

Levels of Internationalization of Multinational Spanish Firms: The Role of the Amount of Committed Equity and the Managerial Attitudes toward Foreignness

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Title

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Abstract

In this study, we investigate how the level of equity invested in foreign ventures and the orientation of the senior management team towards foreign cultures and international markets influence the degree of internationality of multinational Spanish firms. We postulate and empirically illustrate that a geocentric approach (based on a global mindset that remains perceptive to local differences) is associated with a higher level of internationalization. Conversely, modes of entry that imply a greater commitment relative to the equity investment made in the host country, such as the creation of wholly owned subsidiaries, are not necessarily related to the highest degree of internationality. In the current international scenario, the flexibility offered by the establishment of international alliances that imply a lower commitment of equity investment in the foreign country allows for the optimization of the investment made and a significant increase in the level of internationality.

Key words

Internationalization; multinational enterprises; manager attitudes; entry modes; centricity.

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Both the globalization of national economies and the growing internationalization of companies have become increasingly present over the last thirty years

1. Introduction

The attitude, perception or mentality that the chief executive or the top management team (hereafter, TMT) of a company has about foreign cultures and international markets has an important influence on the design of its internationalization strategy. These attitudes or visions “regarding foreignness” shape what in the management literature is known as “centricity.”

Centricity, in other words, the centric profiles/orientation of managers and companies, has been a well-studied concept in International Business (IB), following the pioneering works of Perlmutter (1969a; 1969b; 1969c). This American author classifies businesses into four groups, depending on the centricity of the company’s chief executive or TMT: ethnocentric, polycentric, regiocentric and geocentric companies (hereafter, referred to as the EPRG paradigm).

Both the globalization of national economies and the growing internationalization of companies have become increasingly present over the last thirty years. For the Spanish economy in particular, the severe economic crisis that began in 2008, with a significant drop in the domestic market, meant an additional push towards the internationalization of Spanish companies, which look abroad for new markets or to consolidate those already existing in other countries. In this sense, another relevant aspect in IB is in terms of the methods used by businesses to enter new international markets, given their consequences on performance and the success of the international operation. The different ways of entering the market are associated with a certain capital expenditure or commitment by the company, and accordingly, this capital investment will be larger or smaller in amount for the company, depending on the method selected (exporting, joint company, wholly owned subsidiary, etc.).

This work analyzes the extent to which the attitudes or mentalities of executives (the core members of the TMT) towards foreignness and the amount of capital expended in foreign operations can explain the degree of internationalization of Spanish companies.

The rest of the article is structured as follows: first is a brief review of the attitudes of executives towards foreignness and the main ways for entering new international markets, with the different capital investment needs that are associated with them. The following section briefly presents the database used, the variables and the statistical analysis carried out. The work concludes with a discussion of the results, the implications for executives and the final conclusions.

2. Attitudes of executives towards foreignness: the EPRG paradigm

By the *executive’s international orientation, centricity or centric profile*, we are referring to the dominant attitude the chief executive or the TMT has towards cultures and markets different than their own. This attitude can be ethnocentric, polycentric or geocentric. Calof and Beamish (1994) define centricity in a more detailed manner, as the set of beliefs that are held about the international markets and cultures other than one’s own, which have an influence on the different decisions made by a company, both strategic (the selection of ways of entering international markets) and operational (decisions related to production, marketing or human resources), that affect the performance of the company. The concept was introduced for the first time by Perlmutter (1969a; 1969b; 1969c), who initially applied it to develop a classification or typology of the North American companies that operated in international markets.

The geocentric orientation considers that there are global similarities between cultures and markets

Perlmutter states that the orientation, prevailing philosophy and attitudes of the TMT influence the type or method of internationalization ultimately chosen by the company. He classifies these executive orientations into three overall types of centricity, which in turn originate three types of international businesses: ethnocentric, polycentric and geocentric. Later, Perlmutter (1972) and Perlmutter and Heenan (1974) added a fourth form, the regiocentric company, leading to what eventually came to be known as the *EPRG concept or paradigm* (Schmid & Machulik, 2006; Isidor, Schwens & Kabst, 2011). These attitudes, which reflect the mentality of executives towards foreignness, are explained in simple terms below.

