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International Entry Modes in Brazil and the CAGE Distances Effects

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Thesis presented to Escola de Administração de Empresas de São Paulo of Fundação Getulio Vargas, as a requirement to obtain the title of Master in International Management (MPGI).

Knowledge Field: International Strategy

Adviser: Prof. Dr. Servio Tulio Prado Junior

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Abstract

The international entry mode choices have a relevant importance for the impact they have on successful internationalization strategies. Many theories have been developed to describe which entry mode may be better than another according to the particular situation. The CAGE Distances Framework developed by Ghemawat to identify which dimensions companies should look when develop an internationalization strategy, may be useful to identify also how those dimensions impact on the international entry mode decision. The aim of this thesis is to study which kind of relationship exists between Cultural, Administrative, Geographic and Economic Distances and international entry mode choice. It analyzes a sample of companies that have been entered in Brazil through a logistic regression. According to this analysis, a negative and significant relation between Cultural Distance and need of control exists, a positive one exists between Administrative and Geographic, while no significant relationship has been found with the Economic dimension. Those findings are conceivably explainable through the theories found by scholars, but a deeper analysis that may take into account the specificity of every country is highly recommended, like the one developed with Brazil in this thesis.

Key Words: International Entry Mode, CAGE Distances, Brazil.

Resumo

As opções internacionais de modo de entrada tem siginificativa importância no que diz respeito ao sucesso de estratégias de internacionalização. Diversos modelos teóricos têm sido desenvolvidos para descrever de que maneira um modo de entrada pode ser do que outro de acordo com uma situação específica. O teoria das distâncias CAGE, desenvolvido por Ghemawat visando a identificação de quais dimensões as empresas devem explorar quando desenvolvem uma estratégia de internacionalização, pode também ser útil para identificar como tais dimensões impactam sobre as decisões de modo de entrada em um contexto internacional. O objetivo desta tese é estudar que tipo de relação existente entre Distâncias Cultural, Administrativa, Geográfica e Econômica e a decisão do modo de entrada. Analisa uma amostra de empresas estrangeiras atuantes no mercado Brasileiro por meio de uma regressão logística. De acordo com esta análise, existe uma relação negativa e significativa entre Distância Cultural e necessidade de controle, uma relação positiva entre a Distância Administrativa e Geográfica, enquanto nenhuma relação significativa foi encontrada com a dimensão econômica. Essas descobertas já foram conceitualmente antecipadas por proposições teóricas previamente propostas em outros estudos, mas deve ser considerado que uma análise mais profunda focando especificidades de cada país seria altamente recomendada, tal como o desenvolvido com o Brasil nesta dissertação.

Palavras-chave: modo de entrada Internacionais, CAGE Distâncias, Brasil.

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List of Acronyms

BRIC	Brazil, Russia, India, China
CAGE	Cultural, Administrative, Geographic, Economic
FDI	Foreign Direct Investment
JV	Joint Venture
MNC	Multinational Company
TCT	Transaction Cost Theory
UIM	Uppsala Internationalization Model
WOS	Wholly Owned Subsidiary

1. Introduction and thesis objectives

The analysis of the entry mode choice related to Foreign Direct Investments (FDIs) has been protagonist of the last years of International Business studies. This topic has been extensively studied because of its importance in determining the success of a FDI, mainly in countries where external factors may affect its performance in a wider way. The entry mode choice relates to the decision about the degree of resource commitment and the level of control that the investing firm want to adopt in the host country. Indeed, the company should decide if to invest alone, maintaining the 100% of the shares of the subsidiary located abroad, or rather to share the ownership with at least one other partner. The first mode is an investment through a Wholly Owned Subsidiary (WOS), while the second case is a Joint Venture (JV) investment, which usually is carried out with a local partner in order to leverage on its knowledge about the local market. It is well accepted that this strategic choice depend to a considerable extent on the external uncertainty in the target country (Slangen and van Tulder, 2009)

Emerging economies substantially contributed to the global economic growth in the 21st century thanks to their double-digit growth rates while the rest of the developed world was experiencing a tremendous financial crisis. Within those countries, four in particular became famous for their large population and abundant natural resources: Brazil, Russia, India and China, also known as BRIC. Their developing human capital, strengthening quality of institutional and policy environment started to massively attract FDIs coming from companies located in developed countries that were looking for opportunities of investment abroad. However, developing countries usually have strongly different cultures and underdeveloped institutions if compared with developed countries.

Fundamental differences in norms and values between the home country of a company and the host country of their operations, often create many drawbacks and increase the efforts required to enter in a foreign country, thus it influence their degree of control and resource commitment (Gatignon and Anderson, 1988; Kogut and Singh, 1988). However, prior researches do not provide conclusive results regarding the influence of formal and informal institutional environment on entry mode choice (Yiu and Makino, 2002; Dow and Larimo, 2009; Chang et al., 2012). In the attempt to analyze how those factors affect the entry mode choice, the research will focus in particular on Brazil. This country has been chosen for several reasons. First of all, it is one of the BRIC countries and it has been subject of a large scale of FDI inflow. Furthermore, some peculiarities of the Brazilian market make

it particularly attractive of firm from developed countries. The young population, the expanding middle-class and the highest per-capita income within developing countries make this country the perfect target for many MNCs that are looking for investment opportunities.

However, a successful market entry depends on a large number of factors. Ghemawat (2001) stated that distances between countries, not only depends on physical distance, but also on cultural, administrative/political and economic distances. All these factors can condition external uncertainty, and scholars have studied them from theoretical perspectives like the Transaction Cost Theory one. It is well accepted that differences in culture and country-risk may affect the strategic choices and, according to the Institutional Theory, firms' strategies are moderated by the institutional environment in which they are working in. This has been demonstrated to be particularly true in emerging economies and economies in transaction, where instable situations can highly affect the success of any investment (Peng, Wang and Jiang, 2008)

This thesis seeks to contribute with empirical evidences and analyze how the aforementioned factors affect the choice of entry mode. Its objective is to investigate on which extent the distances identified in the CAGE Distances Framework by Ghemawat between the home and the host country may exert on the entry mode choices. The research will analyze which dimensions are source of external uncertainty that may affect the balancing between need of control and need of collaboration when entering in a new Country. An analysis of 3498 entries by firms located in 19 different countries firms into Brazil offers empirical support for the hypothesis, endowing the sample with a high degree of diversity related to the considered distances. As secondary objective, this thesis will try also to explain the findings through considerations based on specificities of the analyzed country. This study will contribute to the development of entry mode literature by analyzing several sources of external uncertainty and their relative importance on the entry mode. It also contributes to the institution-based view of international business strategy, which emphasizes that "strategic choices are no only driven by industry condition and firm capabilities, but are also a reflection of the formal and informal constraints of a particular institutional framework that managers confront" (Peng et al.,2008) with empirical findings on the interaction of these factors on the entry mode choice. Moreover, the thesis also practically contributes taking into consideration factors that play important role in entering into Brazil, but they may be extendable to other developing economies.

Following this introduction, chapter 2 presents a literature review. After a brief introduction on the importance of internationalization strategies as a contributor for theoretical frameworks useful in this analysis, it will get into the literature on International Entry Modes. Once that the sources of external uncertainty will be defined, the review will present the dimensions of distance that impact on decisions. Chapter 3 presents the methodology and the data features. The results of the models will be presented in Chapter 4, while chapter 5 will discuss them and will draw conclusions. Chapter 6 offers limitations and suggestions for future researches.

