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A comparative analysis of the role of national culture on foreign market acquisitions by U.S. firms and firms from emerging countries

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ABSTRACT

Do firms from emerging economies differ from U.S. firms in their foreign market acquisition strategies? A comparison of cross-border acquisitions by firms from the United States and 18 emerging countries shows that (1) firms from both the United States and emerging countries target countries that are culturally closer to their home countries, (2) a strong interaction effect occurs between market potential and cultural distance for emerging country firms as the market potential increases (i.e., at high market potential, firms from emerging economies are willing to overlook cultural distance), (3) no interaction effect occurs between market potential and cultural distance for U.S. firms, and (4) different cultural dimensions affect the market entry strategies of U.S. firms and firms from emerging countries.

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1. Introduction

Multinational firms' market entry strategies are an important phenomenon in the study of globalization in general and firms' internationalization strategies in particular. Globalization has led these firms to enter distant countries, both geographically and culturally, leading to the potential for both increased benefits and greater risk (Franke and Nadler, 2008). Multinational firms' assessments of environmental risks and benefits influence their international market entry (IME) strategies (Ahmed et al., 2002; Barkema et al., 1996). One such factor that influences multinational firms' perceptions of the risk and uncertainty in the target market is the cultural distance between the home and the target market (Lee et al., 2008).On the other hand, market potential is considered an important host country benefit that encourages IME (Davidson, 1980; Dunning, 1998; Ellis, 2008). This article focuses on both cultural distance and market potential and their impact on an important IME strategy—cross-border acquisitions (CBAs). Although several other variables are relevant in firms' CBA decisions, this study focuses on these two important variables.

A review of the literature on cultural distance and market potential shows the following: First, inconsistency exists in the empirical findings on the impact of cultural distance on firms' IME strategies. For example, while Dow (2000), Johanson and Vahlne (1977), Ojala and Tyrvainen (2007), and Slangen and Hennart (2008) report significant support for the impact of cultural distance on firms' IME strategy, Mitra and Golder (2002) and Rhee and Cheng (2002) report a non-significant impact of cultural distance. Therefore, debate still exists on the role of cultural distance on firms' IME strategy. Second, many of the studies were conducted in the developed world (Lau, 2003), with the major countries of focus being the United States and the United Kingdom; few studies focused on developing countries. Given that international expansion of firms from developing countries is a more recent phenomenon than that of firms from developed countries and that the two sets of firms have generally grown in different business and economic environments, with access to different pools of resources, it is important to study whether the impact of cultural distance and market potential on their IME strategy is similar. Furthermore, in line with the Uppsala internationalization theory (Johanson and Wiedersheim-Paul, 1975), cultural distance is likely to influence firms from developed countries less than firms from developing countries because of their greater experience in foreign operations.

This study addresses these important gaps in the literature. The central questions this study addresses are as follows: Does the market potential of the target country moderate the effect of culture on CBAs? In other words, does market potential override the role of cultural distance as a deterrent for CBAs in an increasingly "flat" world? Are the results from firms from developed countries generalizable to those from developing countries? Specifically, are firms from developed countries less constrained by cultural distance than those from developing countries?

This study addresses these questions using a large data set of CBAs of firms from 18 emerging countries and firms from the United States. The United States was the selected developed country for this study because the existing research focus and findings are primarily related to the

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United States and it is the leading country in terms of the number of CBAs. The 18 emerging countries selected were the most active in carrying out CBAs, and the quantum of activities (e.g., number of acquisitions, dollar value) is comparable in magnitude to that of the United States. Furthermore, the United States represents mature entry activities, and emerging countries represent comparatively newer forays.

The rest of the article is organized as follows: The second section describes the conceptual framework and develops hypotheses. The third section discusses the data and method of analysis. The fourth section presents the empirical results. The fifth section concludes with a discussion of managerial implications and further research directions.

2. Theory and hypotheses

2.1. Conceptual framework

Firms' perceptions of the risk–return tradeoff drive the modes of IME strategies (e.g., exporting, joint ventures, and CBAs), a view that several international marketing researchers support (Papadopoulos et al., 2002; Rothaermel et al., 2006). According to Papadopoulos et al. (2002), managers must consider both the 'pluses' and 'minuses'—commonly expressed in the literature as tradeoffs between 'opportunities and risks', 'costs and benefits', or 'cost and control' (Anderson and Gatignon, 1986; Douglas and Samuel, 1983; Ekeledo and Sivakumar, 1998)—in selecting international markets. Guided by the contingency theory, the position herein is that managers will often select international markets on the basis of a tradeoff between risks and returns/opportunities associated with the target market. In this study, cultural distance between the home and the host country is a risk factor while market potential of a target country offers possible opportunities to firms entering international markets. The theoretical premise here is that managers will give different importance to cultural distance based on whether the market potential of the target country is high or low. In line with previous studies (e.g., Ekeledo and Sivakumar, 1998; Rothaermel et al., 2006) that considered marketing potential an important contingency variable influencing IME decisions, this study proposes that the impact of cultural distance on firms' selection of international markets is contingent on the market potential of the target country.

