



Influence of Country Factors on Entry Mode Through Knowledge and Transactional Cost Economics: Market Entry: Evidence from Construction Firms

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ABSTRACT

Owing to the competition global level economy of world and pattern are promoting to the construction firms to increase into emerging economies. Entry mode has become important for firms. The present paper aims to explore the entry modes which are preferred by construction firms in Malaysia, for their international projects, on whether construction firms choose equity modes, non-equity modes or both modes. 19 questionnaires were filled by respondents by using cross-sectional data technique. This study found that country specific factors (cultural differences and target country risk) influence the entry mode of firms directly and through knowledge and transactional cost economics by applying the multinomial logistic regression. This study contributes theoretically and practically along with this; present study recommends that government should improve internal and external factors to enter the firms for economic development.

Keywords: Entry Mode, External Factors, Internal Factors Emerging Economy

JEL Classifications: M, M5, M21

1. INTRODUCTION

Infrastructural development creates a reduction in communication gap and time consumption along with a reduction in the cost of tariff barriers. Likewise, other factors responsible for the globalization process results in the internationalization of the construction firms with many other opportunities. But the choice/selection of these firms regarding new entry in the market have made them risky i.e., it could lead to failure and results in financial loss to that firm by selection of the wrong choice. It could also lead to loss of opportunities and loss of market share in international markets as well. So the new entry of firm in the concerned market regarding choice has a significant effect on the company. And this situation has made the Malaysian firms risky to start a business even by obtaining permits with respect to cultural differences (Opanasopit, 2016).

Based on the resource-based view, when there is a situation of exploiting a competitive advantage, the firms have to take account the specific context knowledge, i.e., the especially the method of doing the investment that is typical of a specific country. So

if a person has knowledge, he can enter the market the culture difference will not affect more (Hussain and Ishrat, 1999; Kotler and Armstrong, 2001; Lundahl and Skärvad, 1992; Malik, 2010; Madhok, 1997). So there is the probability that cultural differences affect entry mode of firms through knowledge. The cultural differences influence entry mode through transaction cost. As small culture differences lead to low cost and low cost will courage firm to enter the market (Luo, 2001). Additionally, if the construction firms do not have knowledge about the target country risk they can choose the wrong entry mode (Brouthers, 2002). So country risk might influence entry mode through knowledge and transaction cost. If the firm feels that in host country they have risk they need to spend more money in choosing the entry mode. As low risk leads to low cost and low cost will courage firm to enter the market (Luo, 2001). However, the researcher failed to find the previous study that found the impact of cultural differences and country risk on firm's entry mode through knowledge and transaction cost.

Yasmeen and Viswanathan (2016) recommended that there is need to conduct a study on construction firms entry

mode particularly in Malaysia, So, this paper contributes to theoretically, practically and empirically, to conduct a study on the construction firms in an emerging economy of Malaysia. The present study contributes to the literature by founding the impact of cultural differences and country risk on firm's entry mode through knowledge and transaction cost. There are numerous studies that found that cultural differences and target country risk influence entry mode but few studies are available that theoretically say that cultural differences and target country risk influence entry mode through knowledge. So the present study contributes by conducting an empirical study on the influence of cultural differences and target country risk influence entry mode through knowledge.

2. THEORETICAL BACKGROUND AND LITERATURE REVIEW

2.1. Country Factors and Entry Modes

As well as entry mode is concerned, each specific aspect of every destination should be termed as important. Concluding from the past studies, in the host country, the distance among cultural and risk-targeted are the two variables with effect entry mode of the firm. The cultural distances are the differences of the culture of targeted host country in which business to be operated by new entry, and these differences are regarding the behavior of individuals to work with and start a business (Hofstede, 1980). This can be further explained well under Transaction Cost Economics in its application of investment on global level which is the Internalization theory (Anderson and Gatignon, 1986; Bradley, 2005; Buckley and Casson, 1976; Rugman, 1981) that says cultural distance influence to the additional costs which is linked not only with communication but also with information collection methods to decode and code the information (Pak and Park, 2004). Also, cultural distances results in difficulty of integration, adds up internationalization costs and firm then minimum resource of the organizational level of commitment (Randoy and Dibrell, 2002). Owing to this; in the reference to contingency approach, contractual agreements are present to enhance and limit the cultural distances for the entry of new firms to become familiar with the host country (Kim and Hwang, 1992). Also; resource dependency perspective states that to reduce risk regarding cultural distances, the firm took local support to help in the risk sharing aspects product characteristics and avoid mistakes (Contractor and Kundu, 1998; Hennart and Larimo, 1998; Pak and Park, 2004).

