6-2001

# Foreign country priorities in the internationalization process: A measure and an exploratory test on British firms

Timothy Adrian Robert CLARK
*Singapore Management University*, timothyclark@smu.edu.sg

Derek S. PUGH

# Foreign country priorities in the internationalization process: A measure and an exploratory test on British firms

Timothy Clark, The Management Centre, King's College, University of London, The Franklin-Wilkins Building, 150, Stamford Street, London SE1 9NN, UK

Derek S. Pugh, Open University Business School, The Open University, Walton Hall, Milton Keynes MK7 6AA, UK

Published in International Business Review, Volume 10, Issue 3, June 2001, Pages 285-303.

https://doi.org/10.1016/S0969-5931(01)00017-8



Accepted version

Abstract

After a critical analysis of the psychic distance aspect of the Uppsala model of internationalization and empirical studies to test it, this paper proposes a measure to enable comparison between target foreign countries in the priority given them in the internationalization process. An International Priority Index is developed for each target country, and used as the dependent variable in a model to analyze the effects of the independent variables of size of market, affluence of market, geographical distance and cultural distance on foreign country priority choice of home country firms. The measure and the model are given a first test on data obtained from a longitudinal study of the ordering of foreign market entry of 19 British firms. In this study, affluence of market is shown to have more importance than size of market, and geographical distance of country to have greater impact than cultural distance in the choice of ordering of entry.

Keywords

Psychic distance, Cultural distance, Internationalization, International priority, Uppsala

## 1. Introduction

In examining the activity of starting and developing international business some researchers adopt a relatively static model. For example, Dunning, 1981, Dunning, 1988, Hymer (1976), Reid (1983) and Teece (1981) generally examine a firm's foreign expansion as a series of choices dictated by situation specific efficiency considerations and relative transaction costs and benefits. In contrast, others view internationalization as a sequential process of increasing involvement within and across foreign markets. As a number of commentators have noted, there are two approaches to examining the sequential processes by which firms internationalize (Andersen, 1993; Barkema, Bell, & Pennings, 1996; Bell & Young, 1998). The first group of models are based on Rogers' (1962, pp. 81–86) diffusion theory and view the development of export activities as an innovation–adaption cycle (Bilkey & Tesar, 1977, Czinkota, 1982, Cavusgil, 1980).

This article is concerned solely with the second model—the Uppsala Internationalization Model—since it is one of the most cited (Chandy & Williams, 1994) and contested models of internationalization in the international business literature. This model also probably inspired the Innovation-Related Internationalization Models. Johanson and his colleagues at Uppsala University have argued that as firms expand into foreign markets they do so on the basis of incremental steps (Johanson & Wiedersheim-Paul, 1975, Johanson & Vahlne, 1977, Johanson & Vahlne, 1990). Their model postulates that this occurs since most firms experience a large amount of uncertainty when operating internationally. In order to reduce uncertainty with regard to the nature of foreign markets, firms only gradually increase the level of their foreign involvement in small sequential steps since further internationalization is dependent upon firms' existing 'experiential' knowledge bases. It is thus predicated as a process of learning through past experience.

The Uppsala Internationalization Model seeks to explain and predict two aspects of the internationalization of the firm: (1) the step-by-step pattern of institutional development within a particular foreign market (i.e. the 'establishment chain'—from direct exporting to appointing agents to setting up a sales subsidiary to, finally, establishing a production facility); and (2) the expansion of firms across national markets as they move from nations which are proximal to those which are increasingly psychically distant. The focus of this article is on examining the second aspect of the Uppsala model. This aspect predicts that because of the considerable uncertainties associated with operating internationally resulting from the lack of experiential market-specific knowledge (e.g. consumer habits, rules and regulations, cultural and political differences, etc.), firms initially enter psychically close countries before establishing a presence in more distant countries. 'Psychic distance' is therefore defined as factors preventing or disturbing the flow of information between the firm and target nations, including linguistic, institutional, cultural and political factors.

There have been some suggestions that since inter- and intra-business networks are becoming increasingly global, crossing national boundaries with ease, the examination of the impact of cultural differences no longer makes sense in the current business context (see, for example, Håkansson & Snehota, 1989, Håkansson & Snehota, 1995). We consider that this view is not justified since central to the Uppsala model is the notion that past learning impacts on decision making in future periods. Therefore, decision making has to be examined within its historical context; it is not ahistorical. So studies which seek to examine the internationalization process from a longitudinal perspective continue to retain their analytical power and relevance. Indeed, a number of authors have suggested that more such studies are needed to counter the cross-sectional tendency in international business research (see Clark, Gospel, & Montgomery, 1999; Melin, 1997)

This paper has three purposes. The first is to examine the Uppsala concept of 'psychic distance' and the empirical studies using it. The second is to propose a measure of 'international priority' which would allow the international development of firms to be better examined on a longitudinal basis in order to determine whether they follow the suggested stage pattern across countries as suggested by the Uppsala studies. The third purpose is to empirically analyze the factors affecting the priority of foreign country choices in the internationalization process of a sample of 19 British firms.

