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Uncertainty Avoiding Cultural Distance and Foreign Direct Investment Entry Pattern

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Abstract: With the gradual development of economic globalization and the continuous call of China's "Belt and Road Initiative" initiative, the scale of Chinese enterprises' foreign direct investment will further expand, and enterprises face various cultural nuances when conducting foreign direct investment. Among them, the impact of uncertainty avoiding cultural distance on the choice of investment entry mode is particularly significant. In the process of foreign direct investment, enterprises will inevitably face cultural exchanges and collisions between different regions and countries, and differences in languages, cultures, religious beliefs, and values among regions will constitute important factors affecting Chinese enterprises' foreign direct investment. In addition, there are many factors that affect enterprises' OFDI. This paper will sort out the relevant literature on the relationship between cultural distance, host country factors, parent company factors and OFDI entry mode, and briefly expound and explain the role and theory of these influencing factors.

Keywords: uncertainty avoidance; cultural distance; foreign direct investment; entry mode

1. The Relationship Between Cultural Distance and Foreign Direct Investment Entry Patterns

1.1. Cultural distance related theories

So far, there is no clear concept of "culture". Different scholars define "culture" differently, but its core elements are values in the final analysis. Therefore, in order to better define "culture", we should first clarify the components and connotations of values. However, the academic community also maintains different understanding attitudes in this regard. Different understandings of "culture" have led to differences in the academic community's understanding of the dimensions contained in culture. Among them, the most influential is the cultural dimension theory proposed by Hofstede in the 1970s. This theory was obtained through an empirical investigation and research. It used questionnaires in different languages for employees of IBM companies in various countries to focus on analyzing the regional differences in the values of employees in various countries. Therefore, four cultural dimensions are further summarized, namely: power distance, uncertainty avoidance, individualism and collectivism, and rigidity and flexibility. Later scholars supplemented the long-term orientation and short-term orientation, as well as their own indulgence and constraints, and further improved and enriched Hofstede's theory, forming a six-dimensional theory.

Kogut and Singh (1988) proposed the use of Hofstede's cultural dimension to measure cultural distance between countries. Cultural distance is defined as the difference in the score of the target country and the investing country on the Hofstede cultural dimension. Schwartz (1992) believes that Hofstede's cultural dimension theory is not comprehensive enough, and further proposes the Schwartz value structure, which covers a broader cultural value dimension, consisting of autonomy, pleasure, achievement, stimulation, rights, tradition, safety, compliance, fraternity, and kindness.

Cultural distance is considered to be an important factor affecting cross-border cooperation, international market selection, and foreign direct investment decisions. It is generally believed that the greater the cultural distance, the higher the

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complexity and challenge of cross-border operations, which may lead to higher transaction costs and lower investment efficiency. Some studies have shown that cultural distance can be mediated through certain mechanisms, such as building trust, adopting appropriate management strategies and communication methods to reduce the impact of cultural nuance. Cultural distance interacts with other factors to affect international business activities. These theories provide an important perspective for understanding the role of cultural factors in international business, helping companies and policymakers to better evaluate and manage cultural nuance in cross-border operations.

However, the mainstream method of measuring cultural nuance between countries in academia is Hofstede's cultural distance, which is mainly through giving rights distance, uncertainty avoidance, individualism and collectivism, and the corresponding values of the four cultural dimensions. Although many scholars later proposed methods for measuring cultural dimensions and differences among countries, this method has always been a common method for measuring cultural distance between countries at home and abroad and is recognized by scholars around the world.

1.2. The impact of cultural distance on foreign direct investment entry patterns

By studying the existing literatures on the influence of cultural distance on the entry mode of foreign direct investment, it will be found that the research of domestic and foreign scholars has not reached a unified conclusion, and there are still disputes in these research conclusions. The main research conclusions are as follows:

Some scholars believe that the greater the cultural distance, the more willing companies are to enter by means of lower cost, lower risk, and lower control, that is, choosing to enter through mergers and acquisitions. The reason is that Zhen and Minghong (2006) believe that cultural distance will become an obstacle to the exchange of information and the transfer of technology and experience between the parent company and the host country market; and when the cultural nuance is greater, the parent company will be more cautious in choosing the entry mode, and more willing to adopt the entry mode of controlling risks, which will lead to underestimation of the investment value of the host country (Zhen & Lu, 2006). The research conclusions of foreign scholars such as Morosini et al (1998) also show that with the increasing cultural distance between countries, companies are more inclined to adopt cross-border mergers and acquisitions rather than greenfield investment entry models (Morosini et al., 1998).

