DEVELOPMENT AND TESTING OF A RESOURCE-BASED THEORY OF INTERNATIONAL ENTRY MODE CHOICE

DISSERTATION

Presented to the Graduate Council of the University of North Texas in Partial Fulfillment of the Requirements For the Degree of

DOCTOR OF PHILOSOPHY

By

Varinder M. Sharma, B.Sc., M.Sc., M.Tech., M.B.A.

Denton, Texas

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CHAPTER I
LAYING THE FOUNDATION

Introduction

American firms have been deeply involved in world economy since the beginning of the twentieth century, investing in Canada, Russia, and many European, Latin American, Asian, and African countries. According to Southard (1931), foreign operations of U.S. firms, in addition to exporting, included various external forms like agent, branch house, fully controlled subsidiary, minority interest, contract, and licensing agreement. He further notes that often, many U.S. firms starting with agents changed their external forms to subsidiaries over time depending upon the increase in their foreign market activities. Without undertaking any thorough investigation into these firms' choices of various external forms, Southard provides a plain description of the external forms of American firms in a number of foreign markets. His work is the earliest published work on entry modes. The "external forms" of American firms in Southard's work are currently referred to as Foreign Market Entry Modes or simply as Entry Modes of the firm. Since entry mode literature spans over six decades, it is logical to expect
changes in the nomenclature of certain types of entry modes. Wherever necessary, efforts are made to clarify the changes from the old jargon to the current terminology. The following material introduces the reader to a contemporary understanding of entry modes and how firms choose them.

Entry Mode

Root (1987) defines an entry mode as an institutional arrangement that makes possible the entry of a firm's products, technology, human skills, management, or other resources into a foreign country. Gatignon and Anderson (1988) refer to an entry mode as a governance structure that allows a firm to exercise control over its operations. Hill, Hwang, and Kim (1990) define an entry mode as a way of organizing a firm's business activities in a foreign country. In short, an entry mode is a structural arrangement that allows the firm to implement its product market strategy in a host country. By organizational structure it is meant some appropriate combination of a firm's human, capital, and technological resources.

There are two ways in which a firm may implement its product market strategy in a host country: (1) by operating itself or in collaboration with a host country firm, or (2) by engaging in a domestic transaction with another firm which in turn handles the host market operation. If the
firm chooses the first way, it is said to be directly involved in a host market operation. The various forms of arrangements in which the firm is directly involved include exporting through host country intermediary, exporting through company-owned channel, contracting, joint venture, and wholly owned subsidiary. These forms are collectively referred to as direct entry modes (Onkvisit and Shaw 1989). Likewise, if the firm chooses the second way, it is said to be indirectly involved in a host market operation. The examples of indirect entry modes include casual exporting, export brokers, and export management companies. These are collectively called as indirect export modes. The direct and the indirect modes taken together, thus, constitute a complete set of entry modes.

Complete Set of Entry Modes

In the proposed work, a parsimonious representation of the complete set is explained, which includes six types of entry modes: (1) wholly owned subsidiary, (2) joint venture, (3) contractual (licensing, franchising etc.), (4) export through company owned channel, (5) export through host country intermediary, and (6) indirect export. These are the most commonly used modes by firms. Based on the works of Dahringer and Muhlbacher (1990) and Root (1987), the following material briefly describes each of the six modes.
Wholly owned subsidiary (WOS): In this arrangement, both production- and marketing-related activities pertinent to a firm's host market strategy are carried out in the host market. The firm is the sole owner of host country operations.

Joint venture (JV): In this arrangement, both production- and marketing-related activities are carried out in the host market under a shared ownership between a firm and a host firm. There can be a variety of joint ventures depending upon the combination of production and/or marketing arrangements between the firm and the host firm. For example, the firm may invest in production operations and the host firm may invest in marketing operations and vice versa.

Contractual modes (CM): In this arrangement both production- and marketing-related activities are performed in a host market. The firm has no stake in the ownership of host operations rather, it is the host firm that is the sole owner of these operations. There can be a variety of contractual arrangements between the firm and a host firm. Examples of such arrangements include licensing, franchising, and technical agreements.

Export through company-owned channel (EXP-COMPANY): It is an arrangement in which a firm carries out the host country marketing-related activities. The production-related activities, however, are conducted at home. The firm is the sole owner of host market operations. Examples of this arrangement include sales subsidiary and direct export to consumers.

Export through host country intermediary (EXP-HOST INT): It is an arrangement in which a firm performs production-related activities at home. However, marketing-related activities of the firm in the host market are carried out under the ownership of a host firm; the firm has no ownership stake in the host marketing operations. The host firm can be a foreign distributor or an agent.

Indirect export (EXP-IND): In this arrangement, the firm carries out its production- and marketing-related activities at home and has no investment in host country operations. The firm is engaged in domestic transaction with another home country firm which has access to the host market. This firm in turn, conducts the host marketing operations for the firm under its ownership. The exporting firm is not engaged in any form of direct transaction with a foreign market.
These six entry modes can be described in terms of two structural dimensions. These dimensions are:

(1) Type of host country operation--marketing operation, or both marketing and production operations, and

(2) Type of ownership of host country operation--sole ownership of the firm, ownership shared with the host firm, sole ownership of the host firm, or sole ownership of another home firm.

Figure 1 represents the complete set of entry modes in terms of various types of host country operations they allow a firm to perform and their types of ownership. All the six modes entail marketing of a firm's products in a host country. However, in the first three modes, a firm carries out host country production to market its products in that country. These are referred as "Host Production" modes in this study. Also, as described before, the WOS and JV modes taken together are called as FDI modes.

In the last three modes, the firm produces its products in its home country or another country to market them in the host country. These are called as "Export" modes. Of three export modes, the first two, EXP-COMPANY and EXP-HOST INT modes are called as "Direct export" modes, while the third one (EXP-IND) is the indirect export mode. Therefore, the host production modes and the export modes taken together can describe a complete set.
## A COMPLETE SET OF ENTRY MODES

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<th>Ownership of Host Operation(s)</th>
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<tr>
<td></td>
<td>Production</td>
<td>Marketing</td>
</tr>
<tr>
<td>Wholly owned subsidiary (WOS)</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Joint venture (JV) (partnerships, consortium)</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Contractual (CM) (licensing, franchising)</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Export through company-owned channel (EXP-COMPANY) (sales subsidiary, direct export to consumers)</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Export through host country intermediary (EXP-HOST INT) (foreign distributors, agents)</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Indirect export (EXP-IND) (casual exporting, export brokers, export management companies)</td>
<td>No</td>
<td>No</td>
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Figure 1
Theories of Entry Mode Choice

A number of theories have been offered by researchers across the world to explain entry mode choice of the firm. In chronological order, the theories are (1) Hymer's (1976) theory, (2) PLC theory (1966), (3) Internationalization theory (1975; 1977), (4) Internalization theory (1976), (5) Transaction Cost theory (1975, 1986), (6) Dunning's (1977, 1980) Eclectic theory, and (7) Location theories.

It must be pointed out that, the earlier theories of entry mode choice (for example, the first two theories and some of the location theories) commonly combine wholly owned subsidiary and joint venture into one category called the foreign direct investment (FDI). In this regard, these earlier theories do not distinguish between wholly owned subsidiary and joint venture type of entry modes. Also, they do not make distinctions among various export modes. The more recent entry mode theories like internationalization and transaction cost theories are, however, more precise in delineating the export and FDI modes into specific categories. The following material provides a quick review of various entry mode choice theories.

Hymer's theory is the first of its kind which brought an important shift in the paradigm of entry mode analysis from the portfolio investment to the industrial organization paradigm. According to this theory, entry mode choice of a
firm is a function of (1) its monopolistic advantage and (2) the degree of market imperfection for that advantage. Despite its trail-blazing efforts, the theory is limited to explaining the choice between FDI and licensing modes only.

According to the product life cycle (PLC) theory, the entry mode choice of a firm can be explained in terms of the life cycle stage of its product. The theory has been popular among a select group of researchers because (1) it was able to explain Leontief's paradox concerning U.S exports and imports and (2) it resembles with humanity's cradle-to-grave conceptualization about life. The theory explains a firm's choice between two modes only: export (direct and indirect combined together) and FDI modes.

These two theories of entry mode choice described above are founded in Bain's (1956) industrial organizational (IO) theory of the firm. Together, they comprise the IO-based Market Imperfection Paradigm of entry mode choice.

The Internationalization theory explains how the firm's entry mode arrangement evolves over time as a function of (1) market uncertainty and (2) market commitment. According to this theory, firms increase their resource commitment in a foreign market gradually rather than in a lump-sum fashion. This theory became popular during the period spanning late seventies to early eighties because of its simplicity and its ability to allow longitudinal testing of international behavior of firms. However, this theory
explains the choice between four types of modes only: indirect export, direct export (export through host country intermediary), sales subsidiary (export through company-owned channel), and wholly-owned subsidiary modes. The internationalization theory belongs to the Behavioral Paradigm of entry mode choice because of its grounding in Cyert and March's (1963) Behavioral theory of the firm.

According to the Internalization theory, firms engage in wholly owned operations in order to internalize international intermediate product market for certain kinds of knowledge. The market for firm-specific knowledge is imperfect because of (1) inability of buyers to correctly assess the value of the product, (2) limited number of buyers, and (3) difficulty in arriving at a fool-proof contract with a buyer and monitoring that contract. The theory explains a firm's choice between FDI (implicitly wholly owned subsidiary) and licensing modes based on the degree of market imperfection for its knowledge.

Based on the extent of (1) ownership-, (2) internalization-, and (3) locations-specific advantages, Dunning's Eclectic theory explains three types of entry modes: export (does not distinguish between export through host country intermediary and export through company-owned channel), licensing, and wholly owned subsidiary modes. While the possession of an ownership advantage is a precursor to international operations of the firm, the
decision whether the firm would exploit the advantage itself or sell it to another firm is determined by the extent of the internalization advantage. Finally, the choice between host versus home location of production is based upon the extent of compatibility of firm’s ownership advantage with location-specific factors (Dunning 1980). This theory provides an enriched explanation of entry mode choices but falls short in tapping the complete set of entry modes.

According to the Transaction Cost (TC) theory of entry mode choice, entry modes comprise a range of governance structures bounded at one end by a market mode and at the other end by the firm itself. The choice of an entry mode is dictated by the relative efficiency of a governance structure. According to this theory, the market is the most efficient mode to perform an activity under perfect competition because of abundant availability of agents. The threat of replaceability reduces opportunism on the part of agents to a minimum. However, when sufficient amount of assets specific to a market transaction build up, the market no longer remains perfect because of the development of bilateral dependence between the firm and a specific agent. Under these conditions, market fails to perform efficiently as there is strong incentive for the agent to behave opportunistically. Therefore, a firm is better off in performing an activity by itself (Williamson 1975, 1979).
The TC theory is adept at explaining the choice between low control/low ownership and high control/high ownership modes. However, it can not explain the choice between FDI and export modes (Erramilli and Rao 1993). The TC theory is limited in explaining the complete set of entry modes.

The internalization theory and the TC theory of entry mode choice are grounded in Coase’s (1937) theory of the firm. The eclectic theory, on the other hand, has partial grounding in location theory though its foundations lie primarily in Coase’s theory. Together, these three theories comprise the Market Failure Paradigm of entry mode choice. According to this paradigm, the firm and the market are two alternative ways of performing an economic function. Under perfect competition, market is more efficient than the firm because of frictionless flow of intermediate products. When the degree of imperfection in the intermediate product markets increases, the market fails to function efficiently. Under these conditions, the firm is better off in internalizing market transactions.

Location theories consist of a plethora of ad hoc explanations of entry mode choices based on host or home country location-specific factors. These theories, like most of the theories described earlier, explain choices like the choice between a FDI and an export mode, or the choice between a FDI and a contractual mode.
In sum, none of the seven entry mode choice theories explains the complete set of entry modes; they all offer a variety of partial explanations. Therefore, the choices they predict are from incomplete rather than complete set of entry modes. In other words, these theories fail to describe both structural dimensions of entry modes in their entirety. It is shown in Chapter II that these theories are capable of explaining the first structural dimension in its entirety. However, they are unable to fully describe the ownership types relevant to the complete entry mode set. This is because these entry mode theories are founded in theories of firm that make restrictive assumptions about competition. Thus, an entry mode choice theory grounded in a theory of firm, which has relaxed assumption about competition can explain both structural dimensions in their entirety. Such a theory would be ideal for explaining a firm's choice from the complete set of entry modes.

Research Problem

The basic research question of this study is: "How does a firm choose a specific entry mode out of the complete set?" It is obvious from the above discussion that this issue is far from resolved. In fact, no attempt has been made to explain entry mode choice at such a broad and general level. The existing attempts can be described as
partial attempts at best. It would later be shown that there is a strong need for a sound theoretical framework capable of explaining the complete set of entry modes.

Purpose of the Study

The primary purpose of this study is to develop a theoretically sound comprehensive framework which can explain the complete set of entry modes: WOS, JV, CM, EXP-COMPANY, EXP-HOST INT, and EXP-IND modes. In other words, the framework should be fully capable of explaining (1) the types of host country operations and (2) the types of host country ownerships pertinent to these entry modes.

The proposed entry mode choice model is grounded in the Resource-based theory of the firm and is appropriately titled as a Resource-based Model of Entry Mode Choice. The choice of the resource-based theory is based on three considerations. First, like the IO-, the Behavioral-, and Coase’s theories of the firm, the resource-based theory can simultaneously explain the performance of both the production- and marketing-related activities. In other words, it allows the proposed model to describe the type of host country operations dimension in its entirety.

Second, unlike the earlier theories, its assumption about inter-firm competition is fully relaxed. That is, competition among firms is assumed to be dynamic rather than
static. The relaxation of this assumption allows the proposed model to explain various ownership-types pertinent to the complete set of entry modes. In short, the assumptions of the resource-based theory empower the proposed model to explain both dimensions of entry modes in their entirety and hence the entire gamut of entry modes. Finally, the resource-based theory, unlike the traditional theories of the firm, recognizes that each firm is endowed with a unique set of resources. This assumption of uniqueness of a firm allows the resource-based theory to provide a better perspective of a real world firm than the extant theories.

According to the resource-based theory, the ultimate goal of a firm is the maximization of return on its investment. The attainment of this goal is realized through persistent reaping of above normal return on the resources of the firm (Barney 1986a; Dierickx and Cool 1989). Since the above normal return accrues to a firm that has a competitive advantage over its rivals (Barney 1986b; Hirshleifer 1980; Porter 1985), persistence of above normal return necessitates the existence of a sustained competitive advantage. At the operational level, this translates into the achievement of a sustainable competitive advantage based on the firm's resources. The proposed entry mode choice model is developed within this general framework.
Scope of the Research

The proposed study is fairly broad in scope because of following three reasons. First, it is ambitious in its objective to investigate a firm's choice from the complete set of entry modes. Second, because of the highly relaxed assumption about competition in the resource-based theory of the firm, the proposed entry mode choice framework is applicable to firms of any industry structure, oligopolistic or monopolistic. Finally, the entry mode choice framework in this study is developed from the perspective of the firm. It is based on the unique resources of a firm and their ability to generate and sustain a competitive advantage for the firm. In that regard, the framework transcends across the nationality of a firm. However, in the present study, empirical testing is confined to entry mode choices of U.S. firms. Therefore, the findings of the study are expected to be generalizable across U.S firms.

The Proposed Model

As shown in figure 1, a complete set of entry modes can be described by various combinations of specific aspects of two structural dimensions: (1) type of host country operation and (2) type of ownership of host country operation. In the proposed model, the extent of a firm's
actualizability of competitive advantage in production (ACAP), actualizability of competitive advantage in marketing (ACAM), sustainability of competitive advantage in production (SCAP), and sustainability of competitive advantage in marketing-related activities (SCAM) in a host country are the four key constructs that are posited to explain the entire gamut of entry mode choices.

The term actualizability of a firm’s competitive advantage in production- and/or marketing-related activities in a host country represents the likelihood of establishing a position of superiority in the eyes of customers in producing and/or marketing of its products. The term sustainability of a firm’s competitive advantage in production- and/or marketing-related activities in a host country refers to the long term likelihood of maintaining a position of superiority in the eyes of customers in producing and/or marketing of its products.

In line with the views of Dunning (1980) and Gatignon and Anderson (1988), it is the position of this study that the entry mode choice is a sequential decision making process. Starting with the decision to locate its operation, a firm decides about the ownership of those operations. These two decisions specify the choice of its entry mode. The process is briefly described as follows. The higher the ACAP of a firm in a host country, the greater is its probability of producing products in that country.
That is, a firm has a greater likelihood to settle for a host country production mode. On the other hand, if the ACAP is low, there is greater likelihood that it will produce its products outside the host market.

It is also the position of this study that the degree of a firm’s ownership of a host country operation is related to the extent of sustainability of its competitive advantage in that country. Having settled for the location of its operations, a firm decides about the ownership of those operations. If a firm decides to serve a country through a host country production mode, then it has to determine whether to use a contractual or a FDI mode, which is an issue of ownership of host country production operation. This is determined by the degree of SCAP of a firm. If its SCAP is lower, the firm has a greater likelihood of choosing a contractual rather than a FDI mode. The primary reason being that an investment in production operation under conditions of lower SCAP is an invitation to competitive replication. Therefore, being a profit maximizer, the firm is less likely to invest under such conditions.

It is clear by now that a firm deciding to choose a FDI mode has a higher level of SCAP. Given the level of SCAP, the choice between a wholly owned subsidiary and a joint venture is determined by the degree of its SCAM. Under conditions of lower SCAM, the choice of a shared ownership mode allows the firm to buttress its competitive advantage
in the marketing operation in the host country by latching on to the strengths of its partner. On the other hand, if a firm has higher level of SCAM, it does not need a partner. Once again, it is an issue of ownership of the FDI operation. Therefore, the lower the level of a firm's SCAM, the greater the probability of its choosing a joint venture over a wholly owned subsidiary mode and vice versa.

If a firm decides to use an export mode, then depending upon its level of ACAM in a host country, the firm may serve that market through a variety of export modes. If a firm has lower level of ACAM in the host country, it is highly likely that the firm would serve the host country through an indirect export mode otherwise, it may use a direct export mode. The choice between the direct export modes is, however, based on the firm's level of SCAM in the host country. In line with the discussion for choice among host country production modes, a firm has a greater probability of choosing full ownership of host country marketing operation in export modes, if its SCAM is high. On the other hand, if its SCAM is lower, the firm may choose export through a host intermediary mode.

To sum up, the choice of all six modes can be explained by considering whether or not a firm's competitive advantage in production- and/or marketing-related activities is actualizable in a host country and whether or not this advantage is sustainable. Chapter III describes in detail
the resource-based model of entry mode choice. Meanwhile, the following material presents reasons necessitating the importance of the need of a comprehensive framework.

Significance of the Research Problem

As described earlier, this study develops a theoretical framework which is capable of answering the question: "How does a firm choose a specific entry mode from a complete set of entry modes?" The following material offers some key reasons underlying the managerial and theoretical importance of the development of a comprehensive framework.

Managerial Significance of the Problem

Entry mode choice is a vital decision for managers. The importance of the decision stems from three reasons. First, depending upon the choice of an entry mode, a firm may have to engage in substantial long term investment of human, financial, capital, and technological resources. Second, some of the investment in an entry mode may be in assets which are specific to undertaking a given program in a country. In case a firm has to divest out of that market, it would incur huge losses because of the high cost of redeploying such assets (Teece 1980). Finally, firms face more competition from foreign firms now than they did a
decade ago (Ghemawat 1986). This is because of convergence of standards on product quality and cost (Prahalad and Hamel 1990). In short, an entry mode choice decision has serious strategic implications for a firm’s resources and its position vis-a-vis its competitors. A firm making a wrong choice ends up with a strategic blunder and may be left behind in tough competitive conditions.

With its strategic importance, how can it be rationalized that a piece-meal fashion of entry mode choice would produce optimal results for the firm. Managers are obviously expected to look into pros and cons of each major entry mode categories before choosing the one which has the promise of producing the maximum risk-adjusted ROI for their firms (Anderson and Gatignon 1986). According to Chase and Aquilano (1986), in order to arrive at an optimal decision, a firm has to consider all possible alternatives pertinent to the decision. Thus, in order to explain the entry mode choice of a firm, it is extremely necessary to develop a framework that is comprehensive enough to capture the phenomenon. Piece-meal approaches are therefore inappropriate. Moreover, only a comprehensive framework can potentially enable managers to choose the most relevant entry mode from a complete set of entry modes. Due to its high importance to managerial decision making, obviously, a comprehensive framework has greater theoretical implications for academic researchers.
Theoretical Significance of the Problem

There are four key reasons that emphasize the theoretical importance of a comprehensive framework of entry mode choice. First, a comprehensive understanding of entry mode choice is necessary for the development of a coherent theory of international operations of the firm. This is because the choice of an entry mode is an integral part of a firm's international operations (Root 1987). Unless, this choice is comprehensively understood, it would not be possible to develop a coherent theory of international operations of the firm. Second, at present, the entry mode literature is riddled with partial explanations of entry mode choices but none that can explain all choices in one framework. One positive outcome of such proliferation is an enriched understanding of the phenomenon. However, it has resulted in wastage of intellectual efforts because many of these explanations are overlapping. The development of a comprehensive framework will not only minimize such wasteful exercises but would also enable researchers to build bridges across the extant partial explanations.

Third, international trade and investment have grown enormously in the past three decades. They have become significant part of GDPs (Gross Domestic Product) of most countries, advanced or developing. Therefore, entry mode choice can no longer be treated as an ad hoc decision of a
firm. Rather than analyzing in piece-meal fashion, there is an academic need to develop a theoretical framework that can systematically explain a complete set of entry modes.

Finally, theory-related issues are inseparable from managerially-related concerns, though often erroneously considered in isolation from one another (Hunt 1991, p. 151). A sound theoretic construction allows managers to base their decisions on scientific generalizations, the absence of which can only lead to "voodoo" decisions. In other words, the objective of a coherent theory construction is to ultimately assist managers make optimal choices from a set of determinants. In that regard, a comprehensive framework proposed in this study is a step toward the development of a sound theory of entry mode choice of the firm, which in turn would generate robust normative implications for managerial decision making.

In summarizing the above discussion on the importance of the research problem addressed in this study, it is clear both from managerial as well as theoretical perspectives, that the development of a comprehensive entry mode choice framework is of utmost necessity. Furthermore, such a framework should be theoretically sound for future theory construction and useful to managers so that they can make appropriate choices for their respective firms. Having established the importance of a comprehensive framework, the following material justifies the research in this topic.
Justification of the Research

The following reasons justify expending of research efforts on analyzing entry mode choice of the firm. First, as described earlier, thorough understanding of entry mode choice behavior is critical to the (1) building of a sound theory of international operations of the firm and (2) development of a managerially useful framework. Second, many leading scholars have emphasized the importance of the entry mode choice issue. For example, Anderson and Coughlan (1987) refer to entry mode choice as a difficult issue whose impact on the success of the firm is great. Wind and Perlmutter (1977) designate it as a "frontier issue" of international marketing. Third, the importance of a study of entry mode choice can also be gauged from the fact that within the past three decades, at least seven different theories were proposed in the U.S., Great Britain, and Sweden and a number of empirical studies published to explain the phenomenon. However, a comprehensive knowledge of the phenomenon is still eluding the researchers.

Finally, it is the position of this study that the knowledge resulting from research on entry mode choice can be used as a potent tool to assess competitors' marketing strategies (regarding product, pricing, promotion, and distribution) in a host country. This position becomes clear from the following discussion. For example, Kacker
(1975) observes that firms serving host markets through exporting are more likely to engage in selling uniform products rather than modifying them. Similarly, firms selling products requiring extensive after-sales service are likely to use sales subsidiary (Anderson and Coughlan 1987) and wholly owned subsidiary operations (Terpstra 1987). This is because distributors' service efforts often fall short of firm's expectations. Moreover, firm-conducted service operations provide closer contact with customers for future sales (Terpstra 1987). Likewise, a firm choosing wholly owned mode has greater flexibility in expanding or deleting its product line than if it chooses joint venture or licensing modes (Contractor 1984). In short, the choice of an entry mode sheds considerable light on the product strategy of a firm.

A firm's entry mode choice has also considerable influence on its host market pricing strategy. Terpstra (1987) and Onkvisit and Shaw (1989) suggest that a firm operating through export modes uses export pricing strategy—a strategy which incorporates cost of transportation, documentation, import duties, and insurance etc. On the other hand, a firm operating through subsidiaries, joint venture and licensing modes generally uses transfer price policy (rate charged when sale is made among members of a corporate family). Also, it appears that there is a strong relationship between host market promotion policy of a firm
and its entry mode choice. The empirical studies of Anderson and Coughlan (1987), Fagre and Wells (1982), and Tomlinson (1970) support the notion that firms engaging in product differentiation through heavy advertising prefer wholly owned entry modes over shared modes. Lastly, of the four marketing strategies, the host market distribution policy of a firm appears to be most influenced by the entry mode choice. The reason being that a host country entry mode choice is, in fact, the distribution policy of a firm in that country.

Based on the above discussion, it appears that there is a relationship between a firm’s entry mode choice and its host country marketing program. In other words, the specification of a firm’s entry mode choice, to a significant extent, explains its current and potential level of marketing mix. Therefore, research on entry mode choice of firms can be used as an analytical tool to assess competitors’ existing and future marketing strategies.

In summarizing the above description, it can be stated that a research in comprehensive analysis of the entry mode choice phenomenon is highly justified. This is because, it (1) is highly significant for managers and academicians, (2) is a major issue in the views of many leading scholars, and (3) it can lead to the development of an important tool in competitor analysis.
Contributions of the Proposed Framework

The proposed entry mode choice framework is expected to make a substantive contribution to the construction of a sound theory of international operations of the firm as well as to better managerial decision making.

Contribution to Theory Construction

Beginning with Hymer's work, number of attempts have been made at developing a theory of international entry mode choice of the firm. These include the works of Agarwal and Ramaswami (1992), Anderson and Gatignon (1986), Buckley and Casson (1976), Dunning (1980), Erramilli and Rao (1993), Knickerbocker (1973), Johanson and Vahlne (1977), and Vernon (1966). These studies have made significant contributions to the understanding of the entry mode choice phenomenon. Still, as described earlier, none could explain the complete set of entry modes in a single framework. In other words, these theories lag behind the practice of entry mode choice.

The proposed framework attempts to fill this gap between theory and the practice. In this respect, this study is expected to provide a framework consistent with the breadth of the phenomenon. This, in turn, would provide another stepping stone in the construction of a sound theory of international operations of the firm. Furthermore, this
framework is based on the resource-based theory of the firm, and is the first of its kind that applies this theory to a comprehensive analysis of entry mode choice of the firm. The results of this study would, in turn, provide an important empirical corroboration of the applicability of the resource-based theory in the international context.

Contribution to the Practice

The proposed framework makes two important contributions to managerial decision making. First, the framework is decision-oriented. It explains decisions based on managerial analysis of firm-specific resources and host market conditions and the ability of these resources to generate and sustain a competitive advantage in a host country. Therefore, its implementability in decision making does not involve problems found in many of the extant theoretically abstract frameworks. The second contribution of this framework is that it provide a comprehensive decision table, which can facilitate managers in their choice of an appropriate entry mode.

Summary of Chapter I

This chapter pointed out a key problem in the extant literature regarding the explanation of entry mode choice of
the firm. Furthermore, it argued about the importance of the problem and the rationale for the development of a comprehensive framework to resolve the problem. The chapter provided the purpose, the scope, and the justification of the proposed study. In doing so, it laid the foundation for the subsequent chapters of this dissertation. The next chapter provides an exhaustive description of the extant literature on the entry mode choice of the firm. At the end of Chapter II, a case is made for the development of a comprehensive entry mode choice framework founded in the resource-based theory of the firm.

Chapter III includes the development of the proposed framework. Hypotheses are generated for testing the efficacy of the entry mode choice model for U.S. firms. This chapter includes the methodology used in carrying out the empirical testing of the proposed entry mode choice framework. The data analysis and testing of hypotheses is done in Chapter IV. Finally, Chapter V discusses the results and describes the reflections, implications, limitations, and the directions for future research emerging from this study.
CHAPTER II

LITERATURE REVIEW

Introduction

This chapter comprises two sections. The first section is devoted to an extensive analysis of research on entry mode choice behavior of the firm. It includes a comprehensive review of the extant entry mode choice theories. At the end of this review, an overall assessment of the entry mode literature is presented. It is argued that the extant theories are unable to explain the complete set of entry modes because of the restrictive assumptions underlying their theoretical frameworks.

At the end of section I, a case is made for the need of a new theoretical framework to explain the complete set of entry modes. It is argued that an entry mode choice model founded in the framework of resource-based theory of the firm can explain the complete set. Section II is devoted to the necessary groundwork for the development of the proposed model. It includes a detailed description of the resource-based theory of the firm in terms of its (1) assumptions, (2) resources, (3) conceptualization of the firm, (4) competition, and (5) mechanism of achievement of long term profit maximization.
Section I: A Review of Entry Mode Choice Theories

At least seven different theories have been proposed to analyze how firms choose between different entry mode alternatives. These include Hymer’s theory (1976), PLC theory (1966), Internationalization theory (1975), Internalization theory (1976), Dunning’s eclectic theory (1980), Transaction Cost theory (1986), and an assortment of location-based explanations (also referred to as location theories). Except for the location theories, other entry mode theories are grounded in specific theoretical frameworks of the firm. The location theories constitute ad hoc explanations of entry mode choice based on locational factors. Accordingly, they do not constitute any single specifiable theoretical framework.

Hymer’s theory and the PLC theory belong to the IO-based market imperfection paradigm which evolved from Bain’s (1956) Industrial Organizational (IO) theory of the firm. Likewise, the internationalization theory belongs to the behavioral paradigm because of its foundation in Cyert and March’s (1963) Behavioral theory of the firm. The internalization theory, Dunning’s theory and the transaction cost theory comprise the market failure paradigm; they are founded in Coase’s (1937) theory of the firm. Finally, the location theories may be considered to belong to the environment paradigm. Thus, the seven entry mode theories
belong to four paradigms: IO-based market imperfection, behavioral, market failure, and environment paradigms.

There is a shift in the underlying paradigm as one goes from earlier theories (e.g., Hymer's theory) to later ones (e.g., TC theory). Chronologically speaking, it can be inferred that market imperfection was the dominant paradigm of sixties and early seventies and behavioral paradigm of seventies. The market failure paradigm appears to have dominated during the period extending from late seventies until now. The environment paradigm appears to be scattered randomly over the past three decades.

The following material provides a detailed analysis of seven theories under their respective paradigms. The discussion of each entry mode theory includes (a) an identification of the range of entry mode choices explained by it, (b) its theoretical perspective--assumptions, principal explanatory constructs, and their relationships with entry mode choice, (c) empirical evidence, and (d) evaluation of strengths and weaknesses of the theory.

**IO-based Market Imperfection Paradigm**

The IO-based market imperfection paradigm stems from Bain's IO theory of the firm according to which, industries with fewer competitors and higher entry barriers reap above normal returns (Barney 1986c; Porter 1980). In other words,
Bain’s theory assumes that (1) competition among firms of an industry is imperfect and (2) the maintenance of status quo or constancy of such competition is essential for continuous reaping of above normal return on investment (ROI).

According to the IO-based framework, firms create imperfect markets by controlling the number of existing and potential competitors. This is done in two ways. In the first way, they reduce the number of existing competitors by engaging in mergers/acquisitions, or by contractual binding of other firms. In the second way, firms reduce the number of potential competitors by building higher entry barriers through heavy investment in capital-intensive production processes or in differentiation of products (Caves 1980; Porter 1980). In either way, firms create less uncertain competitive environment, maintain status quo of competition among few firms, enjoy greater market power, control output and price, and hence reap above normal ROI (Bain 1956; Barney 1986c). In short, firms attempt to control markets by engaging in practices that reduce the number of rivals.

Hymer’s theory and PLC theory explain a firm’s entry mode choice within this framework. The tendency of a firm to close markets at home is carried to foreign markets as well (Hymer 1976; Vernon 1966). In its entry mode choice, the firm chooses modes that either remove existing foreign competitors or minimize the possibility of new competitors entering the market.
Hymer’s Theory of International Operations

Hymer’s theory of international operations of the firm emerged from his doctoral dissertation (written in 1960, published in 1976) on FDI operations of U.S. firms. According to the theory, a firm having monopolistic advantage in product markets (for example, brand loyalty) or in factor markets (ability to customize products), or both has an incentive to engage in international operations. This advantage creates certain degree of market imperfection in a host country (Kindleberger 1969). Under such conditions, an entry mode that allows a firm to more completely appropriate rent on its advantage is chosen. The term 'rent' implies return on investment (ROI). Some key works published on Hymer’s theory are those of Gruber, Mehta, and Vernon (1967), Horst (1972), Kim and Lyn (1990), Kindleberger (1969), Knickerbocker (1973), and Lall (1980).

Entry Mode Set

Hymer’s theory explains the choice between two types of entry modes: FDI and licensing.

Theoretical Perspective of Hymer’s Theory

Basic Assumptions: The main assumptions of Hymer’s theory are as follows:

1. The possession of a monopolistic advantage is a prerequisite for a firm’s foreign operations.
2. Market for a firm’s advantage is imperfect.

3. Above normal return on a firm’s investment depends upon the reduction of its competition.

**Explanatory Constructs:** "Monopolistic Advantage" of the firm and the degree of "Market Imperfection" are two main constructs of Hymer’s theory. "Monopolistic Advantage" of the firm pertains to an advantage that no host country firm has, or can acquire, and is transferable from the home to the host country (Kindleberger 1969). Also, the advantage should be sufficiently strong to outweigh any potential disadvantages arising from host country operation such as cost of gathering market-related information (Hymer 1976).

The firm may have such an advantage in production or in distribution of goods (Hymer 1976; Kindleberger 1969).

"Market Imperfection" for the firm’s advantage means limited number of buyers of its advantage. This may stem from conditions like existence of small number of buyers, their difficulty in the evaluation of advantage, and inability of contracting parties to arrive at a satisfactory contract.

**Entry Mode Choice Mechanism:** According to Hymer, the higher the degree of market imperfection, lower the probability that the owner may be able to appropriate full rents from its advantage by licensing it. Hymer argues that when there are fewer buyers in a host country, licensing may create problems of sequential monopoly. Sequential monopoly is a situation where a licensor may lose control over its licensee’s output and pricing activities, thereby creating a
potential competitor and hence jeopardizing its full appropriation of rents. As a result, the firm internalizes the advantage. This not only allows the firm to fully appropriate rent on its advantage but helps avoid the emergence of a potential competitor as well.

However, if there are many buyers of a firm's advantage in a country, licensing becomes more attractive (Hymer 1976). This is because with greater number of buyers, there are fewer sequential monopoly problems, better evaluation of advantage, and hence fuller appropriation of returns on the advantage. Another reason for choosing licensing may be a host government’s policy favoring licensing over FDI modes. If markets are divided due to tariffs and transportation costs, licensing may again be a better choice (Hymer 1976).

**Empirical Support**

Hymer's theory has found considerable empirical support. His contention that a firm's possession of an advantage is an essential prerequisite to its foreign operation finds overwhelming support in a number of studies. For example, Miller and Weigel (1972), studying U.S firms' investments in Brazil, found that investing firms had advantage over local firms either in the form of R&D intensity or capital intensity prior to their entry in that country. Lall (1980) reported that product differentiation advantage of U.S. industries appears to promote their
foreign direct investments. Similarly, Gruber, Mehta, and Vernon (1967) found that foreign direct investment is higher in research intensive U.S. industries.