The ethnocentric mentality or attitude implies an orientation towards the country of the chief executive or the TMT. According to this orientation, the main decisions of the company are made at the company's multinational headquarters. The different foreign operations or subsidiaries lack their own autonomy. The TMT understands and interprets the foreign markets, other cultures and international business only through the lens of the values of its own country of origin. In this manner, decisions in the different areas of the company (human resources, finance, production and marketing) merely reflect the same policies and business practices of the country of origin and of the central headquarters. Therefore, according to an ethnocentric mentality, there is no local responsibility. Foreign employees and administrative practices are seen as "inferior" to the "national" ones or those found in the domestic market. For example, the key positions, in both the local and the foreign market, are assigned from the headquarters and to citizens of the same country as the parent company.

On the other hand, a polycentric attitude considers the subsidiaries as true independent entities, and they are given a high level of autonomy. The subsidiary is usually led by executives from the country in which it is located, who have few options to relocate to other subsidiaries or to form part of the administrative team at the headquarters (Roper, Brookes & Hampton, 1999). This mentality understands that the cultures of each country are different, so that each country is very different from the rest. Therefore, it is better for each foreign operation to be led by a citizen of that territory. This way, the different company policies tend to reflect the local practices of the country in which the subsidiary is located. Decisions tend to maximize local responsibility, implying that each country has its own strategy.

The regiocentric mentality is a variation of the polycentric, but with a regional scope (Europe, Latin American, Asia, etc.). Executives with regiocentric orientations recognize that there are similarities among the different countries that make up the same geographic region. This type of company performs its operations, integrates its activities and designs its policies on a regional level. Even the very structure of the company has a regional configuration. In each of the regions, the different international operations or subsidiaries are interconnected and governed by a regional center that acts autonomously and supports and directs the international subsidiaries in its region (Isidor et al., 2011).

Finally, the geocentric orientation considers that there are global similarities between cultures and markets. This mentality attempts to balance global practices with local ones, adopting policies that reflect and reconcile local differences and common global aspects. Best practices and global policies are adopted, but adapted to local conditions. The central headquarters and subsidiaries are integrated around the world and are highly interdependent on one another. For key administrative positions, both at the central headquarters and the subsidiaries, the most qualified executives are chosen, regardless of their nationality or country of origin (Isidor et al., 2011).

The EPRG paradigm has also been used to analyze the company's internationalization processes, according to its two theoretical extremes: the gradual or incremental processes and accelerated processes of internationalization

Perlmutter's EPRG paradigm has had a strong influence and has been used in different areas of the IB literature since it first appeared. In particular, it has been widely used in the area of international human resource management. In this field, there are many contributions that have studied the relationship between the focus when hiring personnel for the subsidiaries (ethnocentric or polycentric) and the performance of that international operation or subsidiary (Konopaske, Werner & Neupert, 2002; Gong, 2003; Colakoglu, Tarique & Caligiuri, 2009). The EPRG paradigm has also been used to analyze the company's internationalization processes, according to its two theoretical extremes: the gradual or incremental processes and accelerated processes of internationalization. In this manner, Isidor et al. (2011) study the possible relation between the EPRG paradigm and the incremental process of internationalization described by Johanson and Vahlne (1977): the gradual emergence of exports, joint ventures, sales subsidiaries, and finally, wholly owned subsidiaries. At the same time, other authors believe that the geocentric mentality of the TMT is a key element to explain the accelerated processes of internationalization that are typical in the born global firms (Harveston, Kedia & Davis, 2000; Knight & Cavusgil, 2004; Weerawardena, Mort, Liesch & Knight, 2007, among others).