2. Literature Review

This chapter introduces the frameworks on which this thesis is based. Therefore, it starts with a brief review of internationalization theories in order to explain which factors usually influence the choice of an investing firm to start operations abroad. The second step presented reflects the logic followed when a firm decides to internationalize, that is to choose the form with which enter the new market. Each entry mode presents many advantages as well as many drawbacks. Here, the framework provided by the Transaction Cost Theory (TCT) helps to identify the sources of uncertainty associated to any Foreign Direct Investment. Such uncertainty perceived by the investing company lies in the formal and informal institutional environment as defined by North (1990).

Institutions provide the structure for transactions to take place and affect the firm's choice of entry mode. As we will see, in the literature about entry modes, the uncertainty associated with the formal institutional environment has been traditionally defined through the concept of Country Risk, and in particular with Political Risk (Zhao, Luo and Suh, 2004), while the uncertainty linked to informal institutional environment has been measured through the concept of Cultural Distance. Therefore, the studies based on the TCT lead to prefer entry forms that require fewer resources when the institutional distance is greater in order to minimize the risks related to uncertainty. However, many other scholars argues that when two countries are separated by a wider distance, firms prefer to exert a higher degree of control over operations in order to be less subjected to environmental uncertainty, favoring entry forms associated with higher resource commitment. This paradox still remains unresolved despite the many scholars' attempts.

Ghemawat (2001) has been the first to state that too often MNCs overestimate foreign markets attractiveness. The explanation lies in the fact they underestimate the "distance" with the market, not only intended as physical distance, but also cultural, administrative/political and economic. In this way, he defined which other variables the firms have to take into consideration when entering into a new foreign market.

2. 1. Internationalization theories

The internationalization process has been protagonist in the last years of International Business studies. It has been defined as "firms' expansion across the borders of global regions and countries into different geographic locations or markets" (Hitt et al., 1997).

Today, more and more firms in almost all major economies operate internationally and also globally for a variety of reasons. The need to expand the market base abroad is often driven by economic objectives. Market potential, spare resources exploitation, resource gaps, acquisition of strategic assets and first-mover advantage are among the most important ones (Wang et al., 2012; Tallman et al., 2005). However, internationalization can be seen as a simple mean of risk reduction. However in this analysis it will be considered as a strategy to gain competitive advantage through an expansion of firm's products or services across the boarders of regions and countries, into different geographic locations or markets, seeking sustained competitive advantage (Hitt, Ireland and Hoskisson, 2007; Nachum and Zaheer, 2005).

Several theories about international expansion and FDI provide the theoretical background to understand the internationalization of firms. It is beyond the scope of this thesis to extensively describe all the theories, but it is worth to review the main theories that describe internationalization process of firms. According to the *International Product Life Cycle* (Vernon, 1966), the internationalization of a firm starts in the early phases of a product life with its simple export to similar countries. Only in a second phase the production process will be gradually delocalized abroad with the aim to strengthen the market position, mainly where substitutes are taking advantage, until the complete decentralization of the complete value chain, seeking cost advantages. Without doubts, this theory presents many limits, however it has introduced the concept of the convenience to internationalize in similar markets and the importance of experience gained with a gradual internationalization. Another noteworthy theory that tries to explain choices in FDIs is the *Eclectic Theory of International Production* by Dunning (1977). It affirms that the success of foreign operations is function of three factors known as OLI Advantages – Ownership, Location and Internalization. Ownership Advantages are defines as unique factors that belongs to a firm and determine its competitive advantage, explaining the decision to try to exploit those advantages abroad. Location Advantages concerns the specific advantages in selecting a specific market, such as exploitation of natural resources or low cost of labor, while Internalization Advantages come from the integration of the markets, explaining the decision on the investment extension. All these concepts have been considered then in the *Uppsala Internationalization Model*, also known as Incremental Theory of Internationalization or The Learning Model (Johanson and Vahlne, 1977; 1990). It affirms that internationalization gradually develop starting from markets that are similar to the home one, in terms of *Psychic Distance*, meant as factors that may affect the information flow and thus hinder the understanding of foreign markets, such

as difference in language, culture, business practices, policies and society. Psychic Distance creates uncertainty which affect the decision-making process and increasing transaction costs (Johanson and Wiederscheim-Paul, 1975). The central point in this theory is the learning-by-doing of the investing firms. Indeed, initially firms adopt entry modes that require lower resource commitment, such as exportation, and when they will gain experience, firms will be confident in adopting entry mode that gradually requires more and more resources.

It is clear that the uncertainty that arises from peculiarities in any specific market have been considered for their influences over strategic entry mode choices. According to Sharma and Erramilli (2004) three common themes emerge in all the aforementioned theories. First, firms enter foreign market to exploit their ownership advantages, which create a sort of monopolistic position. Second, this advantage have to be sustainable and cost-effective transferable across countries. Three, the choice of entry mode is essentially determined by an effective and efficient interplay of its advantages with the relevant host-country factors, such as competition, infrastructure and labor cost.

2. 2. International Entry Modes

As we have seen, there are many factors that determine the firm's aim to go abroad. From an internationalization strategy perspective, it is necessary to identify the best ways to develop a foreign presence. Thus, to conquer new markets, firms have to choose an entry mode. Entry mode strategies are often placed on a continuum going from low resource commitment, like licensing or franchising, to forms that require a higher resource commitment, like acquisition or greenfield investment. An entry mode can be defined as a "structural agreement that allows a firm to implement its product market strategy in a host country either by carrying out only the marketing operations, or both production and marketing operations there, by itself or in partnership with others" (Sharma and Erramilli, 2004). Thus, it entails three key strategic decision with important implication for performance: the location, that is the market to enter, the ownership or scale, which is the degree of commitment, and the timing, if going abroad as first mover rather than follower. Once those three factors have been considered, the managers should then decide the entry mode in order to accomplish their objectives, given the resources available to the firm.

The Transaction Cost Theory (Coase, 1937) played a determinant role in the analysis of the consequences on MNCs performances of entry mode choices. Indeed, it helps to

weight advantages and disadvantages in order to minimize the transaction costs related to every entry mode choice.

2. 2. 1. Non-Equity Entry Modes

This family of entry modes is characterized by a low level of commitment and control. They are essentially contractual modes, thus, are less risky since even if the firm fails, the loss will be small, however, the low control that exerts may cause a higher uncertainty.

Direct and Indirect Exporting were originally considered the first step in entering new international markets, serving as a platform for a future expansion (Kogut and Chang, 1996). It can be realized through a distributor or directly, and has the advantage to lower risks since the exporting firm does not have any involvement in production in the host country. Moreover, the company may also gain from economies of scale. However it can be risky because the firm may face high trade costs and its products may require high transportation costs or do not exploit the benefits from lower production costs in the host country. Furthermore, the firm may face difficulties in identifying the customer needs.