**Strength and Weaknesses of Hymer's Theory**

**Entry Modes:** Hymer's discussion on entry modes is primarily confined to the choice between FDI and licensing modes only. Within FDI modes, the theory does not distinguish between wholly owned subsidiary and joint venture modes. As already stated, the explanation of the choice of FDI mode does not necessarily imply the explanation of the choice of joint venture mode as well. Furthermore, the theory does not address indirect export, export through company owned channel, or export through host country intermediaries. Thus, it provides only a partial explanation of the complete entry mode set.

**Theoretical Perspective:** Prior to Hymer's theory, foreign direct investment was regarded as a firm's investment in a diversified portfolio of assets. The theory convincingly argued for treating FDI as an industrial organizational phenomenon rather than an issue of portfolio of investments. An important outcome of Hymer's argument is that FDI theories following his work shied away from the portfolio investment paradigm. Hymer's work is credited to have set the trend for the theories of Dunning (1980) and Vernon (1966). However, one key problem with Hymer's theory
is that it takes a static view of the firm’s advantage. In reality, the firm’s advantage erodes over time as more competitors enter into the market (Vernon 1966). This puts the theory at a disadvantage in its ability to explain the entry mode choices of the firm under changing conditions.

**Entry Mode Choice Mechanism:** The primary consideration in Hymer’s mechanism for choice between FDI and licensing modes is the degree of market imperfection. Since market imperfections can stem from any number of reasons in goods or factor markets (Kindleberger 1969), Hymer’s theory can explain the firm’s choice between FDI and licensing modes for a variety of reasons. The market imperfection argument, thus, increases the generality of Hymer’s entry mode choice mechanism and is one of the reasons for its continuous deployment in many entry mode theories. For example, market imperfections stemming from the inability of foreign producers to absorb the technically complex knowledge of U.S. firms is the basis of the market failure paradigm of entry mode choice developed by Anderson and Gatignon (1986), Buckley and Casson (1976), Hennart (1988), and Teece (1980).

**Relevance of the Theory:** Hymer’s concept of firm’s advantage has been extensively used by many researchers including Buckley and Casson (1976), Knickerbocker (1973), and Teece (1980) among others in explaining entry mode choices of the firm. The theory, however, suffers from following limitations besides offering partial explanation
of entry mode choices of the firm. As already mentioned, one problem with Hymer’s theory is that it assumes a static view of the firm’s advantage. Another limitation of the theory is its range of applicability; the theory may not be applicable to firms in industries with perfect or monopolistic types of competition.

In sum, Hymer’s theory has made a great contribution to the entry mode literature by spawning other theories like those of Knickerbocker’s (1973) and Vernon’s (1966). Its concepts of "advantage" and "market imperfection" have furnished important tools to analyze the entry mode choice issue. However, in its current form, Hymer’s theory has limited ability to address the choice of an entry mode from the complete set of entry modes.

Product Life Cycle Theory

According to the PLC theory, during the earlier stages of life cycle of a product, a firm continues to satisfy demand for its product from a foreign country through export and establishes its competitive position in that market. However, the competitive advantage of the firm in that market may deteriorate with time as its product enters later stages of life cycle thereby, threatening its competitive position in that market. When this happens, the firm shifts from export to FDI mode to maintain its position in that
market. In short, the PLC theory explains the entry mode choice of a firm as a function of the life cycle stage of its products.

**Entry Mode Set**

The PLC theory explains a firm’s choice between two types of entry modes: FDI and export modes.

**Theoretical Perspective of the PLC Theory**

**Basic Assumptions:** The key assumptions of the PLC theory are as follows:

1. Home country firms have advantage over firms from other countries in knowing about the opportunities in their market because the information flow across national boundaries is not cost-free (Vernon 1966).

2. Products undergo changes in their production and marketing characteristics over their life cycles (Wells 1972).

3. Firms adopt FDI operations in foreign markets only when their existing competitive positions in those markets are threatened by local producers or their domestic competitors (Vernon 1966).

**Explanatory Constructs:** The key construct that explains the entry mode choice under the PLC theory is the life cycle stage of the product. The PLC theory recognizes three chronological stages in the life cycle of a product: the Innovation stage, the Maturity stage, and the Standardized stage (Vernon 1966). As a product moves from the first stage to the subsequent stages, its inputs, production process, and specifications become increasingly
standardized. Along with the product life cycle evolution, the extent of competition faced by the firm in the host market increases as well.

**Entry Mode Choice Mechanism**: According to the PLC theory, during the innovation stage, manufacturers locate production facilities in their domestic country because of four reasons. First, they have greater awareness of home market opportunities. Second, there is greater need for feedback about product performance. Third, they have monopolistic pricing advantage due to low price elasticity of demand for their products. Finally, they have fewer degrees of freedom in their choice of production location due to lack of standardization of products, processes of production, inputs, and the specifications (Vernon 1966). Under these conditions firms satisfy any foreign demand for their products (usually from other advanced countries) through exporting only.

As the product enters the maturity stage of its life cycle, some host country competitors, motivated by higher profit potential, start producing substitutes of the exporting firm's product. The exporting firm perceives it as a threat to its market share. Vernon (1966) contends that this threat is important enough to motivate the exporting firm to locate its production facility in the host market. Further impetus for shifting the production facility to the target host market is provided by the higher
degree of standardization of the product, its specifications, process, and inputs during the maturity stage.

Empirical Support

If the predictions of the PLC theory are true, then companies should export products that are in the early stages of their life cycles and gradually shift to foreign production in later stages. Most empirical studies demonstrate that the exports of products tend to be greater in the early stages of their life cycle than during the later stages. For example, Hirsch (1972) observes that exports of many U.S. electronic products are more competitive in the growth stage than in the maturity stage of their life cycle. Wells (1969) finds that exports of U.S. made consumer durables for high income consumers are greater for newer than for older versions. Similar results are reported in Stobaugh’s (1971) study on proliferation of petrochemical plants and in Poh’s (1987) study on export performance of UK electronics industry. These studies, however, fail to show a gradual tradeoff, over time, between the sales volume through export to sales volume through foreign production. Thus, the empirical support for the predictions of the Product life cycle theory is partial at best.
Strengths and Weaknesses of the PLC Theory

Entry Modes: The theory explains only two types of entry modes: FDI and export modes. Like Hymer's theory, it does not distinguish between a wholly owned subsidiary and a joint venture. Furthermore, within export modes, the theory does not discriminate between indirect export, export through company owned channel, and export through host country intermediary modes. Also, the theory does not explain the contractual type of mode. Consequently, the theory only partially addresses the entry mode choice set.

Theoretical Perspective: The PLC theory is based on the existence of market imperfections across nations. A firm in a country builds its competitive advantage based on the availability of location-specific factors. This advantage later becomes a vehicle for its international operations through export (Vernon 1966). Finally, the firm moves its production operations to foreign markets to maintain its competitive positions in those markets.

The PLC theory recognizes the erosion of a firm's competitive advantage with time due to emergence of new competitors (the host country firms). This is an important advancement over Hymer's assumption about the static nature of the firm's advantage. However, in line with the spirit of the IO-based market imperfection school, the firm reacts to maintain the constancy of competition when its advantage is threatened. The firm engages in FDI to deter
competitors. Like Hymer's theory, the PLC theory is also restricted in its range of applicability to oligopolistic industries only.

**Entry Mode Choice Mechanism:** The entry mode choice mechanism is based on the life cycle stage of a product, which is determined by the sales volume. Such a view is regarded as tautological (Hunt 1991; Tellis and Crawford 1981), because it is difficult to understand whether a product becomes mature due to the stagnation of its sales volume or vice versa. Although intuitively appealing, the testability of the PLC mechanism of entry mode choice is questionable because of the ambiguity whether a life cycle stage is a dependent or an independent variable. On the other hand, the theory's explicit recognition of competition in the firm's entry mode choice is an important contribution to the entry mode literature.

**Relevance of the Theory:** The essence of PLC theory has been used by Knickerbocker (1973) to explain the genesis of oligopolistic structure in certain U.S. industries engaged in FDI operations. The theory is also intuitively appealing because the PLC concept is analogous to the "cradle to grave" human experience.

The theory has made at least one important contribution to the understanding of the entry mode choice phenomenon; it considers the dynamic nature of a firm's competitive advantage. Despite this contribution, the PLC theory has
limited relevance to be potentially pursued as a theory of entry mode choice for a number of reasons. First and foremost, the theory fails to meet the testability criterion, as already explained. The empirical verifiability of the phenomenon is further made difficult by marketers' actions to either prolong or accelerate a stage by a variety of techniques (e.g., promotion). That is, the life cycle stage is artifactual rather than being a positive phenomenon. Second, the PLC theory may have poor contemporary relevance because MNEs introduce products in many markets simultaneously (Giddy 1978). This is in contrast to Vernon's (1966) explanation of the FDI behavior of U.S. manufacturing firms in the post World War II period. Third, the life cycle stages may be more compressed due to the increased rate of new product introduction in the current time than in the sixties or seventies, the period of PLC theory generation. Fourth, the empirical studies that find support for the PLC theory use trade data of sixties and seventies. This raises doubts about the validity of the results in current times. Finally and more importantly, the PLC theory only partially explains entry mode choices.

In sum, the PLC theory has made significant contributions to the understanding of entry mode choices of the firm. However, in its current form the theory has a number of conceptual flaws and more importantly, it is unable to explain the complete set of entry modes.
Summary of IO-based Market Imperfection Theories

The theories of Hymer and Vernon are based on Bain's IO view of the firm which assumes that firms create market imperfection, maintaining of the status quo of which is central to their above normal profits. There are, however, two important differences among these theories. First, Hymer's theory deals with offensive type of foreign investment, whereas Vernon's theory discusses both defensive and offensive types of foreign direct investment. Second, Hymer's theory takes static view of firm's competitive advantage whereas Vernon's theory takes a dynamic view.

The IO-based market imperfection theories have made several contributions to the entry mode literature. First, they caused a paradigmatic shift from treating the foreign direct investment issue as part of a diversified portfolio of a firm to considering it as an industrial organization problem. Second, they emphasized firm-specific advantage to be a necessary condition for international operations of the firm. Finally, these theories show the importance of competition in the firm's entry mode decision. However, they do not explain the complete set of entry modes. Table 1 summarizes the two IO-based market imperfection theories on following attributes: explanatory constructs, range of entry modes explained, and their empirical support.
**TABLE 1**

**IO-BASED MARKET IMPERFECTION THEORIES**

<table>
<thead>
<tr>
<th>Theory</th>
<th>Explanatory Constructs</th>
<th>Range of Entry modes choices explained</th>
<th>Empirical support</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hymer's</td>
<td>Monopolistic Advantage and Degree of Market Imperfection</td>
<td>FDI mode is chosen if the degree of Market Imperfection for the firm's Monopolistic Advantage is higher</td>
<td>Gruber, Mehta, and Vernon (1967); Hymer (1976); Lall (1980); Miller and Weigel (1972).</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Licensing mode is chosen if the degree of Market Imperfection for the firm's Monopolistic Advantage is lower</td>
<td></td>
</tr>
<tr>
<td>PLC</td>
<td>Life cycle stage of the product</td>
<td>Export mode is chosen if the firm's product is in the innovation stage of its life cycle</td>
<td>Hirsch (1972); Poh (1987); Stobaugh (1971); Wells (1969).</td>
</tr>
<tr>
<td></td>
<td></td>
<td>FDI mode is chosen if the firm's product is in the Maturity or the Standardized stage of its life cycle</td>
<td></td>
</tr>
</tbody>
</table>
Behavioral Paradigm

The firm, according to the behavioral theory, operates in imperfect markets (Cyert and March 1963, p.115). The key basis of market imperfection is the lack of perfect information about market. A firm's market knowledge grows gradually over time because of (1) high cost of information acquisition and (2) bounded rationality of its managers. Under such a type of market imperfection, the firm is assumed to be short term oriented, risk averse, and settles for satisficing rather than maximizing profit (Cyert and March 1963). The firm is assumed to exhibit incremental changes in its behavior and abstain from actions that require substantial amount of resource commitment. The Internationalization theory is grounded in this framework.

Internationalization Theory

The term "internationalization" is used to describe the gradual, incremental pattern of a firm's expansion into international markets. During seventies, researchers from Uppsala School (Johanson and Widersheim-Paul 1975; Johanson and Vahlne 1977) proposed the internationalization theory to explain how firms get involved in international operations and make resource commitments to foreign markets. While the theory has been utilized to explain market selection
(Johanson and Vahlne 1977; Davidson 1980a; Erramilli 1991), its role in explaining entry mode choice is of primary interest here.

**Entry Mode Set**

The Uppsala School's model explains four types of modes: no regular export (indirect export), export via independent representative/agent (export through host country intermediary), sales subsidiary (export through company-owned channel), and wholly owned subsidiary. These modes comprise the "establishment chain" and differ from each other in terms of their level of "market commitment." Market commitment is measured by the size of resources required to set up and operate a mode and the extent to which these resources are tied to a specific market. In the indirect export stage, the firm has no resource commitment to the host market whereas resource commitment is maximum at the wholly owned subsidiary stage. The thrust of the model is to explain how a firm moves from the "no regular export" stage to the wholly owned subsidiary stage.

**Theoretical Framework**

**Basic Assumptions:** The main assumptions of the theory are as follows:

1. Decision making is not entirely "rational." Managers lack the ability, willingness and the information needed to make perfectly rational decisions.
2. The decision to commit resources to foreign markets is not the result of a strategy for optimal allocation of resources in which alternative ways of exploiting foreign markets are compared and evaluated.

3. Decision-makers are averse to risk and uncertainty. They are assumed to be reactive rather than proactive.

4. The decision-maker is seen as trying to achieve multitudinous goals by negotiating with fellow participants in the organization; he/she is viewed as being more concerned with "satisficing" rather than with maximizing (Aharoni 1966, p. 30).

Explanatory Constructs: Two constructs are central to the internationalization theory. One of them is "market commitment," which has been explained earlier. The other is "market uncertainty." According to Johanson and Vahlne (1977) market uncertainty is "the decision-makers' perceived lack of ability to estimate the present and future market and market-influencing factors." (p. 29) They assert that market uncertainty occurs primarily because of lack of experiential knowledge about the supply, demand, competition and distribution channels etc of a market. This uncertainty in turn influences internationalization decisions. Johanson and Vahlne define experiential knowledge as the knowledge gained through personal experience in a foreign operation.

Entry Mode Choice Mechanism: According to this theory, a firm sells its products to foreign markets through trading companies prior to its direct entry in those market. It has no regular information channel to any foreign country and hence no resource commitment to any foreign market.
However, when a firm directly enters a foreign market for the first time, it lacks adequate market-specific experiential knowledge. As such, it perceives a high level of market uncertainty. Being essentially risk averse, the firm initially makes a minimal level of market commitment.

The initial operations in the foreign market enable the firm to gain valuable experiential knowledge which leads to a decline in perceived market uncertainty. The lower level of uncertainty result in the firm’s decision-makers becoming more self-confident and aggressive. If opportunities exist for expansion and the firm seeks growth, the firm increases its market commitment by a small amount. This leads to further opportunities for gaining experiential knowledge, resulting in additional decline in uncertainty, which in turn leads to greater market commitment. The process continues in this fashion.

This theory does recognize certain conditions under which exceptions to the establishment chain may occur. For example, the firm may choose higher market commitment modes at the time of entry if the host market is very large, since lower resource commitment modes may be insufficient to meet market demands (Johanson and Wiedersheim-Paul 1975). Firms may not span the entire establishment chain when markets are too small to justify additional resource commitment. Furthermore, there may be jumps in the chain facilitated by the extensiveness of the firm’s international experience.
Empirical Support

In their investigation of the internationalization process in Swedish firms, Johanson and Wiedersheim-Paul (1975) found significant support for the establishment chain. Bilkey and Tesar (1977), Bilkey (1978), and Cavusgil (1984) too find support for this multi-stage model of resource commitment among U.S. exporters. Denis and Depelteau (1985) report that information gathering activities such as participation in fairs and foreign missions seemed to have a powerful effect on export expansion among Canadian firms--especially at the beginning of the export process. In an investigation of UK manufacturing firms, Millington and Bayliss (1990), report that firms significantly rely on market experience and incremental adjustments in their internationalization process, although only in the early stages.

Not all studies have corroborated the predictions of internationalization theory. Sharma and Johanson (1987) report that international expansion patterns of Swedish Technical Consultancy (TC) firms do not conform to the Uppsala model. Erramilli (1991) found that as the international experience of service firms increased, their desire for control followed a U-shaped pattern rather than an upward sloping curve as expected by the theory. In sum, the empirical support for the theory is partial at best.
Strengths and Weaknesses of Internationalization Theory

Entry Modes: The strength of the theory lies in its dynamic view of entry mode choice. It is perhaps the only theory equipped to allow longitudinal investigation of a firm's entry and expansion in a foreign market. However, the theory does not explain contractual and joint venture entry modes.

Theoretical Perspective: The core ideas of internationalization theory flow from the behavioral theory of firm. As such, it enjoys strengths and suffers from weaknesses characterizing the behavioral approach. The traditional economic theories generally assume the firm to exhibit perfectly rational behavior, cost-free nature of information, profit maximization etc. By relaxing these often unrealistic assumptions, the behavioral theory has produced a framework that is a more realistic reflection of the firm's decision process. At the same time, it suffers from a serious shortcoming. For example, the theory assumes imperfect markets but does not take into consideration any specific type of inter-firm competitive behavior associated with imperfect markets like that in IO theory and Coase's theory of the firm. Firms rarely make decisions without considering such aspects.

Entry Mode Choice Mechanism: The internationalization theory describes a simple mechanism for choosing entry modes. The idea that firms make resource commitments in
gradual increments rather than in spectacular strides (Cavusgil 1984) in order to cope with uncertainty appears to be consistent with the findings of a number of studies. However, as Johanson and Vahlne (1977) acknowledge, there are many exceptions to the pattern outlined by the establishment chain. Moreover, reduction of uncertainty may be only one of the forces driving entry mode choice. The theory does not provide a mechanism by which other factors could be taken into consideration. An even more serious limitation is that the central constructs (market uncertainty and market commitment) have not been adequately defined and operationalized. This has made any kind of elaborate empirical testing of the theory infeasible. In short, rigor and formalization are lacking.

Relevance of the Theory: The theory has probably outlived its usefulness. The following conditions must hold for the theory to be truly relevant: (1) slow rate of technological changes, (2) insubstitutability of country-specific experiential knowledge, (3) lack of international competition, and (4) poor inter-market communication. Since, such assumptions seem to be unrealistic in the current time frame, the theory may have little relevance to existing as well as future conditions. Table 2 summarizes the Internationalization theory on three characteristics: explanatory constructs, range of entry mode choices explained, and the empirical support for the theory.
### TABLE 2
INTERNATIONALIZATION THEORY

<table>
<thead>
<tr>
<th>Theory</th>
<th>Explanatory Constructs</th>
<th>Range of Entry mode choices explained</th>
<th>Empirical support</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internationalization</td>
<td>Market Commitment and Market Uncertainty</td>
<td>The theory explains four types of entry modes: Indirect export, Export via independent representatives/agents, sales subsidiary, and wholly owned subsidiary. The Firm enters into international market with indirect export mode and moves successively to independent representative/agent mode, sales subsidiary mode, and wholly owned subsidiary mode with the reduction of market uncertainty.</td>
<td>Bilkey (1977); Bilkey and Tesar (1977); Cavusgil (1984); Denis and Depelteau (1985); Johanson and Wiedersheim-Paul (1975); Millington and Bayliss (1990); Sharma and Johanson (1990).</td>
</tr>
</tbody>
</table>
Market Failure Paradigm

The market failure paradigm evolved from Coase's (1937) theory of the firm according to which, the firm and market are two alternative modes for efficiently accomplishing an economic function at a location. The choice of one mode over the other is based upon its relative efficiency, which, in turn depends upon the type of competition. The theory assumes two forms of competitive environments of a firm: (1) perfect competition and (2) imperfect competition. Under perfect competition, market mode is more efficient than the firm. The reason being that there are several firms in the market willing to work for the firm at the going rate. However, when market becomes imperfect, the cost of market transactions becomes extremely high. The market is said to have failed to efficiently perform economic activities for the firm. Under these conditions, a firm is better off in performing the function by itself (Coase 1937).

The internalization theory, the eclectic theory, and the transaction cost theory of entry mode choice are grounded in Coase’s (1937) theory of the firm; the eclectic theory has partial grounding in the location theory as well. Together, these three theories constitute market failure paradigm. The mechanism of market failure is similar in the internalization theory and the eclectic theory. However, the mechanism of market failure for the TC theory is
slightly different from the other two. For example, in the internalization theory, market failure is anticipated prior to the occurrence of a transaction between the firm and an agent. This happens when the firm finds limited number of buyers for its firm-specific knowledge. Under the TC theory, the market failure is expected to occur after the commencement of a transaction with a market agent. This agent becomes irreplaceable over time because of the sufficient build up of transaction-specific assets. The internalization-, eclectic-, and TC- theories explain entry mode choice of the firm within this framework.

Internalization Theory

The internalization theory emerged from Buckley and Casson's (1976) attempt to explain the growth of American and British multinational firms in the post World War II era. According to this theory, MNEs grow by internalizing international markets for intermediate products. The intermediate product markets include among others, markets for semi-finished goods, firm-specific knowledge, skills, and technology. The theory, however, concentrates upon the internalization of intermediate market for knowledge. In the context of entry mode choice, the theory generates conditions that create strong incentive for a firm to choose a wholly owned subsidiary over licensing mode. Most of the
contribution to the internalization literature has come from Buckley and Casson (1976), Calvet (1982), and Rugman (1982).

**Entry Mode Set**

The internalization theory explains the choice between licensing and wholly owned subsidiary modes.

**Theoretical Perspective of the Internalization Theory**

**Assumptions:** The Internalization theory is based on following assumptions:

1. The firm and the market are two alternative modes of performing an economic function.
2. The goal of a firm is to maximize its long term profit.
3. Certain intermediate product markets are imperfect.

**Explanatory Constructs:** "Firm-specific knowledge" and degree of "Market failure" are two key constructs of the internalization theory that explain the firm's choice between wholly owned subsidiary and licensing modes. Firm-specific knowledge includes skills and technology that are unique to the firm. Such knowledge results from the firm's long term investment in R&D efforts (Buckley and Casson 1976). Firm-specific knowledge has some characteristics of public goods. For example, its exploitation at multiple outlets does not impair its value. However, its inadvertent disclosure can render it valueless to the owner. Market failure is said to occur when there is limited number of buyers for the firm-specific knowledge. Under this
condition, it is extremely difficult for the firm to engage in frictionless market exchanges (Buckley and Casson 1976).

**Entry Mode Choice Mechanism:** Market mode is the most efficient mode under perfect market conditions. However, according to Buckley and Casson (1976), market fails to transact firm-specific knowledge. The failure of the market may arise from factors like buyer uncertainty about the correct value of the firm's knowledge, availability of fewer buyers, and difficulties in having fool-proof short- and long-term contracts.

Market failure conditions decrease the probability of appropriating full returns on its knowledge if the firm decides to license it out to another firm. For example, buyers are likely to be uncertain about their estimates of the current price of the firm's knowledge because of their inability to correctly assess the future value of the same. As a result, they are likely to underprice the firm's knowledge and hence dampen the firm's return on the knowledge. In case of fewer buyers, licensing could also result in monopsonistic conditions (Buckley and Casson 1976). In the monopsonistic condition, the firm has little control over the output and the pricing decisions of the buyer. This, in turn is likely to provide sub-optimal return on the firm-specific knowledge. Lastly, Buckley and Casson (1976) contend that it is difficult and costly to write and police contracts. Under these conditions, the
theory contends that the costs of operating through market mode outweigh the benefits and the firm is better off in avoiding market costs. In short, the higher the degree of market failure for the firm's knowledge, greater the incentive for the firm to choose wholly owned subsidiary mode over licensing mode.

Empirical Support

One of the key limitations of the internalization theory is the lack of available empirical support for its predictions. One reason may be the difficulty of operationalization of the extent of market failure for intermediate products.

Strengths and Weaknesses of Internalization Theory

Entry Modes: The internalization theory in its current form explains the choice between licensing and wholly owned subsidiary modes. Other modes like indirect export, export through host country intermediary, export through company owned channel, and joint venture are not explained. In sum, the theory explains only a partial set of entry modes.

Theoretical Perspective: The internalization theory departs from the traditional perfect competition theory of the firm in terms of its assumption about competition. The theory assumes that markets are imperfect for certain types of firm-specific knowledge. This departure is an important
advancement over the assumption of perfect competition in
the traditional view of the firm. However, the theory fails
to provide any means of operationalizing the degree of
market imperfection in a given host country. As a result,
the theory is limited in explaining the firm's entry mode
choices to dichotomous modes only.

**Entry Mode Choice Mechanism:** The entry mode choice
mechanism offered by the theory is too general to
operationalize. For example, it is difficult to estimate
the cost-benefit neutral point to understand when the firm
will opt for the firm mode over the market mode. This
raises doubts about the testability of predictions of the
theory. Buckley (1988) has expressed similar reservations
about the testability of the theory.

**Relevance of the Theory:** The popularity of the
internalization theory has remained confined to British
economists only. It has failed to attract the interest of
U.S. researchers. This may be due to two reasons: (1) U.S
scholars have a better alternative to the theory--the
transaction cost theory and (2) there are operationalization
problems with the theory.

In sum, the internalization theory is an important
advancement over the traditional perfect competition theory
of the firm. However, the theory suffers from testability
problems and more importantly it provides only a partial
explanation of the complete set of entry mode choices.
Eclectic Theory

As the name suggests, the eclectic theory is made of firm-specific advantage (ownership-specific advantage), Ricardian endowments (location-specific advantage), and Buckley and Casson's (1976) internalization concept (as an internalization advantage). Obviously, the theory is a blend of the traditional trade theory and the internalization theory. Therefore, it covers trade as well as foreign production operation of the firm and has more explanatory power than the individual theories it blends.

In the context of entry modes, the eclectic theory generates a set of conditions of ownership-specific, internalization, and location-specific advantages that explain a firm's choice of an entry mode from a set of export, licensing, and wholly owned subsidiary modes. Most of the work on this theory has remained confined to Dunning himself. Other important contributors are Agarwal and Ramaswami (1992), Sabi (1988), and Yu and Ito (1988).

Entry mode set

The eclectic theory explains three types of entry modes: export, licensing, and wholly owned subsidiary.

Theoretical Perspective of the Eclectic Theory

Assumptions: The key assumptions of the theory are:
1. Possession of an ownership-specific advantage is a necessary condition for the international operations of the firm.

2. Markets are imperfect for the firm's ownership-specific advantages.

3. Location-specific advantages are equally accessible to the firms of all nations.

Explanatory Constructs: "Ownership-specific", "Location-specific", and "Internalization" advantages are three key constructs that explain a firm's entry mode choice. Ownership-specific advantages include the endowments created by the firm itself, like certain types of technologies or skills or certain types of advantages (e.g. patents) that it can purchase from others. These advantages have the characteristics of public goods and hence are exploitable at more than one site with little or no additional cost.

Location-specific advantages entail typical Ricardian endowments that are specific to a given location but are available to any firm of any nationality. These include natural resources, most kinds of labor and proximity to the market, and legal and commercial environment (market structures and government policies) in which those resources are used (Dunning 1980). Internalization advantages to the firm lie in the performance of an economic activity by itself rather than getting it done through the market. These advantages stem from avoiding costs associated with market transactions under imperfect competition.
Entry Mode Choice Mechanism: According to Dunning (1980), the possession of an ownership-specific advantage determines whether a firm would engage in foreign operations or not. Supposing that a firm has such an advantage, then the choice between foreign production and export modes depends upon the extent to which the firm’s advantage matches with the location advantages of host markets. That is, the greater the match, higher the likelihood that the host market would be served by local production than by export (Dunning 1980). The choice between licensing and wholly owned subsidiary modes depends upon whether or not there is any internalization advantage for the firm. The licensing mode is preferred if this advantage is minimal and wholly owned subsidiary mode is chosen if it is substantial.

Empirical Support


Agarwal and Ramaswami’s (1992) study tested the impact of interactions between ownership-specific advantages of
firms in a leasing industry with location-specific and internalization advantages on their entry mode choices. They report that larger and more internationally experienced firms, in their sample, chose wholly owned subsidiary mode over export and joint venture modes in markets with higher potential. Also, firms with higher ability to develop differentiated products chose wholly owned subsidiary mode over contractual mode in markets with higher contractual risks. Finally, firms chose export mode over other modes in countries with higher investment risks. Despite the limited empirical evidence, the eclectic theory appears to have stood well under scrutiny.

Strength and Weaknesses of the Eclectic Theory

**Entry Modes:** The eclectic theory explains export, licensing, and wholly owned subsidiary modes. The theory does not distinguish between indirect export, export through host country intermediary, and export through company owned channel modes. The theory does not explain the joint venture mode. Thus, like previous theories, this theory explains only a partial set of entry modes.

**Theoretical Perspective:** The eclectic theory provides an important advancement over the internalization theory and the international trade theory in terms of its ability to explain entry modes entailing both home and host production locations. However, objections have been raised about the
redundancy of two of its three types of advantages. The strongest criticism of eclectic theory comes from Itaki (1991) on three counts. First, Itaki argues much like Rugman (1986) did, that the ownership-specific advantage stems from the internalization advantage and hence their consideration as two separate determinants of FDI is redundant. Second, the eclectic theory's assumption about the independence of ownership-specific advantage from location-specific advantage is erroneous because, ownership advantage at one location may turn into a disadvantage at another location. In other words, ownership-advantages are themselves location-specific. Finally, Dunning's theory is ambiguous about the sources of location advantages. Despite these criticisms, the theory offers a more comprehensive framework of entry mode choice than the earlier theories.

**Entry Mode Choice Mechanism:** The eclectic theory provides a sequential choice of entry modes. The choice of wholly owned subsidiary mode occurs only when all three types of advantage are synergistic, falling short of which, the firm may choose licensing or export modes.

**Relevance of the Theory:** Even though the eclectic theory was developed in late seventies, it has failed to muster a substantive body of empirical support. Also, the theory has some unresolved conceptual problems (those pointed out by Itaki and Rugman). Finally, the theory is unable to explain the complete set of entry modes. Despite
these limitations, the theory offers an improved framework for analyzing the entry mode choice of the firm.

**Transaction Cost Theory of Entry Mode Choice**

The Transaction Cost theory of entry mode choice stems from Williamson's (1975) Transaction Cost (TC) theory of the firm. Anderson and Gatignon (1986) were the first to apply this theory to analyze a firm's entry mode choice. Subsequent works in this area have largely followed their framework. The key TC-based works that have enriched the entry mode literature are those of Anderson and Gatignon (1986), Anderson and Coughlan (1987), Erramilli and Rao (1993), Gatignon and Anderson (1988), Hennart (1988, 1989), Klein (1989), and Klein, Frazier, and Roth (1990).

**Entry mode set**

Under the TC theory of entry mode choice, entry modes are considered to comprise a continuous range of structures bounded at one end by the market structure (e.g., licensing) and at the other end by the unified governance structure (e.g., wholly owned subsidiary). The market structure allows the lowest amount of control whereas the unified structure allows complete control to a firm in undertaking a transaction; the intervening structures accord varying degrees of control.
For carrying out both production and marketing activities in the host country, the TC framework can explain the choice of an entry mode from a continuous range of modes. Anderson and Gatignon's (1986) operationalization of such a range is bounded by wholly owned subsidiary mode at one end and the licensing mode at the other end. Likewise, for carrying out marketing activities in a foreign country, i.e., for exporting transactions, the TC framework can also explain the choice of an entry mode from a continuous range of modes. Anderson and Coughlan's (1987) operationalization of such a range is bounded by the integrated channel mode at one end and the independent channel mode at the other end.

Theoretical Perspective of the Transaction Cost Theory

**Basic Assumptions:** The main assumptions of the TC theory of entry mode choice are as follows:

1. Firms are efficiency seekers.
2. Market mode is the default entry mode choice under conditions of perfect competition.
3. Human beings have bounded rationality and are opportunistic.
4. Given the conditions of bounded rationality and environmental uncertainty, it is extremely difficult to write, execute, and enforce a fool-proof contract which would minimize the potential of opportunistic behavior by an independent agent.
5. Presence of the transaction-specific assets leads to market failure.

**Explanatory Constructs:** "Transaction-specificity" of an asset is the main construct of the TC theory of entry mode
choice. The transaction-specificity of an asset implies the firm’s investment in physical or human assets uniquely dedicated to facilitate a transaction. When specificity is high, the assets in question cannot be easily redeployed in alternative usages; the reverse is true when the specificity is low. An example of a transaction-specific physical asset would be a plant operating on a specific grade of raw materials and of a transaction-specific human asset would be the firm-specific training of employees.

Entry mode choice mechanism: According to the TC theory, when asset-specificity of a transaction is low and the supplier market is competitive, the firm will maximize its efficiency by contracting out the transaction to an independent agent or a distributor. The reason being that the market forces can take care of the opportunistic behavior of the agent/distributor. However, when asset-specificity to the transaction is high, suppliers and the firm are locked into bilateral dependence. This makes the supplier relatively irreplaceable resulting in market failure. Under these conditions, an agent's opportunistic behavior can only be controlled through stringent contracts and strict enforcement and monitoring. This drives up the TC cost. It is more efficient to internalize the transaction and have employees perform it, because the firm can more easily control the opportunistic behavior of its employees (Williamson 1975, 1979, 1985).
Empirical Support

Empirical evidence from a number of studies supports the assertion of the TC theory that a firm chooses higher control modes in transactions involving higher asset-specificity. The studies of Anderson and Coughlan (1987), Erramilli and Rao (1993), Gatignon and Anderson (1988), Klein (1989), and Klein, Frazier and Roth (1990) all support the choice of higher-control mode over lower-control mode in transactions involving higher asset specificity.

Strengths and Weaknesses of the Transaction Cost Theory

Entry Modes: In principle, the TC theory is equipped to explain a firm’s choice of a mode from a continuous range of entry modes appropriate for carrying out a set of activities (Williamson 1979, 1985). However, the empirical studies of Gatignon and Anderson (1988) and Klien, Frazier, and Roth (1990) were able to demonstrate choices between dichotomous modes only. Moreover, the theory is unable to explain the choice between export modes and foreign production modes (Erramilli and Rao 1993). In short, the TC theory as applied to the entry mode choice phenomenon is restricted in its power to explain the entire gamut of entry modes.

Theoretical Perspective: The TC theory offers a more realistic portrayal of a real world firm than the perfect competition theory. However, the theory is seriously flawed in its contention about the choice of market mode as the
default choice under low asset-specificity conditions. In their recent article, Erramilli and Rao (1993) question the generality of this contention for low asset-specificity conditions. They argue that when the cost of integration is low and the ability of a firm to integrate is high, the firm is more likely to choose a higher control mode than the market mode. The reasons being that integration provides a firm with many non-TC benefits like extension of market power, larger share of profits, avoidance of conflicts with partners, and facilitation of execution of global strategies. Their argument, thus, restricts the efficacy of the extant TC framework in explaining entry mode choices under low asset-specificity conditions.

Entry Mode Choice Mechanism: According to the TC theory, under low asset specificity conditions, market mode is the default mode for carrying out an economic activity because of its higher efficiency. As already described, Erramilli and Rao (1993) have raised questions about the validity of such an entry mode choice mechanism. Therefore, the current form of entry mode choice mechanism offered by the TC theory is questionable.

Relevance of the Theory: The TC theory provides a powerful framework for analyzing many decisions pertaining to strategic operations of a firm. One of its strengths lies in its generalizability to a variety of make-or-buy decisions in marketing. For example, the theory can be used
to explain the firm’s decision to hire sales personnel or use independent representatives (Anderson and Weitz 1986), make or buy components (Walker and Weber 1984), and choose wholly owned subsidiaries or joint ventures (Hennart 1988; Beamish and Banks 1987). However, as already suggested, the ability of the TC theory to explain the firm’s choice among the complete set of entry modes is limited.