## 2. Background

### 2.1. The Uppsala model in relation to the ordering of foreign country priorities

The aspect of the Uppsala Internationalization Model which focuses on the ordering of foreign country activity has been considerably less studied empirically than the aspect which is concerned with the pattern of institutional development within a country (i.e. the 'establishment chain'). The following studies can be cited. Johanson and Wiedersheim-Paul (1975) examined the ordering of entry into foreign countries of four Swedish firms and found that 'psychic distance' had an effect on that order. Davidson, 1980, Davidson, 1983 found that inexperienced firms in the USA exhibited greater preference for near, similar markets than firms with broader international operating experience. According to Davidson (1980, p. 18), his data indicated that 'firms in the initial stage of foreign expansion can expect to exhibit a strong preference for near and similar cultures. Those in the advanced stages of foreign operations will exhibit little if any preference for near or similar cultures.' However, this conclusion was not based on any measure of cultural similarity nor did he conduct a statistical test. Vahlne and Nordström (1992), using a proxy measure of psychic distance termed the Mean Establishment Rank,[1] found little change in the order with which Swedish firms entered markets between 1897 and 1986. They conclude that 'although the distribution between the Nordic countries and Europe varies somewhat over time, it is within the area of these two regions that we find 85–95% of the first three establishments' (p. 20). Other studies which do not focus directly on the complete sequence of foreign involvement may also be quoted in support of the Uppsala approach. Studies have shown that the location of a firm's first international operation is predominately in a neighbouring country; for example, USA to Canada (Kravis & Lipsey, 1982) and Canada to USA (Denis & Depelteau, 1985, O'Grady & Lane, 1996).[2]

A number of other studies have not supported the Uppsala model. Engwall and Wallenstål (1988) found that the order of establishment of operations in foreign countries by three Swedish banks bore no relationship to cultural similarity. Instead, these banks tended to 'move to places where a large number of banks are already established' (p. 152). Benito and Gripsrud (1992) found no support for the proposition that their sample of 93 Norwegian firms made their initial foreign investments in countries culturally closer than those made subsequently. They concluded that their findings 'support the notion that location choices are discrete rational choices and not a cultural learning process' (p. 474). Two studies, using a different research approach, asked managers their views of international development. Sullivan and Bauerschmidt (1990) found no significant differences in European managers' appreciation of the barriers and incentives to internationalization at various stages of the process. Petersen and Pedersen (1997) found that Danish managers considered that the economic driver of increase of sales volume in foreign markets was more important than acquisition of knowledge about foreign markets in the explanation of incremental entry into further markets. Neither of these studies can be said to support the Uppsala Internationalization Model.

Given these conflicting results a further empirical analysis of psychic distance is presented in this paper as a contribution to the continuing debate surrounding this aspect of the Uppsala model. In the next section we suggest that one reason for these mixed results may be the divergent uses of the key concept 'psychic distance'.

### 2.2. The Uppsala concept of psychic distance and its developments

Although the concept of psychic distance had been used in earlier research studies by Beckermann (1956) and Linnemann (1966), discussion and research into the link between psychic distance and the internationalization process was generated by a series of studies of Swedish multinationals (Hörnell, Vahlne, & Wiedersheim-Paul, 1973; Johanson and Vahlne, 1977; Johanson and Wiedersheim-Paul, 1975). However, the method used to operationalize the concept was not discussed in these papers but was described in two later working papers (Vahlne & Wiedersheim-Paul, 1977, Vahlne & Nordström, 1992). As a consequence, the subsequent definition and operationalization of the concept varies considerably within the literature.

These studies of the impact of psychic distance on the internationalization process raise issues of conceptual and operational validity. 'Psychic distance' sounds as though it is a subjective phenomenon—the greater or lesser barriers which a manager feels to initiating market servicing in a particular foreign country, as a result of lack of

information and experience-based knowledge. In fact in the original Uppsala study the concept was operationalized using seven objective indicators of external barriers, namely:

1. Level of economic development in the importing countries;
2. Difference in the level of economic development between Sweden and the host countries;
3. Level of education in the importing countries;
4. Difference in level of education between Sweden and the host countries;
5. Difference in 'business language';
6. Difference in culture and local language;
7. Existence of previous trading channels between Sweden and the respective host countries.

These indicators were measured using publicly available statistics, or where these were not available, data were obtained "from knowledgeable employees of the Swedish Export Board". This information produced a preliminary ranking which was then revised by a panel of business experts. The disjunction between a subjective conceptual definition and an operational set of objective indicators, even though subjectively adjusted, has meant that it has not been possible to develop a fully consistent model. As Langhoff (1997) has forcefully pointed out, it is not possible to conclude that the internationalization process is driven by knowledge based on the firm's experience rather than information in the public domain (as do Johanson & Vahlne, 1977) by using data based on published statistics. This problem may account for the variety of approaches to measuring psychic distance within the literature.

Müller and Köglmayr (1986), Klein and Roth (1990) and Nordström (1991), among others, have developed the subjective approach to psychic distance by asking managers to rate what they see as the comparative difficulties in trading in particular foreign countries. There are a number of problems for this approach. First, the Uppsala Internationalization Model is stated at the level of the behaviour of the firm, yet the data refer to individual managers who, even within one firm, are likely to have considerable variations in their knowledge. Second, if psychic distance is used as a variable to predict, for example, the ordering of entry into foreign countries by the same managers who make the entry decisions, then the results run the risk of lack of independence. It would be a near-tautology to say that managers first enter countries which they subjectively consider to be psychically close, unless there are clearly independent data sources.

Other studies have reinterpreted psychic distance as 'cultural distance'. This is a narrower variable focusing on only one aspect of the original Uppsala definition, namely the differences in culture between the home country and foreign countries. In this approach countries are characterized on the objective cultural dimensions presented by Hofstede (1980), and indices based on his work are used as a measure of cultural similarity and difference. Kogut and Singh (1988), Benito and Gripsrud (1992), Barkema et al. (1996) and Padmanabhan and Cho (1999) are among those who use cultural distance as a variable.

One clear benefit of this disaggregation of the compound concept of psychic distance is that it allows the other objective variables originally included in the Uppsala formulation (such as level of economic development of the target foreign country) to be considered directly in the analysis. The impact of these factors on internationalization can thus be directly assessed, as shown below. But this approach also has problems. It is based on Hofstede's (1980) seminal research on cultural differences in attitudes to work, and the index developed by Kogut and Singh (1988) from that study.[3] But Kogut and Singh use the Hofstede work in rather problematic ways. They form an index for a country by statistically manipulating the particular scores on the four dimensions of culture found in Hofstede's study. Cultural distance is defined as differences between the indices of each country.