Licensing contracts and Franchising involves more resources. Licensing is an agreement where the licensor grants the right over an intangible property to a licensee for an agreed period and within an agreed territory. It is a good option when the firm that want to enter in a new market does not have enough capital for the production abroad, renouncing however to the control over it. In the other hand, Franchising is an agreement where the franchisor sells the right to a franchisee to develop certain business activities in return of a royalty, but unlike the licensing it involves a commitment for a longer term since also the franchisee faces high costs to start the activity. The franchisor avoid many risks in enter a foreign country and can expand faster. However the franchisor has a limited control while his success depends on the success of the franchisee since it works under the franchisor's name.

Also Strategic Alliances are Non-Equity Entry Mode. It is an arrangement between companies that market internationally and, sometimes also between competitors, which have decided to share some resources in order to undertake a mutual beneficial object. It often involves technology transfers, expertise, shared expenses and shared risks, in order to gain competitive advantage summing the efforts of each part. In fact, each partner concentrates on activities that best match their capabilities. A strategic alliance aims for synergies and is an effective opportunity to develop processes and expand into new markets. They are non-equity and non-permanent agreements and thus companies remain independent and separate.

However, also strategic alliances may imply some drawbacks, such as an undermined effectiveness due to a weak alignment of objectives and clashes of corporate cultures.

2. 2. 2. Equity Entry Modes

Carrying out a Foreign Direct Investment (FDI) is a mean for enter a new market and, thus, achieving internationalization. It is defined as an investment made by one actor in an enterprise resident in another economy, reflecting a long-term interest and willingness to control (World Investment Report, 2006). It implies the decision whether to invest alone through a Wholly Owned Subsidiary (WOS), or to share the investment with at least another firm, through a Joint Venture (JV) (Brouthers and Hennart, 2007). These two entry modes are characterized by a higher resource commitment but with a higher degree of control. Both Wholly Owned Subsidiaries (WOSs) and Joint Ventures (JVs) are considered Foreign Direct Investments according to the above definition.

A Joint Venture (JV) is a business agreement in which two or more independent firms agree to pool their resources and develop a new entity, sharing revenues, costs, assets and control. Moreover, risks are lowered also because usually at least one of the parts involved has any experience about the foreign market. Furthermore, in many countries, political restrictions make Joint Ventures with a local partner the only feasible way to enter in the market. However, Joint Venture does not give a full control over operations, so there is the risk of losing control and also conflicts may arise also because of cultural clashes.

In the other hand, Wholly Owned Subsidiaries (WOS) is the case when the parent company owns 100% of the subsidiary's stocks. This new company can be set up as a greenfield operation or acquired through an acquisition, but in both ways the parent has the full control over the operations. However, since the full costs are borne by the company alone, this entry mode imply higher risks since it is the most expensive, requiring the highest commitment.

2. 3. Impact of Distancees on Entry Mode Choice

The attractiveness of a foreign market is attenuated by the distance between the investor's home country and the host one. However, not only the Geographic Distance should be considered, but also Cultural Distance, Administrative (or Political) Distance and Economic Distance. An effective method to take into account all those dimension is the Ghemawat's

CAGE Distances Framework (2001). It provides an effective way to identify all the factors that impact on the attractiveness of a market, and the possibility to overcome TCT limits and bridging it with the Institution-base View if International Business (Brouthers and Hennart, 2007).

2. 3. 1. Institutional Theory

Before proceed with the analysis of the dimensions considered in the CAGE Framework, it may be useful to introduce the Institutional Theory (North, 1990). In the last years, the internationalization literature is primarily addressing the choice of entry mode for a market. According to the Transaction Cost Theory, the external uncertainty associated to the FDI constitutes a main factor conditioning the entry mode choice of firms (Zhao, Luo and Suh, 2004; Brouthers and Hennart, 2007). Institutional Theory integrates the TCT analyzing the impact of institutions over external uncertainty that, in turn, impacts on entry mode choice (Yiu and Makino, 2002).

Quoting North (1990), institutions can be considered as "*rules of the game*" in a society, which shape firms behaviors and their performances. In wide terms, institutions are "*humanly devised constraints that structure political, economic and social interaction, defining legal, moral and cultural boundaries, discriminating what is legitimate from what is not*". North (1990) also introduced the widely accepted distinction between formal and informal institutions. As will be shown in the next paragraphs, the former refers to the set of explicit rules in a society such as laws, regulations, property right protections, and have to be established by an authority. In the other hand, informal institutions are considered as the constraints that people in a society impose upon themselves and structure the relationships, thus are not established but rather inherited by teaching and imitation, setting the national culture (North, 1990).

In this contest, according to Slangen and van Tulder (2009), formal and informal institutional environments of the host country determine the external uncertainty perceived by the investing company, increasing the liability of foreignness. In fact, the uncertainty arising from the characteristics of every specific national market, such as business climate, cultural patterns, structures of the market system and the characteristics of the customers, are factors that may influence the management team decision to internationalize (Delios and Henisz, 2003). The main objective of institutions should be to facilitate transactions while companies

should adapt their strategies to the formal and informal institution environment in order to get legitimacy (Peng et al., 2009).

2. 3. 2. The informal institutional environment - Cultural Distance

Cultural distance is a widely used construct in international business studies. The first that recognized the impact of culture on tasks was the anthropologist Edward Hall. He observed that when describing mushrooms, no two experts describe them in the same way, and it creates problems for the rest of the people that try to identify them. Successively, Cultural Distance has been defined as a distance that reflects the existing differences in values, norms and behavioral rules between two countries (Shenkar, 2001). The national culture determines how people interact with one another, and it is influenced by religious belief, race, social norms and language (Ghemawat, 2001). It increases entry costs, decrease operational benefits and hamper the firm's ability to transfer its core competencies (Gomez-Mejia and Palich, 1997).

The internationalization of firms has been explained as an incremental process, following a sequence of phases starting from markets in close geographic proximity and cultural, political and legal system similar to that of the home country of the MNC. Indeed, according to the Uppsala Internationalization Model, the initial expansion to proximate locations seeks to reduce the risks by avoiding unfamiliar spaces and by selecting entry modes. Therefore, the UIM refers to "psychic distance" to denote the perceived distance between countries and the consequences for the information flow, which is influenced by many aspects such as the language, religion, level of economic development, level of education, geographic distance and corruption (Johanson and Wiedersheim-Paul, 1975; Vahlne and Nordstrom, 1993; Conway and Swift, 2000). Psychic distance and cultural distance are not identical, but rather, they capture different but overlapping phenomena, thus, one is a good proxy of the other (O'Grady and Lane, 1996).

Cultural Distance can also be considered as a proxy for the external uncertainty in the Transaction Cost Theory framework about FDIs. A classic example of how cultural differences may impact on the business environment is the tolerance of Chinese to copyright infringement due to a concept of Confucius that encourages the replication of past intellectual endeavors rather than create new ones. In this contest, any ownership advantage would be lost.

However, some authors like Slangen and van Tulder (2009) argue that Cultural Distance reflects external uncertainty only in the case that the firm decide to invest through WOS, while for JV, it reflects more an internal uncertainty since cultural difference may be a source of misunderstandings with the partner or conflicts with local workforce. As a result, the effect of cultural distance on the choice between Joint Ventures and Wholly Owned Subsidiaries may be ambiguous, making this distance a suboptimal predictor of entry mode choice and thus explain why in the literature has been found contradictory empirical findings about it.