Summary of Market Failure Theories

As already described, the internalization theory explains the choice between licensing and wholly owned subsidiary modes. The TC theory can explain the choice between entry modes that entail host country production and marketing operations. Also, it can provide explanation for the choice between entry modes that involve host country marketing operations only. However, it can not explain the choice between entry modes entailing host country production and marketing operations or marketing operations only. The eclectic theory is capable of explaining the export, licensing, and wholly owned subsidiary modes. In short, these theories only partially explain the range of entry modes. Table 3 summarizes these theories in terms of their explanatory constructs, range of entry modes they explain, and the empirical support for their predictions.
<table>
<thead>
<tr>
<th>Theory</th>
<th>Explanatory Constructs</th>
<th>Range of Entry mode choices explained</th>
<th>Empirical support</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internalization</td>
<td>Firm-specific knowledge and Degree of market failure</td>
<td>FDI mode is chosen if the degree of market failure for the firm-specific knowledge is higher</td>
<td>Not available</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Licensing mode is chosen if the degree of market failure for the firm-specific knowledge is lower</td>
<td></td>
</tr>
<tr>
<td>Transaction Cost</td>
<td>Degree of the Transaction-specificity of an asset</td>
<td>Higher Control Mode is chosen if the degree of transaction-specificity of an asset is higher</td>
<td>Anderson and Coughlan (1987); Brramilli and Rao (1993); Gatignon and Anderson (1988); Klein, Frazier, and Roth (1990).</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Lower Control Mode is chosen if the degree of transaction-specificity of an asset is lower</td>
<td></td>
</tr>
<tr>
<td>Eclectic</td>
<td>Ownership Advantage (OA), Location Advantage (LA), and Internalization Advantage (IA)</td>
<td>OA is essential for all modes. Export mode is chosen if LA favors home market. FDI mode is chosen if LA favors host market and if IA is higher. Licensing mode is chosen if LA favors host market and IA is lower.</td>
<td>Agarwal and Ramaswami (1992); Dunning (1980)</td>
</tr>
</tbody>
</table>
Environment Paradigm

The environment paradigm covers a substantive body of literature that views foreign operations of a firm primarily as a function of host country or home country location-specific factors. Except for a few studies, most works published under the rubrics of this paradigm analyze the impact of a variety of host country factors on the host operations of the firm. Invariably, the factors considered include, economic, social, cultural, and infrastructural factors. The studies under the environment paradigm implicitly assume that a firm carries out FDI operations in a host country to service that market through local production (Davidson 1980b; Root 1987). Therefore, the significance of a host country variable on a firm's choice of FDI operation implies not only the importance of that variable for carrying out host country production operations but also for marketing operations.

Given the scope of this dissertation, the following material reviews studies that analyze the impact of host country factors on a firm's entry mode choice. These studies analyze a firm's choice from a dichotomous set of modes: one of these choices is invariably the FDI mode and the other choice can be licensing or exporting. In short, the choice is between modes that require larger versus lesser resource commitment to host operations.
Host Country Location Theories of Entry Mode Choice

As the name suggests, the host country location theories primarily explain the impact of host country location-specific factors on a firm's choice of an entry mode (Davidson and McFetridge 1985). These factors can be broadly classified into two types. First, there are Ricardian endowments. These include raw materials and population of a location. The population provides both the work force to carry out a firm's operations and market size to consume its offerings. Second, there exists a range of environmental variables that are a function of political, cultural, legal, and infrastructural factors of a host location. Both types of variables are considered crucial to the host operation of a firm as they affect the achievement of its goals (Kobrin 1976). Over the past two decades, a number of studies analyzing the relationship between host country location-specific variables and a firm's entry mode choice have been published. The following paragraphs describe the findings of these studies.

Ricardian Endowments

The Ricardian endowments of a nation consist of its naturally occurring resources and human resources. The literature analyzing the impact of Ricardian endowments on the firm's entry mode choice is, however, lop-sided. Most
studies analyze the effect of market size (demand side of human resources) variable on a firm’s entry mode choice. Only a limited number of studies demonstrate the impact of host country raw materials and labor force (supply side of human resources) variables on the firm’s entry mode choice. The following material describes the impact of market size, raw materials, and labor force variables of a host country on a firm’s entry mode choice.

**Market Size**: Market size of a country indicates its potential to absorb a firm’s production output (Agodo 1978). In Davidson’s (1980b) consideration, the main economic factor motivating a firm to switch from export to FDI mode is the level of demand at which local production becomes more attractive than exporting. Aharoni (1966) also regards host market size as a key determinant of the FDI mode.

Several empirical studies have found strong correlation between the market size and the extent of FDI operations of U.S. firms in various countries. These studies are those of Agodo (1978), Aharoni (1966), Davidson (1980b), Green and Cunningham (1975), Kobrin (1976), Sabi (1988), Scaperlanda and Mauer (1976), and Sullivan (1985). These studies use GDP, GDP per capita, growth rate of GDP, and population size as surrogates of host market size.

In sum, the empirical evidence consistently suggests that the market size of a host country is a key determinant of the FDI behavior of a firm in that country. The larger
the size of a host market for a firm's products, the greater the probability that a firm would carry out production and marketing operations in that market. By implication, licensing or other lesser resource commitment modes may be used for smaller markets (Davidson and McFetridge 1985).

**Raw Materials and Labor Supply:** Bass, McGregor, and Walters (1977) found that size and availability of local skilled work force were important variables in U.S. firms' foreign plant location decisions. Similar results are reported by Moxon (1975). In another study, Agodo (1978) observed that large population size and availability of necessary raw materials were key determinants of U.S. firms' FDI operations in Africa.

In short, these studies show significant impact of host country Ricardian endowments on a firm's FDI operations. In other words, a firm's choice to carry out host country production and marketing operations is significantly related to the availability of necessary raw materials and skilled work force.

**Environmental Factors**

Goodnow and Hansz's (1972) work is credited to be a classic work for analyzing the relationship between entry mode choices of U.S. firms in various countries and the environmental profiles of those countries. They concluded that firms use lesser control modes as they move from "hot"
to "cold" countries. By lesser control modes, they imply overseas agents, distributors, indirect export, licensing etc. The profile for each country in their sample was constructed based on fifty nine variables representing seven environmental factors namely: (1) political stability, (2) market opportunity, (3) economic development and performance, (4) cultural unity, (5) legal barriers, (6) physiographic barriers, and (7) geo-cultural distance. Countries scoring high on factors # 1, 2, 3, and 4 and low on # 5, 6, and 7 were labeled as "hot" countries in the study. Countries scoring exactly opposite were labelled as cold countries; moderate countries fill in between.

In addition to Goodnow and Hansz's work, several studies analyzing the influence of political conditions, cultural distance, tariff barriers, and government policies of host countries on firm's entry mode choice have been published. These are discussed below.

**Political Environment:** The political environment of a host country consists of its: (1) internal political conditions and (2) relationship with the government of investor's country (Nigh 1985; Schollhammer and Nigh 1984). A number of studies analyzing the impact of host country political environment on FDI decisions of U.S. firms have been reported. The empirical studies of Agodo (1978), Aharoni (1966), Fatehi-Sedeh and Safizadeh (1989), Goodnow and Hansz (1972), Kobrin (1979), Kobrin, Basek, Blank, and
Palombara (1980), Maclayton, Smith, and Hair (1980), Root (1987), Root and Ahmed (1978) support the significance of impact of host country political environment on U.S. firm's FDI decisions. These studies used perceptual data. On the other hand, the studies of Bennett and Green (1972), Green and Cunningham (1975), and Kobrin (1976) using econometric data found no significant impact of host country political conditions on foreign direct investment decisions.

Schollhammer and Nigh (1984) argued that studies using econometric data suffer from methodological flaws. By correcting those flaws, they were able to show the impact of host country political conditions on a firm's FDI decision. Thus, it can be inferred that the political environment of a country is a key variable in a firm's decision to establish its production and marketing operations in that country.

**Cultural Distance:** Root (1987) defines culture as the unique lifestyle of a given human society: a distinctive way of thinking, perceiving, feeling, believing, and behaving that is passed on from one generation to another (p. 238). The cultural distance between any two countries represents the extent of dissimilarities between their cultures. Cultural distance has been operationalized in a number of ways. Litvak and Banting's (1968) scale measures cultural distance as the "geo-cultural distance" of a country based on its differences in language, values, attitudes, social perspective, and geographical distance from the U.S.
Another scale devised to measure this variable is that of Hofstede (1980). Other operationalizations include differences in language and religion (Anderson and Coughlan 1987) and psychic distance (Johanson and Vahlne 1977).

The importance of cultural distance as a determinant of entry mode choice emerged from Litvak and Banting's (1968) scale designed to analyze foreign market entry strategies of U.S. firms. Over time, cultural distance as a variable has been incorporated in several entry mode studies. However, researchers are split on the impact of this variable on the entry mode choice of the firm. The following text first describes those studies that support the notion that lesser resource commitment modes are more likely to be used in culturally distant countries. Later, arguments are made questioning the above notion.

find that as compared to their wholly owned operations in "Anglo" countries, U.S. firms chose majority-owned operations in Latin European countries. Erramilli and Rao (1993) report that service firms behaved like manufacturing firms in choosing shared control modes over full-controlled modes in culturally distant countries.

In short, these studies suggest that firms choose larger resource commitment modes in culturally similar markets. Davidson (1983) provides a rationale for the existence of such a relationship when he writes that similarities in languages and cultures facilitate an efficient and effective dissemination of new product information and managers become less concerned about market uncertainties. Moreover, the similarity of a host market allows the firm to transfer its knowledge about pricing, product, promotion, distribution, packaging, and manufacturing technology to that market and reap scale economies (Davidson 1983).

On the other hand, Anderson and Gatignon (1986) posit that the relationship between cultural dissimilarity of a nation and the use of lower resource commitment modes is not straightforward. It is contingent upon a firm's asset-specificity in a that country. They propose that in socially distant countries, a low control mode may be more efficient if the asset-specificity is low otherwise, a high control mode should be used. Their proposition questions
the naivete of the extant view. Also, Johanson and Wiedersheim-Paul (1975) found that Swedish firms despite their entry into culturally similar countries chose to use indirect exporting as a mode of entry before gradually adopting the higher resource commitment mode.

In sum, there is sufficient theoretical ground to infer that the impact of cultural distance on entry mode choice is not as obvious as believed by some researchers. It appears that the importance of this variable can be gauged only in conjunction with economic and political variables of a host country. For example, it is difficult to comprehend a firm choosing a larger resource commitment mode in a small-sized market even if it is culturally similar. This is because, unless the firm is using that market as a sourcing location, such a commitment defies the profit rationale of a firm's FDI operations. From the above discussion, it can be inferred that firms have a propensity to locate their production and/or marketing operations preferably in culturally similar markets but the issue of ownership of those operations may weigh heavily on other considerations.

**Host Government Policies:** Bass, McGregor, and Walters (1977) report that managers consider host government's cooperation with foreign investors as a significant determinant of host production location. Root and Ahmed (1978) observed that a host country's corporate tax policy significantly affected the attractiveness of that country to
U.S. manufacturing investment. Davidson and McFetridge (1985) found that the joint effect of a strict screening process and government restrictions on equity holdings in a country was a strong deterrent to FDI in that market. Gatignon and Anderson (1988) report that American MNCs were less likely to employ wholly owned subsidiaries in countries with legal restrictions on foreign ownership.

In sum, it appears that a firm’s decision to locate its production and marketing operation in a host country is significantly influenced by that host government’s policy toward foreign investment. The more favorable the policy, the greater is the extent of FDI flow to that country. In comparison to economic, social, and political variables, host government policy is less likely to be a decisive determinant of FDI in that country (Root and Ahmed 1978).

**Host Country Infrastructural Factors:** The infrastructure of a country includes roads, harbors, railways, postal service, telecommunication, power and water supplies, and banking facilities. They are necessary for the smooth and efficient performance of production and/or marketing functions (Agodo 1978). In a study involving foreign direct investments of U.S. firms in African nations, Agodo (1978) found a significant relationship between the extent of FDI and the quality of business infrastructure of that nation. Root and Ahmed (1978) observed that among developing nations, those that had better commerce,
transport, and communication infrastructures were more attractive to foreign investors.

In another study involving plant location decisions of U.S. firms in Asia, Latin America, and Europe, Bass, McGregor, and Walters (1977) found the importance of four infrastructural factors. These are: (1) cost of site development, (2) land and construction costs, (3) level of industrialization, and (4) potential for industrial growth. Finally, Michell (1979) suggests that a good infrastructure is essential to the marketing operations of a firm in a country. In short, the presence of an adequate infrastructural arrangements is an important variable in the host country production and marketing operations of a firm.

Summary of Location Theories

Location theories analyze the impact of various host country factors on a firm's choice between a FDI mode and a licensing mode or between a FDI mode and an export mode. One major contribution of these works is the increase in our understanding about key host country factors that impact upon entry mode decision making. Despite this contribution, none of these works provide an explanation of the complete set of entry modes. Table 4 presents the summary of these theories on the explanatory constructs, the range of entry modes they explain, and their empirical support.
<table>
<thead>
<tr>
<th>Explanatory Constructs</th>
<th>Range of Entry mode choices explained</th>
<th>Empirical support</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market Size GNP, GNP per capita, and Market Growth</td>
<td>FDI mode if market size is large; otherwise Export or Licensing mode is chosen.</td>
<td>Agodo (1978); Aharoni (1966); Davidson (1980); Green and Cunningham (1975); Kobrin (1976); Sabi (1988); Scaperlanda and Mauer (1976); Schollhammer and Nigh (1984); Sullivan (1985). Agodo (1978); Bass, McGregor, and Walters (1977); Moxon (1975)</td>
</tr>
<tr>
<td>Raw Material and Labor Supply</td>
<td>FDI mode if there is plenty of raw materials and labor supply</td>
<td></td>
</tr>
<tr>
<td>Political Environment</td>
<td>FDI mode if political environment is stable, otherwise Export or Licensing mode is chosen.</td>
<td>Fatehi-Sedeh and Safizadeh (1989); Nigh (1985); Schollhammer and Nigh (1984).</td>
</tr>
<tr>
<td>Cultural Distance Religions, values, and languages</td>
<td>Higher control mode if similarity is high, otherwise a lower control mode is chosen.</td>
<td>Coughlan and Anderson (1987); Davidson (1980); Gatignon and Anderson (1988); Goodnow and Hansz (1972); Maclayton, Smith, and Hair (1980)</td>
</tr>
<tr>
<td>Host Government Restrictions on FDI</td>
<td>FDI mode if government restrictions on foreign ownership are less; otherwise, JV, or Licensing mode is chosen.</td>
<td>Agodo (1978); Miller and Weigel (1972); Root and Ahmed (1978).</td>
</tr>
<tr>
<td>Host country Infrastructural Factors</td>
<td>FDI mode, if host country infrastructure is developed.</td>
<td>Agodo (1978); Bass, McGregor, and Walters (1977); Root and Ahmed (1978).</td>
</tr>
</tbody>
</table>
Seven entry mode choice theories proposed in the past three decades were discussed in Section I. These theories belong to four different paradigms and collectively comprise the entry mode choice literature. It should be obvious by now that the entry mode choice of a firm has been an issue of considerable interest among scholars in international business. It is a well researched but an issue that still requires a comprehensive understanding. As a result, this topic continues to attract researchers’ attention.

The seven entry mode theories have collectively made tremendous contribution to the understanding of entry mode choice phenomenon—a strategic but a complex issue. Besides providing explanations of limited number of entry mode choices, these theories have generated enough knowledge on three other aspects of entry mode choice. These aspects are: (1) firm-specific nature of entry mode choice, (2) general model of entry mode choice and (3) dynamic nature of the phenomenon. Even though, these three aspects are not central to this dissertation, their consideration along with the central issue—explanation of a complete set of entry modes—provides important insights about three key constraints of an entry mode choice model. That is, an entry mode choice model should (1) be based primarily on firm-specific factors, (2) follow a certain general model,
and (3) show dynamic nature of the firm’s entry mode choice over time. The following material summarizes the review of entry mode choice literature on the number and types of entry modes explained by each entry mode choice theory and the three above mentioned aspects.

Number and Types of Entry Modes Explained

Among the IO-based market imperfection theories, both the Hymer’s theory and PLC theory explain a firm’s choice between two types of entry modes. In the case of Hymer’s theory, the choice explained is between FDI and licensing modes whereas in the case of PLC theory, the choice demonstrated is between FDI and export modes. The internationalization theory explains more entry mode choices than the IO-based market imperfection theories. The theory demonstrates the evolution of a firm’s entry mode choice from indirect export through wholly owned subsidiary mode via export through host country intermediary and export through company owned channel modes.

The three market failure theories—internalization-, eclectic-, and transaction cost theories perform no better than their counterparts in IO-based or behavioral paradigms of entry mode choice. For example, the internalization theory explains the firm’s choice between wholly owned subsidiary and licensing mode, the transaction cost theory
between integrated versus non-integrated modes for host country production and marketing activities or for host country marketing activities separately. The eclectic theory explains the choice between export, wholly owned subsidiary, and licensing modes. Finally, the location theories also describe limited choices only—-one of these choices is invariably the FDI mode and the other (by implication) is either exporting or licensing. In sum, all the seven theories offer only partial explanations of a complete set of entry modes.

Entry Mode Choice—a Firm-Specific Phenomenon

The entry mode choice phenomenon appears to have been viewed explicitly as being driven by firm-specific advantages in all the entry mode theories, except in the case of location theories (Host country advantages). The location theories assume the firm-specific advantage as given and focus on the macro level variables of a host country as key determinants of a firm’s entry mode choice. In short, despite certain idiosyncratic differences among entry mode theories, there appears to be an implied consensus that firm-specific advantage is central to the explanation of a firm’s entry mode choice.
General Model of Entry Mode Choice

Hymer’s theory and PLC theory explain a firm’s entry mode choice for a host country based on the firm’s advantage and its attempts to reduce competition in that host market. Internationalization theory considers the entry mode choice of the firm primarily as a function of its host market familiarity. The ability or the failure of intermediate product markets to efficiently perform transactions for the firm is the chief driving force behind the entry mode choice explanations of the TC and internalization theories. In the eclectic theory, entry mode choice is determined by the most profitable combination of ownership-specific, location-specific, and internalization advantages. Finally, location theories explain the entry mode choice primarily as a function of location-specific factors.

In sum, it appears that the extant theories follow a common model to explain the entry mode choice of a firm. According to this model, entry mode choice of a firm is a function of (1) firm-specific factors and (2) host country factors. Certain studies like those of Flowers (1976), Knickerbocker (1973), Terpstra and Yu (1988) consider industry-specific factors to be a key determinant of entry mode choice in addition to the above mentioned factors. Therefore, it can be inferred that a general model of entry mode choice entails (1) firm-specific, (2) host country-
specific, and (3) industry-specific factors. However, given the primary goal of this study, the industry-specific factor is considered as irrelevant.

Dynamic Nature of Entry Mode Choice Phenomenon

The internationalization theory and PLC theory explicitly consider the dynamic nature of a firm's entry mode choice. The dynamic nature is also evident from the general model of entry mode choice. The firm-, industry-and host country-related factors change over time. For example, over time, firms grow bigger (Penrose 1955), or gain more international marketing experience (Davidson 1980a; Erramilli 1991; Johanson and Vahlne 1977) and, with this, their capabilities to handle risks associated with larger resource commitment also increase. Consequently, firms are expected to modify their entry mode choices (Erramilli 1991). Industry-related factors are also expected to change over time (Harrigan 1985). Similarly, the market conditions cannot be expected to remain stationary; markets for the foreign products grow with economic developments (Vernon 1966). In short, the entry mode choice of a firm exhibits dynamic nature.

Despite enhancing our understanding of the entry mode choice phenomenon in various aspects described, one primary weakness common to all the seven theories is that they do
not explain a complete set of entry modes. Rather, none of
the theories either defines or deploys a complete set. This
raises a question about the appropriateness of these
theories in explaining the complete set of entry modes.

The analysis of these seven theories indicated that
these theories were developed under restricted assumptions
of competitive environment. For example, Hymer's theory and
the PLC theory assume the existence of imperfect competition
in the market where the imperfection is created by firms by
acquiring other firms or building entry barriers. The
internationalization theory also assumes the existence of
imperfect competition a firm is likely to face in the
market. The imperfection, however, is assumed to stem from
lack of perfect information. Finally, the internalization,
the eclectic, and the Transaction Cost theories assume two
types of competition: perfect and imperfect competition.

The assumption about competition indicates as to how
firms are assumed to interact with one another. That is,
what types of inter-firm relationships are expected in the
market place. The more restrictive the assumptions of a
theory are the more limited the set of inter-firm
relationships it can explain. As described before, the
second structural dimension of an entry mode is the
ownership-type dimension which is a dimension of inter-firm
relationship. Therefore, it can be stated that the more
restrictive assumptions about competition a theory of the
firm makes, the lesser freedom it imparts to an entry mode choice theory grounded in it in explaining the range of entry mode choices. A corollary of this statement is that a theory of entry mode choice grounded in a theoretical framework that makes relaxed assumption about competition should be able to explain the complete set of entry modes.

It is the position of this study that the Resource-based theory of the firm because of its highly relaxed assumption about competition has the ability to address the complete set of entry modes in a single framework. The following material provides a description of the Resource-based theory of the firm.

Section II: Resource-based Theory of the Firm

The firm is an entity which combines various inputs (Alchian 1982; Alchian and Demsetz 1972; Conner 1991; McNulty 1968; Singer 1981) to produce and market valuable outputs (Porter 1980, 1985; Thompson 1967). A number of theories have attempted to explain the primary reason of the existence of the firm and how it functions in the market. Some theories that are frequently cited include, perfect competition theory, Bain’s IO theory, behavioral theory, Coase’s theory, and the resource-based theory. On the issue of the basic reason underlying the existence of a firm, the behavioral theory takes a short term perspective: profit-
satisficing. Except for this theory, there is unanimity among other theories that the basic reason for the existence of a firm is long term profit maximization. However, these theories differ from one another regarding how a firm functions in the market place to realize its long term goals and objectives. These differences are discussed next.

The resource-based theory is the most recent theory of the firm. The theory looks at the firm, its competition, and its long term goals and objectives and their achievement from the perspective of the resource endowments of the firm. The theory considers firm-specific resources as the primary determinant of a firm's current and potential product market activities directed at the achievement of its long term goals and objectives.

In earlier theories like the perfect competition theory, the IO-based theory, and Coase’s theory, the firm’s achievement of long term goals is considered to be primarily determined by the market. For example, it is the demand and supply conditions of the market that determine the product market activities of a firm in the case of the perfect competition theory. Likewise, the imperfect nature of the market in the case of IO-based theory, and the market failure in Coase’s theory that underlie the product market activities of a firm. Thus, in relation to the extant theories, the resource-based theory places more emphasis on the resources of the firm than the competitive environment
in describing the product market activities of the firm (Barney 1991; Conner 1991).

The concept of resources is not new to the literature. Its use as a primary basis for explaining international trading can be traced back to the concept of national endowments in Ricardo's work. Similarly, much of the strategy literature recognizes that firms use resources in implementing their product market strategies. This is obvious in the works of Andrews (1971), Chandler (1962), Porter (1985), Rumelt (1974), and Selznick (1957) among others. However, it was only in the eighties and early nineties that significant amount of work was dedicated to the development of a theory of the firm based primarily on its resources. To this effect, the works of Barney (1986a, 1986b, 1986c, 1991), Conner (1991), Dierickx and Cool (1989), Grant (1991), Reed and DeFillippi (1990), and Wernerfelt (1984) among others have made substantive contributions to the development of the resource-based theory of the firm.

The following material first presents key assumptions of the resource-based theory, a conceptualization of the firm, its main long term goal, and the competitive environment it faces. Later, based upon this description, a conceptual model of the firm would be delineated showing how the firm achieves its long term goal.
Assumptions

1. Firms within an industry are heterogeneous with respect to their resources (Barney 1991).

2. The inter-firm heterogeneity may be long lasting because of imperfect immobility of these resources (Barney 1991).

3. A resource is profitable for a firm if can it build resource-barriers against competitors (Wernerfelt 1984).

4. The availability of a substitute depresses the return on the resource to the holder (Wernerfelt 1984).

5. Firm-specific resources are the sources of a firm’s competitive advantage and sustainable competitive advantage stems from the possession of nonreplicable resources (Barney 1991, Dierickx and Cool 1989).

6. The firm exists to maximize its long term ROI (Conner 1991) the route to which is the securing of sustainable competitive advantage.

7. Competition is dynamic in nature.

Resource-based View of the Firm

According to the resource-based perspective, a firm is a bundle of linked and idiosyncratic resources and resource conversion activities (Rumelt 1974). In other words, each firm is unique and this uniqueness may stem from the resources it possesses, their compatibility with one another, and/or the way they are deployed. Furthermore, this uniqueness is relatively long lasting because the resources of the firm are relatively immobile (Barney 1991). The term immobility refers to the degree of difficulty for a
firm to acquire a bundle of resources exactly similar to the firm-specific resources of another firm whether through buying from strategic factor markets or through replication. In short, a firm is a unique entity within an industry.

In comparison to the resource-based theory, the perfect competition theory, the IO-based theory, and the Coase’s theory of the firm take a simplified view of the firm—a homogeneous entity. Therefore, the resource-based theory represents a progress over the extant theories in the sense that it relaxes the assumption of resource homogeneity among them. The theory, however, keeps in tact many of the assumptions from the extant theories like the firm is an efficiency-seeking entity (from Coase’s theory of the firm) and an input-combiner (from the perfect competition theory of the firm). In short, the resource-based theory represents an advancement over the extant theories in modeling a typical real world firm.

Long Term Goal of the Firm

The resource-based theory recognizes persistent above normal return as the main objective of the firm (Barney 1986a, 1991; Conner 1991; Wernerfelt 1984), which ultimately yields long term profit maximization. The concept of above normal return in the resource-based theory is borrowed from the IO-based theory and Coase’s theory of the firm. In
contrast, the behavioral theory considers profit-satisficing rather than profit maximization as one of the many goals of the firm: the theory does not take a long term perspective.

The resource-based theory, however, differs from the IO-based and Coase's view of the firm on the means of reaping above normal returns. Under the resource-based view, above normal returns to a firm are assumed to stem from possession and/or deployment of resources that are difficult or costly to replicate rather than the imposition of output restraints as in Bain's IO theory or the avoidance of opportunism and/or marketing costs as in Coase's theory of the firm.

Type of Competition

The resource-based theory assumes the existence of Chamberlinian competition, i.e., monopolistic competition, in the market place. Monopolistic competition means that each firm in an industry has some elements of a monopolist but has competitors (Chamberlin 1933). Under this type of competition, firms of an industry have unique resources. The heterogeneity of resources allows firms to push competition in directions that favor them relative to other members of the industry. Thus, the competition in an industry is assumed to be dynamic. This assumption is in contrast to that of the extant theories of the firm. As
already described, the behavioral theory assumes imperfect
competition, IO-based theory is based on the constancy of
the imperfect competitive structure, and Coase theory
assumes two types of competition: perfect competition and
imperfect competition arising due to the conditions of
market failure. It is obvious from the foregoing
description that the resource-based theory is the only
type of the firm that fully relaxes structural constraints
of competition: competition is assumed to be dynamic.

Since each firm has the elements of a monopolist and
faces competition, the resource-based theory places
significant emphasis on competitors’ actions to the success
of a firm. For example, competitors can threaten the
success of a firm by duplicating, or by developing
economically efficient alternatives of its resources. In
order to sustain its success over competitors, the firm may
engage in any or a combination of the following activities.
These include acquisition of costly-to-copy resources,
strengthening of existing resource-base, and developing
newer resources (Conner 1991; Wernerfelt 1984).

Mechanism For Long Term Profit Maximization

According to the resource-based perspective, the
ultimate goal of a firm is the maximization of its ROI. The
attainment of this goal is realized through persistent
reaping of above normal returns on the resources of the firm (Barney 1991; Dierickx and Cool 1989). Further, since above normal return accrues to a firm that has a competitive advantage over its rivals (Barney 1986a; Hirshleifer 1980; Porter 1985), the persistence of above normal return requires the firm to have a sustained competitive advantage. Within this framework, the following material delineates a conceptual model showing how the firm establishes and sustains its competitive advantage over its rivals to reap above normal returns on its resources. This model will subsequently become the foundation of the proposed entry mode choice model in Chapter III. Figure 2 shows the model. There are four key constructs in this model: (1) resources, (2) competitive advantage, (3) sustainability of competitive advantage, and (4) above normal return.

Resources of the Firm

The firm is an input combiner (Conner 1991). It uses various resources in a variety of combinations to implement its product market strategy. The resource-based literature delineates a wide assortment of such resources that a firm can use to implement its strategy. For example, Dierickx and Cool’s (1989) examples of firm-specific resources include skills, organizational routines, culture, customer loyalty, and reputation of quality and toughness. Reed and DeFillippi (1990) and Porter (1985, 1990) consider
RESOURCE-BASED GENERAL MODEL OF THE FIRM

DISTINCTIVE COMPETENCIES
ORGANIZATIONAL ROUTINES
CUSTOMER LOYALTY
DEALER LOYALTY
MACHINERY
TRADE CONTACTS
CULTURE

FIRM-SPECIFIC RESOURCES

COMPETITIVE ADVANTAGE

SUSTAINABLE COMPETITIVE ADVANTAGE

ABOVE NORMAL PROFIT

TIME COMPRESSION DISECONOMIES
ASSET MASS EFFICIENCIES
NUMBER OF RESOURCES
INTER-CONNECTEDNESS OF RESOURCES
CAUSAL AMBIGUITY
SUBSTITUTION

FIGURE 2

REPLICATING FACTORS
distinctive competencies of a firm as its key firm-specific resource. The distinctive competencies of a firm entail firm-specific knowledge and the resources necessary to convert that knowledge into products (Reed and DeFillippi 1990). Wernerfelt (1984) provides another set of examples of firm-specific resources. These include brand name, employment of skilled personnel, trade contacts, machinery, and efficient procedures. In short, there is a variety of resources available to a firm to implement its strategy. For a given firm, the range of resources may be determined by its policy of developing them (Dierickx and Cool 1989).

Competitive Advantage

Competitive advantage is the edge that a firm seeks over its rivals by establishing nonrandom links with consumers (Chamberlin 1933). The term nonrandom link implies a unique relationship between consumers and the firm and its offerings. Porter (1985) argues that such linkages are based on the "value" the firm creates for consumers and hence ultimately for itself. By value, he means "the amount buyers are willing to pay for the firm's products." (p.38)

There are two ways in which a firm can create value for consumers and hence for itself. First, by producing and marketing products comparable to those of competitors at a lower cost. Second, by producing and marketing unique products. In the first way, the firm creates more value for
consumers by increasing the buying power of their dollars. This can result in increase of its sales volume. Even if its sale price is at par with that of competition, it ends up with above normal return because of its lower costs. A firm following this route is said to have "Cost Advantage" over its rivals. In the second way, a firm differentiates itself from the competition by creating a unique position for its products. If consumers are willing to pay premium price for the same, the firm can earn above normal ROI. A firm following this course of action is said to have "Differentiation Advantage." In short, a firm may have cost or differentiation advantage or both (Porter 1985), the possession of which helps it to increase its own value.

Resources and Competitive Advantage: According to Barney (1991), Hofer and Schendel (1978), and Uyterhoeven, Ackerman, and Rosenblum (1973), the competitive advantage of a firm emerges from the firm-specific resources it possesses and the pattern in which it deploys them. Similar views are expressed by Porter (1985) in his value chain model where he asserts that the competitive advantage stems from how a firm performs activities in producing and marketing its products. Barney (1991) cogently relates the competitive advantage of the firm, its resources and the product market strategy it implements based on those resources when he writes:

"A firm is said to have competitive advantage over its rivals if it is implementing a value creating strategy not being simultaneously implemented by its existing or potential competitors."
It is obvious from the definition that unique and valuable resources lie at the heart of a firm’s competitive advantage. A resource of the firm is said to be unique if its availability is rare among existing and potential competitors and valuable if it allows the firm to conceive of or implement strategies that improve its efficiency and effectiveness (Barney 1991). In short, a firm’s competitive advantage is primarily determined by its firm-specific resources (Dierickx and Cool 1989). The linkage between firm-specific resources and competitive advantage is shown by a line joining the two in figure 2.

According to Dierickx and Cool (1989), firm-specific resources are developed within a firm by following systematic policies like investment in R&D over a long period of time. That is why they are not tradeable in strategic factor markets and their value can only be realized through their deployment in a firm’s product market strategy (Dierickx and Cool 1989). Therefore, a firm’s product market strategy deploying such resources can provide it a competitive strength and hence above normal returns.

Sustainability of Competitive Advantage

It is in the interest of a firm to ensure that its competitive advantage is enduring. Replication of a firm’s resources is a serious threat to the sustainability of its competitive advantage. It can occur through imitation and
substitution (Dierickx and Cool 1989). The term "imitation" of a firm's resources implies the duplication of a firm's resources and/or its deployment pattern by competitors. By imitating a firm's resources, and/or its deployment pattern, competitors would duplicate the firm's competitive advantage, thereby rendering its competitive advantage less sustainable (Barney 1991; Dierickx and Cool 1989, Reed and DeFillippi 1990). The term "substitution" refers to the creation of an alternative set of equally effective or better resources by competitors. In either case, the firm is unable to sustain its competitive edge and hence can no longer reap above normal rents on its resources.

Obviously, sustainability of its competitive advantage is the prime concern of a firm. No competitive advantage is insurmountable (Ghemawat 1986; Porter 1985). However, the degree of sustainability of the same can be enhanced by the deployment of firm-specific resources that are difficult to replicate. In other words, those resources that are either costly for competitors to acquire or take longer time to accumulate can provide a sustainable competitive advantage to the firm. The following material describes certain characteristics if possessed by the resources of a firm, can enhance the sustainability of its advantage.

Characteristics of Resources: The following six characteristics identified by Barney (1991), Dierickx and Cool (1989), Porter (1980; 1985), and Reed and DeFillippi
(1990) are postulated to limit the extent of replicability of a firm's resources. Of these characteristics, the first five represent the extent of imitability and the sixth the degree of substitutability of a resource.

1. Time Compression Diseconomy for a resource means that its accumulation is time-dependent no matter how much effort a firm's competitors expend over a short period (Dierickx and Cool 1989). Thus, the greater the time it takes to accumulate a resource, the more sustainable the competitive advantage of a firm is.

2. Causal Ambiguity of resource accumulation implies that it is extremely difficult for competitors to fully specify all the determinants of a resource. In other words, the acquisition of the resource is stochastic in nature (Dierickx and Cool 1989). Obviously, the greater the causal ambiguity about a resource, lesser the confidence in replication of that resource.

3. Multiplicity of Resources implies the number of firm-specific resources underlying a firm's competitive advantage. The larger the number of resources, the greater the difficulty for competitors to acquire them and hence, greater the sustainability of its competitive advantage (Porter 1985).

4. Complexity of a resource implies the number of ways in which it is connected to other resources underlying the competitive advantage of a firm. Therefore, the greater the complexity of a resource, the greater the sustainability of the competitive advantage based on this resource (Reed and DeFillippi 1990).

5. Tacitness of a resource implies the extent of noncodifiable components of a resource (Polanyi 1967; Reed and DeFillippi 1990; Teece 1980). Tacitness is quite common in firm-specific resources because certain aspects of these are learned through experience and refined through practice. Therefore, the larger the tacit component in a firm's resources, the greater the sustainability of its competitive advantage.