The first criticism to make is that the index gives the particular scores obtained in a particular study of a particular multinational corporation a much greater importance than is justified by the nature of Hofstede's data. One can agree that Hofstede's cultural maps, based as they are on large-scale surveys of the attitudes of IBM employees in up to 40 countries in the world, are good general estimates of cultural differences without accepting that they are correct to the degree of exactness represented by the detailed figures. Indeed, Hofstede himself argues that the

numbers he presents are likely to be underestimates of the real differences in cultures, since IBM may well, even if unconsciously, recruit biased samples of employees compared with the general population. Thus as one example, Britain comes out higher than the USA on the masculinity dimension in the Hofstede study, although other studies undertaken at that time using different approaches (e.g. Dubin, 1970, Steele, 1977) would suggest that it should be the other way round. This is why Hofstede presents his results as clusters of countries, such as Anglo (to which both Britain and the USA belong), Nordic, more developed Latin, etc. The Kogut and Singh index takes the detailed variations as much more precise than they are intended to be.

The second concern is with the creation of a single index for each country. The Kogut and Singh index is formed by taking the Hofstede scores for each country on the four dimensions, standardizing them to equate the variances, and arithmetically averaging the standard scores. The measure of cultural distance then becomes the difference between the index of the home country and the target foreign country. It is difficult to see the justification for this. Hofstede presents his variables as four orthogonal (i.e. independent) dimensions. Even if empirically they turn out to be oblique dimensions, i.e. correlated to some degree, this does not make them conceptually additive. Hofstede's own approach is to use the factors to determine clusters in four-dimensional space, not to treat them as linearly additive. A cluster approach to cultural distance would appear to be more appropriate and is used in this study. Our approach is outlined in the next section.

## 3. The International Priority Index (IPI)

If, as argued above, the Uppsala Internationalization Model is a longitudinal one covering the life-span of the firm, then the issue of how to analyze effectively the ordering of foreign market entry becomes important. Yet, as discussed in the previous section, many studies have compared only the first foreign country into which each firm has entered. Johanson and Wiedersheim-Paul (1975) presented rank–order correlations between the order in which countries were entered and their measure of psychic distance. But a correlation has to be presented for each firm separately. This is a viable approach when only four firms were considered, but becomes extremely cumbersome when the number of firms considered increases. Davidson, 1980, Davidson, 1983 approach, which is dependent on a pairwise comparison of the ordering of each country entered by the group of firms under examination, appears to be much more effective in dealing with larger samples. We therefore develop his approach into a concept of ‘international priority’ together with an index to measure it.

In defining the concept of ‘international priority’ we begin by focusing on a home country, the internationalization process of whose firms is the subject of study. In relation to this home country, a target foreign country is said to have a high international priority if it is frequently entered first or very high up in the comparative order by firms in the home country. A target foreign country will have a low international priority if it is commonly entered later in the firms' internationalization activities after experience has been gained elsewhere. The proposed measure of this concept is the *International Priority Index* (IPI). The IPI for a particular target country is developed by comparing in detail the comparative order in which all foreign countries have been entered by firms in the home country. For each firm, each foreign country entered is compared pairwise with every other country entered and credited positively (1) if entered first of the pair. It receives no credit (0) if entered later. The sum of credits across all the pairs generated by the firms in the home country which entered the target country, in relation to the total number of entries into this country, gives its IPI. Thus, a target country which is regularly entered high up in the comparative order will get a higher IPI score than one which is entered lower down.

We can illustrate the methodology by reference to the present study (details of which are given below). It is based on a British sample of 19 firms which have entered 42 target countries. The IPI is calculated by comparing each of the 42 countries with every other country and determining the proportion of cases in which entry by the sample firms is initiated in one country before others. Thus, whenever two countries are entered by the same firm a ‘1’ is recorded for the country entered first and a ‘0’ for the country entered second. For each pair of countries, the variable $a_{ij}$ is thus computed to measure the number of instances where an investment has been made by firms in

country *i* before an investment in country *j*. The ratio of $a_{ij}$ to the total number of entries made by those firms forms the IPI for country *i* and can be stated as follows:

$$\mathrm{IPI}_i = \sum_{j=1}^{n} \left[ \frac{a_{ij}}{a_{ij} + a_{ji}} \right]$$

where *n*=the number of countries in which the sample of firms have entered.

For example, in our study the one firm that had entered Argentina had previously entered seven countries and subsequently entered two others. The IPI for Argentina is thus 0.22 (=2/9). Fifteen firms entered the USA, and in addition, between them they also entered 36 other countries, making a total of 114 foreign entries for this subgroup. On 67 occasions the USA was entered before the other country, on 47 occasions afterwards. This gives an IPI for the USA of 0.59 (=67/114). A country like France has a high priority for these firms. The 16 firms which entered it also entered another 30 countries, making a total of 116 foreign entries for this subgroup. France was entered first in 101 of the 116 pairwise comparisons, giving an IPI of 0.87 (=101/116). In contrast, a country like Austria has a low IPI. The two firms that entered it also entered 15 other countries a total of 18 times. But Austria was only entered once before those other countries (IPI=0.06=1/18). As shown in Appendix A, the value of this index ranges across countries from zero to 0.89.

Equipped with the concept of 'international priority' and the index which it generates, it is now possible to investigate more comprehensively the factors affecting the ordering of the choice of target international markets and to test whether they follow this aspect of the Uppsala Internationalization Model.

