



An investigative analysis of the factors influencing degree of involvement in a foreign market

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Abstract

This paper focuses on factors that influence the degree of involvement in foreign markets. Using survey method, the research data was obtained from 112 usable responses from a sample of 500 UK companies which operate in at least two other countries. This represents a usable response rate of 22.4%, and consistent with similar research. The variables are grouped in terms of firm context (competition, organisation structure, competitive advantages, degree of standardisation) and host country context (economic development, culture differences, regulation, political risk). Regression models are used to test the relationship between the independent variables and the degree of involvement. Findings strongly indicate a positive relationship between the degree of foreign market involvement and the level of competition and the degree of foreign market involvement and competitive advantage. Findings weakly support the hypothesis of a positive relationship between the degree of foreign market involvement and economic development. There is weaker evidence to show a negative relationship between the degree of foreign market involvement and the cultural dimensions of individualism and power distance as proposed by Hofstede.

Keywords: Foreign markets; degree of involvement; firm context; competitive advantage.

Introduction

In the context of the global economy, firms have the opportunity to grow their business through the use of product and market expansion (Analogbei, 2013; Chen and Chang, 2011; Park and Sternquist, 2008; Koch, 2001). In order to be able to compete successfully in foreign markets, theory suggests that firms must possess certain ownership-specific characteristics which offer them competitive advantage (Lopes, 2010; Lundan, 2010; Cleeve, 2009;

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Pinho, 2007). In addition to the product itself, these include firm size, structure, managerial and marketing skills, technological know-how or ownership or control of a range of assets (Cantwell, *et al.*, 2010; Dunning, 2009, Gleason *et al.* 2002; Benito *et al.*, 1994). The main purpose of this paper is to study the decision over which entry mode to employ in the different contexts. This lies at the heart of the international strategy of a firm (Koch, 2001). Whilst it is only a part of the overall market entry strategy process, it is clearly a significant factor. This is because the choice of entry mode is believed to be one of the most important decisions of foreign investment, as each entry mode conveys advantages and disadvantages to the investor (Chiao, *et al.*, 2010; Meyer and Estrin, 2001; Wind and Perlmutter, 1977). For example, although wholly owned subsidiary typically requires high resource commitment, it may also offer the best option when firms anticipate market imperfections in the host country, which could undervalue the assets of the firm (Nisar *et al.*, 2012; Park and Sternquist, 2008). The extent to which the firm is seen to be involved in a foreign market is determined, for the purposes of this paper, by evidence of the commitment of resources and the degree of control implicit in the chosen entry strategy to the foreign market.

Literature Review

Amongst the criteria influencing the selection of entry process are likely to be: 1) The culture of the potential foreign market and the 'fit' with firm culture (Malhotra, *et al.*, 2009; Quer, *et al.* 2007; Erramilli and D'Souza 1995); 2) The bargaining power of the firm in relation to the host government; 3) Political factors (instability / political leverage); (Tuomi, 2011; Jimenez, 2010; Luiz and Charalambous, 2009; Asiedu, *et al.*, 2009; Demirbag, *et al.*, 2008; Kehl, 2007 4) Structure of the industry within which the firm operates / expansion strategy (Boateng, 2004); 5) Regulatory framework of the host country (Barthel, *et al.*, 2011; Harvey and Abor, 2009; Acquaaah, 2009; Smith-Hillman and Omar 2005).

Additions to this list include firm-specific advantages, experience and environmental factors, (Nguyen, 2011; Chiao *et al.* 2010; Driscoll, 1995); risk and the extent to which flexibility matters (Quer, *et al.*, 2007; Porter, 1976; Klein, 1989). Most models tend to focus on market and mode selection as being something of a staged process with the firm identifying and screening a country in depth using elements of the criteria shown above, in the context of their overall objectives, (Osei, 2014; Bitzenis *et al.*, 2007, Johansson, 1997; Agarwal *et al.*, 1992). Other corporate strategies and resources indicate larger multinational firms favour entering foreign markets with wholly owned subsidiaries rather than with a JV (Chiao, *et al.*, 2010). A wholly owned subsidiary is preferred to a JV in the case of high levels of competition in the foreign market, when the industry overall is competitive, where the firm has previous international experience and where the firm's ownership advantages are transferrable