6. Substitutability of a firm-specific resource means the availability of alternative resource(s) to competitors (Dierickx and Cool 1989; Porter 1980). The greater the probability that the competitors would come up with a cheaper substitute, the lesser the sustainability of the firm's competitive advantage.
In short, the extent of sustainability of a firm's competitive advantage depends upon the degree of replicability of its resources. A firm's competitive advantage based on firm-specific resources with all these six characteristics is likely to enjoy an extremely high degree of sustainability. In figure 2, the impact of replicating factors on the sustainability of competitive advantage is shown by a line connecting the replicating factors to the linkage between competitive advantage and sustainable competitive advantage.

Above Normal Return

According to economists, a firm is said to have above normal return on its assets if its return is greater than the average return of its industry. In the marketing and management literatures, this is operationalized as "superior" market and financial performance (Bharadwaj, Varadarajan, and Fahy 1993; Barney 1986a).

According to the resource-based theory, the persistence of above normal return is necessary for the long term profit maximization of the firm. Since the competitive advantage of a firm underlies its superior performance, it is logical to conceive that the firm would plough back a portion of its earnings to consolidate its competitive position for the future. Firms normally plough back some portion of their earnings to protect their resources from quick erosion
(Dierickx and Cool 1989), consolidate them, and grow them
(Penrose 1955; Wernerfelt 1984). This behavior is shown by
an arrow connecting the above normal return to the firm-
specific resources in figure 2.

Summarizing the above discussion, it is clear that the
realization of long term profit maximization goal of a firm
in the resource-based perspective is founded on the
following characteristics of its resources. First, the firm
should have unique resources. Second, they should be able
to create value for the firm. Finally, it should be
extremely costly for the competitors to replicate them.
Figure 2 summarizes the functioning of the firm.

Summary of the Resource-based View

The Resource-based perspective reflects the natural
emergence of a comprehensive view of the firm from the
existing views; the comprehensiveness of the view lies in
its ability to partially subsume the existing perspectives
about the firm. Partial subsumption means the incorporation
of assumptions from the existing theories that have proved
realistic over time and purging others that oversimplify the
real firm. Thus, the resource-based perspective is an
enriched version of the firm. The material provided on the
resource-based perspective in this chapter is the basis of
explaining entry mode choices of the firm in Chapter III.
CHAPTER III

DEVELOPMENT OF A RESOURCE-BASED THEORY OF ENTRY MODE CHOICE

Introduction

This chapter provides a resource-based framework to develop an entry mode choice model capable of explaining the choice of six modes: wholly owned subsidiary, joint venture, contractual, export through company-owned channel, export through host country intermediary, and indirect export. Together, these alternatives comprise a complete set of entry modes. The proposed model explains these six choices in a sequential pattern. It first explains the choice of modes entailing host country production and marketing operations over those entailing only host marketing operations. Later, for entry modes entailing host country production and marketing operations, it generates two unique conditions under each of which the firm is posited to choose one mode with greater likelihood relative to other choices. Likewise, the model also generates two conditions for entry modes involving host country marketing operations under each of which a firm is posited to choose one mode more likely over the other modes.

In order to develop such a model, this study chooses a three-step route. In the first step, a conceptualization of
the firm appropriate to the analysis of the phenomenon under investigation is selected. Based on this conceptualization, the primary motive underlying a firm's host country operations is explained in the second step. In the final step, an entry mode choice model is developed that builds upon the first two steps.

The consideration of an appropriate view of the firm is based on the notion that the closer a conceptualization is in representing a perceived real world system, the better it is in capturing the reality (Naert and Leeflang 1978). In this thesis, Porter's (1985) value chain view of the firm is chosen as a guide to develop an entry mode choice model. Other reasons underlying its choice are given in section I.

Before explaining a firm's entry mode choice, it pays to understand the primary motive underlying its entry into a host country. This is because an entry mode is a major strategic investment of a firm that is made in business conditions invariably stacked against it (Hymer 1976). Therefore, it is inconceivable to think of a firm investing in a foreign country without a strong motive. Thus, a model that purports to explain the entry mode choice has to first explain the key motive underlying the international operations of a firm. All seven entry mode choice theories described in Chapter II follow this pattern. Therefore, in line with the literature, this thesis explains the primary motive underlying a firm's international operations before
developing a model of its entry mode choice.

Section I begins with the description of Porter’s view of the firm and the rationale underlying its selection as a guide for this study. Based on Porter’s perspective, an explanation of a firm’s motive for international operations is given. In Section II, a resource-based conceptual framework for international operations of a firm is developed. The concepts developed in this framework are subsequently used to propose an entry mode choice model in section III. This model explains the choices of six entry modes. In this context, hypotheses pertaining to the choice of six entry modes are generated. Section IV is dedicated to the development of a research design to test these hypotheses. This entails the operationalization of variables of interest, listing of the data source, selection of sample size, and the statistical technique used in the analysis of the data.

Section I: The Firm and its Motive for Foreign Operations

The Firm

According to Porter’s (1985) value chain view, a firm performs strategically relevant activities to produce and market its products. These activities comprise five categories of primary and four categories of support
activities: each category is further subdivisible into specific activities. The primary activities are directed at the physical creation of a product, its sale, its transfer to purchasers and the after-sales assistance. These are: (1) Inbound Logistics, (2) Operations, (3) Outbound Logistics, (4) Marketing and Sales, and (5) Service. The support activities are carried out to support the performance of primary activities and themselves. These are: (1) Procurement, (2) Technology Development, (3) Human Resource Management, and (4) Firm Infrastructure. Porter’s (1985) broad description of activities is as follows.

Inbound Logistics activities are connected with receipt, storage, and dissemination of inputs to the production of a product. These include material handling, warehousing, and inventory control etc. Operations activities are associated with conversion of inputs to the final product form. These include machining, assembly, equipment maintenance, packaging, and facility operations etc. Outbound Logistics activities are related with physical distribution of the product to buyers. These include order processing, material handling, and delivery vehicle scheduling etc. Marketing and Sales involve activities directed at providing the product to buyers and inducing them to do so. Some examples of these activities are: advertising, using sales force, channel selection, and pricing etc. Service activities such as installation,
training, repair, product adjustment etc. are provided to buyers to enhance or maintain the value of the product.

Procurement activities are spread throughout the firm (Porter 1985). These range from procurement of raw materials to office supplies. Technology Development activities are directed at improving the performance of any aspect of the firm. These include research in product design, media, process equipment design, and service procedures. Human Resource Management activities include hiring, training, developing, motivating, compensating employees etc. Firm Infrastructure includes activities associated with general management, financing, accounting, and legal affairs of the firm.

Figure 3 shows Porter's value chain perspective of the firm. According to Porter, the primary and support activities are linked with one another in some characteristic fashion. This characteristic fashion is obvious from the figure; the primary activities comprise the main value chain of the firm and the support activities are connected to them through branch chains.

According to Porter (1985), an activity by itself, or in combination with other activities can become a source of competitive advantage for the firm. That is, each activity by itself or in combination with other activities can enhance the value of a firm--value placed by buyers on a firm's products (Porter 1985). Also, he suggests that
PORTER'S VALUE CHAIN CONCEPTUALIZATION OF THE FIRM

FIGURE 1. SOURCE: PORTER (1985)
within an industry, a firm’s value chain may differ from those of others based on its history, strategy, approach to implementing strategy, and the underlying economics of activities. In other words, the value chain model implicitly considers that each firm is unique in how it carries out its activities. Moreover, these activities can be a source of competitive advantage. In this respect, Porter’s view overlaps with the resource-based perspective.

In this study, Inbound Logistics, Operations, and support activities relevant to carrying out a firm’s production operations are considered as its production-related activities. Likewise, the Outbound Logistics, Marketing and Sales, Service, and support activities relevant to carrying out a firm’s marketing operations are clubbed together as its marketing-related activities. The main reason of doing this is to tailor Porter’s view to the requirements of the entry mode choice phenomenon.

**Rationale For the Choice of Porter’s View**

The selection of Porter’s view of the firm as a guide for the development of an entry mode choice model in this study is because of four considerations. First, it is relevant to the phenomenon being addressed in this study. As explained earlier, all entry modes comprising the complete set entail performing of either marketing operations or both production and marketing operations in a
host country. Porter’s model by conceptualizing the firm as a set of production- and marketing-related activities, obviously, facilitates the analysis of entry modes and hence the appropriateness of its use in the proposed model.

Second, it is not in conflict with the theoretical underpinnings of the model. Porter’s view assumes that a firm’s competitive advantage lies in the superior performance of its activities in isolation or in combination with other activities within the firm or in collaboration with its partners. Further, it implicitly assumes the uniqueness of a firm based upon its history of development, strategy, and approach to implementing strategies (p.37-38). These assumptions about the firm overlap with the assumptions of the resource-based perspective. Since the proposed entry mode choice model is founded in the resource-based perspective, the use of Porter’s view as a guide for the model does not violate the theoretical underpinnings of the model and hence its appropriateness for this study.

Third reason for using Porter’s view is that it enhances the implementability of the proposed model. The implementability aspect of Porter’s view lies in its managerial perspective. Since the proposed model also takes a decision-oriented perspective, therefore, the use of Porter’s view enables the development of an implementable model which is recognized as a key criterion of a successful model (Little 1970; Naert and Leeflang 1978).
Finally, Porter's model is adaptive in nature. That is, because of its assumptions about divisibility of value activities, this perspective can be tailored to describe specific behaviors of a broad range of firms. By implication, an entry mode choice model built under the guidance of this view can explain the entry mode choice behavior of a diverse range of firms. With this understanding, the following material explains why a firm carries out marketing- or both production and marketing-related activities in a host country.

Motive Underlying Host Country Operations

The entry mode choice literature suggests that, in a host country, a foreign firm is likely to face more obstacles than a domestic firm. For example, the firm may face different cultural conditions—different language and management practices (Anderson and Gatignon 1986; Davidson 1980a; Goodnow and Hansz 1978), less friendly host country competitors (Hymer 1976), and discouraging host government policies (Gatignon and Anderson 1988; Hymer 1976). These odds increase a firm's cost of host country operations (Hymer 1976). Despite these odds, firms enter foreign markets. This raises an important question: Why does a firm choose to engage in host country operations despite many potential difficulties it is likely to face?
A number of reasons have been put forward to explain the primary motive underlying a firm's foreign market entry. Some of these reasons are: (1) to earn rent on monopolistic advantage (Hymer 1976; Kindleberger 1969), (2) oligopolistic reaction to maintain competitive parity (Knickerbocker 1973), (3) to earn rent on ownership-specific advantage (Dunning 1980), (4) marginal cost of exploiting an advantage in a foreign country is less than the cost of developing it, and (5) to deter local competition (Vernon 1966). Of these, reaping above normal rent on a firm's advantage is the most frequently accepted motive. Contractor (1984, p. 167) expresses this cogently when he writes, "A firm that possesses a differentiated product or a proprietary technology will seek to exploit that advantage in foreign markets." This is because above normal return accrues from the exploitation of such advantage.

The entry mode literature also suggests that the firm-specific advantage underlying a firm's international operations has two key characteristics: it should be (1) strong enough to overcome host country adversarial conditions (Hymer 1976), and (2) cost effectively intra-firm transferrable across countries (Hymer 1976; Teece 1980). In other words, lack of possession of such an advantage is likely to minimize the possibility of international operation of a firm.
The proposed model, due to its grounding in the resource-based theory, also regards the reaping of above normal return on its resources to be the primary motive of a firm’s international operations. According to the resource-based theory, a firm may have access to a variety of resources. However, only those resources in which a firm is uniquely endowed can provide it a competitive advantage necessary for reaping above normal return. Such resources are the distinctive competencies of a firm. The distinctive competencies include both skill and variety generating aspects of firm-specific knowledge and the tangible resources necessary to convert that knowledge into products (Reed and DeFillippi 1990; Subbanarasimba 1990).

The possession of distinctive competencies can yield a firm with cost and/or differentiation type of competitive advantage. The extent of competitive advantage of a firm sufficient enough to neutralize host country odds is, however, likely to depend upon how advanced its distinctive competencies vis-a-vis competitors are. Furthermore, the distinctive competencies of a firm can provide it with a sustainable competitive advantage (Reed and DeFillippi 1990). This is because (1) they are unique resources as they are developed within a firm by following deliberate policies over long time (Dierickx and Cool 1989), (2) it may be difficult for competitors to acquire them because of their non-availability in strategic factor markets, and (3)
markets, and (3) they may be difficult to imitate because not all of their aspects are codifiable (Reed and DeFillippi 1990). In short, the distinctive competencies of a firm, if exploitable in a host country, can become a source of its sustainable competitive advantage.

In theory, a firm can have distinctive competencies in activities related to any of its functional areas like production, marketing, finance, and administration (Hitt and Ireland 1985; Lado, Boyd, and Wright 1992; Snow and Hrebiniak 1980; Subbanarasimha 1990). However, given the phenomenon under analysis in this study, two types of distinctive competencies are considered relevant: distinctive competencies in (1) production-related activities and (2) marketing-related activities. Therefore, in line with the existing theories of entry mode choice, this dissertation posits that the primary motive of a firm to engage in international operations is to exploit its distinctive competencies in production- and/or marketing-related activities. These are firm-specific resources, if cost effectively transferred across nations, can allow a firm to profitably carry out its international operations. They can become a source of sustainable competitive advantage for the firm strong enough to offset host country odds. With this understanding, the following section is devoted to the development of a resource-based model of entry mode choice.
Section II: Framework for International Operations

In this section, a resource-based conceptual framework for explaining the international operations of the firm is developed. In this framework, four constructs are developed that form the core of the proposed entry mode choice model. These constructs are: ACAP, ACAM, SCAP, and SCAM. The rationale underlying the necessity of developing these concepts is described below.

As presented in Chapter I, an entry mode is describable in terms of a unique combination of a specific aspect of each of the two structural dimensions: (1) type of host country operations and (2) type of ownership of host country operations. While the first dimension has two specific aspects: (a) marketing and (b) both production and marketing operations, the specific aspects of the second dimension entail (a) sole ownership of the firm, (b) ownership shared with a host firm, (c) sole ownership of the host firm, and (d) sole ownership of another home firm. Therefore, a model designed to explain the choice of a complete set has to answer the following two questions in their entirety.

1. Under what condition(s) will the firm most likely locate marketing only or both production and marketing operations in a host country? and

2. Under what conditions(s) will the firm most likely choose sole ownership, share ownership with a host firm, or allow a host firm or another home firm to own the host operations.
The answer to the first question provides an explanation for the location of host country production and/or marketing operations and the answer to the second question, the ownership of those operations. The answer to both questions when taken together would explain the choice of the complete set of entry modes.

As stated earlier, the distinctive competencies in production- and/or marketing-related activities are the primary resources that a firm is motivated to exploit in its international production and/or marketing operations. These firm-specific resources are the source of long term above normal return for a firm, the reaping of which, however, requires generation and sustaining of competitive advantage based on them. Therefore, a primary concern of a firm interested in exploiting its distinctive competencies in production- and/or marketing-related activities in a host country is the actualizability of its competitive advantage in production and/or marketing of its products in that country. Once a competitive advantage is actualizable, the next concern is the sustainability of that competitive advantage in the host country.

This study posits that a firm's location of infrastructural arrangement to carry out production- and/or marketing-related activities in a host country is related to the actualizability of its competitive advantage in production- and/or marketing-related operations in that
country. Further, a firm’s choice of the type of ownership of the host country arrangement is related to the sustainability of its actualized competitive advantage. These two issues taken together enable the model to predict a complete set of entry modes. That is why, the constructs, Actualizability of Competitive Advantage in Production (ACAP), Actualizability of Competitive Advantage in Marketing (ACAM), Sustainability of Competitive Advantage in Production (SCAP), and Sustainability of Competitive Advantage in Marketing (SCAM) operations need to be used in a model to explain the complete set of entry modes.

Host Country Location of Infrastructural Arrangements

The following discussion includes a description of Actualizability of Competitive Advantage in production and marketing operations and their theorized relationships with distinctive competencies and host country factors. Additionally, the relationship between the Actualizability of Competitive advantage of a firm and host country location of its infrastructure is established.

Actualizability of Competitive Advantage

Barney (1991) defines competitive advantage as follows:

"A firm is said to have a competitive advantage when it is implementing a value creating strategy not simultaneously being implemented by any current or potential competitors." (p. 102)
The definition implies that a firm's competitive advantage in a market stems from implementing a product market strategy which creates (1) value for the firm and is (2) unique. In other words, if a firm's strategy does not create value or is not unique, the firm does not have a competitive advantage over its rivals.

A firm's entry mode decision for a foreign country entails the start of a production and/or a marketing operation at that location. At the time of entry, a firm can only assess its likelihood of establishing a competitive advantage. Therefore, the above definition needs to be modified to reflect a firm's pre-investment assessment of its abilities to establish a competitive advantage at a given location. In the present study, this is captured by the term "Actualizability of Competitive Advantage." In line with Barney's definition, the actualizability of competitive advantage is defined as follows.

A firm's actualizability of competitive advantage at a location represents its ability to implement a value creating strategy which would not be simultaneously implemented by any current or potential competitors.

Clearly, the definition reflects a firm's concern about the likelihood of implementing a product market strategy that would not only be unique but would also create value for it at a given location. In other words, a firm is looking at possible obstructions or facilitations to the implementation of its product market strategy for a host
country environment. For example, a firm may have necessary distinctive competencies in establishing a cost-based advantage. But, this may be of no use in a country where consumers are price-insensitive. In another scenario, the low-cost producing competencies may not help the firm generate an advantage if the necessary raw materials or labor are too costly to acquire. In short, the actualizability of a firm's competitive advantage in a host country is dependent upon the extent of compatibility of its distinctive competencies with the relevant host country factors.

The actualizability of competitive advantage of a firm in a host country can be expressed in an equation form as a function of its appropriate distinctive competencies and relevant host country factors. In general

\[
\text{ACTUALIZABILITY OF COMPETITIVE ADVANTAGE} = f (\text{DISTINCTIVE COMPETENCIES, HOST COUNTRY FACTORS}) \quad (1)
\]

And, for actualizability of competitive advantage in host country production, the equation is:

\[
\text{ACAP} = f (\text{DISTINCTIVE COMPETENCIES IN PRODUCTION-RELATED ACTIVITIES, HOST COUNTRY FACTORS}) \quad (2)
\]

Likewise, for actualizability of competitive advantage in host country marketing, the equation is:

\[
\text{ACAM} = f (\text{DISTINCTIVE COMPETENCIES IN MARKETING-RELATED ACTIVITIES, HOST COUNTRY FACTORS}) \quad (3)
\]
Where, ACAM and ACAP stands for actualizability of competitive advantage in production and marketing operations respectively. Figure 4 shows the distinctive competencies in production- and marketing-related activities as the firm-specific resources a firm seeks to exploit in a host country. Also are shown the relevant host country factors affecting the actualizability of competitive advantage in production and/or marketing operations. These are connected to the line joining the production and/or marketing-related distinctive competencies and the actualizability of competitive advantage in a host country. The following material provides a brief description of the two types of distinctive competencies and the relevant host country factors.

**Distinctive Competencies in Production**

The distinctive competencies of a firm in production-related activities are its firm-specific resources pertaining to the production of products. These resources include skill and variety generating aspects of specific knowledge and tangible resources necessary to convert that knowledge into products. While a combination of superiority in skills and tangible resources may allow a firm to perform production operations in cost efficient way, the variety generating aspect allows it to deploy resources in various pattern to cope with competitive environment and
CREATION OF COMPETITIVE ADVANTAGES

A) PRODUCTION ADVANTAGES

Distinctive Competencies in Production

Firm-Specific Resources

Host Country Factors

Actualizable Competitive Advantage in Production (ACAP)

Sustainable Competitive Advantage in Production (SCAP)

B) MARKETING ADVANTAGES

Distinctive Competencies in Marketing

Firm-Specific Resources

Host Country Factors

Actualizable Competitive Advantage in Marketing (ACAM)

Sustainable Competitive Advantage in Marketing (SCAM)

Figure 4
stay ahead. In other words, these resources allow a firm to generate variety in its outputs and/or perform its production operations in a cost efficient way. As described earlier, the production-related activities of a typical real world firm include inbound logistics, operations, and relevant support activities. A firm may have distinctive competencies in any or all of them. Superiority in production-related machinery, plant layout, knowhow, patented technology, procedures, organizational routine, and coordination mechanisms are some of the examples of distinctive competencies in production operations.

**Distinctive Competencies in Marketing**

The distinctive competencies in marketing operations of a firm are its knowledge-based and tangible resources associated with carrying out of activities related with the marketing of its product. At a general level, the marketing operation of a firm consists of activities associated with (1) assessment of demand characteristics of a market and (2) demand satisfaction of that market. The assessment of demand in a market entails activities like segmentation of a market based on market research and estimation of demand in each of the segments the company decides to operate in. On the other hand, satisfaction of demand entails carrying out of marketing activities like promotion, pricing, distribution, and customer service. A
firm may have distinctive competencies in some or all of its marketing-related activities. Experience and knowhow in establishing loyalty among channel members and ultimate consumers, in deciphering consumer preferences, possession of a superior marketing research and information system, and maintaining a highly trained sales organization are examples of the distinctive competencies of a firm in marketing-related activities.

As described earlier, because of their uniqueness, distinctive competencies can allow a firm to implement a unique and a value creating strategy in a host country. However, in order to create a competitive advantage, the distinctive competencies have to be exploitable within the conditions of that host market. The following material provides a brief description of how these host country factors may affect the actualizability of competitive advantage in production and/or marketing operations.

Host Country Factors

The literature review in Chapter II showed that availability of necessary raw materials and various host country conditions like the labor supply, political conditions, government policy toward foreign firms, market size, cultural distance, and the availability of necessary infrastructure facilities are significant determinants of a firm's host country production operations. Except for the
availability of necessary raw materials, all other host
country factors are also significant determinants of host
country marketing operations of a firm.

These factors may facilitate or hinder the
actualizability of a firm's competitive advantage. However,
not all of them may equally affect the degree of
implementability of a firm’s value creating strategy. A
description of the influence of these factors on the
actualizability of a firm’s competitive advantage in host
country production- and/or marketing-operations is given
below.

**Raw Materials Availability:** Firms combine valued inputs
to produce more valuable finished outputs (Porter 1985).
Therefore, the availability of appropriate raw materials is
one of the key requirements to carry out the production of a
product at a location. By combining its distinctive
competencies in production with necessary raw materials, it
is possible for a firm to generate a competitive advantage
in the production of its products. However, if necessary
raw materials are not available in a host country, are in
restricted supply, costly to acquire locally, or costly to
ship from another location, it may be extremely difficult
for a firm to actualize a competitive advantage in producing
its product in that country and vice versa.

In certain cases, the extent of increased cost of
acquiring raw materials may prohibit not only the
achievement of cost advantage but also the differentiation advantage. This is because, excessive costs in obtaining the necessary raw materials may nullify the profit margin. In short, free availability of appropriate raw materials in a host country is related to the actualization of a firm's competitive advantage in production operations.

**Skilled Work Force Availability:** Unlike raw materials, firms need skilled personnel (labor, technicians, marketing personnel etc.) to carry out their production and/or marketing operations. Local availability of appropriate work force in a host country is essential to the profitability of a firm's operations. The extent of skill requirements may, however, vary from one firm to another. By combining its distinctive competencies with the efforts of the personnel, it is possible for a firm to generate a competitive advantage in production and/or marketing of its products. However, if the necessary work force is not available in a host country, is in restricted supply, costly to train, costly to acquire locally, or costly to expatriate from another (home) location, it may be extremely difficult for a firm to actualize a competitive advantage in producing and/or marketing its product in that country.

In certain cases, the extent of increased cost of acquiring/building a trained work force may prohibit the achievement of competitive advantage. This is because, excessive costs associated with acquiring/building the
required work force may nullify the profit margin. In short, an adequate supply of appropriately skilled work force in a host country is essential for the actualizability of a firm's competitive advantage in production and/or marketing operations.

**Political Environment:** As described in Chapter II, from the point of view of a firm, the political environment of a host country consists of its internal political conditions and its relationship with the home country of the firm. Assuming that the relationship between a firm's home and the host country are normal, it is the internal political environment of the host country that primarily determines a firm's perception of political conditions of that country.

In the absence of political turmoil, a firm is exposed to normal operating business risks in a host country. Robock (1971) provides a litany of political risks facing a firm when host political conditions take for the worse. These include: confiscation, expropriation, compulsory subcontracting, unilateral revisions in contract agreements etc. Likewise, the emergence of nationalistic feelings may force the firm to change its labels, brand names, and even face a boycott of its products. The sudden emergence of political risks dramatically increase a firm's cost of doing business in a host country. In certain cases, the extent of escalation in these costs may be sufficient enough to offset a firm's actualizability of competitive advantage in host
country production and/or marketing of its products. In sum, existence of stable political conditions in a host country is essential to the actualization of a firm's competitive advantage in production and/or marketing operations.

Host Government Policies Toward Foreign Firms: A government designs policies to serve its citizens by balancing business and consumer interests. For example, the government policies define as to what products to produce, minimum product standards to be observed, and what can be promoted through which medium and when. Finally, it can lay grounds for policies regarding pricing of products and their location of production and distribution (Groo 1971). Guided by the spirit of welfare of its society, a host government's policies toward foreign firms may either facilitate or inhibit the arrival of their products through import or the location of their production plants in that country. Kohlhagen (1979) describes how ASEAN countries (Indonesia, Malaysia, Philippines, Singapore, and Thailand) were attracting foreign investment by giving them tax breaks, favorable exchange rates, liberal capital depreciation etc. On the other hand, Cao (1980) describes ways in which a government can raise tariff and non-tariff barriers to various imports.

In short, a host government policies can raise the cost of doing business for a foreign firm in a country and vice
versa. Therefore, favorable host government posture toward a foreign firm is necessary for the actualizability of its competitive advantage in production and/or marketing of its products in that country.

**Market Size:** From the point of view of a firm, market size determines the size of actual or potential demand for its products. Market size below a certain threshold level may make it extremely unprofitable for a firm to serve a host market through local production. In that case, the firm may serve that market through any of the direct exporting modes. In situations where the level of demand is so low that the cost of direct exporting (say, logistics and marketing operations) may offset the profit from the export transaction, the firm may choose to operate through indirect exporting mode. In short, the market size is a key determinant of the actualizability of a firm's production and/or marketing competitive advantage in a host country.

**Cultural Distance:** In order to implement its product market strategy in a host country, a firm needs certain level of relevant knowledge about that market. The market-related knowledge includes information about the demand and supply conditions, socio-cultural conditions, tastes and preferences, labor policies etc. Such information, however, is not cost-free (Cyert and March 1957). Therefore, a firm has to incur certain costs in order to implement its strategy (Hymer 1976). Obviously, the greater the
uniqueness of the market a firm is entering in, the larger the cost of information acquisition. This escalates the firm's cost of exploiting its production- and/or marketing distinctive competencies. The increase in cost in certain cases may lower the firm's actualizability of production and/or marketing competitive advantage to the extent that the firm may not perform those activities in the market.

On the other hand, as described in Chapter II, firms show greater propensity in establishing their operations in culturally similar countries. A key reason attributed is that when entering such countries, a firm does not have to incur substantive market-related information acquisition costs and can reap greater economies in exploiting its production- and/or marketing-related distinctive competencies (Davidson 1980b). In short, it is clear that the cultural distance of a host country plays an important part in a firm's actualizability of a competitive advantage in producing and/or marketing its products in that country.

**Availability of Necessary Infrastructure:** The infrastructure of a nation consists of its communication, transportation, and energy systems (Dahringer and Muhlbacher 1991). These are the life lines of any economy and are essential to the conducting of business transactions. Their level of development indicates the degree of profitability with which a business can be conducted. The lesser developed they are, the greater the obstructions they offer
to a firm attempting to tap into the available resources as well as to communicate with consumers. For example, poor transportation, bad roads, frequent interruptions in electricity supply, over-burdened media of communication of a location increase a firm's cost of conducting production and or marketing operations. For certain firms, these costs may offset their actualizability of competitive advantage in conducting production and/or marketing operations and they may conduct their operations in another market. In short, a host country infrastructural factors play an important role in a firm's decision to locate its production and/or marketing arrangements in that country.

In sum, host country factors like the availability of appropriate raw materials, skilled labor, market size, political conditions, cultural distance, infrastructure, and host government policies have important bearing on the actualizability of a firm's advantage in production and/or marketing of its products. However, not all of them may be pertinent to a specific firm.

Actualizability of Advantage and Infrastructure Location

As stated earlier, the primary motive of a firm entering a host country is the exploitation of its distinctive competencies in production- and/or marketing-related activities in that country. The exploitation of these resources requires an establishment of an appropriate
arrangement in that country, which means investment of appropriate human, technical, and financial resources. Being a profit maximizing entity, a firm undertakes these actions with the expectation of reaping above normal returns. Therefore, if a firm realizes that it has a lower degree of actualizability of its competitive advantage in an operation in a host country, the likelihood of its reaping above normal returns is also lower. Hence, the probability of its establishing an infrastructural arrangement to exploit its competencies in that country is likely to be lower and vice versa. This forms the basis of the explanation to the first question: under what conditions will a firm most likely to locate its production or marketing operations in a host country? The full explanation would be provided in the hypotheses section.

Ownership Choice of Host Country Operations

As described in Chapter I, the entry modes comprising the complete set include a variety of ownerships of host country operations. While a firm enjoys sole ownership in wholly owned subsidiary and export through company-owned channel modes, it shares ownership with a host country firm in the joint venture mode. In the case of contractual mode, a firm has no claim on ownership in host country operations; these are conducted under the sole ownership of a host firm
which in turn agrees to pay some royalty or fee annually to the firm. Likewise, when a firm chooses to deploy the export through host intermediary mode, it conducts host country marketing operations under the ownership of a host firm. Finally, in the case of indirect export mode, a firm has no ownership interest in host operations which are conducted under the auspices of another home firm.

In choosing an entry mode, along with the decision about location of its appropriate operation, a firm has to decide about the type of ownership of those operations. Will the firm choose sole ownership, or share ownership with a host firm, or allow a host firm or another home firm to assume the ownership of host operations? The selection of ownership type of host operations is a strategically important decision for the firm. This will become clear from the following discussion.

An entry mode decision entails substantive amounts of long term commitment of resources of the firm. A firm has to invest in appropriate human, technological, capital, and financial resources in order to exploit its distinctive competencies in production- and/or marketing-related activities in a host country. The extent of such investment, however, may vary from one firm to another depending upon the product market strategy of the firm.

Also, some of the infrastructural investment in host facilities may be highly specific to a given country, the
redeployment of which in another country is likely to be extremely costly for the firm (Teece 1980). Several examples of such investments can be found in the carrying out of marketing-as well as production-related activities. For instance, the investment in training of employees, specialized machines, or in buildings to run production operations are the examples of host country-specific investments in production operations. Likewise, the investment in building good relations with suppliers and channel members, trade contacts, and experiential knowledge about the market are the examples of host country-specific investment in marketing operations.

In short, a firm's choice to carry out host country production and/or marketing operations entails significant investment of resources. Moreover, such investment may not be fully recoverable in case the firm decides to divest out of the host market. An important question emerges that under what condition(s) is the firm more likely to choose sole ownership, share ownership with a host firm, or allow a host or another home firm to own the host operations?

As described in the beginning of this section, this study takes the position that the issue of choice of ownership-type of a host operation is related to the extent of sustainability of a firm's competitive advantage in that operation in the host country. The following material first explains the concept of sustainability of competitive
advantage and later discusses its relationship with different ownership types.

**Sustainability of Competitive Advantage**

A firm's competitive advantage remains sustained so long as the uniqueness of its value creating product market strategy remains unreplicable by competitors (Barney 1991; Porter 1985). Obviously, the sustainability of a firm's competitive advantage is a function of competitive replication of its actualizable competitive advantage. In the context of foreign market entry, this implies that a firm's assessment of sustainability of its competitive advantage depends upon its judgment of the extent of replication of that advantage by host country competitors. The lesser the threat of replication, the greater the sustainability of competitive advantage and vice versa. A host country competitor can be a local, of another nationality, or another firm from the home country of a firm. Figure 4 also shows the relationship between a sustainable competitive advantage, competitive replication and the actualizable competitive advantage for production and marketing operations. In the equation form, the sustainability of a firm’s competitive advantage can be expressed as:

\[
\text{SUSTAINABILITY OF CA} = f(\text{ACTUALIZABLE COMPETITIVE ADVANTAGE, COMPETITIVE REPLICATION}) \quad (4)
\]
SCAP = f(ACAP, HOST COUNTRY COMPETITIVE REPLICATION IN PRODUCTION)...........(5)

SCAM = f(ACAM, HOST COUNTRY COMPETITIVE REPLICATION IN MARKETING)............(6)

Where SCAP represents the "Sustainability of a Competitive Advantage in Production" and SCAM is the acronym for "Sustainability of a Competitive Advantage in Marketing operations." The terms ACAP and ACAM have been already explained. The following material explains the term "Competitive Replication."

**Competitive Replication**

As described above, competitive replication is the main threat to the sustainability of a firm's advantage. By replicating the advantage of a firm, competitors minimize its ability to earn above normal returns. According to the resource-based perspective, the firm-specific resources lie at the heart of a firm's competitive advantage. Therefore, the replication of a firm's advantage means the replication of that firm's resources. One point needs to be clarified that competitors have their own agenda--their own strategies to implement; replication is not necessarily the way they run their businesses. Therefore, an important question emerges: under what conditions are the competitors more likely to engage in replication? In order to answer this
question, this study posits that competitive replication is comprised of (1) replicability of a firm’s resources and (2) competitors’ intensity to nullify the advantage of the foreign firm.

**Resource Characteristics:** The competitive replication of firm-specific resources takes place through two ways: (1) imitation and (2) substitution (Dierickx and Cool 1989). As discussed in Chapter II, if a firm’s competitive advantage is based on a large number of different distinctive competencies that have certain characteristics like greater time compression diseconomies, greater causal ambiguity in their accumulation, greater complexity, higher tacitness component, and lesser substitutability, it is extremely difficult for competitors to replicate these resources. Hence, the competitive advantage generated by these resources would be highly sustainable. However, on the other hand, if the firm’s advantage lacks some or all of the above resource characteristics, its advantage is more vulnerable to replication (Reed and Defillippi 1990).

**Competitive Intensity:** Competitive intensity represents the competitors’ resolve to neutralize the advantage of a firm that has threatened their market share. Macmillan, McCaffery, and Wijk (1985) report that competitors have a higher propensity to imitate a firm’s products if they perceive that the new product of a firm is a strategic threat to their business and has considerable market
potential. Reed and DeFillippi (1990) also propose that barriers to imitation to a firm's advantage depends upon the competition. In other words, if the competitors' market share is threatened, they are likely to react. Otherwise, they may ignore a firm's new product introduction. Therefore, the extent of competitive replication of a firm's advantage depends upon the resolve and the ability of competitors to replicate its firm-specific resources.

It is obvious from the above description that the greater the extent of competitive replication, greater the threat to the sustainability of a firm's competitive advantage. Philosophically speaking, no competitive advantage is insurmountable (Reed and DeFillippi 1990). Competitors keep on chipping it away. Sooner or later, they catch up with the firm through (1) imitation and/or (2) substitution of the firm's resources (Barney 1991; Dierickx and Cool 1989). Therefore, the sustainability of a firm's competitive advantage reflects the time lag in the replication response of competitors (Ghemawat 1986; Macmillan, McCaffery, and Wijk 1985).

Since a firm has no control over its competitors, the main recourse for the firm to enhance the life of its advantage is to increase the delay in competitors' response time in imitation and/or substitution of its resources. Macmillan, McCaffery, and Wijk (1985) recommend that if a firm can mask the potential of its newly introduced product
and reduce its visibility, it may lower the risk of competitive imitation. Also firms can reduce competitive replication by building resource barriers. This, according to Wernerfelt (1984), can be done by ploughing back part of the earnings into the development of new competencies or reinforcing the existing ones.