2. 3. 2. 1. Measures of Cultural Distance

Traditionally, cultural distance is defined through the Hofstede's concept (1980, 2001). Professor Geert Hofestede studied how values in the workplace are influenced by culture through a database of employees' value scores collected within IBM, between 1967 and 1973 in more than 70 countries. He defines culture as a set of "*collective programming of the mind*" shared by a group of people and distinguishing them from other groups, while the subset *National Culture* refers to the culture that identify group of people that share the same national environment.

Hofstede identified and measured initially four main cultural dimensions - power distance, uncertainty avoidance, individualism and masculinity – and subsequently two more dimensions – long-term orientation and indulgence versus restraints.

- *Power distance*: this dimension expresses the degree to which the less powerful members of a society accept and expect that power is distributed unequally. The fundamental issue is how a society handles inequality among people, if people strive for equality or accept a hierarchical order in which everybody has a place with no needs of further justification.
- *Individualism versus collectivism*: individualism refers to people's behaviour is oriented to a loosely-knit social framework, in which individuals are expected to take care of only themselves while collectivism pertains to societies in which people need to belong to a group, looking after each other in exchange for unquestioning loyalty.
- *Masculinity* represents a preference in society for achievement, heroism, assertiveness and material towards for success, showing competitiveness. The opposite, *femininity*

strand for a preference for cooperation, modesty, caring for the weak and the quality of life.

- *Uncertainty avoidance* express the degree to which the members of a society feel uncomfortable with uncertainty and ambiguity, involving the attitude to try to control the unknown future or not by imposing rules and systems to bring about order and coherence.
- *Long-term orientation*, also known as Confucian dimension, stands for the fostering of virtues oriented towards future rewards, encouraging thrift and perseverance as ways to prepare for the future. On the contrary, *short-term orientation* means a preference to maintain time-honored traditions and norms while societal change is seen with suspicion.
- *Indulgence* stands for a society that allows relative free gratification of basic and natural human drives related to enjoying life and having fun, while *restraints* stand for a society that suppress gratification of needs and regulates it by means of strict social norms.

Hofstede's work has been considered as revolutionary in the undersigning the cultural differences between nations, but it has been object of many criticisms. In particular, Schwartz (1994) has raised several concerns. First of all, Hofstede's survey may not be exhaustive since it was designed to identify national culture dimensions, leaving out some possible relevant question. Secondly, since the sample was limited to IBM employees, they are not representative of the whole population of the country. Therefore, he identified a set of 56 individual values recognized across cultures and thus covering all value dimensions explaining intra-country cultural variation. Then, through further studies, surveys and statistical analysis, he came up with seven meaningful and interpretable dimensions for 38 countries and cultural groups: Conservatism, Intellectual autonomy, Affective autonomy, Hierarchy, Egalitarian commitment, Mastery and Harmony.

2. 3. 2. 2. The impact of Cultural Distance on the entry mode choice

Once that a firm decides to enter in a foreign country through an equity investment, the firm have to decide whether to share its ownership with other firms through a Joint Venture or to exert a full control through a Wholly Owned Subsidiary. Important differences in norms and

values between the MNE's home country and the host country often create operational difficulties and increase the efforts required to enter a foreign country in terms of degree of control and resource commitment when they endeavor to establish overseas operations (Gatignon and Anderson, 1988; Kogut and Singh, 1988). According to Zhao, Luo and Suh (2004) and Brouthers and Hennart (2007), TCT is the most suitable framework to explain pros and cons of both the alternatives, WOS and JV.

One possibility when entering in an unfamiliar foreign country is that the investing firm may prefer to choose a JV in order to gain access to local knowledge of the host country's informal environment. In fact, Collaborate with a local partner endows to leverage his local knowledge and reduce such uncertainty (Hennart, 1988). This assumption is in line not only with the TCT, but also with the contingency approach. Indeed, a lower resource commitment gives the flexibility to quickly modify decisions and easily withdraw in case of failure. However this option implies higher ex-ante transaction costs in discovering a proper partner and drafting a complete agreement, and also increasing management costs in monitoring and dispute settlings (ex-post transaction costs).

On the other hand, other studies found that transaction costs increase along with cultural distance. Thus, a greater cultural distance context involves too much higher transaction costs, leading to prefer WOS to JV and avoid these costs (Hennart, 1988; Erramilli and Rao, 1993). As a matter of fact, Wholly Owned Subsidiary solution allows firms to absorb the external uncertainties through the centralization of the decision-making process, which in turn provides a reduction in communication costs and protects the firm from opportunistic behaviors of any potential partner. Malhotra et al. (2003) argues that this higher commitment is critical mainly when the competitive advantage lies in the knowledge that should be transferred from the home country to the host one, exposing it to high risk of opportunism.

In literature this countersense is known as Cultural Distance Paradox, which has roots in a dual logics: the collaboration rationale and the control one. In fact, each entry mode brings different benefits, but also drawbacks. Therefore MNEs have to balance the need to collaborate with the need to control (Brouthers and Brouthers, 2001). The need to collaborate contends that collaboration with partners form culturally distant countries can leverage partners' local knowledge to bridge cultural gaps and lower the management cost of overseas operations (Kim and Hwang, 1992; Gatignon and Anderson, 1988). Employees from the host country may have difficulties in comprehend or accept the corporate culture, which usually derive from parent company's home country, making conflicts more likely. Collaborating

with a local partner may facilitate the integration, the transfer of local knowledge and lower overall operations costs of the subsidiary (Brouthers and Brouthers, 2001; Wang and Schaan, 2008). On the contrary, the need of control viewpoint argues that the MNE needs the total control of the foreign subsidiary to avoid opportunistic behaviors of the partner and reduce the cost of contracting (López-Duarte and Vidal-Suárez, 2010; Zhao et al., 2004). With higher cultural distance, the difficulties to obtain complete information and understand them increase. Thus, also the evaluation for the potential opportunism of a partner, the future negotiations and enforcing contractual agreement with it is tougher. Under these circumstances, the MNE may prefer WOS as entry mode with full control (Brouthers and Brouthers, 2001).

Up to now scholars have found only inconclusive evidences (Brouthers and Brouthers, 2001; Shenkar, 2001; Tihanyi et al., 2005). To explain the contradictory aforementioned results, Brouthers and Brouthers (2001), introducing the influence of the formal institutional environment, proposed two hypothesis. Managers would prefer Joint Venture as mode of entry as the cultural distance between home and host country increase. However, if host country risk is high, is more likely that managers will prefer wholly owned forms.

2. 3. 3. The formal institutional environment – Administrative/Political Distance

In its original meaning, Administrative Distance is related to historical and political links between Countries. It has been demonstrated that, for example, the relationship colonizer-colony may account for an increase of 900% in commercial transactions. In order to link this dimension to the entry mode choice, Country and Political Risk have been considered in literature since they are given by the likelihood of an unfavorable change in the governmental regime of the country and/or in the policies issued by such a regime and the volatility of the political, economic and social factors are sources of external uncertainty (Henisz, 2000). However, Slangen and van Tulder (2009) argue that the best proxy for external uncertainty is the governance quality of the foreign country.