H_1 : Cultural distance will effect on entry modes of construction firms in emerging economy of Malaysia.

From above hypothesis, it can be derived sub-hypotheses based on the knowledge of host country regarding cultural distances which has already tested by empirically by previous studies (Brown et al., 2003; Hennart and Larimo, 1998; Hennart and Larimo, 1998; Kim and Hwang, 1992; Osborne, 1996; Pak and Park, 2004). This is reflected in the following hypothesis:

H_{1a} : Cultural distance will effect on entry modes of construction firms in emerging economy of Malaysia through knowledge.

And furthermore, the second sub-hypothesis derived from the said main hypothesis is based on the degree of commitment in the host country based on the contracts agreed to support in order to coordinate accordingly by the cultural distances regarding new entry (Aulakh and Kotabe, 19 7; Gatignon and Anderson, 1988; Hill et al. 1990; Kim and Hwang, 1992; Luo, 2001; Nakos et al., 2002; Osborne, 1996).

H_{1b} : Cultural distance will effect on entry modes of construction firms in emerging economy of Malaysia through a degree of commitment.

The next is the country risk that explains economically, political factor social and legal framework. The risk is involved because of the unexpected demand, political instability and uncertainty, variation in cost and in other sudden market behavior, However, in other situation, the alternative situation of argument as per maximum risk can be linked w with firms entry which can lead to lower resources commitment. Based on the above discussion there is possibility of negative link between target country risk and the level of commitment supposed with firm entry type, this shows that the relationship has established the main empirical support (Albaum et al., 2005; Aulakh et al., 1998; Axinn and Matthyssens, 2002; Azofra and Martinez, 1999; Brouthers, 2002; Brouthers and Brouthers, 2003; Contractor and Kundu, 1998; Gatignon and Anderson, 1988; Kim and Hwang, 1992; Luo, 2001; Nakos et al., 2002; Osborne, 1996; Pak and Park, 2004; Pla and Leoin, 2002; Ramon, 2002).

H_2 : Country risk will effect on equity entry modes.

Furthermore, Bradley et al., (2006) the country risk of targeted location is linked with the transaction of costs which refers to political risk or the uncertainty associated with foreign ownership (Pak and Park, 2004; Kotler and Armstrong, 2001. If the firm feels that in host country they have a risk, then they need to spend more money in choosing the entry mode. As low risk leads to low cost and low cost will courage firm to enter the market (Baek, 2003; Brouthers and Nakos 2004; Czinkota and Ronkainen, 2004; Foster, 1998; Hackett, 1976; Luo, 2001).

H_{2a} : Country risk will effect on equity entry modes through transaction cost economics.

Also, the target country risk is associated with the factor of knowledge. To overcome it, the firm will have to concern the local partner in the host country so that it could help the firm to familiarize accordingly (Azofra and Martinez, 1999; Brouthers, 2002; Deardorff, 1985; Falvey, 1994). Thus we can hypothesize that:

H_{2b} : Cultural distance will effect on equity entry modes through knowledge.

3. RESEARCH METHOD

Malik (2010) employed the qualitative method while working out with a quantitative approach and applying Multinomial logistic regression. Hence, Fig 1.1 shows the Framework of the present study.

The population is unknown in this study because in Malaysia the construction firm is not properly and formally. However, <200 construction firms of Malaysia are formally registered as Class A and Grade 7 with CIDB. The sample a random sampling technique is applied to collect the cross-sectional data and the sample size is determined by the rule of thumb Sekaran and Bougie, (2011) one hundred nineteen questionnaires were sent to the respondents, the response rate of construction companies was 53%.