Sustainability of Competitive Advantage and Ownership

Distinctive competencies of a firm are developed through years of painstaking efforts both in financial and human terms. Also, their emergence is stochastic in nature (Dierickx and Cool 1989). They have the ability to help a firm actualize a competitive advantage, and reach its long term goals. Given these characteristics, it is obvious that a firm would try its best to protect its distinctive competencies and hence the competitive advantage based on them from competitive replication.

Although there is no defined upper limit of the durability of an advantage, a firm is expected to be concerned about the sustainability of its advantage at least for the planning horizon of its strategy implementation (Grant 1991). This is because the planning period allows a firm to at least recover its investment. Therefore, the extent of replicability of a firm's resources has an important implication for the extent of investment a firm is likely to make in a host operations. This, as stated
before, is the primary reason underlying the position of
this thesis on the relationship between the ownership of
host operation and the sustainability of the firm's
competitive advantage. Whether a firm would go solo in the
investment or share with a local firm or let a host or
another home firm own the host operations would depend upon
the extent of sustainability of its competitive advantage in
production- and/or marketing operations.

Sole Ownership of the Firm: As described in Chapter I,
entry modes comprising the complete set have host country
marketing or both production and marketing operations.
Therefore, a firm's sole ownership of host operations means
its full investment in marketing operations or both
production and marketing operations if it decides to carry
out only the marketing or both production and marketing
activities respectively.

As described earlier, the exploitation of production
and/or marketing distinctive competencies requires
substantive amount of resource commitment in appropriate
infrastructures. According to the resource-based
perspective, a firm's actions are guided by the spirit of
profit maximization on its investment. That is, the firm
makes investment in an infrastructural arrangement with the
expectation of reaping above normal return. Also, the firm
may continue to reap above normal return so long as its
competitive advantage is not replicated by competitors.
Therefore, if a firm considers that it has a higher degree of sustainability of competitive advantage in a host country, there is greater likelihood that it would like to tap into these resources by itself to earn above normal returns on them for the long run. That is, the firm would have higher level of confidence in the infrastructural investment it is going to make to reap the returns on its competencies.

Another reason for a firm to prefer a wholly owned operation is that it can provide greater protection to its resources than a shared or a host operation owned by a host or a home firm. This is because the probability of leakage about firm-specific resources and its deployment patterns is least in wholly owned ventures. Thus, if a firm has higher sustainability of a competitive advantage, wholly-owned operations allow it to reap above normal rents and at the same time reduce the probability of leakage of its resources which in turn furthers the sustainability of its advantage.

Shared ownership: A firm may choose to go into shared investment with a host country firm if it finds that it (1) lacks certain types of resources and a host firm has it and (2) there is no significant threat of leakage of its resources to its partner. For example, a firm having a higher degree of sustainability of competitive advantage in production-related activities but with lesser degree of sustainability of competitive advantage in marketing-related
activities may enter into a joint venture with a host firm that has the necessary capabilities to market the firm's products. Likewise, if a firm has lesser degree of sustainability of its competitive advantage in production-related activities but has higher degree of sustainability of competitive advantage in marketing-related activities may again enter into a joint venture with a host firm possessing the necessary distinctive competencies in production-related activities. In both cases, the firm enters into a joint venture with another firm to offset its weaknesses in production or marketing operations. Moreover, such shared operations pose lesser threat to the leakage of the firm's competencies than the ones where partners have similar resources because the partners are bringing with them complementary and not supplementary competencies.

The profits from sharing a venture obviously get divided according to the understanding among the partners. However, still a firm may reap above normal return if the synergy developed from sharing allows the venture to earn above normal profit. Further, the firm does not have to invest in certain unwanted resources to actualize its competitive advantage. Trust is another reason for entering a shared operation.

**Host or Home Firm Ownership:** In this case, a firm's host operations are conducted through an infrastructure owned by another firm. This firm can be a host or another
home firm. Such a situation is said to occur when a firm has lower sustainability of its competitive advantage. For example, if a firm intends to serve a host market through exporting and realizes that its competitive advantage in marketing operations is less sustainable, it may implement its marketing program through other firms. A similar situation is possible when a firm has lower sustainability of its competitive advantage in both production and marketing-related activities. The firm may let its host production and marketing operations to run under a host firm. This is because if the firm invests despite low sustainability, its advantage is likely to be replicated. It may not recover even its principal investment. In short, when a firm’s competitive advantage is not sustainable, it has a higher probability of implementing its host market strategy under the ownership of another host firm.

The above conclusions presuppose that a firm has higher actualizability of competitive advantage in production and/or marketing-related activities in a host country. In case, a firm has lower actualizability of competitive advantage in both the production and marketing activities in a host country, its sustainability of competitive advantage for production and marketing is likely to be lower. This is because, the issue of sustainability is assumed to arise only when its actualizability is high. As described before, a firm would keep its operations at home and use another
home firm's marketing infrastructure in a host country to market its products. The above description provides an answer to the second question of the two entry mode questions listed at the beginning of Chapter III.

Section III: Explanation of Entry Mode Choices

This section explains the choice of a complete set of entry modes based on four key constructs developed in this study. These constructs are: ACAP, ACAM, SCAP, SCAM. The entry modes explained here are: Wholly owned subsidiary (WOS), Joint Venture (JV), Contractual Mode (CM), Export through company owned channel (EX-COMPANY), Export through host intermediary (EX-HOST INT), and Indirect exporting (EXP-INDIRECT).

All six modes entail marketing of a firm's products in a host country. However, the first three modes also involve carrying out of production of the firm's products in the host country. These are referred to as "Host country production modes" in this study. The last three modes are "Export modes" as they invariably entail carrying out production operations in the home country of a firm although, it is possible that the firm may produce in a third country to market its products to the target country.

It is the position of this study that entry mode choice is a sequential decision making process. This position is
in line with the views of Dunning (1980) and Gatignon and Anderson (1988). Figure 5 shows the proposed entry mode choice model. It shows the sequence of decision making leading to the choice of an entry mode. According to the model, a firm first looks at the complete set of modes and decides whether to serve the target host country through a host production or an export mode because both types of modes allow the firm to market its products in the host country. This decision is about the location of production operations to serve the host market. Having made this decision, the firm can now focus on the host country production or the export modes to choose an appropriate entry mode.

Choice of Host Country Production Modes

If the firm decides to employ a host country production mode, then it has to decide whether to produce itself or allow a host firm to produce products based on its technology. This is an issue pertaining to the choice of sole versus no ownership (host firm ownership) of the host production operation. If the firm opts for no ownership, it is said to have entered the host country through a contractual mode. Otherwise, the firm is said to have chosen a FDI mode (WOS or JV). Assuming that a firm has elected to use a FDI mode, the next stage in the decision
RESOURCE-BASED MODEL OF ENTRY MODE CHOICE

Figure 5
making is about whether to market its products by itself or through a host firm. This is an issue of ownership of host marketing operation. Given that the firm already owns production operation, the ownership choice translates into the choice between sole ownership of host production and marketing operations and shared ownership. If the firm resolves to have sole ownership of the host operation, it is said to have chosen a WOS mode otherwise a JV mode.

Choice of Export Modes

Likewise, if the firm decides to employ an export mode, it has to determine whether it should serve the host market through its own marketing infrastructure or through the channels of another home country firm that has an established marketing arrangement in that country. This is once again a decision about the location of marketing infrastructure in the host country. In case the firm decides to locate its marketing structural arrangement in the host country, it is said to be serving the host market through a direct export mode. If it decides to use the marketing arrangement of a home country firm to market its products in a host country, it is said to have chosen an indirect export mode. In this case, the firm is actually engaged in domestic transaction with the home firm.
If the firm decides to choose a direct export mode, then it has to determine whether to market its products in the host country by itself or through a host firm. This is an issue pertaining to the choice between the sole versus no ownership (host firm ownership) of the host marketing operation. If the firm opts for the no ownership mode, it is said to be exporting its products through a host intermediary mode. Otherwise, the firm is said to be exporting its products through a company owned channel mode.

As described before, a firm's decision to locate production operation in a host country is primarily determined by its degree of ACAP in that country and its decision to locate marketing operations is based on the degree of its ACAM in the host market. Its ownership decision of production or marketing operation in a host country is dependent upon a firm's level of SCAP or SCAM in that country. This theme reverberates throughout the development and testing of hypotheses pertaining to the explanation of the entry modes comprising the complete set. The following material develops the hypotheses.

Development of Hypotheses

Choice between Host Production and Export Modes

As described before, host country production modes entail production in the host country whereas export modes
involve serving the target market through production of products anywhere other than the target host market. In line with the argument given above, a firm deciding to exploit its distinctive competencies in production-related activities in a host country may have to establish a plant, install necessary machinery, hire and train production and management personnel, arrange for procurement of necessary raw materials and components in that country. Being a profit maximizing entity, it undertakes these actions with the expectation of reaping above normal returns. If a firm realizes that it has lower level of ACAP in a host market, the likelihood of its reaping above normal returns would also be lower. Therefore, instead of locating its production operations in a host country and losing, there is greater likelihood that the firm may produce at home as before or in a third country. Under such conditions, if the firm is still interested in marketing its products in a host country, it can serve the market through an export mode. This leads to the first hypothesis.

H1: The higher the level of ACAP of a firm in a host country, the greater is its likelihood of choosing a host country production mode (wholly owned subsidiary, joint venture, or contractual method) over an export mode (direct or indirect) in serving that market.

Host Production Modes

Having decided to use a host production mode, the next issue for the firm is to choose between a CM, WOS, or
JV mode. The next two hypotheses describe conditions underlying the choice of CM, WOS, or a JV mode. These choices, as described earlier, are related with the level of SCAP or SCAM of a firm in the host country.

Choice between Contractual and FDI modes: In a contractual mode, a firm allows a host firm to produce and market its products in that country and in turn, it receives royalty or some fee from the host firm. On the other hand, in a FDI mode (as defined in this study), a firm undertakes the production operation; the marketing function may be performed by the firm or a host firm. For example, in a WOS mode, it is the firm that is engaged in carrying out both the production and marketing activities whereas in a JV mode, the firm carries out the production activities and its host partner performs marketing activities in the host country. In short, the difference between a contractual mode and an FDI mode is the type of ownership of the host country production operation and as described before, this is related to the level of a firm’s SCAP in the host nation.

The lower sustainability of a firm’s competitive advantage in production-related activities means that resources underlying its advantage are highly replicable. According to the resource-based theory, this is highly likely when the resources underlying a competitive advantage are fewer, easy to acquire, their substitutes are available, or competitors are equally capable.
Under such conditions, a firm is least likely to serve a host country through a FDI (WOS or JV) mode. Any such attempt would be violating the primary reason for the firm's existence--profit maximization--because, competitors would soon catch up with the firm and in certain cases may be able to produce better substitutes or be able to sell similar products at prices lower than the firm's products. Instead of competing and losing, the firm is better off capitalizing whatever it can on its production-related distinctive competencies. The firm, in such a case, is more likely to enter a host market through a contractual mode (licensing or franchising) rather than a FDI mode. In this mode, the firm takes up a dormant role but it may still have control over the host partner in the form of enforcing of quality standards.

This hypothesis finds support in Contractor's (1984) article. According to him, when the technology of a firm is well-defined, simple, mature or standardized, the licensee is proficient or on par with the licensor, and the opportunity cost of licensing is low, licensing is superior to the FDI modes. This leads to the second hypothesis which deals with the choice among host country production modes.

H2: The lower the level of SCAP of a firm in a host country, the greater is its likelihood of choosing a contractual mode over a wholly owned subsidiary or a joint venture mode in serving that market.
Choice between WOS and JV Modes: A firm is said to be using a WOS mode in a host country if it is engaged in carrying out both the production and marketing activities--sole ownership of host operations. On the other hand, in a JV mode, a firm carries out the production activities and its host partner performs marketing activities in the host country--shared ownership of host operations. Once again, the difference between the WOS and JV modes is the type of ownership.

As described before, a firm has a greater likelihood of fully investing in a FDI operation, if it has higher level of long term sustainability of its competitive advantage in that operation. Higher levels of SCAP and SCAM means that given the host market conditions, a firm has higher confidence in not only establishing a competitive advantage in producing and marketing its products in that country but also in the durability of that advantage. Given highly conducive conditions and little or no threat of competitive replication, a firm has an opportunity to realize its long term goals of profit maximization. In other words, a firm is highly likely to establish an appropriate infrastructure by itself to exploit its distinctive competencies in production- and marketing-related activities. This means, it would choose a wholly-owned subsidiary. On the other hand, a firm would go for a shared FDI operation, if it has higher level of SCAP but lower level of SCAM. By doing so,
the firm buttresses its SCAM. Both these FDI modes have higher degree of SCAP. Therefore the choice between the WOS and JV modes is determined by the degree of SCAM.

Although, a WOS mode may entail investment of resources greater than that needed for a joint venture, the benefits of a WOS far outweigh the potential costs associated with the JV mode. First, in a WOS mode, a firm has full control over its operations which allows it to make strategic and operational decisions unilaterally rather than seeking partner’s permission. These decisions include introduction of new products, investment in new equipment, or hiring or firing of staff. Second, the WOS mode may act as the firm’s outpost for the future. Third, a wholly owned operation endows more non-economic benefits to a firm than a shared operation—joint venture or a contractual mode (Erramilli and Rao 1993). Finally, leakage of a firm’s resources is least in a WOS mode which, in turn, further reduces chances of competitive replication.

In short, given the benefits of a wholly owned operation, a firm with higher level of SCAM has a higher likelihood of choosing a WOS over a JV mode. This argument is in line with the views of Dunning (1980), Hymer (1976), and Rugman (1986). This leads to the third hypothesis concerning the choice among FDI modes.

\[ H3: \text{The higher the level of SCAM of a firm in a host country, the greater is its likelihood of choosing a WOS mode over a JV mode in serving that market.} \]
**Export Modes**

Once a firm decides to enter a market through an export mode, it has three options to choose from. It could serve the host market through either of the two direct export modes: EXP-COMPANY, EXP-HOST INT or an indirect export mode. The following material analyzes the firm's choices among the three export modes.

**Choice between Indirect and Direct Export Modes:** Having lower level of ACAP in host country production operations, a firm may still decide to exploit its distinctive competencies in marketing-related activities in a host country. For that, it may have to establish a warehouse, an appropriate channel of distribution, a sales office, recruit, train and motivate marketing personnel, and control its marketing programs in that country. If the firm finds that it also has lower degree of ACAM in marketing operations in the host market, there is greater possibility that it may locate its marketing-related activities outside the host market; in its home market or in a third country. Under such conditions, if the firm is still interested in serving the host market, it can do so through an indirect export mode. In this case, a firm uses the host marketing channels of another home firm to market its products in that country. This leads to the fourth hypothesis of the study which pertains to the choice among export modes.
H4: The lower the level of ACAM of a firm in a host country, the greater is its likelihood of choosing an indirect export mode over a direct export mode in serving that market.

**Choice between Direct Export Modes:** There are two types of direct export modes considered in this study: export through a host country intermediary mode and export through company owned channel mode. In exporting its products through a host country intermediary, the marketing operations of the firm in that country are carried out under the ownership of a local wholesaler, agent, or a retailer collectively referred as host intermediaries. Whereas in the company owned channel mode, the firm itself markets its products in a host country.

As described earlier, a firm would invest fully in a host country marketing operation if it has higher level of long term sustainability of its competitive advantage in marketing operation. Higher level of SCAM means that, given the host market conditions, a firm has higher confidence in not only establishing a competitive advantage in marketing its products in that country but also in the durability of that advantage. That is, the firm considers that it would be able to make special connections with its target market based on its unique firm-specific resources and competitors are not likely to pose serious threats in the foreseeable horizon. Given highly conducive conditions, a firm has an opportunity to realize its long term goals of profit
maximization. In other words, a firm is highly likely to fully invest in appropriate infrastructures to exploit its distinctive competencies in marketing-related activities if it has higher degree of SCAM.

Given such a host country environment, of the two direct export modes, the firm is more likely to serve the host market by EXP-COMPANY mode rather than the EXP-HOST INT mode. Such a mode provides full control over its marketing activities like promotion or after-sales service which are essential to the sustenance of competitive advantage in marketing of its products. Furthermore, this mode provides a firm an asset crucial to its long term success; Johanson and vahlne (1977) describe this asset as market-specific experiential information. Exporting through host country intermediaries may not enable the firm to generate such an asset that any firm needs so badly in its foreign operations (Denis and Depelteau 1985; Johanson and Wiedershein-Paul 1975).

Of course, exporting through a company owned channel requires larger commitment of strategic resources than the resources required in the other mode. However, the benefits of full control over operations, first hand generation of market-specific information, and other non-economic benefits associated with wholly owned operations (Erramilli and Rao 1993) are likely to outweigh such costs. Therefore, under conditions of higher SCAM in a host country, a firm is more
likely to choose EXP-COMPANY mode rather than the EXP-HOST INT mode to serve that market. This leads to the final hypothesis of the study.

H5: The higher the level of SCAM of a firm in a host country, the greater is its likelihood of choosing the export through a company owned channel mode over the export through a host country intermediary mode in serving that market.

Section IV: Methodology

The primary objective of this section is to describe various steps of the research design this study followed to test the hypotheses. The key reason underlying the specification of a research design is the recognition of its strengths and limitations by the researcher and also to inform the research community about the inherent limitations of the findings (Kidder and Judd 1986). This dissertation used survey research design; the rationale underlying the choice of which is given below.

According to Kidder and Judd (1986), when the goal of a study is to answer questions about the distribution of and relationship among characteristics of entities of a population as they exist in their natural settings, survey research is appropriate. The term "naturally occurring phenomenon" in their work means the processes of life as they occur. The firm's choice of an entry mode can be viewed as a naturally occurring phenomenon as it is the way
a firm serves its foreign clients. Given the primary goal of this study, each hypothesis being tested describes the relationship between a unique set of a firm's ACAP, ACAM, SCAP, or SCAM in a host country and the likelihood of its entry mode choice for that country. Therefore, the selection of survey research as the research design for this study is appropriate. Experimental- or quasi experimental-designs are inappropriate for this study as no attempt is being made to manipulate any of the variable(s) of the population of firms.

A typical survey design of acceptable reliability and validity entails the specification of (1) the population of interest, (2) sampling design, (3) measuring instrument, (4) data collection procedure, and (5) data analysis technique. The following matter describes these aspects for this study.

Population

The Target Population is the population of entities to which the findings of a systematically conducted study should be generalizable. Invariably, it is extremely difficult to get a complete listing of a given target population. In the absence of such listings, studies use Survey Populations as surrogates of their target populations: a subset of the target population defined by the practical considerations of a study. For this study,
the target population is the population of firms engaged in international transactions regardless of their country of origin. This is because the entry mode choice model of this study is generalizable to firms of any country. The survey population for this study, however, comprised U.S. firms engaged in direct and/or indirect international operations. Therefore, the findings of this study, to all intents and purposes, should be generalizable to U.S. firms with international operations.

The 1994 edition of the *Directory of American Firms Operating in Foreign Countries* published by Uniworld Publications was used as the source of listing of the survey population. The primary reasons for its selection were the recency of its contents and an exhaustive listing of firms. The 1994 edition of this directory contains 2,560 U.S. firms with 18,340 subsidiaries abroad.

Sampling Design

All manufacturing firms in the *Directory of American Firms Operating in Foreign Countries* were included in the sample. In other words, law-, insurance-, consulting-, wholesaler-, retailer, and banking etc. type of firms were excluded. This decision was made because the entry mode choice model of this study precludes those firms that do not engage in production and/or marketing of tangible products.
Excluding such firms left the available number of firms in the listing to be 1870.

Sample Size

How large the sample size should be? According to the central limit theorem, a sample of at least thirty units is capable of generating estimates that are comparable to the population estimates. As described, this study purports to explain six discrete states of a qualitative variable--entry mode choice. In order to do that, a sample of 180 usable responses of firms would be more than necessary. According to Cohen and Cohen (1983), with this sample size and alpha = 0.5 (type I error), the statistical power of analysis would be more than 97%. Therefore, a size of 180 is expected to produce sample estimates closer to the population values. Furthermore, studies after studies have indicated that usual survey response rates range between 10% to 30%. Given such an inherent limitation of the survey design, it was decided that any sample size less than the remaining list would be risky to the obtaining of an adequate number of usable responses. Therefore, this study regarded all the 1870 remaining firms as the sampling units.

Having developed a sample design, the next stage was to gather data from the sampling firms. This required the development of a measuring instrument of acceptable reliability and validity and systematic execution of the
instrument on the sample. The following material describes the steps undertaken in obtaining reliable and valid data.

Design of the Measuring Instrument

The instrument used in this study primarily contains four scales measuring four key constructs that are central to the testing of the hypotheses of the proposed model. These constructs are: Actualizability of Competitive Advantage in Host Country Production (ACAP), Actualizability of Competitive advantage in Host Country Marketing (ACAM), Sustainability of Competitive Advantage in Host Country Production (SCAP), and Sustainability of Competitive Advantage in Host Country Marketing operations (SCAM) of the firm. Also, the instrument contained variables on (1) host country factors that are considered to affect a firm's host country production and/or marketing operations, (2) a firm's host country performance, and (3) firm's background. Finally, the instrument also included scales for measuring a firm's (1) control over host country marketing operation and (2) degree of customization of marketing activities for the host market. These scales were developed for future studies and would not be discussed henceforth.

The following material describes the procedure used to develop scales of acceptable reliability and validity to measure ACAP, ACAM, SCAP, and SCAM. The steps listed below
follow the scale development guidelines of Churchill (1979) and DeVellis (1991). The actual scales are provided in the appendix A.

Step 1: Operationalization of Variables

Starting with the definitions of ACAP, ACAM, SCAP, and SCAM, separate pools of items measuring respective constructs were generated. The following material shows how the operationalization was accomplished.

Actualizability of Competitive Advantage

The actualizability of a firm's competitive advantage in a host country represents the likelihood of establishing a position of superiority in the eyes of customers of that country. As described earlier, this construct was defined because of its lack of availability in the literature. The primary reason being that the literature has dealt with situations in which a firm already has an established competitive advantage and not with those in which a firm anticipates the establishment of its advantage.

A review of marketing and management literatures revealed that there are a number of ways in which a firm can establish its competitive advantage. For example, Fahey (1989) provides a list of various bases of competitive advantage such as: product line width, size, price, quality,
reliability, availability, performance, styling, and image. Similarly in his study on managerial perceptions of sustainable competitive advantages, Aaker (1989) used a list of thirty one bases of competitive advantage for service and manufacturing firms. Burke (1984) provides a list of fifteen bases to measure managerial perceptions of their firms' strength vis-a-vis competitors. In addition to the above listed works, other studies used in operationalizing the firm's actualizability of competitive advantage in a host country included the works of Barney (1991), Coyne (1986), Day and Wensley (1988), Ghemawat (1986), and Porter (1985). In short, sufficient literature was available to operationalize a firm's Actualizability of Competitive Advantage in host Production and Actualizability of Competitive Advantage in host marketing.

Three observations were made from the review of the marketing and management literatures. First, there is a broad concurrence on several bases of competitive advantage. Second, despite the existence of multiple bases, the literature does not weight any particular basis more than the others. Therefore, any of the bases mentioned above can be a firm's source of competitive advantage. In fact, firms typically seek advantage over the rivals by combining several bases (Fahey 1989). This has an important implication for the nature of scales developed in this study to tap into the constructs ACAP and ACAM. That is, summated
scales would be ideal for measuring these constructs. Third, the bases listed in these works suggest that a firm can establish its competitive advantage in production and/or marketing operations. The material given below pertains to the listing of items for the constructs ACAP and ACAM.

**Actualizability of Advantage in Host Production:** A firm's Actualizability of Competitive Advantage in Production in a host country represents its likelihood of establishing a superiority in producing products in that country vis-a-vis host country competitors. Based on the literature review, it was found that this superiority can be established in a number of ways. These include producing a product line broader than those of competitors (Aaker 1989; Fahey 1989), producing products at a cost lower than the competitors (Coyne 1986; Fahey 1989). Likewise, being the first producer of a product line (Ghemawat 1986), achieving superior quality levels (Aaker 1989; Coyne 1986; Fahey 1989), more frequent introduction of newer product versions (Aaker 1989; Day and Wensley 1988), superiority in production technology (Aaker 1989), and overall leadership (Porter 1985) are the other bases for generating competitive advantage in production are. The following set of statements were developed to tap into the actualizability of a firm's competitive advantage in host production.

1. Producing products at a cost lower than those of host country competitors
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2. Producing product lines broader than those of host country competitors
3. Being the first producer of its kind in the host country
4. Achieving product quality levels superior to the host country competitors
5. Introducing more newer versions than the host country competitors
6. Achieving greater speed in introducing newer versions
7. Achieving overall leadership among competitors in carrying out host production
8. Achieving superiority in production technology.
9. Achieving overall superiority in the production of products

**Actualizability of Advantage in Host Marketing:** The actualizability of a firm's competitive advantage in marketing operations in a host country represents its level of confidence in establishing superiority in marketing its products in that country. Like the actualizability of competitive advantage in production operation, the literature review also showed that there are various bases for generating competitive advantage in marketing of products as well. For example, establishing greater brand loyalty is a basis of a firm's competitive advantage in marketing of its products (Day and Wensley 1988).
Establishing an advantage in promotional activities is another way in which a firm can exert superiority over its rivals (Aaker 1989, Day and Wensley 1988). Likewise, establishing a superior corporate image, competitive pricing (Coyne 1986; Fahey 1989), largest market share (Aaker 1989; Porter 1985), superiority in distribution and logistics (Rosenbloom 1991), superior positioning of products, superior customer service (Coyne 1986; Day and Wensley 1988), and overall advantage in marketing of products are other bases of generating competitive advantage in marketing operations in a host country. These bases together cover the four "P" of marketing. The following set of statements was developed to tap into the actualizability of a firm's competitive advantage in host country marketing operations.

1. Establishing brand loyalty among host country consumers
2. Establishing advantage in promotional activities in the host country
3. Building a superior corporate image
4. Establishing competitive prices
5. Establishing superiority in distribution and logistics
6. Capturing a sizable market share
7. Achieving superior positioning of the product
8. Providing superior service to host country customers
9. Achieving overall competitive Advantage in host country marketing operations
Sustainability of Competitive Advantage

The sustainability of a firm's competitive advantage represents the likelihood of maintaining its superiority over rivals for a long period of time. For this study, the sustainability of a firm's competitive advantage was operationalized for production- and marketing-based competitive advantages as follows.

Sustainability of Advantage in Host Production: The sustainability of a firm's competitive advantage in host country production represents the likelihood of maintaining its superiority over host country rivals in producing its products for a long time. The following statements were constructed based on the works of Aaker (1989), Barney (1991), Burke (1984), Coyne (1986), and Porter (1985).

1. Replication of firm's low cost production advantage by competitors.
2. Continue to produce a product line broader than the host country competitors.
3. Maintaining an edge in quality over competitors
4. Sustaining leadership in introducing newer versions
5. Maintaining superiority in speed of introducing newer versions
6. Losing superiority of producing reliable products
7. Losing position as a product pioneer
8. Losing advantage in superior production technology
9. Continuing overall leadership among competitors in
carrying out host production

**Sustainability of Advantage in Host Marketing**: As in the case of production operations, the sustainability of a firm's competitive advantage in host country marketing operations represents its likelihood of maintaining leadership position vis-a-vis host country rivals in marketing its products in the host country. The following statements based on the works of Burke (1984) and Porter (1985) were developed to capture a firm's confidence level in sustaining its advantage.

1. Maintaining a superior corporate image
2. Continuing to hold brand loyalty among sizable community of consumers
3. Losing edge in promotional activities
4. In maintaining the leadership among channel members
5. Maintaining superiority in distribution logistics
6. Sustaining a sizable market share
7. Maintaining a superior positioning of the product
8. Preserving a superior service to consumers
9. Losing Price competitiveness
10. Overall Competitive advantage in marketing of products.

**Factors Affecting Host Country Operations**

**Market Size**: The size of a host market reflects a firm's assessment of the potential for its products. Based on the works of Agodo (1978), Aharaoani (1966), and Davidson
(1980a), following items were used to tap into a firm's view of a host market size.

1. Expected sales volume for the main product line
2. Expected target market size for the main product line

**Availability of Raw Materials:** Availability of necessary raw materials and components is essential to a firm's actualizability of competitive advantage in producing its products in a host country. Based on the works of Bass, McGregor, and Walters (1977) and Agodo (1978), following items were used to operationalize the availability of necessary raw materials in a host country.

1. Cost of locally available raw materials
2. Quality of locally available raw materials

**Availability of Skilled Work Force:** Skilled work force is essential to carry out production and/or marketing operations. If the personnel for these operations are costly to acquire in a host country, the firm may not be able to profitably produce and/or market its products. The availability of work force in a host country was measured as follows. These items are based on the works of Bass, McGregor, and Walters (1977) and Agodo (1978).

1. Cost of training local labor to the requirements of production operation
2. Cost of training local marketing personnel to the requirements of marketing operation
**Political Environment**: From the perspective of a firm, the political environment of a host country reflects its (1) inner political conditions and (2) relationship with the home country of the firm (Schollhammer and Nigh 1984). A sudden change in the political environment can threaten the profitability of a firm's host operations. The following items based on the works of Agarwal and Ramaswami (1992), Azar (1980), and Root (1987) were used in obtaining managers' evaluation of host country political environment.

1. Chances of worsening of trade relationship between the host and the home country
2. Chances of host country suddenly imposing new restrictions on transfer of firm's earnings.

**Cultural Distance**: The cultural distance between any two nations represents dissimilarities between the language, values, attitudes, perception, and behavior of their residents. The following items used in measuring the cultural distance were based on the works of Anderson and Coughlan (1987), Davidson (1980b), and Goodnow and Hansz (1972).

1. Similarities in business practices
2. Similarities between the customers of the host and home countries
3. Overall cultural similarities

**Host Government Policies**: Governments make policies to enhance the welfare of their residents. These policies
provide the framework as to what can be produced, promoted and consumed etc. These policies invariably favor their local firms and, by default, end up raising the cost of doing business for foreign firms. On the other hand, under certain specific circumstances, governments do encourage foreign firms to locate their production and/or marketing operations in their countries. Based on the works of Bass, McGregor, and Walters (1977), Davidson and McFetridge (1985), Gatignon and Anderson (1988), Root and Ahmed (1978), following items were developed to measure the impact of host government policies on the production and/or marketing operations of the firm.

1. Restrictions on the production of a product line
2. Restrictions on ownership of business operations
3. Restrictions on marketing of a product line

**Host Country Infrastructure:** The economic infrastructure of a country reflects its level of economic development. The following items were based on the works of Agodo (1978), Bass, McGregor, and Walters (1977), Dahringer and Muhlbacher (1991), and Root and Ahmed (1978) to develop a measure tapping into the infrastructure of a host country.

1. Cost of infrastructure development to carry out production operation
2. Cost of infrastructure development to carry out marketing operation
**Host Country Competition:** Competition to a firm’s host country production and/or marketing operations may stem from local firms, firms from other countries, and even from the home country of the firm. The stronger the competitive intensity, the less sustainable is the firm’s advantage (Reed and DeFillippi 1990). Competitors are strongly motivated to neutralize a firm’s advantage if it poses a serious threat to their market position (Macmillan, McCaffery, and Wijk 1985). They can achieve parity by developing imitations and/or cheaper substitutes of the firm’s resources. The following statements measuring competitive intensity are based on the works of Eliashberg and Robertson (1988), Lusch and Lacznia (1987), and Reed and DeFillippi (1990)

1. Number of existing competitors in the host country
2. Intensity of competition from existing competitors
3. Capabilities of existing competitors
4. Overall level of competition in the host country

**Firm’s Performance in the Host Country**

Firm’s performance in the host country after the entry was measured by three items on a 7 point likert scale with 1 denoting extreme dissatisfaction and 7 extreme satisfaction with the performance. These items were previously used by Cavusgil and Zou (1994) and are listed below.
1. Performance in the host country relative to firm’s expectations at the time of entry
2. Performance in the host country relative to overall corporate performance
3. Performance in the host country relative to the host country competitors.

**Firms’ Background at the Time of Entry**

The background of a firm’s entering into foreign markets was measured by the following items used by Cavusgil and Zou (1994). These items tap into a firm’s size, industry, and international experience prior to entering the target host country.

1. Approximate number of years of international experience at the time of entry into the host country
2. Approximate number of countries the firm was operating in prior to its entry into the host country
3. Industry of the firm
4. Total sales volume at the time of entering the host country
5. Approximately total number of employees at the time of entering the host country
6. Total foreign sales as percent of total sales at the time of entering the host country.
Step 2: Purification of Measures

The items were written in a 7 point Likert scale format. The literature is not clear whether a five point scale format is more or less effective than a seven point scale in capturing variations in individual responses. It was decided to use seven and not five scale categories in eliciting responses. Cox (1980) suggests that this allows researchers to tap into more variability in responses. These items were checked for complexity, ambiguity, double-barreledness, and redundancy. At this point, the items comprising the respective scales were subjected to content validity. This entailed asking four experts (college of business faculty members of a university) to give their opinions about the relevance of items for the respective constructs, the quality of items, and any addition or deletion required.

On receipt of feedback from these experts, the scales were appropriately modified and sent to fifteen college of business faculty members of another University for their judgement regarding the extent of domain sampling of the constructs. This time, these experts were given a structured format to give their feedback. A copy of this format is included in the Appendix B. By this time, each of the four scales were left with eight items.

So far the content validity was checked by university professors. It is possible to have differences between the
jargon used by business researchers and that used by business managers. In order to minimize such differences, a two stage process was followed. In the first stage, the scales were shown to international managers of six local firms. They were asked to describe any word(s) used in the scales and in the entire questionnaire that was alien to their working knowledge. Their feedback was helpful in replacing names of certain entry modes with the names commonly used in the business world. After the appropriate modification were made, a pilot study was carried out in which the instrument was sent to a larger group of international business executives.

Step 3: Pilot Study

In the pilot study, the corrected questionnaires were mailed to the Presidents of 100 firms with international operations that are based in the Southeast region. These questionnaires were accompanied with a cover letter requesting their participation and the importance of their responses to the proposed study. Twenty two firms responded within two weeks of mailing out the questionnaire. A review of the responses suggested that there were no problems about comprehension of contents. However, many firms indicated that they were being barraged with such requests and were reluctant to respond. At this stage, the instrument was ready to be administered to the main population. Given the
low response rate in the pilot study, it was decided to undertake some action to increase the motivation to respond to the questionnaire among respondents. This is described in the following material.

Administering of the Survey Instrument

This study used mail survey to obtain the required data. The response rate of a typical mail survey usually ranges between 10% to 30% and rates beyond 30% are considered exceptions to the norm. Moreover, given that the survey respondents of this study are the presidents of firms, the response rate expectations were placed closer to the lower limit of the usual response rates.

According to Alreck and Settle (1985), Fowler (1988), and Henry (1990), poor response to a survey can be attributed to the following reasons: (1) the instrument does not reach some respondents, (2) some respondents refuse to respond, (3) respondents are unable to respond (4) concern about the lack of anonymity of their responses, (5) lack of motivation to respond, and perceiving the survey as "another" survey.