## 4. A model of the factors affecting the ordering of the choice of international markets

Managers have a choice of which countries and markets to enter on first undertaking international business. The literature reviewed at the beginning of this paper indicates that this decision will be affected by a number of factors, of which four are particularly important. Other things being equal, we would expect that countries which exhibit the following characteristics would be more attractive to internationalizing firms in the home country:

1. countries where the markets are large
2. countries where the markets are affluent
3. countries which are geographically close
4. countries which are culturally more akin to the home country.

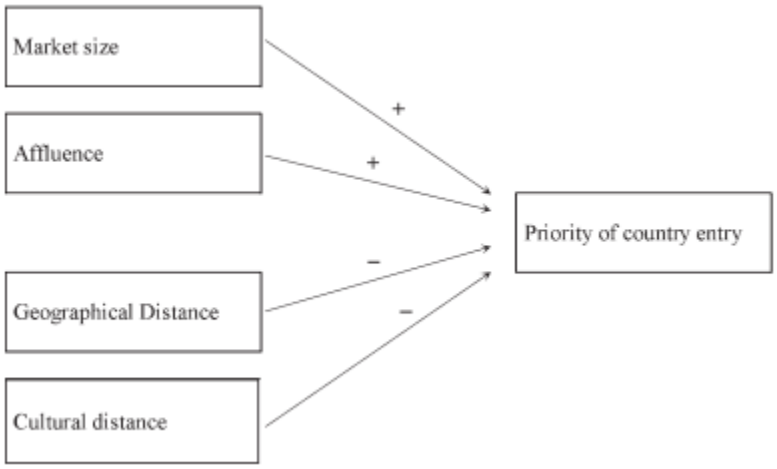
These foreign countries would appear to be more attractive to exporters, and therefore to be entered before those countries with the opposite characteristics (i.e. countries with small, poor markets which are geographically distant and culturally strange). This second group is more likely to be considered by managers as more difficult to enter and survive, in first and other early international moves. It might be noted that in the original Uppsala formulation, the first and third factors (size of foreign market, and physical distance of that market from home country) were considered separately, although the second and fourth factors (affluence and cultural affinity of target market) were included in the concept of psychic distance. The four factors are more appropriately separated out.

The factors are general ones applicable to all home firms intending to enter foreign target countries. Our argument is a longitudinal one, and the entries may take place over a considerable period of time. The factors therefore do not cover special influences which might at particular times be important, such as governmental policies leading to trade distortions, or competitor strengths at certain moments. There may also be ad hominem factors such as family links of particular senior managers to certain foreign countries, as when, for example, Crick and Chaudhry (1995) show that British Asian entrepreneurs export disproportionately early to East African markets. For the

purposes of this analysis we assume that these factors will even out over the longer term, hence the use above of the common economics phrase ‘other things being equal’ to preface these expectations.

The analysis will be concerned with the comparative impact of the four factors listed above on the priority ordering of entry into new foreign markets, the dependent variable being characterized as the IPI measure as shown in Fig. 1. Our purpose it to explore the impact of each factor separately in order to assess its significance, rather than to combine them together as in the original Uppsala studies. This study therefore presents correlation data between individual variables which are a preliminary test of this model and the hypotheses which it generates.

Fig. 1. Factors affecting the priority of international market entry.




It has further been argued that the factors affecting country priority choice themselves change as a result of organizational learning (Barkema et al., 1996, Bell & Young, 1998, Clark et al., 1997). Concern with the size and affluence of the new market may remain but knowledge and experience of international activities may lead to a diminution of the impact of, say, physical distance and cultural distance in making later entry choices. A comparison of the entry choices made at the beginning of the internationalization process with those made later when the process has matured would throw light on these suggestions. This study presents data which makes these comparisons and discusses their implications.

## 5. Research methods

A sample of British-based multinational firms would appear to be particularly appropriate to the test the model suggested above. First, there are considerable numbers of well-established British multinationals which have been internationalizing over a period of decades. Second, the low cultural distance of Britain from other Anglo countries is considerably at odds with its high physical distance from those countries. A test of their relative importance can thus be made. Similarly, the relative impact of cultural distance and economic power (i.e. size and affluence of markets) can be examined.

The empirical results presented below are founded upon the UK element of an international collaborative research project. The common purpose of this international team of researchers is to conduct research which will help in understanding the management implications occasioned by developments within the European Union. The research focus and research methods have been extensively described elsewhere (Clark, 1996). This aspect of the

study examined the internationalization of 25 UK-based firms. However, we were only able to collect detailed information on the total sequence of internationalization for 19 firms.

The method by which organizations were selected and data collected were developed in order to overcome a number of deficiencies which attach to previous studies of the Uppsala Internationalization Model. Three main problems can be identified:

1. Studies focus on different levels within the organization. Some focus on the firm as a whole and others on the operational units which comprise the organization. This distinction is critical since with the increasing importance to national economies of large multidivisional/multiproduct firms the organizational unit being analyzed may determine the extent and type of internationalization observed. Operational units may differ in their degree of international sales activity and number of foreign markets served. Furthermore, some multiproduct firms may have distinct markets for different product ranges. Overall, a firm may have a high percentage of foreign sales, but while some product ranges may mirror this, others may be more domestic in their focus. Hence, the degree and complexity of internationalization can depend on whether the empirical focus is at the group, operational or product level.
2. The Uppsala Internationalization Model is a theory of organizational learning. Learning occurs over the life-span of an organization. Consequently, the original Uppsala study conducted by Johanson and Wiedersheim-Paul (1975) examined the internationalization of four Swedish firms (Atlas Copco, Facit, Sandvik and Volvo) from the year in which they were founded to the early 1970s. Similarly, Engwall and Wallenstål (1988) collected data on the foreign entry of three Swedish banks from the first year in which they expanded into foreign markets. Therefore, a proper test of the Uppsala model should examine the process by which a firm internationalizes over its life-span. A number of studies which sought to apply the Uppsala model to the internationalization of firms have focused on particular periods in a firm's history. For example, Barkema et al. (1996) examined the internationalization of 13 large non-financial Dutch firms between 1966 and 1988. Their study and those which adopt a similar approach (e.g. Kogut & Singh, 1988, Padmanabhan & Cho, 1999) ignore the impact in this time period of learning which may have resulted from expansion into foreign markets in earlier time periods.
3. Finally, and related to the previous point, most studies of cultural distance are not replications of the original Uppsala study since they focus on particular modes of market servicing rather than the full range. For example, Davidson, 1980, Davidson, 1983 studied the effect of host country characteristics and corporate experience on foreign direct investment (FDI) location decisions. Similarly, Benito and Gripsrud (1992) examined the impact of cultural distance on the locations of FDIs. Finally, Barkema et al. (1996) examined the impact of cultural distance on the longevity of joint ventures vs. wholly-owned subsidiaries start-ups vs. acquisitions. Focusing on a narrow range of servicing modes has at least two important implications. First, the sequence of the establishment of FDI across countries may differ from the pattern of initial entry in these countries. For example, a firm may enter France before Germany, but establish FDI in Germany before France. Second, those countries in which a firm uses other modes of foreign market servicing (e.g. exporting and licensing) are excluded. Focusing on a subgroup of the countries in which a firm operates may therefore give a distorted and incomplete picture of its geographical development.

Given these problems the present sample of British firms was selected in ways which attempt to overcome the criticisms made above by focusing on the operating unit, the ‘whole-life’ time span and the full range of market entry modes. We began by defining the population from which the sample is taken as the largest 1000 firms in the UK, as ranked by sales turnover, provided they manufactured in the UK. We then distinguished between two levels within these organizations: the holding company and the operating firm. Potential participants were approached at the operating firm level (i.e. the level at which it manufactured rather than just owned). This means that each of our organizational units is concerned with only one, relatively narrow, range of products (e.g. pharmaceuticals, food) and the factors affecting internationalization decisions will be relatively homogeneous. The first step in internationalization was defined in terms of Buckley et al.'s (1989) and Clark et al.'s (1998)

Logical Model of Foreign Market Entry. In this model when firms initially enter a foreign market they can do so by exporting, licensing or engaging in FDI.

Information was collected by in-depth interviews with senior managers of the organizations, including those responsible for international marketing and the management of international operations. This was supplemented by published information on the history of each operating firm. As a result we were able to obtain information on the pattern of international expansion of each operating firm in every market which they currently service, or had at one time serviced. Melin (1997, pp. 75–76) refers to this as biographical longitudinal research in that the whole international development of an organization is identified from its founding to the present time.

## 6. Measures and hypotheses

The independent variables are defined as below, and the data for each of the 42 countries covered in this study are given in Appendix A:

1. *Size of market* is defined as foreign country GDP, 1980 (UN data).
2. *Affluence of market* is defined as foreign country GDP per head of the population, 1980 (UN data).
3. *Geographical distance* is defined as distance of foreign country capital from home country capital, in this case London (data from Whittaker's Almanac)
4. A cluster approach to the concept of *cultural distance* is taken based on the work of Ronen and Shenkar (1985). They reviewed eight studies including Hofstede's (1980) and have described differences in work attitudes and practices across a large number of countries. They have shown that the work cultures of some countries are closer together while others are farther apart. They therefore propose distinctive clusters of countries (e.g. Anglo, Latin, Germanic). This leads us to use a cluster concept of 'cultural distance' which summarizes this work by ordering the clusters in terms of their degree of difference from the cluster of the home country. *Cultural distance* is defined as the degree of difference of the cultural cluster to which the target foreign country belongs from the cultural cluster to which the home country (in this case, Britain) belongs.

Following Ronen and Shenkar (1985) and Hickson and Pugh (1995) a set of clusters was defined as shown in Table 1. Each target country which the sample firms entered was classified according to its cultural cluster and its distance (i.e. difference) from the British home culture. Since Britain is part of the Anglo cluster, other countries in that group were given the shortest cultural distance of '1'. The ascending order of cultural distance of clusters from the home British culture is as suggested by the authors quoted above, namely: Nordic cluster (scored '2'), Germanic cluster (scored '3'), Latin cluster (scored '4'). The remaining countries were considered to be culturally furthest away and were scored '5'. This simple classification seems to be a much more realistic characterization of cultural distance than the Kogut and Singh (1988) approach, discussed above.

As shown in Fig. 1, these independent variables will be investigated for their impact on the dependent variable of the model, the *International Priority Index*, as defined above. The IPI for each target country is given in Appendix A.

**Table 1. Cultural clusters and their 'cultural distance' from Britain**

| |
|---|
| *Anglo cluster (cultural distance=1)* |
| Australia, Canada, Ireland, New Zealand, South Africa, USA |
| *NORDIC cluster (cultural distance=2)* |
| Denmark, Finland, Netherlands, Norway, Sweden |
| *GERMANIC cluster (cultural distance=3)* |
| Austria, Germany, Luxemburg, Switzerland |
| *LATIN cluster (cultural distance=4)* |
| Argentina, Belgium, France, Italy, Mexico, Portugal, Spain |
| *REST OF WORLD cluster (cultural distance=5)* |
| Egypt, Greece, Hungary, India, Indonesia, Japan, Kuwait, Nigeria, Pakistan, Poland, Saudi Arabia, Singapore, Sudan, Taiwan, Thailand, Turkey, UAE, Zambia, Zimbabwe |

The model suggests the following hypotheses:

Hypothesis 1:
Larger countries (higher GDP) will have a higher IPI; i.e. they will be the recipients of international activity before smaller ones (which will therefore have a lower IPI).
Hypothesis 2:
More affluent countries (higher GDP per capita) will have a higher IPI; i.e. they will be the recipients of international activity before poorer ones (which will therefore have a lower IPI).
Hypothesis 3:
Countries geographically closer to the home country will have a higher IPI; i.e. they will be the recipients of international activity before geographically distant ones (which will therefore have a lower IPI).
Hypothesis 4:
Countries culturally closer to the home country will have a higher IPI; i.e. they will be the recipients of international activity before culturally distant ones (which will therefore have a lower IPI).
Consideration of the learning process in internationalization decisions suggests further hypotheses to be examined.
Hypothesis 5:
The first three countries entered in the process will have larger markets (higher GDP) than the last three countries entered.
Hypothesis 6:
The first three countries entered in the process will be more affluent (higher GDP per capita) than the last three countries entered.Hypothesis 7:
The first three countries entered in the process will be geographically closer than the last three countries entered.
Hypothesis 8:
The first three countries entered in the process will be culturally closer than the last three countries entered.

## 7. Results and discussion

Hypotheses 1—4 above were investigated through correlation analysis. The correlation matrix obtained is shown in Table 2. The results in Table 2 show strong support for Hypothesis 2. More affluent countries, as represented by GDP per capita, are higher in priority for entry over poorer countries. Size of market, as represented by the country GDP, shows no such effect, and Hypothesis 1 is not supported. There is also strong support for Hypothesis 3, geographically distant countries being lower down in priority for entry than geographically nearer ones.

Table 2. Correlation coefficients of factors affecting the priority of international market entry

| | Market size (GDP log scale) | Affluence (GDP per capita) | Geographical distance to capital (log scale) | Cultural distance | IPI |
|---|---|---|---|---|---|
| Market size (GDP log scale) | – | 0.12 ($p$=0.24) | −0.06 ($p$=0.36) | −0.27 ($p$=0.04) | 0.19 ($p$=0.12) |
| Affluence (GDP per capita) | – | – | −0.28 ($p$=0.04) | −0.22 ($p$=0.09) | 0.51 ($p$=0.001) |
| Geographical distance to capital (log scale) | – | – | – | 0.22 ($p$=0.08) | −0.35 ($p$=0.01) |
| Cultural distance | – | – | – | – | −0.24 ($p$=0.06) |

There is very weak support for the impact of cultural distance on priority decisions, with culturally strange countries having some tendency to be lower down on the priority list (though the correlation of −0.24 just misses the 95% confidence level). These results indicate that some countries which are geographically close to Britain but psychically distant (e.g. France, Belgium, Germany, The Netherlands, Italy) have a higher priority than members of the psychically close but geographically distant ‘Anglo’ cultural group (e.g. Australia, New Zealand, USA). But this Anglo group is given priority over many other European countries such as Austria, Norway, Spain and Portugal.

The results of the examination for the effects of learning are shown in Table 3. Once again it is affluence and geographical distance which show strong relationships and so Hypotheses 6 and 7 are supported. The GDP per capita of the last three countries entered is clearly less than the first three (difference at the 95% confidence level) and the geographical distance is considerably greater (difference beyond the 99% confidence level). While the market size (GDP) is less on average, the difference is not large enough to support Hypothesis 5 clearly (less than 95% confidence level). The cultural distance is not significantly different, and Hypothesis 8 is not supported.

**Table 3. Comparison of first three countries entered with last three countries**

| Variable | Mean first three entries | Mean last three entries | *t*-value |
|---|---|---|---|
| Market size (GDP log scale) | $668k | $387k | 1.84 ($p$=0.08) |
| Affluence (GDP per capita) | $13.5k | $9.6k | 2.15 ($p$=0.05) |
| Geographical distance to capital (log scale) | 1.2k mls | 3.0k mls | −3.70 ($p$=0.002) |
| Cultural distance | 3.11 | 3.41 | −0.94 ($p$=0.36) |

In general, the data presented here on British operating units underline the importance of economic drivers in the internationalization process. The potential of a market as exhibited by its affluence is a main factor affecting the priority of foreign country choice. The economic and managerial costs of geographical distance from a new market also have a major impact on the order of countries chosen. The internationalizing behaviour of these British firms over considerable periods appears to echo the subjective importance given to potential of foreign markets by the Danish managers in Petersen and Pedersen's (1997) survey.

But the data on first and last entries suggest that cultural distance does not generate a major learning task which has to be progressively overcome by managers. In these organizations there is clearly sufficient cultural confidence to expand where the market seems most attractive from the beginning. In this sense the Uppsala model is not supported.

## 8. Conclusion

The paper has made a number of contributions to the debate on the predictive validity of the Uppsala Internationalization Model. It has focused in particular on that part of the model concerned with expansion across countries. This highlights a progression from those countries which are psychically close to those which are psychically distant. First, we have sought to conduct a true test of this aspect of the Uppsala model by developing a research approach which overcomes a number of the methodological problems endemic to previous studies of this type. Second, the development of a new measure—the International Priority Index—and the adoption of a more appropriate measure of cultural distance have enabled the debate to become more empirical. Third, the examination of the comparative impact of economic, geographical and cultural factors on the ordering of foreign entry across countries on a sample of British operating units is helpful in that in Britain the economic and geographical factors in internationalization are clearly separate from the cultural ones.

Our results show that while there is undoubtedly some impact of cultural factors in the internationalization process, the impact of the economic drivers of market potential and geographic distance must be recognized as having primacy. Thus, national culture does not appear to be as crucial a factor on this element of internationalization as the Uppsala Internationalization Model suggests.