Ultimately, Perlmutter's EPRG typology is based on the observation that companies behave differently when they operate abroad. Its organizational behavior, and therefore, the type of EPRG configuration finally created would basically depend on the centric mentalities, orientations or attitudes held by the TMT. It would be these attitudes of the main manager or the TMT that would most directly affect the final orientation of the company or its centric profile, and not other aspects outside the company, such as the characteristics of the environment or the industry.

In terms of centricity, our work intends to find out whether a certain centric attitude or mentality on the part of the chief executive or TMT is associated with a greater degree of internationalization of Spanish companies already operating abroad.

3. The main modes of entering foreign markets

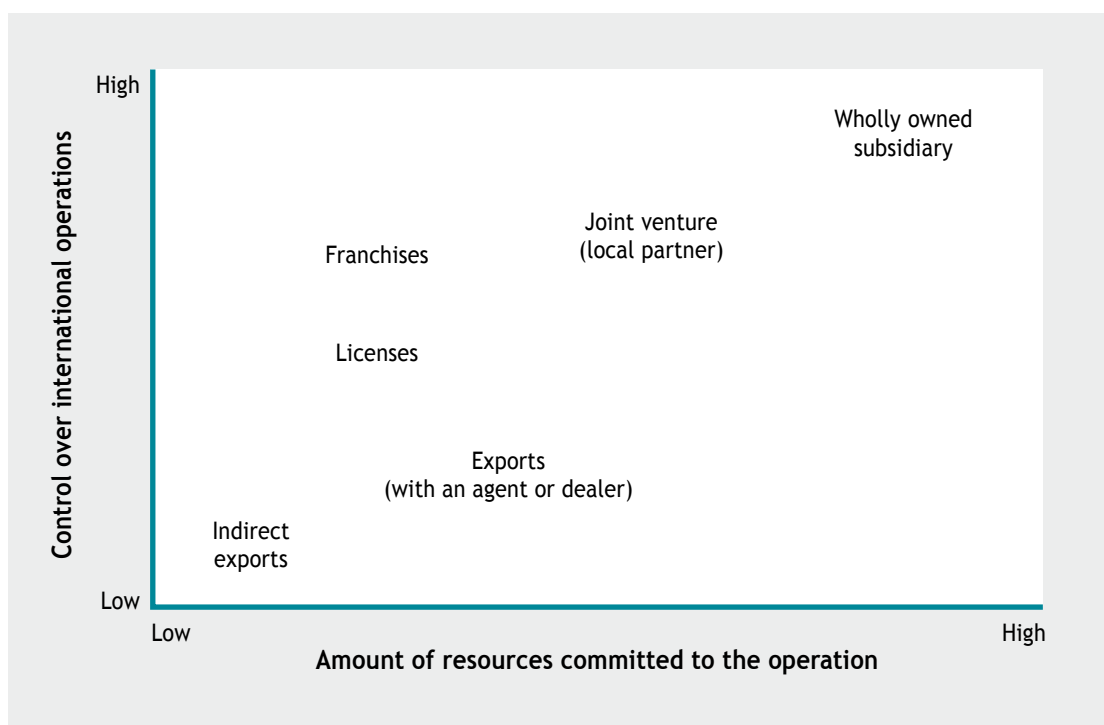
Following Sharma and Erramilli (2004), we can define the mode of entering a new market as the structural agreement that enables a company to implement a commercialization strategy for its products in a foreign country, either performing only commercialization operations (exports) or engaging in operations of both production and commercialization, by themselves or in association with other companies (contractual modes, joint companies or wholly owned subsidiaries). There are different modes of entering the market and different criteria for classification. Some modes may be contractual (dealers, franchises or licenses) or non-equity modes, while others might mean an investment of social capital or equity modes, a true extension of the company abroad: joint ventures, sales subsidiaries or production subsidiaries. The latter two modes may involve subsidiaries that are created in an ad hoc manner (green fields) or acquired through a merger or buyout process.