In order to minimize reduction in response rate due to the reasons cited above, following remedies were undertaken during the administering of the instrument. These remedies are suggested in the works of Fowler (1988) and Alreck and Settle (1985). First, the sampling frame being used in the
study was chosen to be the 1994 list of U.S. firms engaged in international operations. By using the latest list, the number of firms going out of business was reduced. Second, the survey packets were personally addressed to the presidents of firms. Third, an information sheet was included in the packet to minimize nonresponse due to lack of comprehension. Fourth, cover letters were personalized requesting the respondents' participation. Fifth, sending the results of the study to respondents was used as a motivator for their participation. Sixth, respondents were assured of the anonymity of their responses. Finally, reminders were mailed to nonrespondents reminding them of the importance of their responses to the outcomes of the study.

The survey packets mailed to the presidents contained (1) a copy of the questionnaire, (2) cover letter, (3) an information sheet explaining the key terms used in the questionnaire, (4) a blue sheet of paper for requesting the results of the study, and (5) a postage paid return envelope of size # 10. The outgoing survey was mailed through first class mail in 9 X 11 clasp envelopes to ensure that the contents are delivered in reasonably good (uncrumpled) conditions. In short, every effort was made to enhance the credibility, importance, and hence, the response to the survey.
An entry mode is an infrastructure that exhibits a variety of arrangements. There are six such arrangements considered in this study. These are: WOS, JV, CM, EXP-COMPANY, EXP-HOST INT, and EXP-IND modes. As described earlier, the proposed model predicts the choice of these modes in a sequential pattern. In the first stage, the model predicts the choice of host production modes over the export modes. In the second stage, the model analyzes the choice within host country production modes and the export modes respectively. Within the host production modes, the model predicts the choice of a contractual mode from the FDI modes. Finally, the model predicts the choice of a JV mode over a WOS mode. Likewise, within the export modes, the model predicts the choice between direct export modes and the indirect export mode. Finally, within the direct export modes, the model predicts the choice of a EXP-COMPANY mode over the EXP-HOST INT mode. The following material describes the statistical technique chosen to explain various entry mode choices and the rationale underlying the selection of this technique.

In mathematical terms, an entry mode can be conceptualized as a qualitative variable with certain distinct states. In this study, at each sequential stage of the proposed model, two modes of a set represent the two
states of the qualitative variable, entry mode. For example, host production and export modes represent two states of the qualitative variable complete set of entry modes. Likewise, the contractual mode and the FDI modes represent two states of the qualitative variable, host country production modes.

There are two key statistical tools that are appropriate for the analysis of the research question of this study: binomial logistic regression and discriminant analysis. Both techniques belong to the family of regression techniques using discrete dependent variable. However, the binomial logistic regression technique is superior to the discriminant analysis method in the sense that there is no assumption about multivariate normality of the predictor variables (Afifi and Clark 1990; Hosmer and Lemeshow 1989). Furthermore, this technique is considered to provide superior maximum likelihood estimates of coefficients even when all predictor variables become discrete and the probabilities of outcome become smaller (O’Hara, Hosmer, Lemeshow, and Hartz 1982). Therefore, this study chose the binomial logistic regression as the statistical tool for testing the hypotheses.

Being a classification technique, applications of logistic regression are found in a wide range of academic disciplines including marketing, economics, and sociology (Afifi and Clark 1990). Historically, the use of this
technique was confined to medical research. In the entry mode literature, a number of studies have deployed this technique to predict entry mode choices of U.S. firms. These studies include those of Agarwal and Ramaswami (1992), Chu and Anderson (1992), Erramilli and Rao (1993), Gatignon and Anderson (1988), and Klein, Frazier, and Roth (1990).

The binomial logistic regression models the relationship between the dichotomous qualitative outcomes of a group of entities and their determining characteristics. The entities can be individuals or firms with discontinuous and/or continuous type of characteristics. In a typical study, this method anchors one of the dichotomous states of the dependent variable as the reference state and predicts the probability of occurrence of outcome in the other state. The choice of this state depends upon the statistical package. This study used SAS package for testing of hypotheses because it is considered to be a leading software in binomial logistic regression analysis. In the SAS package, the reference state is denoted with a default value of 0; the other state acquires a value of 1. The method calculates a logit function for state 1. The logit function of this state is then used to calculate the probability of occurrence of an outcome in that state. In short, the method can be used to classify an assortment of entities based upon how they score on a set of predictor variables.
This multivariate statistical technique is highly appropriate for analyzing the research question of this study. The following material describes the dependent and the independent variable for entry mode choices in each stage of the model. For each entry mode choice, the mathematical form of the entry mode choice model and the logit function is also given.

**Host Country Production versus Export Modes**

The dependent variable for this stage of the entry mode choice model is dichotomous with levels: host country production modes and export modes. The independent variable is ACAP. The mathematical form of the entry mode choice model is:

\[ P(\text{Choice of Host country Production modes over Export modes}) = f(\text{ACAP}) \]  

The logit function for this model is given by equation 2.

\[ g(X) = \beta_0 + \beta_1 * \text{ACAP} \]  

**Contractual Modes versus FDI Modes**

The dependent variable for the choice between contractual and the FDI modes is obviously dichotomous with levels: contractual modes and FDI modes. The independent variable is SCAP. The mathematical form of the entry mode choice model is:
\[ P(\text{Choice of Contractual modes over FDI modes}) = f(\text{SCAP}) \] (3)

The logit function for this model is given by equation 4.

\[ g(X) = \beta_0 + \beta_2 \times \text{SCAP} \] (4)

**Wholly owned subsidiary versus Joint venture Modes**

The dependent variable for the choice between a wholly owned subsidiary and a joint venture mode is, once again dichotomous with levels: wholly owned subsidiary mode and joint venture mode. The independent variable is SCAP.

The mathematical form of the entry mode choice model is:

\[ P(\text{Choice of Wholly owned subsidiary mode over Joint venture mode}) = f(\text{SCAM}) \] (5)

The logit function for this model is given by equation 6.

\[ g(X) = \beta_0 + \beta_3 \times \text{SCAM} \] (6)

**Indirect versus Direct Export Modes**

The dependent variable for this choice is dichotomous with levels: wholly owned subsidiary mode and joint venture mode. The independent variable is ACAM. The mathematical form of the entry mode choice model is:

\[ P(\text{Choice of Indirect Export mode over Direct Export modes}) = f(\text{ACAM}) \] (7)

The logit function for this model is given by equation 8.
Finally, the dependent variable for this choice is also dichotomous with levels: company owned channel mode and the host country intermediary mode. The independent variable is SCAM. The mathematical form of this entry mode choice model is:

\[ P(\text{Choice of company owned channel mode over Host country intermediary mode}) = f(\text{SCAM}) \] (9)

The logit function for this model is given by equation 10.

\[ g(X) = \beta_0 + \beta_1 \times ACAM \] (8)

\[ g(X) = \beta_0 + \beta_1 \times SCAM \] (10)

In all these equations, the Beta term with subscript "0" represents the constant. All other Betas represent the logistic regression coefficients of respective terms. These coefficients are determined using the maximum likelihood approach. The overall efficacy of a model is determined by the log-likelihood value of the model. The log likelihood value follows the chi-square statistics; large chi-square and small p values indicate the significance of a model. The significance of an individual variable is determined by the Wald Chi-Sq. test. It is the square of the ratio of the coefficient of a variable with its standard error. Large value for a variable indicates the significance of that
variable in the model. The logit function for an entry mode can be used to calculate the estimated probability of the choice of that mode with respect to its reference mode. The general formula used to calculate the probability of the choice of an entry mode is given by the following equation.

\[ P(Y=1/X) = \frac{\exp(g(X))}{1+\exp(g(X))} \] ....(11)

With the obtaining of necessary data and the selection of appropriate data analyzing technique, the next step is the analysis of data leading to testing of hypotheses. This is described in Chapter IV.

Summary of the Chapter

Chapter III entailed a three step process of development of a resource-based entry mode choice model that could explain the complete set of entry modes. In developing this model, the primary motive underlying a firm's international operation was specified. Based on this motive, a resource-based framework explaining the international production and marketing operations of a firm was developed. Within the limits of this framework, the proposed entry mode choice model was developed. The model entails sequential decision making process leading to the choice of various entry modes.
CHAPTER IV

RESULTS

Chapter IV is dedicated to the reporting of the results of this study. These results are presented in three sections. Section I presents the findings on the response to the survey of this study and the key characteristics of the responding firms. The characteristics analyzed in this study include the industrial distribution of firms, their size, and their degree of involvement in international operations. The sample is also analyzed for the types of entry mode chosen by firms for their most recent entries and the distribution profile of these entries over time. The analysis also brings out the degree of satisfaction expressed by firms on their performances in their most recently entered countries. Finally, this section analyzes the nonresponse bias in the sample.

Section II describes the Cronbach’s alpha reliability coefficients of the four measurement scales developed for this study. Also included in this section are the results on the factor structures of the respective scales. Finally, Section III presents the findings resulting from the testing of the hypotheses of the study. With this background, the following material introduces the reader to the detailed presentation of findings of Section I.
Response Rate

Survey packets were sent to 1870 manufacturing firms. Each packet contained a cover letter addressed to the president of the firm, a questionnaire, a help sheet explaining key terms used, a request for the results of the study, and a stamped return envelop. Of these, 212 packets returned undelivered because of two main reasons (1) some firms in the mailing list had wrong addresses and (2) some respondents were no longer employed at the target firms. Of the remaining 1658 firms, 104 refused to participate in the study. The reasons commonly given were: a deluge of such requests, no time for responding, and company policy of not divulging firm-specific facts. Of the remainder 1554 sampling firms, 190 returned the completed questionnaires thereby generating an effective response rate of 12.22%.

The response rate of this study is low but not unusual for populations comprising Presidents/CEOs. This rate is within the range obtained in a number of larger survey studies entailing responses from CEOs or senior executives of corporations. For example, the studies of Achrol and Stern (1988), Anderson, Chu, and Weitz (1987), Dwyer and Welsh (1985), Samiee and Walters (1991) managed to obtain response rates ranging between 15% to 24%.
Out of 190 returned questionnaires, 13 were rejected because they were incomplete on items central to the testing of hypotheses. Of the remaining 177 usable responses, 163 were used for testing the model as 14 came after the analysis had begun.

Overall Sample Characteristics

Tables 5 through 10 exhibit overall characteristics of the responding firms. These characteristics include the industrial background of firms, their size in terms of number of employees and total annual sales, their years of international experience, experience from operations in number of countries, and their foreign sales as percentage of total sales prior to their most recent entries.

Industrial Distribution of Firms

Table 5 shows the industrial distribution of firms. From the table, it is clear that the sample shows a wide representation of industries ranging from those producing agriculture-related products to those producing sophisticated measuring instruments. Among these, there is a dominant representation by the chemical and allied products (SIC code 28), fabricated metal products (SIC code 34), machinery and computers (SIC code 35), and electronic and electric (SIC code 36) industries.


<table>
<thead>
<tr>
<th>INDUSTRY</th>
<th>FREQUENCY</th>
<th>PERCENT</th>
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<tbody>
<tr>
<td>Agricultural products</td>
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<td>0.61</td>
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<tr>
<td>Mining &amp; Quarrying</td>
<td>3</td>
<td>1.84</td>
</tr>
<tr>
<td>Construction</td>
<td>2</td>
<td>1.22</td>
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<td>Food &amp; Kindred products</td>
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<td>Paper &amp; Allied products</td>
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<td>Printing &amp; Publishing</td>
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<td>Primary Metal Industries</td>
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<tr>
<td>Fabricated Metal products</td>
<td>23</td>
<td>14.11</td>
</tr>
<tr>
<td>Machinery &amp; Computers</td>
<td>38</td>
<td>23.31</td>
</tr>
<tr>
<td>Electronic &amp; Electric</td>
<td>24</td>
<td>14.72</td>
</tr>
<tr>
<td>Transportation equipment</td>
<td>4</td>
<td>2.46</td>
</tr>
<tr>
<td>Measuring Instruments</td>
<td>9</td>
<td>5.53</td>
</tr>
<tr>
<td>Misc. Manufacturing industries</td>
<td>3</td>
<td>1.84</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>163</strong></td>
<td><strong>100.00</strong></td>
</tr>
</tbody>
</table>
Size of Firms

Like their industrial representation, the responding firms also exhibit great diversity in terms of their size. The size of a firm is invariably measured in terms of its annual sales volume and/or the number of employees (Anderson and Coughlan 1987; Cavusgil and Zou 1994; Gatignon and Anderson 1988). It is commonly assumed that the larger the number of employees in a firm or the larger its sales volume, the greater is the size of that firm. In this study, these two measures of size comply with the recent study of Cavusgil and Zou (1994). Firms were asked to report their size in terms of their (1) total number of employees and (2) total annual sales in dollars at time of their entries described in the study.

Table 6 exhibits the distribution of responding firms in terms of their number of employees. The firm size ranges from fewer than 50 employees to 5000 or more. As the table shows, the sample is fairly evenly distributed in terms of small, medium, and large firms. Table 7 shows the distribution of responding firms in terms of their total annual sales in dollars. It is clear that the firms exhibit diversity in dollar sales volume extending from annual sales of less than 1 million dollars to more than $2 billion dollars. The data in these two tables suggest that firms of all sizes are engaged in international operations and such ventures are not solely confined to larger firms.
### TABLE 6

**TOTAL EMPLOYEES OF FIRMS AT TIME OF ENTRY**

<table>
<thead>
<tr>
<th>EMPLOYEES</th>
<th>FREQUENCY</th>
<th>PERCENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 50</td>
<td>17</td>
<td>10.50</td>
</tr>
<tr>
<td>50 - 199</td>
<td>22</td>
<td>13.58</td>
</tr>
<tr>
<td>200 - 499</td>
<td>28</td>
<td>17.28</td>
</tr>
<tr>
<td>500 - 1999</td>
<td>43</td>
<td>26.54</td>
</tr>
<tr>
<td>2000 - 4999</td>
<td>22</td>
<td>13.58</td>
</tr>
<tr>
<td>5000 or more</td>
<td>30</td>
<td>18.52</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>162</strong></td>
<td><strong>100.00</strong></td>
</tr>
</tbody>
</table>

*Frequency Missing = 1*
<table>
<thead>
<tr>
<th>SALE (MILLION DOLLARS)</th>
<th>FREQUENCY</th>
<th>PERCENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than $1 million</td>
<td>9</td>
<td>5.55</td>
</tr>
<tr>
<td>1 - 9.99</td>
<td>19</td>
<td>11.73</td>
</tr>
<tr>
<td>10 - 99.99</td>
<td>48</td>
<td>29.63</td>
</tr>
<tr>
<td>100 - 499</td>
<td>48</td>
<td>29.63</td>
</tr>
<tr>
<td>500 - 1999</td>
<td>23</td>
<td>14.20</td>
</tr>
<tr>
<td>Above 2000</td>
<td>15</td>
<td>9.26</td>
</tr>
<tr>
<td>Total</td>
<td>162</td>
<td>100.00</td>
</tr>
</tbody>
</table>

Frequency Missing = 1
Involvement in International Operations

What is the extent of responding firms' involvement in international operations prior to the most recent entry? Firms in the sample exhibit a diverse range of international involvement in terms of their (1) years of international experience, (2) operations in number of foreign countries, and (3) foreign sales. Table 8 exhibits distribution of firms in terms of their years of international experience. It is clear from the table that firms in the sample had international experience ranging from less than five years to more than 40 years. However, more than 70% of the firms had more than 10 years of international experience.

Table 9 shows the distribution of firms in terms of their operations in number of countries at the time of their most recent entry. More than 96% of firms had operations in at least one foreign country and more than 64% firms had operations in more than 10 countries at the time of their most recent entry. Only 3.7% of firms had no international operations prior to their current entry.

Table 10 exhibits the distribution of firms in terms of their foreign sales as a percentage of total sales. The foreign sales of about 22% of firms constituted less than 10% of their total sales. However, for more than 65% of firms, foreign sales constitute 10% to 50% of have their total sales. Only 11.73% of firms have foreign sales exceeding 50% of their total sales.
### TABLE 8

YEARS OF INTERNATIONAL EXPERIENCE AT TIME OF ENTRY

<table>
<thead>
<tr>
<th>YEARS OF EXPERIENCE</th>
<th>FREQUENCY</th>
<th>PERCENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to 5 years</td>
<td>27</td>
<td>16.67</td>
</tr>
<tr>
<td>6 - 10 years</td>
<td>20</td>
<td>12.34</td>
</tr>
<tr>
<td>11 - 24 years</td>
<td>38</td>
<td>23.46</td>
</tr>
<tr>
<td>25 - 39 years</td>
<td>36</td>
<td>22.22</td>
</tr>
<tr>
<td>40 years or more</td>
<td>41</td>
<td>25.31</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>162</strong></td>
<td><strong>100.00</strong></td>
</tr>
</tbody>
</table>

Frequency Missing = 1
<table>
<thead>
<tr>
<th>COUNTRIES</th>
<th>FREQUENCY</th>
<th>PERCENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>NONE</td>
<td>6</td>
<td>3.70</td>
</tr>
<tr>
<td>Up to 5</td>
<td>37</td>
<td>22.84</td>
</tr>
<tr>
<td>6 - 10</td>
<td>15</td>
<td>9.26</td>
</tr>
<tr>
<td>11 - 24</td>
<td>31</td>
<td>19.14</td>
</tr>
<tr>
<td>25 - 39</td>
<td>25</td>
<td>15.43</td>
</tr>
<tr>
<td>40 or more</td>
<td>48</td>
<td>29.63</td>
</tr>
<tr>
<td>TOTAL</td>
<td>162</td>
<td>100.00</td>
</tr>
</tbody>
</table>

Frequency Missing = 1
<table>
<thead>
<tr>
<th>SALE</th>
<th>FREQUENCY</th>
<th>PERCENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>00 % - 10 %</td>
<td>37</td>
<td>22.84</td>
</tr>
<tr>
<td>11 % - 20 %</td>
<td>33</td>
<td>20.37</td>
</tr>
<tr>
<td>21 % - 30 %</td>
<td>28</td>
<td>17.28</td>
</tr>
<tr>
<td>31 % - 40 %</td>
<td>24</td>
<td>14.82</td>
</tr>
<tr>
<td>41 % - 50 %</td>
<td>22</td>
<td>13.58</td>
</tr>
<tr>
<td>Above 51 %</td>
<td>18</td>
<td>11.11</td>
</tr>
<tr>
<td>TOTAL</td>
<td>162</td>
<td>100.00</td>
</tr>
</tbody>
</table>

Frequency Missing = 1
Countries Most Recently Entered

Table 11 shows the list of countries entered most recently by U.S. firms and their frequency of entries in those countries. These entries extend across Asian, African, European, Latin American, and Middle Eastern countries. China was the most frequently entered country followed by Mexico, India, Germany, U.K., and Japan. This pattern is not surprising since China, Mexico, and India have been the major emerging markets recently. Entries were also made into Russia and erstwhile Soviet block countries like Belorus, Estonia and Poland.

Distribution of Entries Over Time

Table 12 exhibits the distribution of firms in terms of the year of their most recent entries. The most recent entries of 81.6 % of firms occurred between 1990 and 1995. About 12 % of firms had their most recent entries during eighties followed by 3.68 % during seventies and 1.84 % prior to 1970. Given the fact that the vast majority of entries were over the past five years, the data is relatively contemporaneous and can be expected to be generally reliable.

Types of Entry Modes Chosen

Table 13 shows the distribution of firms in terms of entry modes chosen in their most recently entered countries.
<table>
<thead>
<tr>
<th>COUNTRIES</th>
<th>FREQUENCY</th>
<th>PERCENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>CHINA</td>
<td>24</td>
<td>14.72</td>
</tr>
<tr>
<td>MEXICO</td>
<td>16</td>
<td>9.82</td>
</tr>
<tr>
<td>INDIA</td>
<td>11</td>
<td>6.75</td>
</tr>
<tr>
<td>U.K.</td>
<td>10</td>
<td>6.13</td>
</tr>
<tr>
<td>GERMANY, JAPAN</td>
<td>9 (EACH)</td>
<td>5.52 (EACH)</td>
</tr>
<tr>
<td>POLAND, RUSSIA</td>
<td>6 (EACH)</td>
<td>3.68 (EACH)</td>
</tr>
<tr>
<td>AUSTRALIA, BRAZIL, CHILE, ITALY</td>
<td>5 (EACH)</td>
<td>3.08 (EACH)</td>
</tr>
<tr>
<td>KOREA, THAILAND</td>
<td>4 (EACH)</td>
<td>2.45 (EACH)</td>
</tr>
<tr>
<td>FRANCE, INDONESIA, SINGAPORE, TAIWAN</td>
<td>3 (EACH)</td>
<td>1.84 (EACH)</td>
</tr>
<tr>
<td>EUROPEAN COMMUNITY, FINLAND,</td>
<td>2 (EACH)</td>
<td>1.23 (EACH)</td>
</tr>
<tr>
<td>GUATEMALA, IRELAND, MALAYSIA,</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SAUDI ARABIA, SWITZERLAND</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ARGENTINA, BELGIUM, BELORUS,</td>
<td>1 (EACH)</td>
<td>0.61 (EACH)</td>
</tr>
<tr>
<td>CANADA, CZECH REPUBLIC, ESTONIA,</td>
<td></td>
<td></td>
</tr>
<tr>
<td>HUNGARY, JAMAICA, LEBANON, MONGOLIA,</td>
<td></td>
<td></td>
</tr>
<tr>
<td>NEW ZEALAND, NICARAGUA, NIGERIA,</td>
<td></td>
<td></td>
</tr>
<tr>
<td>PERU, PHILIPPINES, SOUTH AFRICA,</td>
<td></td>
<td></td>
</tr>
<tr>
<td>TURKEY, VENEZUELA</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>163</strong></td>
<td><strong>100.00</strong></td>
</tr>
</tbody>
</table>
TABLE 12

DISTRIBUTION OF ENTRIES OVER TIME

<table>
<thead>
<tr>
<th>YEAR OF ENTRY</th>
<th>FREQUENCY</th>
<th>PERCENTAGE OF ENTRIES</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990 - 1995</td>
<td>133</td>
<td>81.60</td>
</tr>
<tr>
<td>1980 - 1989</td>
<td>20</td>
<td>12.27</td>
</tr>
<tr>
<td>1970 - 1979</td>
<td>6</td>
<td>3.68</td>
</tr>
<tr>
<td>Prior to 1970</td>
<td>4</td>
<td>2.45</td>
</tr>
<tr>
<td>TOTAL</td>
<td>163</td>
<td>100.00</td>
</tr>
</tbody>
</table>
TABLE 13

TYPES OF ENTRY MODES CHOSEN

<table>
<thead>
<tr>
<th>Entry mode</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wholly owned Subsidiary</td>
<td>33</td>
<td>20.2</td>
</tr>
<tr>
<td>Joint Venture</td>
<td>39</td>
<td>23.9</td>
</tr>
<tr>
<td>Contractual</td>
<td>12</td>
<td>7.4</td>
</tr>
<tr>
<td>Export through company owned channel</td>
<td>29</td>
<td>17.8</td>
</tr>
<tr>
<td>Export through host intermediary</td>
<td>43</td>
<td>26.4</td>
</tr>
<tr>
<td>Indirect Exporting</td>
<td>7</td>
<td>4.3</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>163</strong></td>
<td><strong>100.00</strong></td>
</tr>
</tbody>
</table>
It is clear from the table that export through host country intermediary was chosen by 26.4% of firms, joint venture by 23.9%, wholly owned subsidiary by 20.2% and export through Company owned Channel by 17.8%. The contractual mode was chosen by 7.4%, and indirect export mode by 4.3% of firms. These last two modes seem to be less preferred by American firms with international operations.

Performance of Firms

Three items were included in the questionnaire to elicit firms' performance in their most recently entered countries. These items are: firms' performance in host countries relative to (1) expectations at time of entry, (2) host country firms and (3) their overall corporate performance. Firms were asked to report their performance on seven point Likert scales with 1 being extremely dissatisfactory and 7 being extremely satisfactory.

Table 14 exhibits the distribution of firms in terms of their performance relative to their expectations at time of entry. While, 15.7% of firms were somewhat to extremely dissatisfied, 11.3% were neither dissatisfied nor satisfied with their performance. However, 66.7% of firms were somewhat to extremely satisfied with their performance.

Table 15 exhibits the distribution of firms in terms of their performance relative to host country competitors. While 11.4% of firms were somewhat to extremely
dissatisfied, 20.2% were neither dissatisfied nor satisfied with their performance. However, the performance of 68.4% firms ranged from somewhat satisfactory to extremely satisfactory.

Table 16 exhibits the distribution of firms in terms of their reported performance relative to their overall corporate performance. While 25.4% of firms were somewhat to extremely dissatisfied with their performance, 19.6% were neither dissatisfied nor satisfied with their performance. However, the performance of 55% firms ranged from somewhat satisfactory to extremely satisfactory.

Summarizing the above results, it can be inferred that the data consists of responses from firms that belong to a wide spectrum of manufacturing industries. These firms represent small, medium, and large sized companies and exhibit a diversity in terms of their international involvement. In their recent entries, these firms have targeted emerging markets throughout the world. Their entry mode choices range across the complete set of entry modes. As regards their performance in the most recently entered countries, firms, once again, exhibit a wide diversity in their responses. However, majority of the responding firms show some degree of satisfaction. The above description suggests that the data is likely to exhibit higher degree of representativeness of U.S. firms engaged in international operations.
### TABLE 14

**FIRMS' PERFORMANCE IN HOST COUNTRIES**  
**RELATIVE TO THEIR EXPECTATIONS AT TIME OF ENTRY**

<table>
<thead>
<tr>
<th>Performance</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extremely dissatisfactory</td>
<td>3</td>
<td>1.90</td>
</tr>
<tr>
<td>Dissatisfactory</td>
<td>4</td>
<td>2.53</td>
</tr>
<tr>
<td>Somewhat dissatisfactory</td>
<td>18</td>
<td>11.39</td>
</tr>
<tr>
<td>Neither satisfactory nor satisfactory</td>
<td>28</td>
<td>17.72</td>
</tr>
<tr>
<td>Somewhat satisfactory</td>
<td>47</td>
<td>29.75</td>
</tr>
<tr>
<td>Satisfactory</td>
<td>41</td>
<td>25.95</td>
</tr>
<tr>
<td>Extremely satisfactory</td>
<td>17</td>
<td>10.76</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>158</strong></td>
<td><strong>100.00</strong></td>
</tr>
</tbody>
</table>

*Frequency Missing = 5*
TABLE 15

FIRMS' PERFORMANCE IN HOST COUNTRIES
RELATIVE TO THEIR HOST COUNTRY FIRMS

<table>
<thead>
<tr>
<th>PERFORMANCE</th>
<th>FREQUENCY</th>
<th>PERCENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extremely dissatisfactory</td>
<td>3</td>
<td>1.91</td>
</tr>
<tr>
<td>Dissatisfactory</td>
<td>6</td>
<td>3.82</td>
</tr>
<tr>
<td>Somewhat dissatisfactory</td>
<td>9</td>
<td>5.73</td>
</tr>
<tr>
<td>Neither dissatisfactory nor satisfactory</td>
<td>33</td>
<td>21.02</td>
</tr>
<tr>
<td>Somewhat satisfactory</td>
<td>34</td>
<td>21.66</td>
</tr>
<tr>
<td>Satisfactory</td>
<td>49</td>
<td>31.21</td>
</tr>
<tr>
<td>Extremely satisfactory</td>
<td>23</td>
<td>14.65</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>157</strong></td>
<td><strong>100.00</strong></td>
</tr>
</tbody>
</table>

Frequency Missing = 6
<table>
<thead>
<tr>
<th>PERFORMANCE</th>
<th>FREQUENCY</th>
<th>PERCENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extremely dissatisfactory</td>
<td>5</td>
<td>3.19</td>
</tr>
<tr>
<td>Dissatisfactory</td>
<td>12</td>
<td>7.64</td>
</tr>
<tr>
<td>Somewhat dissatisfactory</td>
<td>24</td>
<td>15.29</td>
</tr>
<tr>
<td>Neither dissatisfactory nor satisfactory</td>
<td>30</td>
<td>19.11</td>
</tr>
<tr>
<td>Somewhat satisfactory</td>
<td>35</td>
<td>22.29</td>
</tr>
<tr>
<td>Satisfactory</td>
<td>35</td>
<td>22.29</td>
</tr>
<tr>
<td>Extremely satisfactory</td>
<td>16</td>
<td>10.19</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>157</strong></td>
<td><strong>100.00</strong></td>
</tr>
</tbody>
</table>

Frequency Missing = 5
Respondents versus Nonrespondents

In order to examine the generalizability of the results of this study, nonresponse bias in the data was examined in three ways. The higher the nonresponse bias, the greater the generalizability of the results over the population of firms with international operations. The first comparison was made between the responding and the nonresponding firms based on their SIC (standard industrial classification) codes to see whether the responses represented the entire manufacturing sector or was limited to few industries. A second comparison was made between responding and nonresponding firms based on the distribution of their employees to check whether the responses were limited to small, medium, or large firms. Finally, a comparison was also made between early and late respondents to see whether the early respondents had certain preference for a limited range of entry modes. Following is the description of the results for the three comparisons.

Table 17 shows differences between the responding and the nonresponding firms in terms of the distribution of their SIC codes. As is clear from the table, certain SIC codes are grouped together. This was done in order to (1) keep the number of categories to a manageable level, (2) leave no cell empty, and (3) at the same time increase frequencies of certain cells above unity. The chi-square value is statistically insignificant ($\chi^2=8.129$ with df= 8).
which shows that the SIC distribution of responding firms is not different from that of nonresponding firms.

Table 18 shows the difference between the responding and nonresponding firms in terms of their distribution of number of employees. The chi-sq. value is found to be insignificant again ($\chi^2 = 3.925$ with df = 5) showing that the two distributions are not different from each other. The results from tables 17 and 18 show that the sample is representative of internationally active U.S. firms.

Table 19 shows if there is any difference in the pattern of entry modes chosen between early and late respondents. The 163 responses for this study were obtained between January 18, 1995 and March 3, 1995. February 9 was chosen as the mid point of this period. Firms responding between January 18 and February 9 were regarded as early respondents and those responding after February 9 were considered as late respondents. The chi-square value is insignificant ($\chi^2 = 1.2029$ with df = 5) shows that there is no significant difference between the distributions of early and late respondents in terms of their entry mode choices.

Evidence presented in tables 17-19 provides optimism that the results are not likely to be tainted with nonresponse bias despite the low response rate. Therefore, the results of this study can be considered to exhibit a high degree of generalizability across the population of U.S. firms with international operations.
<table>
<thead>
<tr>
<th>SIC GROUPINGS</th>
<th>RESPONDENTS</th>
<th>NONRESPONDENTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>1, 14, 17 Agricultural, Mining &amp; quarrying and Construction</td>
<td>6</td>
<td>22</td>
</tr>
<tr>
<td>20 Food and Kindered Products</td>
<td>5</td>
<td>45</td>
</tr>
<tr>
<td>23 Apparel &amp; Leather products</td>
<td>6</td>
<td>65</td>
</tr>
<tr>
<td>24, 32 Lumber &amp; finished products, Stone, Clay, Glass, and Concrete products</td>
<td>8</td>
<td>60</td>
</tr>
<tr>
<td>26, 27 Paper, Printing &amp; Publishing</td>
<td>7</td>
<td>59</td>
</tr>
<tr>
<td>28, 29, 30 Chemicals, Petroleum, Rubber &amp; Plastics</td>
<td>26</td>
<td>235</td>
</tr>
<tr>
<td>33, 34 Primary &amp; Fabricated Metal Products</td>
<td>27</td>
<td>166</td>
</tr>
<tr>
<td>35, 36, 37, 38 Machinery, Computers Electronic, Electrical Transportation, &amp; Measuring Equipment</td>
<td>75</td>
<td>659</td>
</tr>
<tr>
<td>39 Misc. Manufacturing Industries</td>
<td>3</td>
<td>53</td>
</tr>
</tbody>
</table>

TOTAL 163 1364

Chi-Sq = 8.129; df = 8. No significant difference between Respondents and Nonrespondents.
<table>
<thead>
<tr>
<th>NUMBER OF EMPLOYEES</th>
<th>RESPONDENTS</th>
<th>NONRESPONDENTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 50</td>
<td>17</td>
<td>91</td>
</tr>
<tr>
<td>50 - 199</td>
<td>21</td>
<td>174</td>
</tr>
<tr>
<td>200 - 499</td>
<td>28</td>
<td>217</td>
</tr>
<tr>
<td>500 - 1999</td>
<td>43</td>
<td>394</td>
</tr>
<tr>
<td>2000 - 4999</td>
<td>23</td>
<td>205</td>
</tr>
<tr>
<td>5000 and over</td>
<td>30</td>
<td>283</td>
</tr>
<tr>
<td>TOTAL</td>
<td>162</td>
<td>1364</td>
</tr>
</tbody>
</table>

Chi-Sq = 3.925; df = 5. No significant difference between Respondents and Nonrespondents.
<table>
<thead>
<tr>
<th>ENTRY MODES CHOSEN</th>
<th>EARLY RESPONDENTS</th>
<th>LATE RESPONDENTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wholly Owned Subsidiary</td>
<td>24</td>
<td>18</td>
</tr>
<tr>
<td>Joint Venture</td>
<td>16</td>
<td>14</td>
</tr>
<tr>
<td>Contractual Mode</td>
<td>9</td>
<td>3</td>
</tr>
<tr>
<td>Export through Company Owned Channel</td>
<td>16</td>
<td>13</td>
</tr>
<tr>
<td>Export through Host Country Intermediary</td>
<td>24</td>
<td>19</td>
</tr>
<tr>
<td>Indirect Export</td>
<td>4</td>
<td>3</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>93</strong></td>
<td><strong>70</strong></td>
</tr>
</tbody>
</table>

Chi-Sq = 1.2029; df = 5. No significant difference between early and late respondents.
Tables 20 through 23 show how four constructs ACAP, ACAM, SCAP, and SCAM were measured. Each construct has eight items; for each item, the tables show item-total correlations. Following Nunnally's (1978) suggestions, Items # 1 and 2 of ACAP and # 4 of ACAM and # 7 of SCAM were dropped from the respective scales because of low item-total correlations. These items were excluded from estimation of the reported value of cronbach's reliability coefficient for ACAP, ACAM, AND SCAM. Finally, six items measured ACAP, seven items represented ACAM, eight SCAP, and seven comprised SCAM.

Table 24 shows values of means and standard deviations of the four constructs. It was described earlier that items for each scale were measured on 7 point likert scale. The mean value for ACAP was found to be 4.87 with a standard deviation of 1.39. For ACAM, the mean value was 4.95 with a standard deviation of 1.02. Similarly, the mean value for SCAP came out to be 4.47 with a standard deviation of 1.23. Finally, the mean value for SCAM was 4.73 with a standard deviation of 1.08.

Table 24 also shows intercorrelations between ACAP, ACAM, SCAP, or SCAM. These range between .33 and .54, which shows that the constructs are only moderately correlated. Finally, it was found that the value of cronbach's reliability coefficient alpha for ACAP = 0.90, ACAM = 0.87,
SCAP = 0.93, and for SCAP alpha = 0.90. These values are shown in parentheses in the table and for all scales, these are greater than Nunnally's (1978) suggested acceptable value of 0.7. Such high values of reliability coefficients and the distinctness of constructs as apparent from their intercorrelations show that the constructs are being reliably measured by the respective scales. These numbers are particularly impressive given that all of these scales are being proposed and used for the first time.

Factor Analysis: After checking for reliabilities, all items belonging to the four scales were subjected to component factor analysis with varimax rotation. Because of their cross-loading pattern, items #5 from ACAM, and #5 and #6 from SCAM have to be dropped. The resulting 25 items produced simpler factor structure with four factors with items loading in accordance with the desired pattern. Table 25 shows the factor structure of the scales, factor loading of items and their communalities. All items with a single asterisk have factor loadings greater than 0.4 as loadings beyond 0.4 provide meaningful interpretation of a factor structure (Hair, Anderson, and Tatham 1987).