**Acknowledgements**

We thank Jorma Larimo, Roger Strange, the three referees and the participants of the Marcus Wallenberg Symposium on Critical Perspectives on Internationalization (Department of Business Studies, Uppsala University, 10–11 January 2000) for their perceptive comments on earlier drafts of this paper.

## References

Andersen, O. (1993). On the internationalization process of firms: a critical analysis. Journal of International Business Studies, 24, 209–231.

Barkema, H. G., Bell, J. H. J., & Pennings, J. M. (1996). Foreign entry, cultural barriers and learning. Strategic Management Journal, 17, 151–166.

Beckermann, W. (1956). Distance and the pattern of intra-European trade. Review of Economics and Statistics, 28, 31–40.

Bell, J., & Young, S. (1998). Towards an integrative framework of the internationalization of the firm. In G. Hooley, R. Loveridge, & D. Wilson, Internationalization: process, context and markets (pp. 5–28). London: Macmillan.

Benito, G. R. G., & Gripsrud, G. (1992). The expansion of foreign direct investments: discrete rational location choices or a cultural learning process? Journal of International Business Studies, 23, 461–476.

Bilkey, W. J., & Tesar, G. (1977). The export behaviour of small Wisconsin manufacturing firms. Journal of International Business Studies, 8, 93–98.

Buckley, P. J., Pass, C. L., & Prescott, K. (1989). The implementation of an international market servicing strategy in UK manufacturing firms. British Journal of Management, 1, 127–136.

Cavusgil, S. T. (1980). On the internationalization process of firms. European Research, 8, 273–281.

Chandy, P. R., & Williams, T. G. E. (1994). The impact of journals and authors on international business research: a citation analysis of JIBS articles. Journal of International Business Studies, 25, 715–727.

Clark, T. (1996). European human resource management. Oxford: Blackwell.

Clark, T., Gospel, H., & Montgomery, J. (1999). Running on the spot? A review of twenty years of research on the management of human resources in comparative and international perspective. International Journal of Human Resource Management, 10 (3), 520–544.

Clark, T., Pugh, D. S., & Mallory, G. (1997). The process of internationalizing in the operating firm. International Business Review, 6, 605–623.

Crick, D., & Chaudhry, S. (1995). Export practices of Asian SMEs: some preliminary findings. Market Intelligence and Planning, 13, 13–21.

Czinkota, M. R. (1982). Export development strategies: US promotion policy. New York: Praeger.

Davidson, W. H. (1980). The location of foreign investment activity: country characteristics and experience effects. Journal of International Business Studies, 11, 9–22.

Davidson, W. H. (1983). Market similarity and market selection: implications of international marketing strategy. Journal of Business Research, 11, 439–456.

Denis, J. E., & Depelteau, D. (1985). Market knowledge, diversification and export expansion. Journal of International Business Studies, 16, 77–89.

Dubin, R. (1970). Management in Britain: observations of a visiting professor. Journal of Management Studies, 7, 183–198.

Dunning, J. H. (1981). International production and multinational enterprise. London: Allen and Unwin.

Dunning, J. H. (1988). Explaining international production. London: Unwin Hyman.

Engwall, L., & Wallensta˚l, M. (1988). Tit for tat in small steps: the internationalization of Swedish banks. Scandinavian Journal of Management, 4, 147–155.

Ha˚kansson, H., & Snehota, I. (1989). No business is an island: the network concept of business strategy. Scandinavian Journal of Management, 5 (3), 187–200.

Ha˚kansson, H., & Snehota, I. (1995). Developing relationships in business networks. London: Thomson International.

Hickson, D., & Pugh, D. S. (1995). Management worldwide: the impact of societal culture on organizations around the globe. Harmondsworth: Penguin.

Hofstede, G. (1980). Culture's consequences. Beverly Hills, CA: Sage.

Ho¨rnell, E., Vahlne, J.-E., & Wiedersheim-Paul, F. (1973). Export och Utlandsetableringar (Export and foreign establishments). Stockholm: Almquist & Wiksell.

Hymer, S. (1976). The international operations of national firms: a study of direct foreign investment. Cambridge, MA: MIT Press.

Johanson, J., & Vahlne, J.-E. (1977). The internationalization process of the firm—a model of knowledge development and increasing foreign market commitment. Journal of International Business Studies, 8, 23–32.

Johanson, J., & Vahlne, J.-E. (1990). The mechanism of internationalization. International Marketing Review, 7, 11–24.

Johanson, J., & Wiedersheim-Paul, E. (1975). The internationalization of the firm—four Swedish cases. Journal of Management Studies, 12, 305–322.

Klein, S., & Roth, V. J. (1990). Determinants of export channel structure: the effects of experience and psychic distance reconsidered. International Marketing Review, 7, 27–38.

Kogut, B., & Singh, H. (1988). The effect of national culture on the choice of entry mode. Journal of International Business Studies, 19, 411–432.

Kravis, I. B., & Lipsey, R. E. (1982). The location of overseas production and production for export by US multinational firms. Journal of International Economics, 12, 201–223.

Langhoff, T. (1997). The influence of cultural differences on the internationalization process of firms. In I. Bjorkman, & M. Forsgren, The nature of the international firm. Copenhagen: Handelshojskolens Forlag.

Linnemann, H. (1966). An econometric study of international trade flows. Amsterdam: North Holland.

Melin, L. (1997). Internationalization as a strategy process. In H. Vernon-Wortzel, & L. H. Wortzel, Strategic management (pp. 72–93). New York: Wiley.

Mu¨ller, S., & Ko¨glmayr, H.-G. (1986). Die psyshiche distanz zu Auslandsma¨rkten. Schmalenbachs Zeitschrift fu¨r betriebwirtschaftliche Forshung, 38, 788–804.