to the host market (Pinho, 2007; Ekeledo and Sivakumar, 2004; Bell, 1996). Smarzynska, (2000) found that firms who are technological or marketing leaders in their sector are less likely to undertake joint ventures than firms who lag behind them. Erramilli et al. (1990) reveals that some types of service firms select the less involved mode of exporting as their strategy. Morschett et al (2008) identified after-sales service determinants, while Ball et al (2008) modelled 10 lower-involvement approaches to information-intensive soft service firms. The trade-off is between risk and return with the final entry mode choice likely to be determined by resource availability and the need for control (Boonlua, 2011; Bronzini, 2007). This paper discusses the related literature review, hypotheses and finished with findings and conclusion.

Variables related to the firm

Competition: The changing pattern of competition influences the decision of the international firm to control its subsidiaries overseas (Eden and Dai, 2010; Dunning, 1998; Norvell et al., 1995; Doz et al., 1981). Bell (1996) pointed out that when competition is intensive a wholly owned subsidiary is not a suitable mode of entry as it creates additional capacity. In contrast, a joint venture might have more capability to face intense competition. Porter (1985) points out that a firm may be less likely to enter a market if there are a number of competitors rather than a dominant firm that is potentially less sensitive to focus strategies. Bell (1996) finds that international firms prefer a greater level of control when competition is high, the firm has high international experience, and the relative size of the firm is large. However, Hill et al. (1990) indicate that international firms who challenge in a highly competitive environment will choose a joint venture. Gomes-Casseres (1990) finds a positive effect between competition and the degree of involvement, but other studies find no effect at all (e.g. Larimo, 1993). This will lead to the following hypotheses.

H1 The greater the level of competition, the higher the degree of involvement in the overseas market.

Organisation Structure: The higher the extent to which the subsidiary depends on the parent firm, the higher the possibility of centralising all decisions at the headquarters (Garnier, 1982); the higher the risk of misinterpreting the management messages (Rugman et al., 1989) where each structure has different costs and benefits. Capabilities interact with ownership control to moderate the role of perceived risk (Forlani et al., 2008). This will lead to the following hypotheses.

H2 The more centralised is the firm's organisation structure, the higher the degree of involvement in the overseas market.

Competitive Advantage: the adaptation of a global perspective has become increasingly essential in planning a marketing strategy and gaining a

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competitive advantage (Ma, 2004; Keegan, 1983; Fisher, 1984; Cavusgil et al., 1984). For the purposes of this paper, competitive advantage was identified with the following variables: low cost, (Whitelock et al., 1997; Phillips et al., 1983; Walters et al., 1989) innovation, (Ford and Tucker, 1987; Hennart and Park, 1993; Kogut et al., 1988), marketing research (Hofer et al., 1978; Khandwalla, 1977) and breadth of strategic target (Hood and Young, 1979; Murray, 1988; Porter, 1987). Therefore,

H3a The adoption of a low cost-approach to competitive advantage will lead to a higher degree of involvement.

H3b The adoption of an innovation-approach to competitive advantage will lead to a higher degree of involvement.

H3c The adoption of a market research approach to competitive advantages will lead to a higher degree of involvement.

H3d The adoption of a breadth of strategic target-approach to competitive advantage will lead to a lower degree of involvement.

Host country context in relation to the degree of involvement

The Economic and political Development variable emphasises the extent of development in the host country that makes its market more or less attractive to the MNE. Nations vary in their per capita income and in other areas such as energy consumption, level of education and infant mortality. For example, the higher the level of education, the greater the buying power of consumers and the capabilities of local firms will lead the MNE to choose a joint venture entry mode since the country has something to offer (Kouztsov, 2009; Majocchi and Presutti, 2009; Park and Sternquist, 2008; Bronzini, 2007; Bell, 1996; Gomes-Casseres, 1989; Kobrin, 1987; Yang and Lee, 2002). According to Pan et al (2014) stated that the more favourable the institutional environment's the higher the degree of ownership higher. *This will lead to*

H4 The greater the degree of economic development in the host market, the higher the degree of involvement.

H5 The higher the political risk in the host country, the lower the degree of involvement in the overseas market.