Different policies and political instability are great source of uncertainty when carrying out a FDI. A clear example about how a government may affect an entry mode decision is to be find in the fact that, mainly in developing countries, government want to keep control over some strategic industries, thus they allow a foreign investment only if it is

carried out with a local partner. The term "Governance Infrastructure" is commonly used to represent the entire formal institutional environment of a country, covering the overall public institutions and policies created by government as a framework for economic, legal and social relations (Slangen and van Tulder, 2009; Globerman and Shapiro, 2003). When a firm enters in a country with a poor governance quality, is easy to think that it will need more control over operation in order to avoid potential opportunistic behaviors in a situation where agreement are difficult to enforce. Low enforceability of contracts gives room to partner's opportunistic behaviors since there are low probability to be caught and punished. In this scenario, MNE's managers will hesitate to collaborate with a local partner. As a matter of facts, inadequate enforceability of legal agreements reduce the firm's willingness to collaborate with a local counterpart due to the increase in costs of contracting (Roy and Oliver, 2009). On the contrary, if governance quality is good, the probability that the partner will behave opportunistically is reduced, increasing the MNE's willingness to cooperate. Zhou and Poppo (2010) found that if the MNE perceive a satisfactory legal contracts enforcement, it is more likely that they will rely more on formal contracts to safeguard transactions, suggesting that this enforceability facilitates the cooperation of a foreign MNE with a local partner.

Hence, we can conclude that even in a culturally distant country, if the governance ensures an acceptable contract enforceability that can protect MNEs from opportunistic behaviors of potential partners, JV choice will be more attractive than WOS (Chang et al., 2012).

2. 3. 4. Geographic Distance

Another distance that must be included when weighing advantages and drawbacks of every entry mode is the Geographic Distance. Considering the TCT framework, an increasing in physical distance between markets implies increasing costs of transportation and communication. This idea has been base for the Gravitational Model of International Commerce by Tinbergen (1962), where the commercial flow between two countries shows a negative proportion to their distances. Geographic Distance not only influences the transportation costs of material products, but also for services. It has been demonstrated that services are negatively affected by distance, mainly due to the difficult in retrieving information. Often, physical distance means different times zones and also different calendars

and different habits that can affect the business (Olson and Olson, 2000) despite the globalization and the new technologies in communication and transportation

2. 3. 5. Economic Distance

Economic Distance may measure the differences in wealth between countries. It describes the level of economic development of a country and it may affect the transferability of technologies and knowledge. But it is also a proxy for the development of infrastructure and the educational level of a country. Likewise, similar economic characteristics may mean a similar wealth of the population, thus is more likely that consumer behaviors of the people are similar, increasing the adaptability of a product to a foreign market. According to March (1991), to succeed in a foreign market, companies should explore new resources available in the new market, but also leverage on the replicability of knowledge already developed. Therefore, is more likely that the market entry succeed when two countries have similar economic characteristics.

2. 4. Hypothesis formulation

According to the aforementioned literature review, is possible to state that the CAGE Distances Framework well adapts to the analysis of external uncertainty that a company may face when enter in a foreign country (Ghemawat, 2001). The thesis will proceed in this sense by analyzing if this kind of influence may be extended and thus if a certain kind of relationship between the external uncertainty determined by distance dimensions and strategic entry mode choices.

First of all, I will look how every dimension may affect entry mode choices, and if it may change when those dimensions are analyzed jointly. According to Erramilli and Rao (1993), a negative relationship between degree of control and Cultural Distance is expected. Indeed, an increasing cultural distance may imply a higher need of a partner who knows the market and thus to leverage on its knowledge in order to seek success in the market, but a Joint Venture also imply a lower degree of resource commitment since the investment is shared with another identity. About the Administrative/Political Distance, it is possible that an increase in this dimension may lead to a higher will to invest alone since it is probable that contracts would receive a lower protection from local laws in case of any eventual opportunistic behavior of the partner (Slangen and Van Tulder, 2009). An increasing in

Geographic Distance in literature has always been associated to an increase in transportation and communication costs, both frequently necessary to managers in case of JV since they would have to deal with the local partner in order to come up with effective decisions. Therefore is easy to think that a higher Geographic Distance would be associated with a higher degree of control needed and thus with WOS. Finally, Economic Distance is hypothesized to negatively affect the choice of WOS since big disequilibrium between the wealth of two populations lead to think to a higher need of a partner that would be good in identify the preferences of the customer base, that is supposed to highly differ from the one that is usually served.

To conclude, this thesis will try to propose a synthetic indicator that may be able to identify the relationship between all those analyzed distances and the strategic entry mode choice. Moreover, has been created also a synthetic indicator that take into account only the dimensions considered in the Institutional Theory – the formal environment represented by the Cultural Distance and the informal environment represented by the Administrative Distance – in order to try to find a significant indicator able to predict companies' behaviors with its perspective.

3. Methodology

This thesis analyzes 3498 companies that are operating in the Brazilian market. Specifically, the companies are settled in 15 Western European countries, US, China, Russia and India and must be involved in at least one Foreign Direct Investment between Wholly Owned Subsidiary and Joint Venture, analyzed through cross-sectional data. The information about the sample have been collected from *Orbis*, a worldwide directory of company information, and *Zephyr*, a database of corporate finance deals, both provided by Bureau van Dijk and contain company information of over 85 million companies updated very frequently. To be considered, the parent companies have to be involved in at least a Joint Venture with a Brazilian partner or must have the full control of a subsidiary with the 100% of its shares. With these thresholds, 3263 WOS (93,3%) and 235 JV (6,7%) that are still active, have been identified – see Table 1 for a breakdown of parent companies' home countries. Given that the research seeks information on strategic international entry mode decisions and that firms may use more than one entry mode, they are accounted not more than once for each decision.

The country level data are collected from multiple secondary sources and the quantitative data will be analyzed using logistic regression analysis, which is the most common method in FDI research according to Canabal and White (2008).

	WOS	JV	TOT		WOS	JV	TOT
Portugal	74	13	87	United Kingd	180	17	197
Spain	249	21	270	Austria	15	1	16
Italy	242	9	251	Denmark	104	1	105
Belgium	71	3	74	Norway	63	3	66
Germany	243	18	261	Sweden	86	4	90
Switzerland	171	5	176	USA	1129	86	1215
Netherland	111	8	119	China	50	16	66
Finland	44	5	49	Russia	6	1	7
France	322	12	334	India	74	10	84
Luxemburg	29	2	31	TOT	3263	235	**3498**

Table 1 – Breakdown of Wholly Owned Subsidiaries (WOS) and Joint Venture (JV) listed by host countries.

3. 1. The choice of Brazil as focal country

Brazil has been chosen because of the large scale of FDI in the countries, ranking as 1st in Latin America and 6th globally (UNCTAD World Investment Report, 2015). The Federative Republic of Brazil is the largest economy in Latin America and the fifth largest country in the world in terms of both population and area. In the last decade it has raised interests because

of a high growth, which led Brazil to become the world's seventh-largest economy for GDP. It still depends on export of iron ore, soya, other raw material and farm products, but less than in the past. The young population, expanding middle-class and the highest per-capita income between BRICS made Brazil interesting in terms of investment opportunities and as importer. The government is proactive and relatively stable, but the situation may rapidly change. However, corruption still remains a big issue and it involves that Brazil ranks 72nd on 180 countries in the International Transparency Survey.