4. MEASUREMENT OF VARIABLES

Three type of the firm have been selected in the present study, the respondents will be requested to chose EQ (equity mode) NEQ (non-equity mode) or that chose both EQ and NEQ. To collect the data the questionnaire is adapted from previous research of Luo (2006) and Datta, et al., (2009).

In this paper, the dependent variable has three categories EQ (equity mode) NEQ (non-equity mode) and both EQ and NEQ. The nature of the dependent variable is nominal that is divided into three categories, so, the multinomial logit model suits to be applied to test the hypothesis. However, Isa et al., (2014) used the same model to determine the influence of various variables on entry mode. Hence, the econometric model of this study is as follows:

$$EM = \beta_0 + \beta_1 CD_i + \beta_2 TCR_i + \beta_3 (CD*KN)_i + \beta_4 (CD*TC)_i + \beta_5 (CR*KN)_i + \beta_6 (CR*TC)_i + ei... \quad (1)$$

$$WS: Pr (y = j | x_i) = \frac{\text{Exp}(\beta_{0,j} + \beta_{1,j}x_{i1} + \beta_{2,j}x_{i2} + \beta_{3,j}x_{i3} + \beta_{4,j}x_{i4} + \beta_{5,j}x_{i5} + \beta_{6,j}x_{i6})}{\sum_{j=1}^4 \text{exp}(\beta_{0,j} + \beta_{1,j}x_{i1} + \beta_{2,j}x_{i2} + \beta_{3,j}x_{i3} + \beta_{4,j}x_{i4} + \beta_{5,j}x_{i5} + \beta_{6,j}x_{i6})} \quad (2)$$

EM represent to the entry mode of construction firms in Malaysia, CD represent the cultural differences, CR represent to target country risk, KN represent to knowledge and finally, TC represent to transactional cost, Where $\beta = \beta_j$ represent to vector of characteristics particular jth respondents, and β_j is a vector of coefficients respectively. The MNL model explain to each response probabilities once this study know the probabilities for $j=0..j$.

As per the descriptive analysis, 54% firms are applying EQ, NEQ is applied by 9% firms while 62% firms are applying both EQ and NEQ in doing their international projects of construction in the ASEAN. In the South Asia, 27% Malaysian are doing their construction projects and the rest were doing projects in other regions.

5. RESULT AND DISCUSSION

According to the below Table 1, the overall model is significant as the $P > \chi^2 = 0.0000$. In both cases (Both and NEQ compare to EQ) risk of the target country and cultural differences are in a negatively significant relationship. In the case of small cultural difference among both countries with low level of country risk, it can

Figure 1.1: Framework of the study

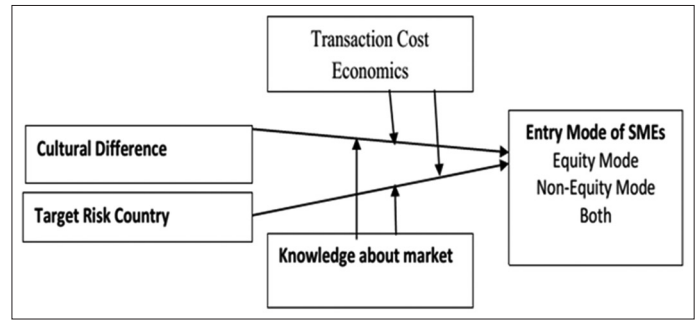


Table 1: Results of multinomial logit estimation

Model 1	NEQ relative to EQ		Both relative to EQ	
	Coefficient	SE	Coefficient	SE
Cons	17.495	9.626	18.546	7.265
CD	-0.538	0.242**	-0.584	0.265**
CD*KN	3.382	1.613**	0.55220	0.2652*
CD*TC	2.590	1.292**	0.8609	0.3977**
CR	-5.256	2.6795**	-4.5424	2.074*
CR*KN	4.509	2.394***	3.429	1.610**
CR*TC	1.427	0.679***	1.1622	0.5174**

