

## **A Conceptual Model for Culture Impact on Entry Mode and Network Mobility of Multinational Enterprises**

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*This study constructs a 2 x2 model and propose that when multinational enterprise from high context culture entering into a low context culture country, the better way is to employ a high stock structure option as its entry mode, and bring its home network links into the host country; when entering into high context culture, the better way is to employ low stock structure option, and bring its home network links into the host country. For multinational enterprise from low context culture, when entering into a high context country, employing low stock structure option and cultivating links in the host country is the better way for survival; when entering into a country also with low context culture, employing high stock structure option as its entry mode, and cultivating links in the host country is more beneficial.*

**Field of Research:** International Business, Cross Culture

### **1. Introduction**

Culture is the summation of the common value systems, beliefs, behaviors, customs and attitudes of every member in the society. With the growing importance of globalization today, enterprises have ample opportunities to conduct commercial activities within the cultural background of other countries. When different cultures meet, knowing the essence of the other party's culture will greatly facilitate communication, thereby making the partnership effective. Besides the importance in this practical aspect, knowledge in the culture of the host country is also useful in the management of multinational enterprise. Many researchers had provided useful suggestions on this issue, but these studies mainly focus on multinational enterprises that are already operating in the host country, bringing up management issues concerning things to note in business operations and relating to culture. As for the influence of culture in determining the decision-making of the multinational enterprise before entering a host country, such as: the choice of entry mode, and if there is a need for network shift, it is rarely discussed. Also, research on relationship between

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international enterprise and culture tends to be a unilateral focus on management implication between the culture of the host country and its further extension. The dyad relation between the home country and host country's culture is seldom looked into.

For these reasons, this study will base on the cultural model proposed by Hall (1976) to consider the dyad relation between the home country and the host country, and to discuss how entry modes and network mobility of multinational enterprises will differ when multinational enterprises in high and low context culture are placed in host countries of varying degree of cultural contexts. For our purpose, first, the literatures of these issues are discussed. Then this paper describes a 2 x 2 model to delineate the relationships between the various context culture of host and home country. Finally, several propositions based on the above model are proposed and discussed.

## 2. Literature Review

This section will review the influence of culture on entry mode and network. First, a brief introduction of Hall's (1976) culture model will be discussed. Then, the calculation and perception of transaction costs under different cultures will be introduced. Third, the effect of culture on entry mode will be reviewed.

### *2.1 Hall's high context culture and low context culture*

Hall (1976) proposed a cultural model that uses high culture context and low culture context as its measuring standard. High context and low context each represents an extreme end of a continuous scale, and every country lies on one point of the scale, which indicates the degree of cultural context of that particular country.

In high context culture, human relationships are closely knitted. In such complex relationships, there is a need for social strata to direct various types of relations. Every individual are required to exert self-control, that is, not to express their feelings easily through words, and the key to communication is through simple vocabulary and body language, to bring out the implicit message. In low context culture, every individual is independent, and relations between each individual are loosely connected. Hence communications are straight forward and not strongly affected by situational factors (Hall, 1976). We will now look at social orientation, commitment, responsibility, conflicts, communication and preference in dealing with new situations to further define the meaning of high and low context.

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### **2.1.1 Social orientation**

Relationships between members in a high context culture are close, and such link implies commitment, expectations and principle of mutual benefit. Such culture emphasizes a lot on submission and group-based learning, and being different is not welcomed. At the same time, distinction between the in-group and out group is also significant and important in such culture. In low context culture, human to human links are not that strong, and relationships are fragmented and scattered, not closely knitted. Every bond can be forged or broken base on interests and benefits, making the mobility of the links flexible (Hall, 1976).