Cultural Difference: recent studies have measured the cultural difference between the home and the host country with either country cluster (Malhotra, et al., 2009; Cavusgil et al., (2008; Quer, et al. 2007; Erramilli and D'Souza, 1995; Ronen et al., 1985) or by index (Kogut et al., 1988) or both (Barkema et al. 1996; Bell, 1996). The Ronen et al. (1985) study is based on eight cross cultural studies. The index study is based on Hofstede's (1980) four dimensions of national culture: power distance, uncertainty avoidance, individualism versus collectivism, masculinity versus femininity.

Dubin (1975) and Davidson et al. (1980) point out that differences in culture between different countries could influence the choice of entry mode, because of its influence regarding the cost and uncertainty of the alternative modes of entry into the overseas market. Shane (1994) finds that cultural distance is associated with higher control entry modes. Erramilli and Rao, 1993; Benito, 1996; Barkema, Bell and Pennings and Debanjan and Golder, 2002, 1996 all found joint ventures are preferred when there is a large cultural distance between the home and host market. Kogut and Singh (1988) and Hennart and Park (1993) found that the risk involved where home and host country cultures vary are so great that it leads firms to select less risky entry options (also see Cavusgil *et al.*, 2008). Therefore,

H6. The greater the cultural differences between home and host country, the lower the degree of involvement in the overseas market.

Research Methods

Considering the empirical and positivist nature of our investigation and the need to reach a wider population of respondents in the collection of data, survey method was adopted (Saunders, et al., 2012; Brennan, et al., 2011; Bryman and Bell, 2011; Brand, 2008). A questionnaire was therefore constructed in relation to the objectives and research questions of this study using validated measures of the concepts, obtaining general information about the background of the respondents and their firms, and information on host country details, for two different countries where firms have ongoing overseas operations. The two countries were selected from two prepared lists generated from differences in culture and economic development, and constructed so the countries on each list were maximally different in terms of the host country context items.

Table 1. Variable Measures

Variable	Measure	Supporting Lit.
Degree of involvement	Involvement in manufacturing know-how; marketing know-how; marketing expertise; R&D resources; R&D personnel; production and marketing personnel and distribution system.	Kim and Hwang (1992)
Competition	Product development, pricing strategy, quality, choice of supplier, wages and labour policy, administration and supervision, organisation and, sharing resources with the overseas market.	Doz et al., (1981) Porter (1985) Bell (1996) Gomes-Casseres (1990)

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Organisation structure	The size of the organisation measured by number of employees, sales revenue and market capitalisation, and the level of the authority in the organisation.	Pugh et al. (1969)
Competitive advantage	Identified as a concentration on either low cost, innovation, marketing research or breadth of strategic target	Dess and Davis (1984).
Degree of standardisation	Respondents were asked to evaluate the changes that had been made to the features or the ingredients of the product before sending them overseas, for example, product features, quality, brand name, service, distribution, positioning; packaging/labelling and promotional approach.	Takeuch and Porter (1986) Levitt (1983) Sorenson and Wiechmann (1975) Jain (1989)
Economic development	GNP per capita (US\$), energy consumption per capita, infant mortality per 1000 live births and the percentage of illiteracy aged 15+.	Bell, 1996
Cultural difference	Based on Hofstede's four dimensions: individualism, power distance, uncertainty avoidance and masculinity	Hofstede (1984, 1990)
Regulation	The degree to which legal regulation (e.g. health, safety, and technology) in the foreign market is similar to those in the host market.	Cavusgil et al. (1993)
Political risk	Measured according to the instability of the host country political system; likelihood of host government taking actions to limit the firm's ownership of the foreign venture; likelihood of the host government constraining the foreign operation by instituting policies with respect to price control and local content requirement.	Kim et al. (1992)

The study's information requirements necessitated obtaining respondents familiar with the firm's international strategy. Further, the respondents needed to be familiar with the home country and the overseas country environments and the impact of the environment upon the firm's policy. These criteria identify the firm's Chief Executive Officer as being the most likely respondent. The sample frame used for selecting these firms was obtained from Who Owns Whom (1995/1996), Key British Enterprises (1996) and Kompas (1989/1990). Only firms recently engaged in international marketing were