2.2. Role of cultural distance

Several studies report substantial support for the impact of cultural distance on IME (e.g., Davidson, 1983; Dow, 2000; Johanson and Vahlne, 1977; O'Grady and Lane, 1996; Ojala and Tyrvainen, 2007; Rothaermel et al., 2006; Slangen and Hennart, 2008). The impact of cultural distance becomes even more important when firms decide to enter into alliances, partnerships, and/or CBAs. In comparison with other modes of entry, for CBAs, managers have the added responsibility to merge not only national culture but also corporate cultures (Barkema et al., 1996). This increases the likelihood of CBA failures. Indeed, many studies report that cultural distance hinders post-merger integration and suggest that it is the main cause of acquisition failures (Daniels and Metcalf, 2001). Difficulty in merging firms' cultures accounts for nearly one-half of all acquisition failures (Doney et al., 1998). The costs to integrate people, work ethics, and behavior rise with the increasing cultural distance between the firms, thus reducing firm value (Chatterjee et al., 1992; Cho and Padmanabhan, 1995). Moreover, the high cultural distance between the host and the home country also increases the costs of adaptation, performance monitoring, handling of inter-firm conflict, information sharing, transfer of strategic resources, and protection against the opportunistic behavior of the target firm (Gatignon and Anderson, 1988; Li and Guisinger, 1992; Zhao et al., 2004). Thus, cultural differences increase executives' uncertainty about the success of their cross-border operations because of increased levels of risk (Ahmed et al., 2002; Gatignon and Anderson, 1988). These differences create friction in understanding partners' languages, values, and non-verbal cues, leading to conflict, which lowers commitment and trust between the firms (Hau and Evangelista, 2007). Thus:

Hypothesis 1. The greater the cultural distance between the home country and the target country, the fewer is the number of CBAs by firms from developing countries.

Hypothesis 2. The greater the cultural distance between the home country and the target country, the fewer is the number of CBAs by U.S. firms.

Although a negative effect of cultural distance on the number of CBAs is expected, the strength of this negative effect should vary between U.S. firms and developing country firms. According to the Uppsala internationalization theory (Johanson and Wiedersheim-Paul, 1975), firms follow a gradual internationalization process; that is, they first enter culturally close countries and, after learning of foreign markets and operations, gradually enter more distant countries. Because most U.S. firms began the internationalization process much earlier, they may have adequate international experience and are likely to be less influenced by cultural distance. In contrast, firms from developing countries have less international experience and have only recently begun internationalizing; thus, they should be more wary of cultural differences. Empirical evidence supports this view. Ojala and Tyrvainen (2007) investigate the influence of cultural distance on the sequence of international market selections for small and medium-sized enterprises. From a sample of 51 software firms from Finland, they find that cultural distance had a significant, negative impact on the first two international market selections, though for subsequent market selections, cultural distance had no impact. These results are similar to those that Davidson (1983) and Dow (2000) report. In a study of 315 Australian manufacturing exporters, Dow (2000) finds that though cultural distance is a significant factor in determining international market selection, its impact is reduced for subsequent selections. Thus:

Hypothesis 3. The negative effect of cultural distance on the number of CBAs is lower for U.S. firms than for firms from developing countries.

2.3. Moderating role of market potential

As mentioned previously, the market potential of the target country is an important contingency variable in firms' IME strategies (Ekeledo and Sivakumar, 1998; Rothaermel et al., 2006). That is, the size of the target market, whether large or small, entails different degrees of impact on the risk (or, as in this case, the cultural distance) between the two countries. Thus, the market potential influences managers' tradeoff between associated risks and returns for a foreign market (Papadopoulos et al., 2002; Rothaermel et al., 2006). While cultural distance poses a risk that firms must manage and eventually overcome, market potential represents the rewards associated with entering a target country—a notion in line with the foreign direct investment (FDI) theory. According to the market-seeking FDI theory, market potential is one of the most important host country benefits encouraging FDIs (Davidson, 1980; Dunning, 1998; Ellis, 2008). This has been true for firms from developed countries, but recent CBAs by developing country firms suggest a similar strategy. For example, in its recent global acquiring spree, the Tata Group has concentrated most of its acquisitions in large developed markets (e.g., acquisition of Corus and Tetley in the United Kingdom and Eight O'Clock Coffee in the United States; Accenture report, 2006; Knowledge@Wharton, 2006).

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