The selection of the most appropriate mode of entry into a new foreign market is a strategic decision of crucial importance to the company (Delios & Beamish, 2004; Tanganelli & Schaan, 2014). First of all, this is true because it has important implications for the company's performance. On the other hand, it will determine whether the company will have control and full ownership over the international operation. And furthermore, it is a decision with important long-term implications: once the entry mode has been established, it will be very costly to change it or make corrections to it, given the high costs implicit in a change.

In this work, we will focus on the three main modes most frequently used for entering foreign markets: exports, joint ventures and wholly owned subsidiaries (Brouthers & Hennart, 2007; Morschett, Schramm-Klein & Swoboda, 2010). Table 1 summarizes the main modes of entry, according to the level of capital investment required (high or low) and the level of control that they allow over international operations.

Table 1

Main modes of entry according to degree of control and capital commitment



Source: author's own work, adapted from Bartlett and Beamish (2013).

Of these three basic modes of entry, exports (EX) do not imply participating in the share capital (as it is a non-equity mode), but joint ventures (JV) and wholly owned subsidiaries (WOS) do represent a capital commitment (as they are equity modes). Furthermore, in this context of capital disbursement, JV imply a smaller capital investment than WOS, given that, by definition, JV have at least one partner.

With regard to the mode of entry, we will first analyze whether the company is increasing or decreasing its capital commitment (equity) in its international activity. This will be done by observing the changes between one mode of entry and another. It is thus understood that changing from EX to JV or from JV to WOS implies an increase in the capital committed to the foreign operation, while a change from WOS to JV, from WOS to EX or from JV to EX implies a decreased capital commitment in the international operations in which the company is involved. We will then go on to analyze how increases or decreases in the capital commitment to the previously observed international operations affect the degree of internationalization of Spanish companies.

The selection of the most appropriate mode of entry into a new foreign market is a strategic decision of crucial importance to the company

4. Sample, measurements and statistical analysis

4.1. Sample

The analysis was carried out on a database created from the results of a survey administered to Spanish multinational companies¹. The questionnaire was designed to obtain the centric or attitudinal profile of the chief executive (or TMT) towards foreign markets and cultures, the different modes of entry used and different information about the company, on both an internal and a contextual level. 250 Spanish multinational companies were selected based on the information from the directories of the Higher Council of Spanish Chambers of Commerce and the ACICSA that met the following requirements: they had been in existence for at least 25 years, have participated in at least one international operation other than exports during the last ten years and are relatively medium-sized (no more than 800 employees and an annual turnover of up to €600 million). The questionnaire was administered in 2012; the response rate was 24% and the final number of complete valid responses was 45. These 45 companies together made 99 changes in modes of entry between the years 2000 and 2010, with the mode of entry serving as the unit of analysis. Only 5 of the 45 companies have between 500 and 800 employees; the rest have less than 500. In each case, among other aspects, information was obtained on the age of the company and its years of international experience, the different modes of entry it has used and the year of each change, the centric orientation/attitude of the chief executive (or TMT), its sector, overall turnover and international billing.

4.2. Measurements

To measure the degree of internationalization, the variable we are seeking to explain, we used the percentage of international sales as compared to total sales that occurred in 2011. This index, which varies between 0% and 100%, is commonly accepted as an indicator of the degree of internationalization of a company. We call this variable “Internationality.”

In addition, different variables were designed to be able to determine the centric profiles of the chief executive or TMT, such as those corresponding to increases or decreases in capital commitment based on the three modes of entry analyzed (EX, JV and WOS). The variable “CapitalReduction” thus reflects the changes in the mode of entry that imply a reduction of the capital commitment with regard to the previous mode. Given the three modes of entry studied, this would correspond to the changes from WOS to JV, from WOS to EX or from JV to EX. The “ChangetoWOS” variable computes the changes in the modes of entry to WOS; therefore, these would be changes in modes of entry from EX to WOS or from JV to WOS. Likewise, the “ChangetoJV” variable reflects the changes in mode of entry to JV; i.e., from EX to JV or from WOS to JV.