The number of factors retained was based on the most commonly used criterion of retaining factors with eigen value greater than or equal to unity. These four factors together explain 68.75% of the variance. All items pertaining to SCAP load on Factor 1. Likewise, all items
TABLE 20
ITEM-TOTAL CORRELATIONS AND RELIABILITY ESTIMATE
OF THE SCALE FOR ACAP

<table>
<thead>
<tr>
<th>ITEMS</th>
<th>ITEM-TOTAL CORRELATION</th>
<th>Coefficient Alpha</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Being the first producer of our main product line in the host country</td>
<td>.24 **</td>
<td></td>
</tr>
<tr>
<td>2. Producing the main product line at a cost lower than that of host country competitors</td>
<td>.37 **</td>
<td></td>
</tr>
<tr>
<td>3. Producing a broader product line than that of competitors</td>
<td>.73</td>
<td></td>
</tr>
<tr>
<td>4. Producing more reliable products than those of competitors</td>
<td>.82</td>
<td>.90</td>
</tr>
<tr>
<td>5. Achieving superior quality level than those of competitors</td>
<td>.79</td>
<td></td>
</tr>
<tr>
<td>6. Introducing new product versions more frequently than competitors</td>
<td>.68</td>
<td></td>
</tr>
<tr>
<td>7. Establishing superiority in production technology over competitors</td>
<td>.69</td>
<td></td>
</tr>
<tr>
<td>8. Achieving an overall competitive advantage in production of products over host country competitors</td>
<td>.67</td>
<td></td>
</tr>
</tbody>
</table>

** item was dropped
### TABLE 21

**ITEM-TOTAL CORRELATIONS AND RELIABILITY ESTIMATE OF THE SCALE FOR ACAM**

<table>
<thead>
<tr>
<th>ITEMS</th>
<th>ITEM-TOTAL CORRELATION</th>
<th>Coefficient Alpha</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Establishing an advantage in promotional activities</td>
<td>0.64</td>
<td></td>
</tr>
<tr>
<td>2. Building a superior corporate image relative to competitors</td>
<td>0.69</td>
<td></td>
</tr>
<tr>
<td>3. Establishing greater brand loyalty than competitors</td>
<td>0.56</td>
<td></td>
</tr>
<tr>
<td>4. Establishing competitive prices</td>
<td>0.26 **</td>
<td>0.87</td>
</tr>
<tr>
<td>5. Capturing the largest market share</td>
<td>0.56</td>
<td></td>
</tr>
<tr>
<td>6. Providing superior customer service relative to competitors</td>
<td>0.72</td>
<td></td>
</tr>
<tr>
<td>7. Establishing superiority in distribution and logistics over competitors</td>
<td>0.70</td>
<td></td>
</tr>
<tr>
<td>8. Achieving an overall competitive advantage in marketing of products over host country competitors</td>
<td>0.80</td>
<td></td>
</tr>
</tbody>
</table>

** item was dropped
### TABLE 22

ITEM-TOTAL CORRELATIONS AND RELIABILITY ESTIMATE
OF THE SCALE FOR SCAP

<table>
<thead>
<tr>
<th>ITEMS</th>
<th>ITEM-TOTAL CORRELATION</th>
<th>Coefficient Alpha</th>
</tr>
</thead>
<tbody>
<tr>
<td>Long term Likelihood of...</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Competitors replicating our low production cost advantage</td>
<td>0.65</td>
<td></td>
</tr>
<tr>
<td>2. Competitors neutralizing our advantage in producing a broader product line</td>
<td>0.73</td>
<td></td>
</tr>
<tr>
<td>3. Our firm losing its edge in quality over competitors</td>
<td>0.74</td>
<td></td>
</tr>
<tr>
<td>4. Losing superiority in producing reliable products</td>
<td>0.81</td>
<td>0.93</td>
</tr>
<tr>
<td>5. Losing an edge in introducing new products more frequently than competitors</td>
<td>0.79</td>
<td></td>
</tr>
<tr>
<td>6. Losing its position as a pioneer</td>
<td>0.77</td>
<td></td>
</tr>
<tr>
<td>7. Competitors neutralizing our advantage in superior production technology</td>
<td>0.78</td>
<td></td>
</tr>
<tr>
<td>8. Losing our overall competitive advantage in production of products over host country competitors</td>
<td>0.84</td>
<td></td>
</tr>
<tr>
<td>ITEMS</td>
<td>ITEM-TOTAL CORRELATION</td>
<td>Coefficient Alpha</td>
</tr>
<tr>
<td>----------------------------------------------------------------------</td>
<td>------------------------</td>
<td>-------------------</td>
</tr>
<tr>
<td>Long term Likelihood of...</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Firm losing its edge in brand loyalty over host competitors</td>
<td>.71</td>
<td></td>
</tr>
<tr>
<td>2. Firm losing its advantage of superior corporate image</td>
<td>.69</td>
<td></td>
</tr>
<tr>
<td>3. Firm losing its competitive edge in promotional activities</td>
<td>.78</td>
<td></td>
</tr>
<tr>
<td>4. Firm losing its superiority in distribution and logistics</td>
<td>.80</td>
<td>.90</td>
</tr>
<tr>
<td>5. Host country competitors eroding our market share</td>
<td>.66</td>
<td></td>
</tr>
<tr>
<td>6. Firm losing price competitiveness</td>
<td>.60</td>
<td></td>
</tr>
<tr>
<td>7. Firm continuing to provide superior customer service</td>
<td>.32 **</td>
<td></td>
</tr>
<tr>
<td>8. Firm losing its overall competitive advantage in marketing of products over host country competitors</td>
<td>.76</td>
<td></td>
</tr>
</tbody>
</table>

** item was dropped
TABLE 24

MEANS, STANDARD DEVIATIONS, INTERCORRELATIONS, AND COEFFICIENT

ALPHA RELIABILITY ESTIMATES FOR ACAP, ACAM, SCAP, AND SCAM

<table>
<thead>
<tr>
<th>VARIABLES</th>
<th>MEAN</th>
<th>SD</th>
<th>ACAP</th>
<th>ACAM</th>
<th>SCAP</th>
<th>SCAM</th>
</tr>
</thead>
<tbody>
<tr>
<td>ACAP</td>
<td>4.87</td>
<td>1.39</td>
<td>(.90)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ACAM</td>
<td>4.95</td>
<td>1.02</td>
<td>.48</td>
<td>(.87)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SCAP</td>
<td>4.47</td>
<td>1.23</td>
<td>.54</td>
<td>.33</td>
<td>(.93)</td>
<td></td>
</tr>
<tr>
<td>SCAM</td>
<td>4.73</td>
<td>1.08</td>
<td>.36</td>
<td>.44</td>
<td>.49</td>
<td>(.90)</td>
</tr>
</tbody>
</table>

Sample Size N = 163. Reliability estimates appear in parentheses on the diagonal.
<table>
<thead>
<tr>
<th>ITEMS</th>
<th>SCAP</th>
<th>ACAP</th>
<th>ACAM</th>
<th>SCAM</th>
<th>h²</th>
</tr>
</thead>
<tbody>
<tr>
<td>Likelihood of ...</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Producing a broader product line</td>
<td>18</td>
<td>78 *</td>
<td>16</td>
<td>5</td>
<td>.66</td>
</tr>
<tr>
<td>Producing more reliable products</td>
<td>19</td>
<td>87 *</td>
<td>15</td>
<td>10</td>
<td>.82</td>
</tr>
<tr>
<td>Achieving superior quality level</td>
<td>20</td>
<td>83 *</td>
<td>15</td>
<td>13</td>
<td>.77</td>
</tr>
<tr>
<td>More frequent introduction of new product versions</td>
<td>15</td>
<td>71 *</td>
<td>28</td>
<td>12</td>
<td>.60</td>
</tr>
<tr>
<td>Establishing superiority in production technology</td>
<td>28</td>
<td>68 *</td>
<td>25</td>
<td>6</td>
<td>.61</td>
</tr>
<tr>
<td>Achieving an overall competitive advantage in producing a product line</td>
<td>27</td>
<td>64 *</td>
<td>18</td>
<td>21</td>
<td>.57</td>
</tr>
<tr>
<td>Establishing an advantage in promotional activities</td>
<td>6</td>
<td>18</td>
<td>73 *</td>
<td>13</td>
<td>.61</td>
</tr>
<tr>
<td>Building a superior corporate image</td>
<td>-3</td>
<td>25</td>
<td>75 *</td>
<td>21</td>
<td>.68</td>
</tr>
<tr>
<td>Establishing greater brand loyalty</td>
<td>13</td>
<td>6</td>
<td>71 *</td>
<td>5</td>
<td>.52</td>
</tr>
<tr>
<td>Providing superior customer service</td>
<td>12</td>
<td>17</td>
<td>78 *</td>
<td>12</td>
<td>.66</td>
</tr>
<tr>
<td>Establishing superiority in distribution and logistics</td>
<td>8</td>
<td>24</td>
<td>73 *</td>
<td>19</td>
<td>.63</td>
</tr>
<tr>
<td>Achieving an overall competitive advantage in marketing a product line</td>
<td>22</td>
<td>16</td>
<td>77 *</td>
<td>25</td>
<td>.72</td>
</tr>
</tbody>
</table>

NOTE: Printed values are multiplied by 100 and rounded to the nearest integer. Values greater than 0.4 have been flagged by an ‘*’.  

Table 25 Contd. on to the next page...
Table 25 Contd...

**ROTATED FACTOR PATTERN FOR ACAP, ACAM, SCAP, and SCAM**

<table>
<thead>
<tr>
<th>ITEMS</th>
<th>SCAP</th>
<th>ACAP</th>
<th>ACAM</th>
<th>SCAM</th>
<th>h²</th>
</tr>
</thead>
<tbody>
<tr>
<td>Long term likelihood of...</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Competitors replicating low production cost advantage</td>
<td>78 *</td>
<td>-5</td>
<td>18</td>
<td>7</td>
<td>.64</td>
</tr>
<tr>
<td>Competitors neutralizing in producing a broad product line</td>
<td>79 *</td>
<td>12</td>
<td>0</td>
<td>13</td>
<td>.66</td>
</tr>
<tr>
<td>Losing edge in quality</td>
<td>72 *</td>
<td>30</td>
<td>7</td>
<td>16</td>
<td>.64</td>
</tr>
<tr>
<td>Losing superiority in producing reliable products</td>
<td>76 *</td>
<td>34</td>
<td>3</td>
<td>20</td>
<td>.75</td>
</tr>
<tr>
<td>Losing edge in more frequent introduction of new product versions</td>
<td>71 *</td>
<td>38</td>
<td>10</td>
<td>24</td>
<td>.73</td>
</tr>
<tr>
<td>Losing position as a pioneer</td>
<td>73 *</td>
<td>29</td>
<td>8</td>
<td>25</td>
<td>.69</td>
</tr>
<tr>
<td>Competitors neutralizing advantage in superior production technology</td>
<td>81 *</td>
<td>16</td>
<td>15</td>
<td>17</td>
<td>.71</td>
</tr>
<tr>
<td>Losing overall competitive advantage in producing a product line</td>
<td>83 *</td>
<td>21</td>
<td>17</td>
<td>17</td>
<td>.80</td>
</tr>
<tr>
<td>Losing edge in brand loyalty</td>
<td>23</td>
<td>15</td>
<td>12</td>
<td>80 *</td>
<td>.73</td>
</tr>
<tr>
<td>Losing advantage of superior corporate image</td>
<td>15</td>
<td>19</td>
<td>10</td>
<td>85 *</td>
<td>.78</td>
</tr>
<tr>
<td>Losing edge in promotional activities</td>
<td>17</td>
<td>5</td>
<td>18</td>
<td>88 *</td>
<td>.83</td>
</tr>
<tr>
<td>Losing edge in competitive superiority in distribution and logistics</td>
<td>31</td>
<td>0</td>
<td>29</td>
<td>73 *</td>
<td>.71</td>
</tr>
<tr>
<td>Losing overall competitive advantage in marketing a product line</td>
<td>18</td>
<td>19</td>
<td>24</td>
<td>72 *</td>
<td>.63</td>
</tr>
</tbody>
</table>

Variance explained by each factor

<table>
<thead>
<tr>
<th>FACTOR1</th>
<th>FACTOR2</th>
<th>FACTOR3</th>
<th>FACTOR4</th>
</tr>
</thead>
<tbody>
<tr>
<td>5.342228</td>
<td>4.258630</td>
<td>3.877363</td>
<td>3.705585</td>
</tr>
</tbody>
</table>

Final Communality Estimates: Total = 17.183807

Proportion of the total variance explained = 68.74 %
pertaining to the constructs ACAP, ACAM, and SCAM load on Factors 2, 3, and 4. The above described loading patterns of items along with high levels of reliability coefficient are indicators of the construct validity for the four constructs being measured.

SECTION III: TESTING OF HYPOTHESES

This section reports the results of testing of five hypotheses proposed in Chapter III. The reader is referred to figure 5. The hypothesis H1, predicting the choice of a host production mode over an export mode is tested first. Then, within the host production modes, hypothesis H2 tests the efficacy of the prediction of choice between a contractual and FDI modes. Finally within the host production modes, H3, predicting the choice between a wholly owned subsidiary and a joint venture is tested. Having explained the host production modes, the subsequent subject matter tests hypotheses pertaining to export modes. The hypothesis H4 predicting a firm's choice between an indirect export mode and direct export modes is tested next. The last hypothesis tested is H5. It predicts the choice between exporting through a company owned channel mode and the exporting through a host country intermediary mode. The following material tests these hypotheses in the sequence described.
Choice between Host Production and Export Modes

The hypothesis H1 predicted the relationship between a firm’s actualizability of competitive advantage in production-related activities in a host country and its location of production operations in that country. This hypothesis was tested by Model #1. The dependent variable of this model is a dichotomous variable with two levels: host production modes and export modes. The predictor variable of the model is ACAP, which is a continuous variable. The model tested the hypothesis H1 using a binomial logistic regression on the main dataset of the study. The results are presented in row #1 of table 26. The table shows the coefficient of the intercept and the predictor variable and the chi-square statistic of the model. The table also shows the percentage of choices correctly classified by the model. Another statistic, referred as Klecka’s tau, is also provided for the model.

The Model #1 exhibits a chi-square value of 28.871 with DF=1 and is highly significant at p-value of 0.0001. This shows that the model exhibits significant improvement over a model with constant term only. In other words, ACAP is positively and significantly related with a firm’s location of production operation in a foreign country. Hence, the hypothesis H1 is strongly corroborated. A corollary of the above conclusion is that the lower the ACAP of a firm in a
host country, the greater the likelihood of its serving the host country through exporting rather than through producing in the host country.

The model correctly classifies 64.4% of entry mode choices entailing host country production. The classification effectiveness of the model can also be gauged from Klecka' Tau—a statistic that indicates the degree to which a model improves the correct classification of observations as compared to the classification by chance. For this model, the Klecka's Tau is 0.29, which suggests that the model commits 29% fewer errors than chance-based classification.

In order to test the hypotheses pertaining to host production and export modes, the main dataset of the study containing 163 observations was divided into two subsets: subset #1 and subset #2. The subset #1 contained 84 observations on entry modes involving host production operations and the subset #2 entailed 79 observations pertaining to the export modes.

**Host Production Modes**

As described before, hypotheses H2 and H3 predict the choice of host production entry modes. The following material first tests for the hypothesis H2 pertaining to the choice of a contractual mode over the FDI modes. Later, the testing of hypothesis H3 is described.
Choice between Contractual and FDI modes

The hypothesis H2 predicted that a firm with lower degree of SCAP in a host country has a greater probability of choosing a contractual mode over the FDI modes. This hypothesis was tested by Model #2. The dependent variable of model #2 is, once again, a dichotomous variable with two levels: contractual modes and FDI modes. The predictor variable of the model is a continuous variable, SCAP. The hypothesis H2 was tested using a binomial logistic regression on the data contained in subset #1 of the study. The results are presented in row #2 of table 26.

The Model #2 exhibits a chi-square value of 8.992 with DF=1 and is highly significant at p-value of 0.0027. In other words, SCAP is positively and significantly related with a firm’s choice of ownership of production operation in a foreign country. Hence, the hypothesis H2 finds strong empirical support. Alternatively, the lower the SCAP of a firm in a host country, the greater the likelihood of its serving the host country through a contractual mode rather than a FDI mode.

The model correctly classifies 88.1% of entry modes entailing host country production. For this model, the Klecka’s Tau is 0.51, which suggests that the model commits 51% fewer errors than chance-based classification.
### TABLE 26

**LOGISTIC REGRESSION RESULTS**

*(N=163)*

<table>
<thead>
<tr>
<th>Model</th>
<th>Dependent variable</th>
<th>Intercept</th>
<th>ACAP</th>
<th>ACAM</th>
<th>SCAP</th>
<th>SCAM</th>
<th>Model Chi-Sq.</th>
<th>Correct Classification</th>
<th>Klecka's Tau</th>
</tr>
</thead>
<tbody>
<tr>
<td># 1</td>
<td>Host Prod. vs Export modes</td>
<td>0.0263</td>
<td>0.9916</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>28.871</td>
<td>df=1 p=0.0001</td>
<td>64.4 %</td>
</tr>
<tr>
<td># 2</td>
<td>FDI vs Contractual modes</td>
<td>2.0450</td>
<td>...</td>
<td>...</td>
<td>0.9433</td>
<td>...</td>
<td>8.992</td>
<td>df=1 p=0.0027</td>
<td>88.1 %</td>
</tr>
<tr>
<td># 3</td>
<td>Wholly owned subsidiary vs Joint venture</td>
<td>-0.1731</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>0.0822</td>
<td>0.103</td>
<td>df=1 p=0.74</td>
<td>51.4 %</td>
</tr>
<tr>
<td># 4</td>
<td>Direct vs Indirect export modes</td>
<td>3.1023</td>
<td>...</td>
<td>1.3978</td>
<td>...</td>
<td>...</td>
<td>12.519</td>
<td>df=1 p=0.0004</td>
<td>91.1 %</td>
</tr>
<tr>
<td># 5</td>
<td>EXP-COMPANY vs EXP-HOST INT.</td>
<td>-0.4772</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>.4854</td>
<td>2.991</td>
<td>df=1 p=0.08</td>
<td>52.8</td>
</tr>
</tbody>
</table>
Choice between WOS and JV modes

The hypothesis H3 predicted that a firm with higher degree of SCAM in a host country has a greater probability of choosing a WOS mode over a JV mode. This hypothesis was tested by Model #3. The dependent variable of model #3 is, once again, a dichotomous variable with levels: WOS mode and JV mode. The predictor variable of the model is a continuous variable, SCAM. The hypothesis H3 was tested using a binominal logistic regression on the data contained in subset #1 after eliminating observations for the contractual mode. There were 72 observations remaining in the subset #1 after eliminating the cases pertaining to the contractual mode. The results are presented in row #3 of table 26.

The Model #3 has a chi-square value of 0.103 with DF=1 and is insignificant with a p-value of 0.74. In other words, the model with SCAM as a predictor is unable to discriminate between the choice of a WOS and JV. Hence, given the data, the hypothesis H3 does not find empirical corroboration. Since the model is insignificant, its prowess in correctly classifying entry modes is meaningless.

Export Modes

As described before, hypotheses H4 and H5 predict the choice of export modes. The following material first tests
for the hypothesis H5 pertaining to the choice of an indirect export mode over the direct export modes. Later, the testing of hypothesis H5 is described.

Choice between Indirect and Direct Export modes

Hypothesis H4 predicted the relationship between a firm's level of actualizability of competitive advantage in marketing operation in a host country and its location of marketing operations in that country. Like the model for the location of production operations, a binomial logistic regression with ACAM as the predictor variable and the choice between indirect and direct modes as the dichotomous dependent variable was run to test this hypothesis. Model #4 tested this hypothesis on the data in subset #2 of the study. Of the total number of 79 observations comprising this dataset, 72 are on entry modes that entail host country marketing operations in which a firm is directly involved--export through company owned channel and export through host country intermediary. The remaining 7 observations belong to indirect export entry mode.

The results are presented in row #4 of the table 26. The table shows the coefficients of the intercept and the predictor variable and the chi-square statistic for the model. The model 4 has Chi-square value of 12.519 with DF=1 and is significant at p-value of 0.0004. In other words, ACAM is positively and significantly related with a firm's location of marketing operation in a foreign country.
Hence, based on the data of the study, the hypothesis H4 finds strong empirical corroboration.

The model correctly classifies 91.1% of entry modes entailing host country marketing. The Klecka' Tau for this model is 0.45, which is a significantly high value for the predictive accuracy of a model over chance-based classification.

Choice between Direct Export Modes

The hypothesis H5 predicted that a firm with higher degree of SCAM in a host country has a greater probability of choosing a EXP-COMPANY mode over the EXP-HOST INT mode. This hypothesis was tested by Model #5. The dependent variable of this model is, once again, a dichotomous variable with two levels: EXP-COMPANY mode and EXP-HOST INT mode. The predictor variable of the model is a continuous variable, SCAM. The hypothesis H5 was tested using a binomial logistic regression on the data remaining in subset #2 after eliminating observations for indirect export modes. The results are presented in row #5 of the table 26.

The model #5 exhibits a chi-square value of 2.991 with DF=1 and is significant at p-value of 0.08. In other words, SCAM is positively and significantly related with a firm's ownership of marketing operation in a host country. Hence, the hypothesis H5 finds support, of course, this also means that the lower the SCAM of a firm in a host country, the
greater the likelihood of its serving the host country through a EXP-HOST INT mode rather than a EXP-COMPANY mode.

The model correctly classifies 52.8% of entry modes entailing host country marketing operations only. For this model, the Klecka's Tau is 0.02, which suggests that the model commits only 2% fewer errors than chance-based classification.

Summary of the Chapter

Chapter IV described the results of this study in three sections. Section I provided the survey response and the demographic characteristics of the sample. It was observed that despite the low response rate, there was no significant difference between the respondents and the nonrespondents. Section II showed the results on the reliability estimates of the four scales, ACAP, ACAM, SCAP, and SCAM. Also, in this section, the results of factor analysis showed that the scale items loaded on to the proper constructs. Finally, in Section III, the hypotheses testing was carried out using the logistic regression. The results of hypotheses testing were summarized in table 26. The findings reported in this chapter show that the resource-based theory of entry mode choice developed in this study is able to explain the choice of a complete set of entry modes. Next, Chapter V discusses the limitations, implications, and directions for future research emerging from this study.
A firm has a variety of modes to choose from in entering a foreign market and these modes form a complete set. How does it choose an entry mode to implement its product market strategy in a foreign country? It is one of the most important strategic decision made by a firm interested in becoming international. The key reason being that this decision is considered to have direct consequences on the success of the firm (Anderson and Coughlan 1987). Obviously, a firm is expected to evaluate pros and cons of available alternatives before selecting one option that would maximize its ROI. Consequently, the issue of entry mode choice has been a subject of ongoing interest among international business researchers across the world. The following material provides some reflections on the efforts of researchers in entangling this complex issue.

Reflections

Over the past three decades, at least seven major theories have been proposed to explain a firm’s choice of an entry mode. Each of these works have offered new knowledge on the conceptualization of this issue. For example, based
on these works, it is now known that entry mode choice is a
dynamic choice and has significant influence on the host
country marketing program of the firm. It was also shown
that almost all of the published works have followed a
general model of entry mode choice which specifies the entry
mode choice of a firm as a function of its firm-specific,
industry-specific, and host country factors.

As described before, these theories have attacked the
entry mode choice issue from four paradigmatic orientations.
Starting with the seminal theory of Hymer in late sixties to
the work of Anderson and Gatignon in late eighties, four
paradigms were used to conceptualize the entry mode choice
issue. These included the market imperfection, behavioral,
market failure, and environmental paradigms. Despite their
heroic efforts, these theories have been able to provide
only partial explanations to the entry mode choice question
which, inherently requires a comprehensive solution.

Accomplishments of this study

This study took up the challenge to provide a
comprehensive explanation to the entry mode choice issue.
In order to do that, it first analyzed the reasons
underlying the inabilitys of the extant theoretical
frameworks in explaining the complete set of entry modes.
It was revealed in Chapter II that the primary reason for
the failure of these theories in explaining the complete choice set was the restrictiveness of their assumptions about competition. This assumption explains the types of inter-firm relationships that can be explained by a theoretical framework. The more relaxed this assumption in a theory is, the greater the leverage it accords the theory in explaining the finesse in the gradient of inter-firm relationships and vice versa.

As described before, the complete set exhibits a wide variation on the ownership dimension of entry modes. These ownership types correspondingly represent a variety in inter-firm relationships in a firm's international operations. Therefore, accounting for this variation requires the framework to be able to conceptualize the finesse in the inter-firm relationship. The extant theories of entry mode choice were handicapped in doing so. The primary reason underlying their shortcoming was the restrictiveness of the assumption about competition made by their underlying theories of the firm.

Having realized this problem, this study decided to look into the literature for a new theory of the firm that has relatively relaxed assumption about competition. Fortunately, the resource-based theory of the firm was available. Although in its prime stage of development, sufficient amount of literature was available to develop a resource-based theory of entry mode choice in this study.
Starting from the foundations upward, a resource-based entry mode choice theory was constructed within the assumption of the resource-based theory of the firm. Chapter III was dedicated to the development of this framework. The development of this theory enabled the proposition of an entry mode choice model that explains the choice of a complete set of entry modes.

The proposed model utilized four new constructs, ACAP, ACAM, SCAP, and SCAM in offering a comprehensive explanation of the entry mode choice issue, hitherto defying the imagination of scholars. The testing of the entry mode choice model showed significant support for the hypotheses. To sum up, this study developed a resource-based theory of entry mode choice which was used to construct a model that explains the complete set of entry modes. Like any systematic scientific investigation, this study has a set of implications, limitations, and explores the directions for future research. Starting with the assessment of theoretical implications, the following material acknowledges the limitations of the study and offers possible directions for future research.

Theoretical Implications

Three important implications for the literature can be drawn from the study. First, this study offers a holistic
way of conceptualizing entry modes in that, it considers the complete set of entry modes. Based on two structural dimensions, (1) location of host country operation and (2) type of ownership of those operations, the study defines a complete set of entry modes. The set entails modes that require conducting of host country production and those that require the conducting of marketing operations only in the host country. A representation of the complete set defined here entails six modes: wholly owned subsidiary, joint venture, contractual, export through company owned channel, export through host country intermediary, and indirect export modes. The elements of implicit recognition of the existence of complete set of entry modes can be found in the works of Dahringer and Muhlbacher (1991), Goodnow and Hansz (1972), Johanson and Wiedersheim-Paul (1975), and Root (1987). These works, however, stopped short of recognizing it. In that regard, the holistic conceptualization of entry modes is a logical advancement of the perspectives of entry modes used in the works.

By analyzing the complete set of entry modes in a single framework, the study lays foundation for future research with a more comprehensive perspective. The primary reason for adopting a holistic approach is that the entry mode choice of a firm for a country is not a decision made in isolation from its decision about marketing programs for that country. The entry mode decision obviously requires a
careful analysis of pros and cons of all possible alternatives open to a firm before an appropriate mode is chosen. That is why, such a decision is usually made by the top corporate officers of a firm. Therefore, any piecemeal solution to the problem is likely to be suboptimal. In this context, the study offers a comprehensive model for explaining choices of a complete set of entry modes.

The second contribution of this study is the entry mode choice explanations given by the model. Though preliminary, these explanations should find greater relevance to the theoreticians. This is because the model is able to explain a complete set of entry modes in a single framework, which hitherto was considered extremely difficult. This is perhaps the first application of the resource-based theory in explaining entry mode choice behavior of firms. Since the resource-based theory is the most contemporaneous theory of the firm that is considered to offer a better conceptualization of the firm than the earlier theories, this model should provide a fertile ground for thoughtful discourse among scholars. Such an intellectual discourse is essential for the development of a comprehensive theory of international operations of the firm.

Finally, the third contribution of this study to the literature is that it offers four measurement scales. These scales assess a firm's likelihood of establishing a competitive advantage at a location in production-related
activities, marketing-related activities, and the sustainability of those advantages over long term. Studies in the past have measured a firm’s competitive advantage when it had already established that advantage. These scales tap into the likelihood of establishment of the advantages. Therefore, the scales of this study allow a researcher to glean into the process of development of a firm’s competitive advantage. Such ability is unavailable with the extant scales.

As described before, the scales developed for this study are: ACAP, ACAM, SCAP, SCAM. The values of Chronbach’s Alpha for these scales were found to be 0.88, 0.86, 0.93, and 0.90 respectively. Based on the results of factor analysis, these scales show high degree of content validity which is a key step toward measuring construct validities of these scales. Such high values of reliability coefficients of these scales and the simplicity of their factor structures, in turn, corroborates the efficacy of Churchill’s (1979) systematic approach to scale development. Furthermore, because of their higher reliability and content validity, these scales show promise for their usefulness in future research on entry mode choice behavior of firms. These scales may also find use in analyzing the development and growth of small scale firms in third world countries in their domestic or foreign operations at different locations.
Implications of the Results of the Study

This study attempted to explain a firm's choice of six entry modes using a sequential model as described before. These modes are commonly used by firms to enter foreign countries. Of the six modes, three entail carrying out of production and marketing operations in a host country, the other three entail only the marketing operations. The following material discusses the results of the study. In all, five hypotheses explaining choices among six modes were tested sequentially. The following material first describes the sequence of testing of hypotheses and the results of testing later.

Sequence of Testing

The sequence for hypotheses testing used in this study is in line with the works of Anderson and Gatignon (1988), Dunning (1980), and Root (1987). The hypothesis H1, predicting the choice of a host production mode over an export mode was tested first. Then, within the host production modes, hypothesis H2 tested the efficacy of predicting the choice between contractual and FDI modes. Finally, H3, predicting the choice between a wholly owned subsidiary and a joint venture was tested. Having explained the host production modes, the subsequent subject matter tests hypotheses pertaining to export modes. The hypothesis
H4 predicting a firm's choice between an indirect export mode and direct export modes is tested next. The last hypothesis tested is H5 predicting the choice between exporting through a company owned channel and exporting through a host country intermediary.

Results of Testing

The hypothesis H1 predicting the choice of a host production mode over an export mode based on a firm's level of ACAP was strongly supported by the data at a p-value of 0.0001. The model testing the hypothesis could correctly classify 64.4% of entry modes entailing host country production. The Klecka's Tau for this model is 0.29, which suggests that the model commits 29% fewer errors than chance-based classification. This hypothesis states that a firm is more likely to choose a FDI mode for a host country if it has a higher level of actualizability of competitive advantage in production in the host country. Unlike the PLC theory, this statement does not suggest whether the ACAP of a firm would be higher or lower in a given stage of its product life cycle. Therefore, a strong empirical support for this hypothesis questions the predictions of the PLC theory according to which a firm chooses a FDI mode over exporting in the later stages of its life cycle.

On the other hand, the corroboration of H1 offers validity to the findings of Bass, McGregor, and Walters
(1977), Goodnow and Hansz (1972). Unlike a plethora of other studies, these works like the present study have attempted to take a holistic view of the host market in explaining FDI operations of U.S. firms.

The hypothesis $H_2$ predicting the choice between a contractual mode and FDI modes was also strongly supported at p-value of 0.0027. The model testing this hypothesis could correctly classify 88.1% of entry modes entailing host country production. For this model, the Klecka's Tau is 0.51, which suggests that the model commits 51% fewer errors than chance-based classification. This hypothesis states that a firm would show greater propensity to choose a contractual mode over a FDI mode if the level of its SCAP is lower. In a way, the support for this hypothesis is a support of Hymer's results. However, this support not back Hymer's advocated basis for the choice of FDI mode. Hymer suggested that controlling of competition is essential to the survival of a firm's advantage. This study, on the other hand, advocates that the primary way of enhancing the life of a firm's advantage is the controlling of its policies directed at creating unique and valuable resources. The support for $H_2$ has important implications for managers. That is, a careful and deliberate policy is essential for the generation of superiority in the market. This may require investment in R&D activities in appropriate areas of the firm.
The hypothesis H3 predicting the choice between a wholly owned subsidiary mode and a joint venture JV mode was not supported by the data of the study. The model testing this hypothesis was insignificant. Therefore, its prowess in correctly classifying entry modes is meaningless.

The Hypothesis H4 predicting a firm's choice between indirect export mode and direct export modes was strongly corroborated at p-value of 0.0004. The model testing this hypothesis managed to correctly classifies 91.1% of entry modes entailing host country marketing. The Klecka' Tau for this model is 0.45, which is a significantly high value for the predictive accuracy of a model over chance-based classification. The empirical corroboration of this hypothesis provides an indirect support to the findings of Upsala school according to which, a firm moves to a direct export mode from an indirect export mode when its experiential knowledge about the market has risen to a level that makes the firm comfortable in increasing its market commitment. In a way, it is a statement about the development of a firm's superiority in a given market. However, this semblance of support for the findings of Upsala school does not corroborate their gradual resource commitment view of entry mode choice.

Finally, the hypothesis H5 predicting the choice between exporting through a host intermediary and a company owned channel was also supported at p-value of 0.08. This
model correctly classified 52.8% of entry modes entailing host country marketing operations only. For this model, the Klecka's Tau is 0.02, which suggests that the model commits only 2% fewer errors than chance-based classification. The empirical support for this hypothesis questions the time delayed approach to entry mode choice advocated by the Upsala school.

In this study, five out of six hypotheses were strongly supported. These results have at least two implications. First, they overwhelmingly support this study's attempt at using a holistic approach for entry mode analysis. Second, the results corroborate the validity of using the resource-based theory of the firm in entry mode analysis. Finally, these results support this study's assertions about the contemporary irrelevance of the PLC, theory, Hymer's theory, and the Internationalization theory in explaining the entry mode choices of firms in the high-paced competitive environment.

Limitations of the Study

There appear to be three main shortcomings of this study. First, the study in its current form, is primarily restricted to the analysis of firms that manufacture tangible products. For analyzing the entry mode choices of service firms, the model needs to be modified to include
characteristics unique to service firms. Second limitation is that the scales developed in this study, though show higher reliabilities, and content validity, have not been tested for convergent and discriminant validity. As a result, unless a substantive body of empirical findings emerges, the scales should be used with caution.

Third limitation of the study stems the research design. Survey research design was used to gather data for testing the model of the study. Therefore the data gathered suffers from weaknesses characterizing the design. One such weakness commonly experienced is the low response rate and this study was no exception to the rule. Although the tests comparing respondents with nonrespondents on various characteristics show that there could have been no difference in the results had the nonrespondent responded, higher rates could have given more confidence in the interpretation of the findings of the study. Another weakness common to survey design is that respondents may give distorted responses to items when asked to rate the degree of weakness of their firms on those items. Finally, this is a new theory in the entry mode literature. Moreover, this study entails the first testing of the predictions of the new theory. Therefore, the findings of this study though encouraging should be interpreted with caution. Moreover, no causal generalization can be made at this juncture.
Directions for Future Research

The following directions for future research seem to emerge from the study. First, the proposed model offers a fertile ground for refinement, modification, or improvement of the proposed framework. This, in the language of Kuhn (1967) offers enormous opportunities for mopping and cleaning of the framework. Second, the model in its current form can be extended to explain a number of foreign production modes like sourcing, production in free trade zones franchising etc. Third, the model can be extended to explain the entry mode choices of service firms by incorporating appropriate characteristics unique to service firms. Fourth, the model of resource-based entry mode choice proposed in this study has the potential for explaining the relationship between a firm's choice of an entry mode for a foreign country and its degree of customization or standardization of marketing strategies for that market. Finally, this study open up the possibilities of developing an analytical tool targeted at analyzing competitive strategies.