### **2.1.2 Commitment**

As members in a high context culture are closely bonded, naturally there will be a high degree of cohesion, and commitment to complete tasks of common activities (Hall, 1976). As such, giving your word is very important, and usually one promise will led to be a life-long obligation. In cases of unclear relationship or when trust is not yet built up, members in a high context culture tends not to make pledges easily (Hall, 1976). Hence, when conducting commercial activities with countries with high context culture, it will be important to have an introducer who is reputable, and it will better if he is from the in-group. Members from a low context culture, on the other hand, tend to have less of the strong sense of commitment mentioned above (Hall, 1976).

### **2.1.3 Responsibility**

Under a high context culture, links between members are close and social hierarchy is clear, with people at the top are responsible for the actions of their subordinate. Therefore top-down decision-making model is often seen in such a culture. In low context culture, responsibility in an organization is scattered and distributed, so when mistakes occurs, the scapegoat tends be the subordinate, not those in authority (Hall, 1976).

### **2.1.4 Conflict Management**

People in a high context culture tend to suppress their real feelings to avoid direct confrontation, so as to maintain social harmony and bonding. Hence, face-saving is important to members in a high context culture (Tse et al., 1988). Communications by members in high context culture tends to be covert and implicit; this is to reduce the chance for direct confrontation. For instance, correcting someone's speech when talking is seldom seen in a high context culture (Kim et al., 1998). As for members in a low context culture, they will not purposely avoid direct confrontation. Expressing dissatisfaction, championing self interest is a matter of fact. Criticisms are direct and

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formal, as contrast to high context culture, where it is subtle, focusing more on the meaning behind the speech (Czinkota & Ronkainen, 1990).

### 2.1.5 Communications

For members in a high context culture, message derived from slight movements in body language, expressions and gestures are far more important than the words used during communication. As such, to understand the communication context of members in a high context culture, we must put the words into the context at that time, and not to just comprehend it base on words alone (Hall, 1976). For example in Asia, major commercial transactions may not consist of a lot of clear, detailed written contracts. It is more dependent on mutual trust and chemistry. In a low context culture, communication content between members is clear and specific. Most of the information will be contained in the words. From the surface meaning of the terms and sentence structures, one can deduce the meaning of the other party. Hence in deciphering the speeches of members in a low context culture, one would not need to consider too many issues such as the background and the context in which the speech was made (Onkvisit & Shaw, 1993).

### 2.1.6 Dealing with new situation

Members in a high context culture tend to be unwilling to be different. They are also apprehensive in facing totally new or unfamiliar environment. They hope to follow a certain set of rules of tradition (Hall, 1976). To them, they need to re-build the hidden rules when faced with brand new surroundings. In contrast, members from a low context culture thrive better in a new environment and they tend to come up innovative methods to cope and adapt (Hall, 1976).

## 2.2 *Perceptions of transaction costs under different cultures*

As mentioned above, members from different cultures have differing views on social orientation, commitment, responsibility, conflict management, communication and in dealing with new situation, and this will further influence the perception in transaction costs.

Transaction cost refers to the various cost sustained from initiating to closing a transaction. It can be divided into pre-transaction and post-transaction stage; the former will include searching costs, bargaining costs and contracting costs. Searching cost is the cost involved in the search of the object of transaction. Bargaining cost refers to the cost to bring both parties from non-consensus to an agreement. The cost

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is closely dependent on factors such as the degree of mutual chemistry and if information held by both parties are complementary. Contracting costs refers to cost sustained in bring the agreement into words.

Post transaction stage, on the other hand, involves monitoring costs and enforcement costs. Monitoring costs refers to the cost sustains in avoiding fraud or putting a stop to inaction by the other party. Enforcement costs refer to the safeguarding of the terms in the contract, such as legal cost, so as to make sure that contractual parties will uphold the agreement.

Members in high context culture values human to human link, so when they enter into partnership, it tends to be long-lasting and mutually dependent. With the understanding and chemistry build from such long term partnership, one can correctly grapple with the implicit or covert message in the speech of the other party. Hence transaction costs are relatively low. In addition, with the mutual trust built up from the cooperation and recommendation by reputable introducer, this will greatly reduce searching costs (Noordewier et al., 1990). Bargaining costs are also reduced, with the enhanced mutual understanding and the narrowing of mutual cognitive differences. As for contracting costs, since a member from high context culture does not prefer detailed contracts (Hall, 1976), the costs involved are also lower.