The attitudes or mentalities of the chief executive or the TMT are reflected by the “Centricity” variable. This is an ordered categoric variable that is assigned a value of 1 if the attitude is ethnocentric, a value of 2 if it is polycentric or regiocentric and a value of 3 if it is a geocentric attitude or mentality. The score 1-2-3 is obtained from the questionnaire administered to the chief executive or TMT of each company. To obtain the type of attitude, the executive or TMT is asked to score the orientation or mentality taken in ten different types of business decisions, in such a way that the centricity is

¹ We understand “Spanish multinational companies” to mean those Spanish companies with headquarters in Spain that conduct operations in multiple countries.

assessed based on how it is reflected in the main business decisions made by the organization over a period of ten years. Based on these scores and using weighted averages, the centric profile of the company is obtained, which reflects its attitude to foreign markets and cultures. Table 2 shows the part of the survey on centricity or the attitude of the executive towards foreignness.

Table 2

Portion of the questionnaire on the attitudes of the chief executive

For the following areas indicated below, please indicate which of the four focuses your company followed and which focus you think it should follow. Write 1, 2, 3 or 4. Do not worry if your answers do not seem to be consistent in all areas.

1 = Spanish focus; 2 = local focus; 3 = regional focus; 4 = global focus*

Decisions	How decisions are currently made	How decisions should be made
Capital expenses	()	()
Prices	()	()
Dividend distribution policy	()	()
Product selection or design	()	()
Production planning and control	()	()
Quality control	()	()
Marketing and sales policies and programs	()	()
Purchasing and supplier selection	()	()
Finance and accounting procedures	()	()
Selection and promotion of executives for subsidiaries	()	()

Extract of the survey given.

* *Spanish focus* is understood to be an ethnocentric attitude; *local focus* is a polycentric attitude; *regional focus* is a *regiocentric attitude*; and *global focus* is a *geocentric attitude*.

Finally, different control variables are also introduced: the size of the company in terms of the number of employees ("Size"); the age of the company or the number of years since it was founded ("CompanyAge"); its international experience, operationalized based on the number of years in which the company has been present in the international market prior to 2011 ("InternationalEx"); the sector, distinguishing the manufacturing companies ("ManufacturingInd"); and the propensity to change the mode of entry into the foreign market, assessed by the total number of changes made by each company ("NumChanges"). Table 3 summarizes the descriptive statistics of the variables used.

Table 3
Descriptive statistics of the variables

Variable	Observ.	Mean	Standard dev.	Min.	Max.
Internationality	99	53.54	19.14	17.14	94.12
CapitalReduction	99	0.20	0.40	0.00	1.00
ChangetoWOS	99	0.33	0.47	0.00	1.00
ChangetoJV	99	0.12	0.33	0.00	1.00
Centricity	99	1.94	0.78	1.00	3.00
Size	99	288.58	197.43	85.00	800.00
InternationalExp	99	26.33	13.16	10.00	70.00
CompanyAge	99	61.63	29.90	21.00	131.00
ManufacturingInd	99	0.55	0.50	0.00	1.00
NumChanges	99	3.83	2.30	1.00	9.00

4.3. Statistical analysis

A multiple regression analysis was carried out using the OLS technique, or estimating the ordinary least squares, using robust standard errors that generate a more consistent estimate. This technique makes it possible to determine the influence of the independent variables described above on the independent variable, in our case, the internationality of the company. The coefficients of the independent variables will tell us, according to the sign, the increase or decrease in the propensity towards internationality as each of these variables changes. It is also demonstrated that there is no risk of multicollinearity among these variables. Table 4 shows the results obtained, which we comment on below.