Table 2. Means, Standard Deviations and Spearman Rank Order correlations

	Mean	S. D	1	2	3	4	5	6	7	8	9	10	11	12	13	14
1-Degree of Involvement	2.297	0.897														
2- Competition	3.164	0.761	.359***													
3- Organisation Structure	2.98	0.535	-.048*	-.143**												* P<.10 ** P<.05 *** P<.01
4- Low cost	4.5	0.577	0.015	.236***	-.139**											
5- Innovation	3.257	0.975	0.093	0.026	-0.082	0.107										
6- Marketing research	3.339	0.97	.148**	0.055	-0.014	0.106	.386***									
7- Focus	3.181	0.855	0.019	-0.049	0.026	0.033	.127*	-.183***								
8- Degrees of Standardisation	3.875	0.829	-.390***	-.266***	0.017	-0.054	-.227***	-0.075	-0.104							
9- Economic Development	2.65	2.555	0.046	0.082	0.011	0.005	.115*	.151**	0.016	-.142**						
10- Individualism	64.934	23.807	-0.039	0.103	-0.043	-0.018	-0.002	0.06	-0.074	-0.05	.730***					
11- Power Distance	53.325	16.879	0.008	-0.091	0.099	0.05	-0.014	-0.017	0.072	0.006	-.490***	-.608***				
12- Uncertainty Avoidance	60.864	21.075	0.02	-.161**	0.051	0.042	0.098	.132*	0.015	0	-0.066	-.257***	.493***			
13- Masculinity	55.907	16.218	-0.021	0.025	0.11	-0.036	0.035	.122*	0.019	-0.017	.207***	.253***	-.445***	-.269***		
14- Regulation	2.159	1.544	0.071	-0.087	-0.009	0.005	-0.081	0.029	-0.106	-.157**	0.005	-0.097	0.094	0.037	0.001	
15- Political risk	1.713	0.788	.412***	.185***	-0.002	.132*	0.101	-0.001	-0.041	-.293***	-.326***	-.332***	.200***	-0.031	-0.011	.301***

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selected. This reduced the target population size to 750 firms of those 700 international UK firms were contacted by telephone in order to enlist their co-operation with the research. A total of 500 of them agreed to receive the questionnaires. Following two sets of mailings, 112 usable completed questionnaires were returned; a response rate of 22.4 %. It was felt that this was a sufficiently large response level to minimise the problem of response bias.

Findings and Discussion

Correlations between the degree of involvement and the independent variables are for the most part weak and non-significant (Table 2). There are four significant correlations between: the degree of involvement and competition, market research, degree of standardisation and political risk. Competition and market research have the expected sign, but degree of standardisation and political risk do not have the expected sign.

Table 3. Results of Regression Analyses

Variable	Model 1 Firm Con- text	Model 2 Host Country Con- text	Model 3 Full Model
	Beta	Beta	Beta
Competition	.373***		.329***
Organisation Structure	.049		.048
Low cost	-.094		-.154**
Innovation	-.034		-.056
Market Research	.155**		.197***
Breadth of strategic target (focus)	.062		.065
Degree of Standardisation	-.236***		-.168**
Economic Development		.228**	.105
Individualism		-.097	-.168*
Power Distance		-.089	-.199**
Uncertainty Avoidance		.059	.126*
Masculinity		-.009	-.015
Regulation		-.089	-.083
Political risk		.489***	.414***
R sq	.261	.198	.402
Adjusted R sq	.233	.169	.353
F	9.199***	6.816	8.249***

* $p < .10$; ** $p < .05$; *** $p < .01$

Multiple regression analyses (Table 3) in Model 1 captures the effects of the firm characteristics on the degree of involvement. Model 1 is significant at the $p < 0.01$ level. The coefficients for competition ($p < .01$), market research ($p < .05$) and degree of standardisation ($p < .01$) are significant. The signs on the significant coefficients of competition and market research are as

anticipated, but the sign on the degree of standardisation is contrary to that expected.