Since 2014, the annual growth dropped mainly due to a reduced demand from the large middle class, shrinking exports and lower commodity prices. Nowadays, rising inflation, high interest rates, weak currency and political uncertainty led to a stagnation in 2014 and to a contraction in 2015, with the high probability that the economy will struggle well beyond, due to an eroding competitiveness and a worsening business environment, resulting in a drop of the investments. Even though, the government is still working hard to continue to attract foreign investment. A clear example is the new infrastructure concessions program of USD 64 billion over five years unveiled by President Dilma Rouseff.

Brazilian business climate benefits from generally open policies towards FDIs and Brazilian companies show the highest R&D spending in Latin America, even if the technological level is still low. Doing business in Brazil for a foreign MNC implies many challenges. According to the World Bank's *Ease of Doing Business 2015 Report*, Brazil ranked 123rd out of 189 countries, gaining three position in comparison with the previous year, but still low in the rank, well beyond the most of the other countries in the Latin America and Caribbean Region. This bad performance is the result of an excessive level of red tape that continue to prevail in the country's business regulation, high taxes, trade barriers and lack of reforms by the Brazilian government.

The sum of all the indirect costs to bear when dealing with government procedures, the lack of infrastructures, excessive employee benefits required compared with their training level, the environmental laws and the intricate tax structure is known as the "*custo Brasil*". Moreover, the high taxes levy on some import products, such as cars, make essential for foreign companies to be directly present in the market. For instance, the number of procedures required in order to start a business is 11 that takes in average 102 days, while in the rest of the Latin American region, the average number of procedures is 8, which take 29 days. Another interesting comparison between Brazil and Latin America concern the tax structure. In Brazil, paying taxes requires 2,600 hours per year, while the average of the region is 361 and the average of the OECD countries is 177. The 40.5% of the profit is spent

for labor taxes and other contributions to employees, to compare with the 13% of LatAm and 24% of OECDs (doingbusiness.org, 2015). Moreover, the World Economic Forum ranks Brazil as 74th of 140 countries for the quality of the infrastructures, with a score of 3.9 on 7, which is not the worst over Latin America and Caribbean countries, but is clear that it is far to be competitive (World Economic Forum, 2015).

Therefore, doing business in Brazil often means to resort to an expert to help in following bureaucratic issues (Erns & Young Terco, 2011). As a matter of facts, Brazilian business culture heavily relies on strong personal relationships (Barbosa, 1995). Indeed, building Joint Ventures with local partners often means to invest time and visit them frequently in order to build a relationship strong enough. Furthermore, companies that want to do business in Brazil should know about how important are emotional resources in order to do business and also to deal with the public sector. However, is not easy to find an adequate partner. The poor educational level makes difficult to find the right person endowed with all the skills required to deal with complex reality such as multinational companies.

As it is said before, Brazil, is recognized as one of the most important growing markets. Despite the high attractiveness of the market potential, trade barriers, cultural distance and political and economical risks are considered as the main obstacles to the internationalization. To sell products and services in Brazil, foreign companies need to have a legal representation in Brazil because whatever is sold need to be invoiced. The *Nota Fiscal* has to be issued at the point of sale and the identification number of the seller has to be written on it. Since that identification number is assigned only to registered legal entity in Brazil, local presence is necessary.

According to the Transaction Cost Theory, a low commitment mode should be chosen, where the resulting loss of control can be compensated by forming business networks in order to gain local knowledge. Joint Venture are common in Brazil, mainly because Brazilian partners are required to compete in segments of the government procurement market or in other market subjected to government regulation, such as capital goods, telecommunication and insurance. However, the great external uncertainty mainly due to insufficient rights protections makes Wholly Owned Subsidiaries more attractive in order to be sure to protect the critical knowledge and technological resources.

3. 2. Dependent Variable

The Entry Mode variable indicates the entry mode chosen. Therefore, the dependent variable is a dichotomous variable classifying entry mode that takes the value 1 when the investment has been made through a full ownership and 0 otherwise. In the regressions, the likelihood that the investment is made through a WOS is explained by the independent variables defined below.

The dependent variable will be defined as:

$$Y = \beta_0 + \beta_1 X_{Cultural\ Distance} + \beta_2 X_{Administrative\ Distance} + \beta_3 X_{Geographic\ Distance} + \beta_4 X_{Economic\ Distance} + \beta_5 X_{CD+AD+GD+ED} + \beta_6 X_{CD+AD}$$

3. 3. Independent Variables

Cultural Distance (CD) has been much researched variable in international business literature. A larger cultural distance between the home and host country will lead to a higher uncertainty and will increase transaction costs of doing business. The distance between Brazil and each country has been measured through the measure that originates from Kogut and Singh's work (1988) based, in turn, on the Hofstede's six-dimension cultural distances.

$$CD_j = \sum_{i=1}^{n} \frac{(I_{ij} - I_{is})^2 / V_i}{n}$$

CD_j = distance between target country and the j-th one

I_{ij} = index of the i-th cultural dimension in the j-th country

I_{is} = index of the i-th cultural dimension in the home country

V_i = variance of the index of the i-th dimension

n = number of cultural dimension considered

The *Administrative/Political Distance* (AD) has been measured through different steps. This study adopts the World Bank's *Worldwide Governance Indicator 2015*, which is one of the most used in literature to measure the quality of the governance in each country (Chang et al., 2012). In 1996 the World Bank started to collect surveys on the quality of the government of 212 countries in the world through six dimensions: voice and accountability,

political stability and absence of violence, government effectiveness, regulatory quality, rule of law and control of corruption. To each dimension is assigned a score where a higher value correspond a better governance quality. Then, to synthetize those dimensions into a composite measure that indicate the overall quality has been used the index developed by Kogut and Singh. In order to include the direction of this distance according to the theory carried out by Hernández and Nieto (2015), hence the relative position of the origin country compared to the destination country, the sign of the distance has given by the sum of the distance on each of the analyzed dimension.

The *Geographic Distance* (GD) between Brazil and each country has been measured through the distance between capitals of each country, introduced in logarithmic form in the models following the indications by López-Duarte and Vidal-Suárez (2013).

The *Economic* Development *Distance* (ED) seeks to catch the differences in the economic development between Brazil and the companies' home countries. It has been measured as the ratio between the GDP pro-capita of each country and the Brazilian one. Information has been obtained from report by the World Bank.

Two other variables have been included as a composition of the previous indicators: CAGE, which is the sum of all the previous variables, and CA, the sum of Cultural Distance and Administrative Distance. Those variables have been created in the attempt to find different ways to calculate cross-national distances, to see if it is possible or not to synthetize the other dimensions into a singular index with an higher explanatory power

Table 2 offers an overview over the aforementioned dimensions.