$P > \chi^2$: 0.000, Log likelihood: -613.181 Pseudo R²: 0.32, **** and * denote that the corresponding coefficient is significant at the 1%, 5%, and 10% level, respectively. This study considers significant value from 1% to 10%. EQ is the base outcome, SE: Standard error

increase the entry of construction firms in the emerging economy of Malaysia. Particularly, if the construction firms feel that there is a low level of risk and cultural difference in the hosting country the firms will like to do business in the host country and because they will feel that their objectives can be achieved by completing their assignment in the peaceful and expected environment. Betterment in the both factors (cultural difference and country risk) will push to the firms to perform in a way that is fit the preferred course for their construction firm. The findings of this study are in line with Leo, 2001 and Isa et al., 2014.

The coefficient of the interaction term between knowledge, transactional cost and country-specific factors (culture differences and country risk) is significant, explaining that the influence of country-specific factors on the construction firm's entry mode depends on the knowledge and transactional cost. The results of the present paper are in line with a previous study (Aulakh and Kotabe, 1997; Brouthers, and Moussetis, 2002; Luo, 2001; Madhok, 1997; Pak and Park, 2004).

Marginal Effect

To explain probabilities of choosing the category of firm entry mode, this study calculate the marginal effects. Thus it is essential to evaluate all the outcomes, the marginal change in all (category) outcomes. For instance, using the predictors of x_1, x_2, x_3 , (the predictors) and $P_r (y=2): P_r (y=1), P_r (y=3): (P_r (y=1))$ usually indicate to the base category, $Y=1$. In multinomial logit, the Marginal effects are applied to examine the effect of change as a result of a unit change:

$$\frac{\partial p_{ij}}{\partial x_i} = p_{ij}(\beta_j - \hat{\beta}_i), \text{ Where the probable}$$

Table 2: Marginal effect of the MNLM

Variable	EQ	NEQ	Both
CD	(-0.001)*	(0.201)	(-0.026)**
CR	(-0.224)*	(-0.824)	(-0.088)*
KN	(0.023)**	(0.245)*	(0.873)**
TC	(-0.013)***	(0.342)	(-0.039)**

**** and * denote that the corresponding coefficient is significant at the 1%, 5%, and 10% level, respectively. The figures in parenthesis are P values. EQ is the base outcome

$\hat{\beta}_i = \sum_i p_{ij} \beta_i$ = is the probability of weighted average of β_i when there is computation of a single factor the marginal effects will change owing to P_{ij} changes with the factors (x_i), when the marginal effect is positive if $\beta_j > \beta_i$.

According Table 2 the marginal effect of CD, CR, KN and TC as per the probability of EQ mode of the firm and both (EQ and NEQ) are found statistically significant. Hence, if a CD is are not bearable and as per expectations then the probability of EQ and both is expected to decline by 0.001% and 0.026%, respectively. The probability of construction firms in the both case (EQ and NEQ) is expected to decrease and are not supportive. The probability of the firm in the case of EQ is expected to decrease and in the case of firms perceive property right system are not in support of construction firms. The marginal effect of CR on the probability of EQ and Both are statistically significant to enter into the Malaysian economy. In the case of construction firm has CR the probability EQ and both will increase by 0.224% and 0.08%, respectively. The marginal effect of the KN and TC determinants on the probability of EQ, NEQ and Both are statistically significant. Hence, construction firm notices that they have KN and less TC factors, the construction firm's probability EQ, NEW and both will increase, respectively.

6. CONCLUSION

Present paper concludes that entry mode selection by construction firms in Malaysia depends on country-specific factors, knowledge, and transactional cost economics. To test the hypothesis the cross-sectional data was collected from construction firms working in Malaysia; by applying multinomial logit model, this study found that country specific factors (cultural differences and target country risk) influence the entry mode of firms directly and through knowledge and transactional cost economics.

The present paper contributes to both aspect theoretically and practically and also recommends that government of Malaysia should amend the policies to minimize the cultural differences and transactional cost to enhance the number of construction firms and stay of construction firms in Malaysia. This study recommends that the further studies should examine the direct impact of monitoring costs, bargaining costs, bonding cost and maladaptation costs on market entry of firms.

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