Model 2 captures the effects of the host country environment on the degree of involvement. This model is not significant. There are two variables with significant coefficients: economic development ($p < .05$) and political risk ($p < .01$). While economic development has the anticipated sign, political risk does not. Model 3 is the full model including all the independent variables, which offers a stronger, multivariate test of the hypotheses and allows examination of how both firm characteristics and host country environment simultaneously affect the degree of involvement. The model is significant at the $p < .01$ level ($F = 8.249$, $R^2 = .40$). Individual coefficients for competition ($p < .01$), low cost ($p < .05$), market research ($p < .01$), degree of standardisation ($p < .01$), individualism ($p < .10$), power distance ($p < .05$), uncertainty avoidance ($p < .10$) and political risk ($p < .01$) are significant. The signs on the coefficients of competition, market research, individualism and power distance are as anticipated, however, the signs of low cost, degree of standardisation, uncertainty avoidance and political risk are not as expected.

The hypothesised set of relationships are clearly supported in only two instances, competition and market research, in that the variables are significant with the hypothesised sign in both models in which they are included.

The findings indicate that when a highly competitive market is encountered, international firms will prefer a high degree of control entry mode such as a joint venture or a wholly owned subsidiary which implies that this will give the firm a better opportunity to deal with the competition (Talay and Cavusgil, 2009; Telesio, 1977). The results accord with the findings of Bell's study (1996) that a wholly owned subsidiary is preferable to a joint venture when a highly competitive market is considered. However, the findings of this study are also in line with Gomes-Casseres's (1990) findings which show that there is a significant relationship between competition and the degree of involvement with regards to the preference for joint ventures.

Of the four competitive advantage variables, only for the market research variable is there any support for the hypothesised relationship. Overall, however, the findings for the competitive advantage variables indicate little support for the hypothesised relationships. Nevertheless the findings point to the importance of market research to firms seeking to become involved in foreign markets.

It is clear that the level of economic development is an important factor for many firms deciding to become involved in foreign markets (Kouznetsov, 2009). There will be a tendency for such firms to prefer a high degree entry mode the more developed the host country. This finding is in line with those of Bell (1996) and Kobrin (1987) who reported that firms prefer to enter developed countries with high degree entry modes (JVs) than they do develop-

ing countries. An important reason for this is that local firms in developed countries can offer the entering firm more than local firms in developing countries can in terms of commercial experience and a better educated workforce (Bell, 1996; Gomes-Casseres, 1990). The findings showing a significant negative relationship between individualism and power distance and the degree of involvement supports the view that foreign firms will prefer a lower involvement mode the greater the cultural difference between countries (Davidson et al., 1985; Kogut et al., 1988). Some firms may select a low entry mode such as exporting to avoid the conflict that can be created when cultural difference is great. Other firms may prefer JVs to WOSs when countries entered have a dissimilar culture (e.g. Bell, 1996; Davidson, 1982; Erramilli, 1991; Erramilli and Rao, 1993).

Conclusions

This study examined the relationship between firm characteristics and host country environment on the degree of foreign market involvement. Findings strongly support the hypotheses of a positive relationship between the degree of foreign involvement and the level of competition and the degree of foreign involvement and competitive advantage based on market research. Findings weakly support the hypothesis of a positive relationship between the degree of foreign involvement and economic development and the hypotheses of a negative relationship between the degree of foreign involvement and the cultural variables of individualism and power distance. Other findings do not support the hypothesised relationships.

The above findings have some implications. First, the highly significant relationship between high degree of involvement and competition suggests a recommendation of high involving strategies in a competitive environment. This is justifiable as firms may need to make quick modification in strategies and market offering in response to competition, and high degree of involvement strategy such as wholly owned subsidiary offers owners the required voting rights to facilitate the required modification. Second, competitive advantage based on market research offers the firm greater understanding of the market conditions and how to provide market offering efficiently and effectively. Theoretically, these findings add to the assertion that a firm's knowledge of a market influences the choice of entry mode, due to the perceived reduction of risks and uncertainties.

Every research has limitations, and this research is no exception. The relationships were examined with a sample of UK firms and their foreign affiliates. There is the possibility that the findings may have been influenced, somewhat, by the home country characteristics of the sample used. Caution must be applied in generalising the findings beyond UK firms. It is therefore recommended that more research should be carried out to further investigate the relationship between firm characteristics and host country environment

on the degree of foreign market involvement using samples of firms from other home countries. Further refinement of some of the variables examined in this study would also be useful, in particular the characteristics of competitive advantage, the measure of economic development and the nature of cultural difference.

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