	Cultural Distance (CD)	Administatrive Distance (AD)	Geographic Distance (GD)	Economic Distance (ED)	CD+AD+GD+ED (CAGE)	CD + AD (CA)
Portugal	0,6636	0,9969	3,6872	1,6756	7,0232	1,6604
Spain	0,2414	0,7445	3,7123	2,0944	6,7926	0,9859
Italy	1,1397	0,3412	3,9717	2,1746	7,6273	1,4810
Belgium	1,0016	1,5894	3,9796	2,6703	9,2409	2,5910
Germany	1,4844	2,0945	4,0072	2,8608	10,4468	3,5789
Switzerland	1,3497	2,6684	3,9735	3,5994	11,5910	4,0181
Netherland	1,7844	2,3918	3,9878	2,9687	11,1328	4,1762
Finland	1,0250	2,7402	4,0509	2,5169	10,3330	3,7652
France	0,5337	1,3438	3,9676	2,5093	8,3544	1,8775
Luxemburg	0,6240	2,4491	3,9804	6,0439	13,0974	3,0732
United Kingdom	1,9448	1,8558	3,9732	2,4652	10,2390	3,8006
Austria	2,0812	2,2245	4,0033	2,8870	11,1961	4,3058
Denmark	2,8274	2,3533	4,0139	2,7623	11,9569	5,1807
Norway	1,8006	2,5143	4,0218	4,1576	12,4942	4,3149
Sweden	2,5463	2,4413	4,0355	2,8610	11,8841	4,9876
USA	1,6687	1,4566	3,8744	3,3655	10,3653	3,1253
China	1,9482	-0,7654	3,2460	0,8186	5,2474	1,1828
Russia	1,3711	-0,7907	4,0693	1,5134	6,1632	0,5804
India	0,8708	-0,2516	4,1584	0,3595	5,1370	0,6191

Table 2 – overview of independent variables. **Source**: Author's elaboration.
Note: CD calculated through Kogut-Singh Index of Hofstede's six dimensions of National Culture; CA calculated through Kogut-Singh Index of World Bank's *Worldwide Governance Indicator 2015*; GD calculated logarithm of flying distance between Brasilia and the capital of every considered country; ED calculated as ration of the GDP pro-capita of each country and one of Brasil.

4. Results

This chapter describes the results and findings of the logistic regressions and thus the different factors' effects on entry mode choices. Table 3 reports the means, standard deviations and correlation coefficients between the variables. As expected, the correlation between the variable CAGE and the other variables is high since it is a composition of them, as well as the variable CA with CD and AD, but this will not affect the regressions since those variables will be analyzed in a separate and alone way. Moreover, is possible to notice that also the Economic Distance correlates highly with the variable relating to Administrative Distance. This may be explained because institutions in poorer countries are often less developed. However, multicollinearity is not a concern since the Variance Inflation Factors (VIF) of the multivariate regression models are well below the generally accepted threshold of 10.

		Mean	S.D.	1	2	3	4	5	6	7
1	WOS	0,9328	0,25	1						
2	CD	1,6823	0,815	-0,009	1					
3	AD	1,8462	0,831	0,0204	0,6607	1				
4	GD	3,9733	0,102	0,0422	0,6573	0,513	1			
5	ED	2,7328	0,582	0,0243	0,316	0,7057	0,4129	1		
6	CAGE	10,235	1,956	0,0144	0,8256	0,9368	0,6669	0,7505	1	
7	CA	3,5284	1,5	0,0064	0,9094	0,913	0,6415	0,5627	0,9676	1

Table 3 – Means, Standard Deviations and Correlations

Table 4a and Table 4b report the results of the different logistic regression models that have been estimated using different combinations of the considered dimensions in order to analyze their influence on the entry mode decision. The Likelihood Ratio Test (LRT) has been performed in order to test the goodness of fit of the models in comparison to the null model, which is the case where no independent variables are included. Therefore, a lower p-value means a better fit of the data to the model.

	Model 1			Model 2			Model 3			Model 4			Model 5		
	coeff	s.d.	p	coeff	s.d.	p	coeff	s.d.	p	coeff	s.d.	p	coeff	s.d.	p
Const	2,7057	0,1575	***	2,4602	0,155	***	-2,981	2,2604	0,1872	2,1482	0,3383	***	2,5728	0,1677	***
CD	-0,0442	0,0833	0,5961										-0,1893	0,1104	0,0862
AD				0,0939	0,078	0,2291							0,2085	0,1001	0,0372
GD							1,4149	0,5707	0,0132						
ED										0,1782	0,1235	0,149			
CAGE															
CA															
LRT		0,2821			1,409			5,5957			2,164			4,383	
p (LRT)		0,5954			0,2352			0,018			0,1413			0,1117	

***: p<0,005

Table 4a – Logistic regression estimates of entry mode choice (WOS=1); Each model is estimated considering only the constant and the dimension in which the coefficient appears.

Model 6			Model 7			Model 8			Model 9			
coeff	s.d.	p	coeff	s.d.	p	coeff	s.d.	p	coeff	s.d.	p	
-6,751	2,7953	0,0157	-6,4797	2,7428	0,0182	2,3372	0,3509	***	2,5712	0,1704	***	Const
-0,386	0,1308	0,0032	-0,362	0,1217	0,0029							CD
0,21	0,152	0,1678	0,156	0,1098	0,1552							AD
2,499	0,7617	0,001	2,3796	0,7247	0,001							GD
-0,0958	0,186	0,6067										ED
						0,0288	0,034	0,3961				CAGE
									0,0169	0,0448	0,7047	CA
	14,7768			14,5211			0,7123			0,1431		LRT
	0,0052			0,0023			0,3987			0,7052		p (LRT)

Table 4b – Logistic regression estimates of entry mode choice (WOS=1); see above.

Specifically, Model 1 to Model 4 are estimated including only one of the basic dimensions analyzed for time; Model 5, Model 6 and Model 7 are estimated using different combinations of the previous dimensions in the same model; Model 8 and Model 9 are estimated using the composed dimensions CAGE and CA in the attempt to find different ways to calculate cross-national distances, to see if it is possible or not to synthetize the other dimensions into a singular index with an higher explanatory power by testing it on entry mode research.

As it is possible to see in Table 4a, Cultural Distance, Administrative Distance and Economic Distance singularly considered do not have any significant influence on the entry mode, but also the models do not have explanatory power either. However things change when Geographic Distance is considered alone. In this case, the LRT value of the Model 3 is 5,596 (p<0,05), indicating a good explanatory power of the model. The coefficient of Geographic Distance is 1,42 (p<0,05), showing a positive influence on entry mode, so companies are more likely to chose WOS as the geographic distance increase.

The explanatory power of Model 5, Model 6 and Model 7 show a high explanatory power with all LRT higher than 4 (p<0,15). However, the explanatory power of Model 6 and

Model 7 are much higher than Model 5. Moreover, it is possible to note that the Economic Distance included in Model 6 has no statistical significance of its coefficient. Thus, we can conclude that apparently Economic Distance does not play any influence on the entry mode decision. In Model 7, Cultural Distance has a coefficient of -0,362 ($p<0,01$) showing a negative influence on entry mode, revealing that firms from more culturally distant countries are more likely to prefer JV rather than WOS. Conversely, Model 7 reveals the positive influence of Administrative Distance, with a coefficient of 0,156 ($p=0,1552$). Firms appear to be more likely to choose WOS as their entry mode when enter in a country with higher differences in the formal institutional environment as previously defined, but there may be doubts over its effect since the slightly high p-value. Moreover, Model 7 confirms also the positive influence of Geographic Distance with a coefficient of 2,38 ($p<0,01$).

Model 8 and Model 9 do not have any explanatory power, thus we can conclude that basing on this sample there is no possibility to gather more variable in only one index.