Nordstro¨m, K. A. (1991). The internationalization of the firm: searching for new patterns and explanations. Stockholm: IIB, Stockholm School of Economics.

O'Grady, S., & Lane, H. W. (1996). The psychic distance paradox. Journal of International Business Studies, 26, 309–333.

Padmanabhan, P., & Cho, K. R. (1999). Decision specific experiences in foreign ownership and establishment strategies: evidence from Japanese firms. Journal of International Business Studies, 30, 25–44.

Petersen, B., & Pedersen, T. (1997). Twenty years after—support and critique of the Uppsala internationalization model. In I. Bjo¨rkman, & M. Forsgren, The nature of the international firm. Copenhagen: Handelshojskolens Forlag.

Reid, S. D. (1983). Firm internationalization, transaction costs and strategic choice. International Marketing Review, 1, 44–56.

Ronen, S., & Shenkar, O. (1985). Clustering countries on attitudinal dimensions: a review and synthesis. Academy of Management Review, 10, 435–454.

Steele, F. (1977). Is the culture hostile to organization development? The UK example. In P. H. Mirvis, & D. N. Berg, Failures in organization development and change. New York: Wiley.

Sullivan, D., & Bauerschmidt, A. (1990). Incremental internationalization: a test of Johanson and Vahlne's thesis. Management International Review, 30, 19–30.

Tayeb, M. H. (2000). The management of international enterprises: a socio-political view. Basingstoke: Macmillan.

Teece, D. J. (1981). The multinational enterprise: market failure and market power considerations. Sloan Management Review, 22, 3–17.

Vahlne, J.-E., & Wiedersheim-Paul, E., 1977. Psychic distance—an inhibiting factor in international trade. Working paper 77/2, Department of Business Administration, University of Uppsala.

Vahlne, J.-E., & Nordstro¨m, K.A., 1992. Is the globe shrinking? Psychic distance and the establishment of Swedish sales subsidiaries during the last 100 years. Working paper 92/3, Institute of International Business, Stockholm School of Economics.

## Appendix A.

| Country | Geographic distance (miles) | Cultural distance[a] | GDP ($m) | GDP per capita | IPI[b]($) |
|---|---|---|---|---|---|
| Argentina | 6915 | 4 | 154005 | 5666 | 0.22 |
| Australia | 10563 | 1 | 151145 | 10210 | 0.26 |
| Austria | 790 | 3 | 76882 | 10250 | 0.06 |
| Belgium | 217 | 4 | 119493 | 12080 | 0.86 |
| Brazil | 5452 | 4 | 249725 | 2021 | 0.27 |
| Canada | 3241 | 1 | 259997 | 10585 | 0.53 |
| Denmark | 608 | 2 | 66321 | 12964 | 0.52 |
| Egypt | 2194 | 5 | 22100 | na | 0.11 |
| Finland | 908 | 2 | 51624 | 10440 | 0.41 |
| France | 215 | 4 | 655305 | 12137 | 0.87 |
| Germany | 588 | 3 | 813498 | 13304 | 0.64 |
| Greece | 1500 | 5 | 40147 | 4181 | 0.89 |
| Hungary | 923 | 5 | 22147 | 4632 | 0.00 |
| India | 4180 | 5 | 162694 | 241 | 0.11 |
| Indonesia | 7295 | 5 | 72482 | 472 | 0.17 |
| Ireland | 279 | 1 | 16296 | 5243 | 0.50 |
| Italy | 895 | 4 | 395520 | 6907 | 0.62 |
| Japan | 5956 | 5 | 1040456 | 8873 | 0.27 |
| Kuwait | 2903 | 5 | 27581 | 20143 | 0.60 |
| Luxembourg | 217 | 3 | 4545 | 12819 | 0.56 |
| Mexico | 5529 | 4 | 186331 | 2591 | 0.00 |
| Netherlands | 230 | 2 | 169386 | 11855 | 0.68 |
| New Zealand | 11692 | 1 | 23818 | 7578 | 0.56 |
| Nigeria | 3107 | 5 | 88222 | 894 | 0.22 |
| Norway | 722 | 2 | 57713 | 14035 | 0.39 |
| Pakistan | 3935 | 5 | 28626 | 339 | 0.00 |
| Poland | 912 | 5 | 55036 | 4322 | 0.00 |

| Country | Geographic distance (miles) | Cultural distance[a] | GDP ($m) | GDP per capita | IPI[b]($) |
|---|---|---|---|---|---|
| Portugal | 972 | 4 | 25067 | 2474 | 0.30 |
| Saudi Arabia | 3067 | 5 | 115963 | na | 0.50 |
| Singapore | 6756 | 5 | 11343 | 4595 | 0.19 |
| South Africa | 5602 | 1 | 79563 | 2639 | 0.52 |
| Spain | 773 | 4 | 211781 | 5617 | 0.35 |
| Sudan | 3071 | 5 | 8246 | na | 0.22 |
| Sweden | 908 | 2 | 124137 | 14882 | 0.24 |
| Switzerland | 468 | 3 | 101629 | 15928 | 0.25 |
| Taiwan | 6685 | 5 | na | na | 0.38 |
| Thailand | 5928 | 5 | 33450 | 709 | 0.50 |
| Turkey | 1770 | 5 | 56918 | 1266 | 0.44 |
| UAE | 3425 | 5 | 29629 | 40587 | 0.89 |
| USA | 3665 | 1 | 2606630 | 11416 | 0.59 |
| Zambia | 4800 | 5 | 3883 | 649 | 0.33 |
| Zimbabwe | 5156 | 5 | 5323 | 747 | 0.22 |

(na, data not available)

[a]Figures based on scores in Table 1.

[b]Figures based on International Priority Index as elaborated earlier in text.