There are also some scholars who hold the opposite view, arguing that the greater the cultural distance, the more willing companies are to adopt the greenfield investment entry model (Barkema and Vermeulen, 1998; Drogendijk and Slangen, 2006) or adopt the sole proprietorship model (R & A, 2006). Du and Wang (2017) studied the influencing factors of the choice of FDI entry mode from the perspective of transaction cost, and the research conclusion shows that with the continuous increase of cultural distance, companies across the border are more likely to choose the greenfield investment mode to enter the foreign market. This is because when the cultural nuance between countries is greater, it is difficult for overseas subsidiaries to have a comprehensive understanding and grasp of the parent company's business philosophy and mode of operation, so when woodworking companies use greenfield investment to enter the host country market, they can hire and cultivate new people who have not yet come into contact with other management methods. These industries have strong plasticity of trust, so they can identify with the parent company's business philosophy and mode of operation, and at the same time have a greater sense of belonging to the company (Du & Wang, 2017).

The last point of view is different from the above two points of view, they believe that the influence of cultural distance on the choice of FDI entry mode is not absolute. Pan and Lu (2006) believe that although cultural nuance will make enterprises more cautious and strictly control risks when choosing the entry mode of FDI, but with the continuous optimization and improvement of the business environment of the host country and the accumulation of relevant experience of enterprises, the cultural nuance obstacles they encounter will become smaller and smaller, that is, cultural distance is no longer an important factor affecting the choice of FDI entry mode of enterprises (Zhen & Lu, 2006).

2. The Relationship Between Host Country Factors and Foreign Direct Investment Entry Patterns

2.1. Political factors in the host country

The relationship between the political factors of the host country and the entry mode of foreign direct investment is an important topic in international business research. Political factors usually include political stability, government policies, political risks, political systems, etc. These factors may have a significant impact on the international investment decisions of enterprises. Based on the relevant research of previous scholars, the influence of the political factors of the host country on the entry mode of foreign direct investment mainly lies in two aspects: national risk and policy system.

The country risks of the host country that enterprises face in foreign direct investment mainly include expropriation risk, ownership risk, and degree of localization. Demirbag (2008) and other scholars believe that as the country risk of the host country increases, enterprises are more inclined to choose the cross-merger model with lower control to enter other countries (M. et al., 2008). On the contrary, some scholars such as Asiedu and Esfahani (2001), Lopez-Duarte and Vidal-Suarez (2010), Shieh and Wu (2012) believe that the higher the country risk of the host country, the more likely enterprises are to choose the greenfield investment model to enter.

The policy system includes investment incentives and government efficiency, and an effective policy system can help enterprises better leverage their own advantages in foreign markets. Scholars such as Gomes-Casseres (1988), Mutinelli and Piscitello (1998), Luo (2001) argue that the more negative the policy system of the host country, that is, the more policy restrictions, the more likely enterprises are to choose investment models that go beyond mergers and acquisitions; conversely, the policies of countries and regions that want to stimulate foreign investment will further attract enterprises to adopt greenfield investment models to enter the market. However, there are still contradictions in the research conclusions of domestic and foreign academic circles in this regard. For example, Kim (2009) believes that the more favorable the policy system of the host country, the more willing the parent company is to enter through the merger and acquisition model, and Du et al. (2017) believes that Chinese multinational enterprises are more inclined to choose the greenfield investment model to enter the host country with higher policy risks. However, Elango (2005), Demirbag et al. (2008) argue that the policy system of the host country does not significantly affect the choice of OFDI entry mode.

2.2. Economic factors of the host country

The economic factor of the host country is one of the key factors affecting the choice of the entry mode of OFDI, and its influence on the choice mode of OFDI is mainly manifested in two aspects: market conditions and economic risks.

First of all, market conditions can be expressed in terms of market size and market potential. Mutinelli and Piscitello (1998) found that when companies enter the host country market, if their market size is larger, the more likely they are to choose the cross-border M & A model to enter; while Zhu (2018) believes that the larger the international market size, the more likely they are to choose the greenfield investment model to enter the international market (Zhu, 2018). Li et al. (2015) show that the growth rate of the host country market has a significant positive impact on the choice of cross-border M & A entry mode by companies. This is because when the market is growing rapidly, if green field investment is adopted, the parent company cannot seize part of the benefits brought by the market growth due to the slow pace of green field investment into the city (Li et al., 2015).

Secondly, different scholars have different opinions on the relationship between economic risk and foreign direct investment entry mode. Zhu (2018) believes that the lower the host economic risk, the more likely companies are to choose a greenfield investment model to enter the international market. But in contrast, Anderson and Gatignon (1986) concluded that the host country economic risk is positively correlated with the choice of a greenfield investment model by companies to enter the international market.

3. The Relationship Between Parent Company Factors and Foreign Direct Investment Entry Patterns

The existing domestic and foreign literatures mainly study the influence of the parent company's own situation on the choice of foreign direct investment entry mode from factors such as the company's transnational experience, science and technology and rights, as well as the company's size.