5. Discussion of results and conclusions

The aim of this thesis is to analyze how different forms of distance between countries may condition the choice of international entry mode. It is well accepted in the Entry Mode literature that the choice of MNEs between entering foreign countries through Wholly Owned Subsidiaries or through Joint Ventures depends to a considerable extent to the external uncertainty in the target country associated with the distances with the parent's home country.

This thesis provides conclusive results relative to the need to include in the analysis many forms of distance between countries by examining several way to capture the extent of how external uncertainty influences the entry mode choice. In particular, the results are analyzed looking at the peculiarities that drive the choice between WOSs and JVs when internationalize in a particular country, which is Brazil. The results show that Cultural Distance, Administrative Distance and Geographic Distance play a relevant role in the choice of investment mode through their interaction, but not always when considered in an isolated way.

The international business literature has widely recognized that Cultural Distance influences firms' entry mode choice. However, the debate about its effect on the level of resource commitment is still open since scholars have found only inconclusive evidences (Brouthers and Brouthers, 2001; Shenkar, 2001; Tihanyi et al., 2005). Some of them agree that in more culturally distant countries, a lower resource commitment would give more flexibility and a lower risk due to a lower capital exposition and to the possibility to leverage the partner's knowledge about the market. On the other hand, many other scholars argue that taking into the organization such a culturally different partner would lead only to conflicts, thus a full-control solution would protect from opportunistic behaviors. According to the regressions performed in this analysis, Cultural Distance does not always play a relevant role in the choice of investment mode, but its statistical significance increases in all the models where more than one dimension are included. The findings show that a negative relation exists between Cultural Distance and the choice of the entry mode, so firms prefer to choose collaborative solutions when enter in a more culturally distant country, thus tend to opt for Joint Ventures. Nevertheless, this may be a peculiarity of the Brazilian business environment. Indeed, as it is previously said, Brazilians strongly rely on personal relationships when doing business, so the benefits perceived from having a local partner may compensate the time and other resources needed in order to build those relations for foreign investors.

The analysis confirms also that Administrative Distance have a positive impact on entry mode decisions, implying that when entering a more distant country, firms opt for WOS. However the statistical significance of its influence is weak since its p-value is higher than 0,2 when considered alone and 0,155 when interact with Cultural Distance and Geographic Distance. Firms from more developed regulatory environment may face greater problems to enforce contractual agreement when they enter in countries with less developed regulatory framework, thus the risks coming from potential opportunistic behaviours from an eventual partner could offset all the benefits coming from a collaboration. This is particularly true in Brazil, where in the judicial system takes incredibly long time, and it may affect the business opportunities of a firm, so they may prefer to internalize as more transactions as possible.

Geographic Distance displays positive and statistically significant relations, revealing that firms located more geographically distant prefer to exert full control through Wholly Owned Subsidiaries. A possible explanation could be that when physical distance increases, firms perceive that more control is needed to avoid delays in the decision-making process due to different time-zones or long travels in case there is the need to meet the hypothetical partner. Finally, the Economic Distance does not show any robust result, as it is not significant in any estimated model.

Specifically, the current analysis proposes that mangers, when taking strategic decisions about international entry modes, should take into account different forms of distance. In particular, Cultural Distance, Administrative/Political Distance and Geographic Distance. It confirms that differences in culture and in institutions between countries have an impact on entry mode decisions, but also find out that Geographic Distance still plays a relevant role in this decision despite the wide range of new technologies that make the world '*flatter*' (Friedman, 2005), and that differences in the population wealth do not affect entry mode decisions.

This study also bridge the Transaction Cost Theory perspective with the Institutional-Based View of the international business studies, since the former focuses on the considerations about cost convenience in relation with problems of opportunism, while the latter emphasizes the need to respond to the institutions of any host country when making strategic decisions (Peng et al., 2008). Indeed, it analyzes Cultural Distances and differences in the Political Risk from both prospective, enriching them with taking into consideration also country-specific conditions that may influence strategic choices.

Moreover, the findings may have implications for managers. The insights generated may enhance the understanding of determinants of international entry mode decisions, providing a framework to use as basis when taking strategic decisions on internationalization. Indeed, the analysis indicate which factors bear in mind for their relevance and how to adapt them considering particular issues that may characterize a business environment, specially in development countries where it may be affected by political instability and other factors, such as weak juridical system or underdeveloped infrastructures.

Considering a practical view of the mode, if any management team would internationalize through a FDI in Brazil, they should retrieve the necessary information for Brazil and also for their home country, that are Hofstede's six dimensions of national culture and calculate its Kogut-Singh Index; the World Bank's *Worldwide Governance Indicator* and calculate its Kogut-Singh Index and the logarithm of the flying distance between the capital of their country and Brasilia. The second step consists in multiply the previous dimension times the coefficients estimated for the dimension CD, AD and GD. If the sum of them is lower than 0.5, the management team should prefer to enter the Country through Joint Venture. Conversely, if the sum is higher than 0.5 they should enter through Wholly Owned Subsidiary, while if the sum is 0.5 the choice will be irrelevant. Therefore, managers should considerate and balance the benefits and drawbacks coming from each entry mode in relation to the Cultural Distance, Administrative/Political Distance and Geographic Distance. The extendibility to this model in a general case between two given country may be true, but it would need more researches on the estimation of the coefficients.

6. Limitations and future research suggestions

The current analysis provide implication and contributions, but has limitations as well. Since the analysis is developed on a sample that consider companies internationalized in a specific country, ignoring whether they are present in other countries or not, it may somehow influence the outcomes. Moreover, the biggest part of the considered firms are located in Western Europe and USA, countries with a very low degree of political risk. Furthermore, the geographic distance within European countries from Brazil is not relevantly different. It becomes advisable to carry out new studies including different target countries and a more differentiated sample from the home-country point of view. Also an analysis of a split in the database into developed and developing country would be interesting, both from the home-country and host-country point of view.

Secondly, the analysis investigates the role of distances only when firms are choosing between WOSs and JVs without examining other available forms. Including a wider range of entry modes may improve the validity of the model. Some interferences with the validity of the models may be given by the extensive recourse to minority investments that are only a financial way to reduce financial risks.

Another improvement that would approach the study to Ghemawat's CAGE Distance Framework would be to select specific sectors and look at the differences between them since they may be affected by differences in specific strategic choices in order to going deeper in the understanding of the relevant factors that influence the entry mode choices. Therefore, focusing on a specific sector can provide more valuable results when putting specific weights on each individual distance measure.

To be able to improve the regression models, the dataset would need to be expanded by a larger amount of information over a larger number of years. Since Cultural Distance, Political Distance and Economic Distance may change year by year, a better comparison could be achieved by considering those distances in the year when operation started. Further improvement can be achieved using longitudinal data rather than cross-sectional data, also considering all the companies that internationalized, and not only the active firms, in order to be able to capture which conditions led to the failure of the subsidiary/JV.

Moreover, in order to make a solid comparison between the countries, all the countries should have a comparable number of observations. A more balanced sample may provide better results on those. Finally, we should bear in mind that in the real world there are many variables that affect entry mode choice, such as the size of the parent company or its

previous international experiences. To get a indication of all variables affecting entry mode, more variables should be used, however this is out of the scope of this thesis since it is focused on the influence of the distances in all its meanings, and this might affect the significance of the individual relationships.

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