategy to Enter India's Multi-Brand Retail Industry

Walmart would continue to wait for appropriate time and opportunity to enter India's multi-brand retail business. If it decides to do so, it may do it on its own, it may take an India partner, or it may acquire a competitor.

E-Commerce

Online retailing giant Amazon.com plans to invest \$2 billion to expand its operations in India that it began in February 2012. Similarly, Flipkart, India's largest e-retailer, is planning to raise \$1 billion to expand its business. According to Boston Consulting Group, Internet users in

India are expected to increase from 120 million in 2011 to 330 million by 2016; and their online shopping has room for growth. (Zack, 2014)

Walmart is also starting its own B2B online business to participate in India's growing online business market.

Based on these data and information, the following hypothesis is presented:

H8 Walmart would continue to evaluate its various strategies to remain in India or to quit India.

CONCLUDING THOUGHTS: INDIA'S FDI STRATEGY

India has some its own strategic choices to make too.

Multiple Stakeholders, Conflicting Interests

India's retail industry is at cross roads. Its modernization, on the one hand, would destroy millions of small businesses and the related jobs. It, on the other hand, would also improve country's infrastructure, create millions of different kinds of jobs, allow farmers and producers to receive more for their efforts, and allow consumers to pay less for their purchases as they shop in stores which more consumer friendly in several ways.

India needs additional capital and modern techniques of technology and management to modernize its age-old, inefficient and expensive retailing industry.

Large international retailers such as Walmart, Carrefour, and Tesco; and India's own large organized retailers such as, in addition to Bharti Retail, Future Group's Pantaloon Retail, Spencer's Retail, Reliance Retail, Birla More, and Tata's Westside are already providing some such resources. However, much more needs to be done.

However, the large and growing retailers, foreign or Indian, single brand or multi-brand, are also known for hurting small businesses and killing their jobs; millions of them.

This opposite environment of creative destruction would play out irrespective of the origin of the modern retailing firms, whether they are national or foreign.

China Example

FDI in retail in China provides a good benchmark for FDI in retail in India. China first allowed FDI in its retail in 1992 at 26%. It gradually increased it to 100% in 2004 in selected cities, as it tried to protect and strengthen its own retailers. (Dutta, 2011.)

India's Strategy

Thus, on the one hand, it appears logical for India to go slow in allowing FDI in its retail sector, as it tries to protect its small scale businesses. However, on the other hand, it also makes sense for India to recognize that China, one of its major competitors in the world markets, is already years ahead in the retail business in terms of its efficiency and effectiveness as they relate to different stakeholders. It, therefore, would make good sense for India to expedite the flow of FDI in its retail industry.

If India slows down in modernizing its retail industry, it would also continue to fall behind the countries such as China in developing its export business. Why would an importer pay more for Indian produce or products when it can get them at much lower prices elsewhere such as from China?

Under these circumstances, India should adopt a strategy, on the one hand, of facilitating the modernization of its retail industry. And, on the other hand, it should also take all the necessary steps to take proper care of its people who would be adversely affected by retail industry modernization.

It should be recognized that the modernizing retailing would increase per person output, the total national GDP, and the average per capita GDP; as it would also reduce the total cost of production. In other words, the modern retailing would increase the total size of the rotli (Indian bread), as compared to its size currently rolled out by its grossly inefficient retailing industry.

India should then use its increasing size of rotli to take proper care of its people who are hurt by the modernization, in retailing or elsewhere, by providing them the benefits such as follows: Unemployment compensation; medical care; general and specialized education to prepare for different jobs and opportunities; and low cost loans and guidance to start new businesses.

It would be a win-win phenomenon for India, not a zero-sum game.

Based on these data and information, the following hypothesis is presented:

H9 It is in India's major interest to promote modern retailing in the country. It should develop comprehensive laws and regulations to help it grow at a rapid rate; including its FDI component. It should also establish equally comprehensive laws and regulations to help the millions of small entrepreneurs who would be unemployed by the growth of its modern retail industry.

ACKNOWLEDGEMENTS

Thanks are due to Mr. Sungsik Choi, the author's Graduate Assistant for his research assistance; and to Pace University for making his valuable help available to the author. The author is also thankful to all the sources which have been used in writing this case study article.

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