3.1. Transnational experience

Zhang and Shen (2015) took the manufacturing industry as a research sample. After empirical research and analysis, it is shown that the more experienced the enterprise is in internationalization, the more likely it is to adopt the entry mode of crossing mergers and acquisitions (Zhang & Shen, 2015). This conclusion coincides with the views of foreign scholars Davidson and Mcfetridge (1985), who believe that the more experienced the enterprise is, the stronger its ability to integrate resources and communicate and cooperate with the outside world. In the case of having these advantages, the enterprise is more likely to choose to enter the overseas market with low control over the merger and acquisition mode.

However, some scholars have come to the opposite conclusion, such as Gatignon and Anderson (1988), Gomes-casseres (1989), Hennart (1991) and other scholars believe that the more experienced the enterprise is, the more inclined it is to choose the greenfield investment model to enter the host country market. This is because the more experienced the multinational company is, the easier it is to understand the various situations of the host country, and the better it can deal with various emergencies that will occur in the host country or the risks faced by overseas investment. At this time, it is more inclined to enter the host country market with the greenfield investment model. On the contrary, if the parent company still chooses the greenfield investment model to enter the international market despite the lack of transnational experience, it may face greater risks and challenges, which may reduce the return on investment and even further lead to the failure of the company's overseas investment.

3.2. Science and technology and patents

The scientific and technological content of an enterprise is often directly proportional to the number of patents it has, which means that the more powerful the enterprise's science and technology, the more patents it will have. At the same time, these two are also one of the important indicators to measure the strength of an enterprise. The more powerful the science and technology and patents, the greater the value of the enterprise. Wang Fang and Shenke Association (2015) found through empirical research that the higher the R & D investment of an enterprise, the more the enterprise's science and technology and patents, the more likely the enterprise is to choose the green field investment entry method. The reason is that in order to ensure its comparative advantage in this regard, the parent company strictly controls its overseas subsidiaries to prevent the leakage of its related core technologies and patents (Wang & Shen, 2015). In addition, foreign scholar Elango (2005) subdivided proprietary knowledge, including explicit knowledge and invisible knowledge, and believes that if the proprietary knowledge of enterprises is explicit, they tend to choose the cross-border merger and acquisition model to enter the overseas market; if the proprietary knowledge of enterprises is implicit, they tend to choose the greenfield investment model.

3.3. Company size

Gao (2015) based on the empirical analysis of Chinese listed enterprises' foreign direct investment (FDI), it is shown that the size of the parent company has a significant positive impact on its choice of cross-M & A entry mode, that is, the larger the company size, the more likely it is to choose cross-M & A to enter the overseas market (Gao, 2015). The contradictory view is that Chen and Chang (2011) believe that large-scale companies have relatively good resources, talents, and ability to cope with risks, so they are more inclined to choose greenfield investment to enter the overseas market. However, foreign scholars Lopez-Duarte and Vidal-Suarez (2010) argue that the size of the parent company has no significant impact on the choice of OFDI entry mode.

4. Summary

The existing literature has conducted a comprehensive study on the entry mode of foreign direct investment from various aspects. Scholars at home and abroad have not only studied the influence of cultural distance, host country factors, parent company itself and other factors on the choice of foreign direct investment entry mode, but also provided many viewpoints and provided a certain space and direction for further research and exploration by scholars in the future. First of all, although there are many research literatures at home and abroad on the entry mode of foreign direct investment, the conclusions reached by different scholars in related aspects are different and even contradictory. The reason is that scholars have studied different enterprises, countries or regions from different angles and different situations, and the conclusions reached are not universal. Secondly, most of the traditional literatures study the direct impact of cultural distance on the choice of FDI entry mode, without considering the indirect impact of factors such as parent company itself and host country on it, and many literatures explore this issue from the perspective of transaction cost, but lack from the perspective of uncertainty avoidance to study the influencing factors of FDI entry mode. Finally, the existing literatures on FDI entry mode mostly focus on developed countries, and rarely on the impact of FDI entry mode of listed companies in developing countries, especially China.

Based on this, future research can conduct in-depth analysis of the FDI data of China’s large and overseas listed companies, investigate the impact of uncertainty avoidance cultural distance on the FDI entry mode of China’s large listed companies, and on this basis, introduce the host government’s attitude towards FDI and the parent company’s core technology as adjustment variables into the path of uncertainty avoidance cultural distance affecting the FDI entry mode, so as to further test the host government’s attitude towards FDI and the parent company's core technology on the relationship between uncertainty avoidance cultural distance and Chinese listed companies’ FDI entry mode.

The research of this paper provides a new perspective for scholars to study the issues related to the entry mode of foreign direct investment in the future. At the same time, it also further sorts out the impact of uncertainty avoidance of cultural distance on the entry mode of foreign direct investment and the influence of other related external factors. In addition, the research conclusions of this paper are also for listed companies in China that plan to invest overseas. When choosing an overseas entry mode, they must not only combine their own factors, but also consider domestic and foreign market factors, etc., in order to choose a better model to enter the overseas market. Therefore, this paper also has practical reference value and guiding significance.

Conflict of Interest

The author declares that she has no conflicts of interest to this work.

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