However, when entering into a new environment or new market, members from high context culture are deprived of the strong links mentioned above. It will be difficult to rely on reputation or a middleman to search for business partners. Hence, higher costs are incurred in searching for partnership and more time is needed to understand the other party before deciding whether to build a long term trust relationship. This will also result in the increase of monitoring and enforcement costs. Besides this, unfamiliarity with each other, unsuitability of home country operating procedures and communication methods in the new environment, and confusion of the other party, will also widen misunderstandings, which results in a natural rise in bargaining cost. In the aspect of fixing contracts, it will be difficult to decide the level of details needed, thereby increasing the contracting costs.

### *2.3 Entry modes of multinational enterprise under different cultures*

From what is mentioned above, we know that multinational enterprises from high context culture will face relatively higher transaction costs when entering a host country; therefore they have to adopt an entry mode that will reduce transaction costs.

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Using equity structure as a basis, we can roughly divide the entry mode into two, using stock equity ratio from low to high: Joint Venture of different ratio (JV), and Foreign Direct Investment (FDI).

There are two viewpoints as of which mode of entry can decrease transaction costs; the first being the stock ratio is as low as possible, the second, the stock ratio is as high as possible (Anderson & Gatignon, 1986). Researchers who propose the former think that social cultural distance will cause uncertainty in the enterprise's internal control. Hence if the social cultural distance is wider, usually the degree of control by the multinational enterprise will be lower (Root, 1983). In such cases, allowing the subsidiary company to function according to the local culture and operating method will largely reduce the cost in training, communication and control.

Researchers suggesting high stock ratio will decrease transaction costs believe that multinational enterprise do not trust local management techniques and business partner, instead they prefer their own way of doing things. Hence they would want a higher stock ratio, so as to control the subsidiary company, and implement their operating method in the host country (Biven & Lovell, 1966). Richman and Copen (1972) also pointed out that the host countries have different expectations of the operating methods of foreign enterprises. Therefore, multinational enterprise can move away from the norm of the local environment and use a different system to operate.

Although the two above-mentioned viewpoints are contrasting, we may be able to integrate it if we make use of Hall's (1976) cultural model that probe into the cultural distinctions (not restricted to differences only) between the home and host country. In the following section, we will look at the framework of study and discuss various propositions based on the literature review in this section.

### **3. Conceptual Framework**

This study aims to look at the influence of culture on entry mode and network mobility. The framework will focus on the dyad relationship between the culture of the home and host country. This study does not employ the traditional cultural difference method, or just narrowly focusing on the amount of cultural differences. Instead, considerations are made on the possible different cultural combinations between the home and host country. A 2 x 2 model is set, and four combinations can be obtained. See table 1. Base on the four situations, we will further elaborate on the how they incurs transaction costs

and their influences on entry mode and network mobility.

**Table 1. Combinations of dyad relations between home and host countries**

		Home Country	
		High Context	Low Context
Host Country	High Context		
	Low Context		

#### 4. Analysis and Findings

##### *4.1 Multinational enterprise from high context culture entering host country with low context culture (High→Low)*

When a multinational enterprise from a high context culture enters a country with low context culture, it faces problems where it is hard to put down into words or rules its implicit knowledge, way of doing things and operating methodology. So if the entry mode chosen is a non-stock structure or low stock structure option, it will increase communication and education costs. Hence it is good to opt for an entry mode where stock ownership is higher, such as FDI. Also, for multinational enterprise from a high context culture, there will be the above-mentioned problem of communication costs when working with supplier from country with low context culture. This will create the tendency for the originally fixed home production network links to be moved overseas, instead of building new networks in the host country. In addition, as low cultural context countries do not have a lot of established traditions or unwritten rules, nor do they have plenty of human favors or human relationships issues to manage, this is also why multinational enterprise from high cultural context countries would prefer to bring their own people over, instead of cultivating links with the host country's business community or governmental organization.