To sum up, the present study offers a new paradigm for international business researchers. The use of this paradigm allows researchers to analyze the phenomenon of foreign market entry as a network of interrelated rather than isolated decisions. This holistic approach can lead to
the development of a comprehensive theory of international operations of the firm. The preliminary empirical results of the study are highly encouraging. This study, however, like any other systematically conducted study has its own share of methodological limitations as described before. Notwithstanding these flaws, the framework proposed in this work offers tremendous opportunities for furthering our understanding of the international operations of firms initiated by Southard (1937) and later developed by Vernon (1966), Hymer (1976), Buckley and Casson (1976), Dunning (1980), Anderson and Gatignon (1986).
APPENDIX A
January 12, 1995

Dear Mr. :

I am Assistant Professor of Marketing at the Christopher Newport University. For my doctoral thesis, I recently proposed a resource-based theory of international entry mode choice, which in the view of my dissertation committee is the most comprehensive theory proposed so far. Through this theory, I plan to explain foreign market entry mode choices of firms and their decision making leading up to those choices. For testing the explanatory power of my theory, I am surveying a nationwide sample of executives of internationally active U.S. firms and you are a part of that sample. Please find appended with this letter a questionnaire, an information sheet, a request for results of the study (blue sheet), and a stamped return envelope.

U.S. firms are known to use a variety of entry modes—exporting, licensing, wholly owned subsidiary, and joint venture etc. to enter foreign markets. The existing theories terribly fall short in explaining such a diverse range of entry mode choices. On the other hand, the framework of my theory can. Furthermore, it has the ability to provide strategic implications for firms that plan to enlarge or divest their existing foreign business operations.

Mr. , I will be extremely grateful if you participate in this study and provide information on your firm’s decision making during the most recent entry mode choice for a foreign market. The information, comments, and insights that you will provide would enable me to test the robustness of the proposed theory. I am confident that the results of this study would not only provide foreign market entry-related implications for U.S. firms but would also influence the thinking of researchers in this field.

Mr. , your response is invaluable anytime you care to make but an early reply would enable me to meet the deadline for completion of my degree. Your participation is completely voluntary. If, for any reason, you choose not to participate in the study, I would be grateful if you ask another executive in your company familiar with foreign operations to complete the questionnaire. I assure you of confidentiality of your response.

Please complete the questionnaire and return it to me in the stamped envelope provided. I will be very happy to send you (1) a general summary of results and/or (2) a comparison of your firm’s entry strategy vis-à-vis other firms in your industry if you return the blue sheet along with completed questionnaire as well.

Thank you very much.

Sincerely,

Varinder M. Sharma
(Assistant Professor of Marketing)
I. INFORMATION ABOUT MOST RECENT FOREIGN MARKET ENTRY

A. Most recently, which foreign country did your firm enter?

(Please choose ONE entry you are familiar with or were personally involved with)

B. Approximate year of entry

C. Please describe the PRINCIPAL PRODUCT LINE your firm introduced in this host country?

D. Which ONE of these entry modes BEST describes your firm’s business operation AT TIME OF ENTRY into THIS HOST COUNTRY? For definitions of these terms, please see the enclosed assistance sheet.

(Check ONE mode only)

<table>
<thead>
<tr>
<th>TYPE OF ENTRY MODE</th>
<th>AT TIME OF ENTRY</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Wholly Owned Subsidiary (Direct Foreign Investment with 100 percent ownership)</td>
<td></td>
</tr>
<tr>
<td>2. Joint Venture with Majority Equity</td>
<td></td>
</tr>
<tr>
<td>3. Joint Venture with Equal Partnership (50/50)</td>
<td></td>
</tr>
<tr>
<td>4. Joint Venture with Minority Equity</td>
<td></td>
</tr>
<tr>
<td>5. Licensing</td>
<td></td>
</tr>
<tr>
<td>6. Franchising</td>
<td></td>
</tr>
<tr>
<td>7. Exporting through firm’s Foreign Sales Subsidiary/Branch</td>
<td></td>
</tr>
<tr>
<td>8. Exporting Directly to the End Users</td>
<td></td>
</tr>
<tr>
<td>9. Exporting through a Host Country Firm (distributor/wholesaler/agent)</td>
<td></td>
</tr>
<tr>
<td>10. Exporting through another U.S.-based firm (agent/manufacturer/cooperative/distributor)</td>
<td></td>
</tr>
<tr>
<td>11. A Collaborative Agreement (please specify)</td>
<td></td>
</tr>
<tr>
<td>12. Any other mode (please specify)</td>
<td></td>
</tr>
</tbody>
</table>
E. Please indicate to what degree you AGREE or DISAGREE with each of the following statements concerning your firm's entry mode choice AT TIME OF ENTRY into this host country.

<table>
<thead>
<tr>
<th>Disagree strongly</th>
<th>Agree strongly</th>
</tr>
</thead>
</table>

WE CHOSE THIS ENTRY MODE . . .

1. Because we generally use the same mode
to enter all foreign countries .......................... 1 2 3 4 5 6 7

2. After analyzing all available entry mode options ........................................ 1 2 3 4 5 6 7

3. Because it would give us the greatest competitive advantage .......................... 1 2 3 4 5 6 7

4. Because of limited financial resources ........................................ 1 2 3 4 5 6 7

F. Please indicate to what degree you AGREE or DISAGREE with each of the following statements.

<table>
<thead>
<tr>
<th>Disagree strongly</th>
<th>Agree strongly</th>
</tr>
</thead>
</table>

WE ENTERED THIS HOST COUNTRY TO . . .

1. Limit competitive threats to our strategic interests .......................... 1 2 3 4 5 6 7

2. Gain access to technology and knowhow ........................................ 1 2 3 4 5 6 7

3. Beat saturation in the U.S. market ........................................ 1 2 3 4 5 6 7

4. Gain easier access to other countries in this geographic region .......................... 1 2 3 4 5 6 7

5. Exploit business opportunities in this emerging market .......................... 1 2 3 4 5 6 7

II. HOST COUNTRY FACTORS AT THE TIME OF ENTRY

G. For each of the following items, please give your assessment about THIS HOST COUNTRY'S BUSINESS CONDITIONS relative to the U.S. at the TIME OF ENTRY into this country.

<table>
<thead>
<tr>
<th>Extremely small/low</th>
<th>Extremely large/high</th>
</tr>
</thead>
</table>

AT TIME OF ENTRY INTO THIS HOST COUNTRY . . .

1. Expected sales volume for our main product line was .......................... 1 2 3 4 5 6 7

2. Expected target market size for our product line was .......................... 1 2 3 4 5 6 7

3. Chances of unexpected worsening of trade relationship between this host country and the U.S. were .......................... 1 2 3 4 5 6 7

4. Chances of this host country suddenly imposing new restrictions on transfer of our firm's earnings were .......................... 1 2 3 4 5 6 7
<table>
<thead>
<tr>
<th></th>
<th>Extremely small/low</th>
<th>Extremely large/high</th>
</tr>
</thead>
<tbody>
<tr>
<td>5.</td>
<td>Similarities between business practices of this host country and that of U.S. were</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>6.</td>
<td>Similarities between customers of this host country and that of U.S. were</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>7.</td>
<td>Overall similarities between culture of this host country and that of U.S. were</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>8.</td>
<td>Cost of locally available raw materials was</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>9.</td>
<td>Quality of locally available raw materials was</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>10.</td>
<td>Cost of training local labor to the requirements of our production operation was</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>11.</td>
<td>Cost of training local marketing personnel to the requirements of our marketing operation was</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>12.</td>
<td>Host government restrictions on production of our product line were</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>13.</td>
<td>Host government restrictions on marketing of our product line were</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>14.</td>
<td>Host government restrictions on our ownership of business operation(s) were</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>15.</td>
<td>Cost of infrastructure development to carry out production operation was</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>16.</td>
<td>Cost of infrastructure development to carry out marketing operation was</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>17.</td>
<td>Number of existing competitors in this host country was</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>18.</td>
<td>Intensity of competition from existing competitors was</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>19.</td>
<td>Capabilities of existing competitors were</td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td>20.</td>
<td>Overall level of competition in this host country was</td>
<td>1 2 3 4 5 6 7</td>
</tr>
</tbody>
</table>
III. ESTABLISHMENT AND SUSTAINABILITY OF COMPETITIVE ADVANTAGE IN THIS HOST COUNTRY

For a firm entering a foreign country, ESTABLISHMENT OF COMPETITIVE ADVANTAGE means the likelihood of achieving an edge over the competitors in that country. On the other hand, SUSTAINABILITY OF COMPETITIVE ADVANTAGE means the likelihood of maintaining that edge for a long time.

Items on this page represent various ways in which firms establish their COMPETITIVE ADVANTAGE over their rivals. Please respond to each item by circling a number. Please respond EVEN IF YOUR FIRM DID NOT PRODUCE OR MARKET its products in this host country.

H. ESTABLISHMENT OF COMPETITIVE ADVANTAGE IN PRODUCTION

AT TIME OF ENTRY INTO THIS HOST COUNTRY, OUR FIRM'S . . . Extremely Extremely
small/low large/high

1. Likelihood of being the FIRST PRODUCER of the product line
   (page 1 #C) in this host country was ........................................ 1 2 3 4 5 6 7

2. Likelihood of producing this product line AT A COST LOWER than
   that of competitors was ....................................................... 1 2 3 4 5 6 7

3. Likelihood of producing a BROADER product line
   than that of competitors was .................................................. 1 2 3 4 5 6 7

4. Likelihood of producing MORE RELIABLE products
   than that of competitors was .................................................. 1 2 3 4 5 6 7

5. Likelihood of achieving SUPERIOR QUALITY LEVEL
   than that of competitors was .................................................. 1 2 3 4 5 6 7

6. Likelihood of introducing new product versions
   MORE FREQUENTLY than the competitors was .............................. 1 2 3 4 5 6 7

7. Likelihood of establishing SUPERIORITY in
   PRODUCTION TECHNOLOGY over competitors was ........................ 1 2 3 4 5 6 7

8. Likelihood of achieving an OVERALL COMPETITIVE ADVANTAGE
   in PRODUCING our products in this host country was ................. 1 2 3 4 5 6 7

I. ESTABLISHMENT OF COMPETITIVE ADVANTAGE IN MARKETING

AT TIME OF ENTRY INTO THIS HOST COUNTRY, OUR FIRM'S . . . Extremely Extremely
small/low large/high

1. Likelihood of establishing an ADVANTAGE IN
   PROMOTIONAL ACTIVITIES over competitors was ....................... 1 2 3 4 5 6 7

2. Likelihood of building a SUPERIOR CORPORATE IMAGE
   relative to competitors' was ................................................. 1 2 3 4 5 6 7
AT TIME OF ENTRY INTO THIS HOST COUNTRY, OUR FIRM’S...  

<table>
<thead>
<tr>
<th>Item</th>
<th>Extremely Small/Low</th>
<th>Extremely Large/High</th>
</tr>
</thead>
<tbody>
<tr>
<td>3. Likelihood of establishing GREATER BRAND LOYALTY than that of competitors was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>4. Likelihood of establishing COMPETITIVE PRICES was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>5. Likelihood of capturing the LARGEST MARKET SHARE in the host country market was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>6. Likelihood of Providing SUPERIOR CUSTOMER SERVICE relative to that of competitors was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>7. Likelihood of establishing SUPERIORITY in distribution and logistics over competitors was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>8. Likelihood of achieving an OVERALL COMPETITIVE ADVANTAGE in MARKETING of our products in this host country was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
</tbody>
</table>

Each of the following items represents a firm’s ASSESSMENT about the likelihood of SUSTAINING its COMPETITIVE ADVANTAGE over its rivals for a LONG TIME. Please respond to each item by circling a number.

J. SUSTAINABILITY OF COMPETITIVE ADVANTAGE IN PRODUCTION

<table>
<thead>
<tr>
<th>Item</th>
<th>Extremely Small/Low</th>
<th>Extremely Large/High</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Long term likelihood of competitors REPLICATING our low production-cost advantage was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>2. Long term likelihood of competitors NEUTRALIZING our advantage in producing a broad product line was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>3. Long term likelihood of our firm LOSING its edge in quality relative to competitors was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>4. Long term likelihood of our firm LOSING its superiority in producing reliable products was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>5. Long term likelihood of our firm LOSING its edge in introducing newer products more frequently than competitors was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>6. Long term likelihood of our firm LOSING its position as a PIONEER was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>7. Long term likelihood of competitors NEUTRALIZING our advantage in superior production technology was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>8. Long term likelihood of our firm LOSING ITS OVERALL COMPETITIVE ADVANTAGE in PRODUCING its products was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
</tbody>
</table>
K. SUSTAINABILITY OF COMPETITIVE ADVANTAGE IN MARKETING

AT TIME OF ENTRY INTO THIS HOST COUNTRY . . .

<table>
<thead>
<tr>
<th></th>
<th>Extremely small/low</th>
<th>Extremely large/high</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Long term likelihood of our firm LOSING its edge in brand loyalty</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>over host country competitors was</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Long term likelihood of our firm LOSING its advantage of</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>superior corporate image was</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Long term likelihood of our firm LOSING its competitive edge</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>in promotional activities was</td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Long term likelihood of our firm LOSING its competitive</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>superiority in distribution and logistics was</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Long term likelihood of host country competitors ERODING</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>our market share was</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Long term likelihood of our firm LOSING its</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>price-competitiveness was</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. Long term likelihood that our firm would CONTINUE to provide</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>superior customer service was</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8. Long term likelihood of our firm LOSING ITS OVERALL</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>COMPETITIVE ADVANTAGE in MARKETING its products was</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

IV. OUR FIRM'S INFLUENCE OVER ITS MARKETING ACTIVITIES IN THIS HOST COUNTRY

L. Please circle a number that best describes YOUR FIRM'S DEGREE OF INFLUENCE on each of
the following host country Marketing activities pertaining to your principal product line.

<table>
<thead>
<tr>
<th></th>
<th>Extremely small/low</th>
<th>Extremely large/high</th>
</tr>
</thead>
<tbody>
<tr>
<td>AT TIME OF ENTRY, OUR FIRM'S INFLUENCE OVER . . .</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Selection of PRODUCTS in the host country was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>2. Selection of BRAND NAMES of products was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>3. Design of PRODUCT LABELS was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>4. Design of PACKAGING for products was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>5. Selection of ADVERTISING MESSAGES for the host country was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>6. Development of SALES PROMOTION PROGRAM was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>7. Management of SALES PERSONNEL was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>8. Decisions pertaining to DISTRIBUTION and LOGISTICS in the host country was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>9. Decision about DISTRIBUTORS' handling of products was</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>10. Decisions about PRICING OF PRODUCTS to</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>local wholesalers/retailers was</td>
<td></td>
<td></td>
</tr>
<tr>
<td>11. Decisions about PRICING OF PRODUCTS to</td>
<td>1 2 3 4 5 6 7</td>
<td></td>
</tr>
<tr>
<td>final customers was</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
V. CUSTOMIZATION OF MARKETING ACTIVITIES 
FOR THIS HOST COUNTRY

M. For each of these items, please circle a number that best describes the extent of CHANGES made, AT TIME OF ENTRY, to your marketing activities in this host country RELATIVE TO YOUR MARKETING ACTIVITIES IN THE U.S. Also, for each item, circle the letter "V" or "M" indicating whether those CHANGES were voluntary or mandatory (to comply with host government regulations).

<table>
<thead>
<tr>
<th>Extremely small/low</th>
<th>Extremely large/high</th>
<th>Voluntary/ Mandatory</th>
</tr>
</thead>
</table>

AT TIME OF ENTRY, CHANGES MADE TO...

1. The FORMULATION/DESIGN of our principal product line were ......... 1 2 3 4 5 6 7 V M
2. The LABELS of our product line were ............... 1 2 3 4 5 6 7 V M
3. The BRAND NAME(S) of our product line were ................. 1 2 3 4 5 6 7 V M
4. The PACKAGING of our product line were .................. 1 2 3 4 5 6 7 V M
5. The POSITIONING of our Product line were ................... 1 2 3 4 5 6 7 V M
6. Our firm's ADVERTISING MESSAGE were ........ 1 2 3 4 5 6 7 V M
7. Our firm's SALES PROMOTION program were ................. 1 2 3 4 5 6 7 V M
8. Our firm's SALES PERSONNEL policy were .................. 1 2 3 4 5 6 7 V M
9. Our firm's PRICING policy for local wholesalers/retailers were ............. 1 2 3 4 5 6 7 V M
10. Our firm's PRICING policy for final customers were .............. 1 2 3 4 5 6 7 V M
11. The firm's LOGISTICS and DISTRIBUTION were ................ 1 2 3 4 5 6 7 V M
12. Our policy of SEEKING COOPERATION from wholesalers/retailers were .............. 1 2 3 4 5 6 7 V M
13. Our policy of SELECTING wholesalers/retailers were .............. 1 2 3 4 5 6 7 V M
14. Our Policy of SELECTING distribution channels were ............. 1 2 3 4 5 6 7 V M
VI. ABOUT OUR FIRM

N. OUR FIRM'S PERFORMANCE IN THIS HOST COUNTRY . . .

1. Relative to our EXPECTATIONS AT TIME OF ENTRY is
   (Extremely dissatisfactory) 1 2 3 4 5 6 7 (Extremely satisfactory)

2. Relative to our OVERALL CORPORATE PERFORMANCE is
   (Extremely dissatisfactory) 1 2 3 4 5 6 7 (Extremely satisfactory)

3. Relative to our HOST COUNTRY COMPETITORS is
   (Extremely dissatisfactory) 1 2 3 4 5 6 7 (Extremely satisfactory)

O. OUR FIRM'S BACKGROUND . . .

1. Approximate NUMBER of YEARS of INTERNATIONAL EXPERIENCE AT TIME OF ENTRY
   into this host country were __________

2. Approximate NUMBER of COUNTRIES in which our firm was already operating
   AT TIME OF ENTRY into this country was __________

3. Please specify the principal INDUSTRY your firm is in ___________________________

4. Our firm's approximate TOTAL ANNUAL SALES AT TIME OF ENTRY into this country was
   ___ less than $1 million, ___ $1 million--$9.99 million, ___ $10 million--$99.99 million,
   ___ $100 million--$499.99 million, ___ $500 million--$1.999 billion, ___ above $2 billion

5. Approximately TOTAL NUMBER OF EMPLOYEES in our firm AT TIME OF ENTRY
   into this host country was
   ___ less than 50, ___ 50-199, ___ 200-499, 
   ___ 500-1999, ___ 2000-4999, ___ 5000 or more

6. Our firm's TOTAL FOREIGN SALES AS A PERCENTAGE OF TOTAL DOLLAR SALES at the
   time of entering this host country was
   ___ 0%-10 %, ___ 11%-20%, ___ 21%-30%, 
   ___ 31%-40%, ___ 41%-50%, ___ above 51%

P. If your firm is CURRENTLY employing a DIFFERENT ENTRY MODE in this host country for
   the same principal product line, please specify that mode below. (You may refer to the list of entry
   modes provided on the first page).

Q. Any other comments you would like to make about your firm's foreign market entry experience in
   this host country.

______________________________________________________________________________

PLEASE ACCEPT MY SINCERE THANKS FOR YOUR PATIENCE AND COOPERATION

Varinder M. Sharma
REQUEST FOR RESULTS OF THIS STUDY

PLEASE RETURN THIS PAGE WITH YOUR RESPONSE

To the best of my knowledge, this study is one of the most comprehensive studies on international entry strategies conducted so far. I would like to share the results of this study with you. Please complete the items in this page and return it with the completed questionnaire in the envelope provided in this package.

Please check here, if you are interested in the general summary of findings of this study.

and/or

Please check here, if you are interested in a comparative analysis of your firm's international entry strategy with that of other members in your industry.

Please write below the name and address to which results are to be sent or send your business card along with the completed questionnaire.

________________________________________

________________________________________

________________________________________

________________________________________
FOR YOUR ASSISTANCE

The questionnaire accompanying this sheet was developed with three objectives. It should be (1) highly reliable and valid, (2) of adequate length, and (3) self-explanatory. I have tried to achieve these objectives following an iterative process involving feedback from Presidents, Vice Presidents, and International Business Executives of twenty-five internationally-active U.S. firms, six international business researchers and nine faculty members of two universities. It was considered that certain terms in the questionnaire may need elaboration. This sheet of paper provides elaboration of those terms to assist you (if you need) in completing the questionnaire.

PLEASE DO NOT RETURN THIS SHEET WITH YOUR RESPONSE

Elaboration of Certain Terms Used in the questionnaire

*Host Country* for a U.S. firm, is a foreign country in which it has production and/or marketing operations.

*Product Line* of a firm entails a family of closely related products. An example of a product line is frozen foods. Another example is men's undergarments etc. A U.S. firm may be marketing several product lines in a host country but the one that is central to its business operations in that country is considered as its Principal Product Line.

*Production Operation* of a firm entails carrying out activities relevant to the production of its products. These activities may include procurement of necessary raw materials and components, hiring and training of a manufacturing work force, establishment of a production infrastructure etc.

*Marketing Operation* of a firm entails carrying out activities relevant to the marketing of its products. These activities may include hiring and training of marketing personnel, marketing research, and management of products, pricing, promotion, and channels of distribution etc.
Entry Mode of a U.S. firm is an arrangement that makes possible the entry of its products, technology, human skills, management, or other resources into a foreign country.

Wholly Owned Subsidiary of a U.S. firm in a foreign country is a type of direct foreign investment in which the firm carries out production and marketing of its products under its 100 percent ownership.

Joint Venture of a U.S. firm in a foreign country is a type of direct foreign investment in which both the production and marketing of products are carried out in that country. The arrangement is a shared ownership between the U.S. firm and a host country firm.

Joint Venture with Majority Equity is an arrangement in which the U.S. firm holds the dominant share of equity—owns more equity than any other host country partner.

Joint Venture with Equal Partnership is an arrangement in which the U.S. firm holds equity roughly equal to all partners or the largest host country partner.

Joint Venture with Minority Equity is an arrangement in which the U.S. firm holds equity less than the largest host country partner.

Licensing or Franchising is an arrangement in which production and marketing of a U.S. firm's products are carried out in a host country under the sole ownership of a local firm. The U.S. firm receives fee or royalty from such a business operation. However, it has no ownership stake in that operation.

Collaborative Agreement of a U.S. firm entails a type of strategic cooperation (other than Joint Venture, Licensing, or Franchising) with a foreign firm. Examples of collaborative agreements are Research Partnership to develop a product or a process of mutual interest, a Consortium etc.

Exporting through Firm's Foreign Sales Subsidiary is an arrangement in which a U.S. firm carries out the marketing operation for its products in a host country. The production of those products is, however, conducted in the U.S. or in a third country.
Exporting Directly to End Users is an arrangement in which a U.S. firm exports its products directly to end users in a host country from its production base in the U.S. or in a third country.

Exporting through a Host Country Firm is an arrangement in which a U.S. firm exports its products to a host country through a host country distributor or an agent or a wholesaler from its production base in the U.S. or in a third country. The host country firm is responsible for marketing those products in that country.

Exporting through Another U.S.-based firm is an arrangement in which a U.S. firm "A" exports its products to a foreign country through another U.S. firm "B" which has a marketing channel in that country. The firm "B" carries out all the necessary marketing activities for the products of firm "A" in that country.

I hope the elaboration of terms provided in this sheet would give appropriate clarification (if needed) to complete the appended survey. If you still need more information, please feel free to call me. My office number is (804) 594-7272. Your comments are very valuable to the testing of this theory. I will be looking forward to receiving your comments, insights, and information in the returned questionnaire.

Thank you very much

Varinder M. Sharma
Dear Professor:

I have developed a survey instrument to gather data for my dissertation from Presidents/executives of U.S. firms with international operations. Through this instrument, I am attempting to tap into managerial decision making regarding selection of appropriate entry modes for their firms.

An entry mode is an infrastructural arrangement that a firm establishes to conduct its business operations (Production and/or marketing operations) in a foreign market. A wholly owned subsidiary, sales subsidiary, joint venture, and exporting through host country distributors or through other U.S. firms are examples of entry modes of U.S. firms.

There are four key sections in the instrument: HOST COUNTRY FACTORS, ESTABLISHMENT OF COMPETITIVE ADVANTAGE IN THE HOST COUNTRY, SUSTAINABILITY OF COMPETITIVE ADVANTAGE IN THE HOST COUNTRY, AND CUSTOMIZATION OF MARKETING STRATEGIES FOR THE HOST COUNTRY. Each section contains several items that purport to tap into managerial appraisal of host country environment and the ability of the firm to establish and sustain its competitive advantage over the host country competitors. These items have been developed from a thorough review of the pertinent literature bases.

I need your help in appraising the face and content validities of this instrument. The format for your feedback is appended with this request. Your feedback means a lot to me and will go a long way in fine tuning the instrument to obtain data of higher reliability and validity. Please return the survey instrument along with the completed feedback format to me or place it in my mailbox by Friday (28th October 1994).

Thank you very much

Varinder M. Sharma

Management & Marketing Department
FORMAT FOR YOUR FEEDBACK ON THE SURVEY QUESTIONNAIRE

FEEDBACK ON THE CONTENTS OF QUESTIONS A, B, C, D, AND E OF THE SURVEY

Please read questions A, B, C, D, and E in the survey before responding to questions 1 through 5.

1. Any problem(s) in structure of sentences in questions A, B, C, D, or E? (please circle "Yes" or "No" as your choice. If you circle "Yes" for a question, please specify the problem in the space provided along side that question.

<table>
<thead>
<tr>
<th>Question</th>
<th>A</th>
<th>Problem</th>
<th>Yes</th>
<th>No</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Question B</td>
<td>Problem</td>
<td>Yes</td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>Question C</td>
<td>Problem</td>
<td>Yes</td>
<td>No</td>
<td></td>
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<tr>
<td>Question D</td>
<td>Problem</td>
<td>Yes</td>
<td>No</td>
<td></td>
</tr>
<tr>
<td>Question E</td>
<td>Problem</td>
<td>Yes</td>
<td>No</td>
<td></td>
</tr>
</tbody>
</table>

2. Any Ambiguity in these Questions? (please circle only one choice for each question.

<table>
<thead>
<tr>
<th>Question</th>
<th>A</th>
<th>Yes</th>
<th>No</th>
<th>If yes, please specify</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Question B</td>
<td>Yes</td>
<td>No</td>
<td>If yes, please specify</td>
<td></td>
</tr>
<tr>
<td>Question C</td>
<td>Yes</td>
<td>No</td>
<td>If yes, please specify</td>
<td></td>
</tr>
<tr>
<td>Question D</td>
<td>Yes</td>
<td>No</td>
<td>If yes, please specify</td>
<td></td>
</tr>
<tr>
<td>Question E</td>
<td>Yes</td>
<td>No</td>
<td>If yes, Please specify</td>
<td></td>
</tr>
</tbody>
</table>

3. Any word or phrase that can be considered as offensive to respondents? (please circle only one choice)

<table>
<thead>
<tr>
<th>In question A</th>
<th>Yes</th>
<th>No</th>
<th>If yes, please specify</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In question B</td>
<td>Yes</td>
<td>No</td>
<td>If yes, please specify</td>
</tr>
<tr>
<td>In question C</td>
<td>Yes</td>
<td>No</td>
<td>If yes, please specify</td>
</tr>
<tr>
<td>In question D</td>
<td>Yes</td>
<td>No</td>
<td>If yes, please specify</td>
</tr>
<tr>
<td>In question E</td>
<td>Yes</td>
<td>No</td>
<td>If yes, please specify</td>
</tr>
</tbody>
</table>
4. Any term or phrase used in questions A, B, C, D, or E that requires elaboration to increase comprehension of respondents? Please specify those terms in the space provided below.

5. This questionnaire would ultimately be used to gather data from corporate managers. In your opinion, to what extent would it be difficult for corporate managers to comprehend the contents of this page? On scale of 1 to 7 where 1 represents extremely difficult to comprehend and 7 represents extremely easy to comprehend, please circle a number that best characterizes your opinion.

1 2 3 4 5 6 7

6. FEEDBACK ON THE CONTENTS OF QUESTION F OF THE SURVEY

Please read question F of the survey before providing feedback on it.

Question F is developed to tap into a U.S. firm's appraisal of business environment in a foreign country. The business environment of a country includes eight key components like market size, political conditions, cultural factors, availability of necessary raw materials, availability of skilled work force, government policies toward foreign businesses, infrastructure, and competition.

Question F of the survey contains eight such components. Multiple items are listed under each component. For a component, each item is developed to represent a specific aspect of that component. In other words, items listed under each component should belong to that component.

In your opinion, to what extent does an item listed under a component represent that component? For each item listed under respective components in question F of the survey, please give your assessment by choosing a number from the scale given below and listing in the space provided along side that item.

1 2 3 4 5 6 7
(Extremely low) (Extremely high)
Host Country Market Size
The degree of representativeness of the First item is_____
The degree of representativeness of the Second item is_____

Host Country Political Conditions
The degree of representativeness of the First item is_____
The degree of representativeness of the Second item is_____
The degree of representativeness of the Third item is_____

Host Country Cultural Factors
The degree of representativeness of the First item is_____
The degree of representativeness of the Second item is_____
The degree of representativeness of the Third item is_____
The degree of representativeness of the Fourth item is_____

Availability of Raw Materials in the Host Country
The degree of representativeness of the First item is_____
The degree of representativeness of the Second item is_____
The degree of representativeness of the Third item is_____

Availability of Skilled Work force in the Host Country
The degree of representativeness of the First item is_____
The degree of representativeness of the Second item is_____
The degree of representativeness of the Third item is_____
The degree of representativeness of the Fourth item is_____

Host Government Policies toward Foreign Businesses
The degree of representativeness of the First item is_____
The degree of representativeness of the Second item is_____
The degree of representativeness of the Third item is_____

The degree of representativeness of the Fourth item is_____ 
The degree of representativeness of the Fifth item is______
The degree of representativeness of the Sixth item is______
The degree of representativeness of the Seventh item is______

Host Country Infrastructure
The degree of representativeness of the First item is______
The degree of representativeness of the Second item is_____
The degree of representativeness of the Third item is_____ 
The degree of representativeness of the Fourth item is_____
The degree of representativeness of the Fifth item is_____
The degree of representativeness of the Sixth item is_____ 

Host Country Competition
The degree of representativeness of the First item is______
The degree of representativeness of the Second item is_____
The degree of representativeness of the Third item is_____ 
The degree of representativeness of the Fourth item is_____

7. FEEDBACK ON THE CONTENTS OF QUESTION G OF THE SURVEY

Question G is developed to tap into a U.S. firm's assessment of the chances of establishing its competitive advantage over a host country's competitors in Producing its products in that country. This assessment is based on the firm's appraisal of the business environment in that country. Seven items are listed under this question. Each item represents a specific way in which a firm may appraise its chances of establishing competitive advantage in Producing its products in a host country.

In your opinion, to what extent does each item of question G represent a firm's assessment of establishing its competitive advantage in Producing its products in a host country? For each item of question G, please give your appraisal by choosing a number from the scale given below and listing in the space provided along side that item.
8. FEEDBACK ON THE CONTENTS OF QUESTION H OF THE SURVEY

Question H is developed to tap into a U.S. firm's assessment of the chances of establishing its competitive advantage over a host country's competitors in Marketing its products in that country. This assessment is based on the firm's appraisal of the business environment in that country. Seven items are listed under this question. Each item represents a specific way in which a firm may appraise its chances of establishing competitive advantage in Marketing its products in a host country.

In your opinion, to what extent does each item of question H represent a firm's assessment of establishing its competitive advantage in Marketing its products in a host country? For each item of question H, please give your appraisal by choosing a number from the scale given below and listing in the space provided along side that item.

1  2  3  4  5  6  7

(Extremely low) (Extremely high)

The degree of representativeness of the First item is______
The degree of representativeness of the Second item is______
The degree of representativeness of the Third item is______
The degree of representativeness of the Fourth item is______
The degree of representativeness of the Fifth item is______
The degree of representativeness of the Sixth item is______
The degree of representativeness of the Seventh item is______
9. FEEDBACK ON THE CONTENTS OF QUESTION I OF THE SURVEY

Question I is developed to tap into a U.S. firm's assessment of the chances of sustaining its competitive advantage over a host country's competitor in producing its products in that country. This assessment is based on its appraisal of the competitive environment in that country. Seven items are listed under this question. Each item represents a firm's appraisal of the chances of sustaining a specific basis of competitive advantage in producing its products in a host country.

In your opinion, to what extent does each item of question I represent a firm's assessment of chances of sustaining its competitive advantage in producing its products in a host country? For each item of question I, please provide your appraisal by choosing a number from the scale given below and listing in the space along side that item.

1 2 3 4 5 6 7
(Extremely low) (Extremely high)

The degree of representativeness of the First item is_____
The degree of representativeness of the Second item is_____
The degree of representativeness of the Third item is_____
The degree of representativeness of the Fourth item is_____
The degree of representativeness of the Fifth item is_____
The degree of representativeness of the Sixth item is_____

10. FEEDBACK ON THE CONTENTS OF QUESTION J OF THE SURVEY

Question J is developed to tap into a U.S. firm's assessment of the chances of sustaining its competitive advantage over a host country's competitor in marketing its products in that country. This assessment is based on its appraisal of the competitive environment in that country. Six items are listed under this question. Each item represents a firm's appraisal of the chances of sustaining a specific basis of competitive advantage in marketing its products in a host country.

In your opinion, to what extent does each item of question J represent a firm's assessment of chances of sustaining its competitive advantage in marketing its products in a host country? For each item of question J, please provide your
appraisal by choosing a number from the scale given below and listing in the space along side that item.

1 2 3 4 5 6 7

(Extremely low) (Extremely high)

The degree of representativeness of the First item is_______
The degree of representativeness of the Second item is_______
The degree of representativeness of the Third item is_______
The degree of representativeness of the Fourth item is_______
The degree of representativeness of the Fifth item is_______
The degree of representativeness of the Sixth item is_______

11. FOR FEEDBACK ON THE CONTENTS OF QUESTION K

Question K is developed to tap into a U.S. firm’s efforts to customize its marketing strategies for a host country. Customization is done based on the firm’s appraisal of the business conditions in that country. A firm’s marketing strategies entail: product strategy, promotion strategy, distribution strategy, and the pricing strategy. Multiple items are listed under each of the four strategies. For each of them, items are developed to represent a firm’s efforts in customizing specific aspects of that strategy. In other words, items listed under each strategy represent that strategy.

In your opinion, to what extent does each item of a strategy in question K represent that strategy for each item of question K, please provide your appraisal by choosing a number from the scale given below and listing in the space along side that item.

1 2 3 4 5 6 7

(Extremely low) (Extremely high)

Customization of the Product Strategy for the Host Country

The degree of representativeness of the First item is_______
The degree of representativeness of the Second item is_______
The degree of representativeness of the Third item is_______
The degree of representativeness of the Fourth item is_______
The degree of representativeness of the Fifth item is_____

12. Customization of the Promotion Strategy for the Host Country
The degree of representativeness of the First item is_____
The degree of representativeness of the Second item is_____
The degree of representativeness of the Third item is_____

Customization of the Distribution Strategy for the Host Country
The degree of representativeness of the First item is_____
The degree of representativeness of the Second item is_____
The degree of representativeness of the Third item is_____
The degree of representativeness of the Fourth item is_____

Customization of the Pricing Strategy for the Host Country
The degree of representativeness of the First item is_____
The degree of representativeness of the Second item is_____
The degree of representativeness of the Third item is_____

Any general comments about the instrument?

Thank you very much for your valued feedback
Please return the survey instrument along with the completed feedback format to me or place in my mailbox at the earliest.
REFERENCES


Denis, Jean-Emile and Daniel Depelteau (1985), "Market Knowledge, Diversification, and Export Expansion," Journal of International Business Studies, 16 (Fall), 77-89.


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