##### *4.2 Multinational enterprise from high context culture entering host country with high context culture (High→High)*

Although both parties hail from countries with high cultural context, each party has its own set of rules and ways of doing things. Hence it is important for the multinational

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enterprise to familiarize itself with the norms and unwritten rules of the host country, and not neglecting cultivation of links and human relationships. As a result, in terms of ratio of stock ownership, it could be lower than the first case (high→low). As for partnership, it will be useful to search for someone with considerable connections, which will serve as a bridge to familiarize with the local customs. In terms of network mobility, high context culture country will still trust its own members, and at the same time believes that it is hard to master the implicit norms of the high cultural context host country. Therefore, when building local links, it will still cost more. With this in mind they will consider bringing over the trusted production network that is cultivated in the home country.

### *4.3 Multinational enterprise from low context culture entering host country with high context culture (Low→High)*

When a multinational enterprise from a low context culture enters into a country with high context culture, it may not be familiar with the implicit messages, or the norms and workings of the local culture. Be it manufacturing production or sales and marketing, there is a need to understand the above mentioned implicit norms, so when entering the host country, multinational enterprise will prefer a low stock structure, which is entering into joint venture with the local manufacturer. As for network mobility, shifts in relationships within country with low context culture are relatively flexible and based on actual benefits instead of relations. Also, actions can be regulated, explained and listed using written contracts, hence building good relationships with the manufacturer of the host country is of utmost importance. For this reason, multinational enterprise will not bring over its home network; instead they will cultivate new links in the host country. In the past, there isn't much research on the consideration of joint venture in solving the problems of multinational enterprise entering a high cultural context host country. But with the rise of East Asian economies, such discussions will become more and more important.

### *4.4 Multinational enterprise from low context culture entering host country with low context culture (Low→Low)*

As both parties communicate in a clear and definite manner, there is no need to increase the stock structure ratio to find a local business partner in order to understand local values and norms. As long as the multinational enterprise abides by the local laws and system, the transaction will proceed smoothly. Hence the multinational enterprise will prefer to enter via a high stock structure mode, which is using FDI. In the case of



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network mobility, multinational enterprise from low cultural context can obtain published information to understand the local system and information relating to the business partner. Relative to high context culture country, the network links of the low context culture country is not as strong, and home network of the multinational enterprise is more flexible. Therefore, when multinational enterprise conducts overseas investment, they will not bring over their home networks, but instead building new links in the host country.

Refer to Table 2 for the summary of the above findings:

**Table 2. Summary of findins**

Home Country→	Host Country	Preferred Entry Mode	Network Mobility
High→	Low	High Stock Structure/ FDI	Bring home network to host country
High→	High	Low Stock Structure/ Joint Venture	Bring home network to host country
Low→	Low	High Stock Structure/ FDI	Cultivate network in host country
Low→	High	Low Stock Structure/ Joint Venture	Cultivate network in host country

## 5. Conclusion

This study constructs a 2 x2 model and sheds a light on the impact of culture on the entry mode and network mobility. This study also helps to deepen our understanding about the importance of culture to International business. There are also several practical insights for the multinational enterprise. For multinational enterprise from high context culture, the better way to entering into a host country with low context culture is to employ a high stock structure option as its entry mode, for example FDI, and bring its home network links into the host country. Moreover, when multinational enterprise from high context culture enters a host country with high context culture, the better way is to employ low stock structure option, for example joint venture, and bring its home network links into the host country.

For multinational enterprise from low context culture, when entering into a high context

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country, employing low stock structure option, for example joint venture and cultivating links in the host country is the better way for survival. Furthermore, when a multinational enterprise from low context culture enters into a country also with low context culture, employing high stock structure option as its entry mode, for example FDI, and cultivating links in the host country is more beneficial.

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