Table 4
Summary of the statistical results

	Coefficients	S. e.
CapitalReduction	11.29*	4.71
ChangetoWOS	14.51***	3.57
ChangetoJV	10.48**	3.53
Centricity	3.94†	2.34
Size	-0.03***	0.01
InternationalEx	0.14	0.13
CompanyAge	-0.22***	0.05
ManufacturingInd	12.54**	4.55
NumChanges	-1.96*	0.83
Constant	56.7***	10.07
NumberObservations	99	
R squared	0.46	
F-value (9.89)	16.94	
Prob> F	0.00	

† $p < .10$

* $p < .05$

** $p < .01$

*** $p < .001$

The fact that the size is increasingly less important in explaining greater processes of internationality is consistent with recent processes of rapid globalization in many small companies (born global firms)

5. Discussion of the results

The first three variables enable us to analyze how an increase or decrease in capital commitment in the changes in mode of entry used by the company affects its internationality. If we consider the three basic modes (EX, JV and WOS) as three values (0, 1 and 2, respectively), changes from 2 to 1, from 2 to 0 and from 1 to 0 would mean changes to modes of entry that imply a reduction of capital, while changes from 0 to 1, from 0 to 2 and from 1 to 2 would be changes to a new mode of entry that implies an increase in the capital commitment to the international operation. Analyzing the first three variables, we can conclude the following:

The coefficient of the “CapitalReduction” variable, which measures the reduction of the capital committed in the new mode of entry used, is both positive and statistically significant, so we can state that a mode of entry that implies a lower investment of capital positively affects the level of internationality. The “ChangetoJV” variable reflects a change from EX to JV or from WOS to JV and is associated with a positive and significant coefficient with a value of 10.4. Accordingly, a change from EX to JV is associated with greater internationality by the company, as occurs with a change from WOS to JV. On the other hand, the “ChangetoWOS” variable which would reflect a change from EX to WOS or from JV to WOS, is also positive and statistically significant.

If we consider altogether all the coefficients related to reductions of capital, some interesting results are observed. The reduction in capital represented by changing to joint ventures (changing from WOS to JV) implies adding the coefficients 11.3 from “CapitalReduction” and 10.4 from “ChangetoJV”, thus affecting the propensity towards internationality of the company by more than twenty percentage points (21.7). In addition, the reductions in capital in favor of exports (changing from WOS to EX or from JV to EX) are associated with a positive change of 11.3 percentage points in the propensity towards an increase in internationality. This allows us to conclude that if the capital is reduced, the most significant increase in the propensity towards internalization is obtained by changing from wholly owned subsidiaries to joint ventures.

Furthermore, with the “Centricity” variable we measure the attitude towards new markets and foreign cultures held by the chief executive or TMT. Accordingly, the higher the value, the more geocentric the attitude is. We see that it has a positive and statistically significant coefficient, so it can be stated that the greatest levels of geocentrism are associated with higher levels of internationality.

The values associated with the size of the company (“Size”) have a significant negative coefficient. This indicates that a smaller size would be associated with greater internationality, contradicting the logic that larger company size generally facilitates greater international expansion, by having more resources to bear the costs of internationalization. Two observations can be made. The first is that the coefficient, in spite of being negative, has a very low value that is practically negligible (−0.03), and thus the clearest interpretation would be to say that size does not matter in terms of a greater or lesser propensity towards internationality. This leads us to our second comment: the fact that the size is increasingly less important in explaining greater processes of internationality is consistent with recent processes of rapid globalization in many small companies (born global firms). New information and communication technologies, as well as the reduction of transport costs, among other factors, facilitate the internationalizing activity of small companies. Along the same lines, we frame the results for the “InternationalEx” variable, which measures the prior

Experience carries an increasingly lower weight, as does the age of the company, to explain greater internationality of the company

experience a company has in international operations. It provides a result that is not significant, and thus we can conclude that international experience is not associated with greater internationality. Experience carries an increasingly lower weight, as does the age of the company (reflected in the “CompanyAge” variable), to explain greater internationality of the company. The age of the company presents a significant negative coefficient, although with a very low value (0.14), indicating that younger companies tend to be more likely to internationalize, according to the born global firm theory. Finally, when taking into account the industry, we see that manufacturing companies on average are associated with higher internationality values. This result is logical, given that many services are consumed locally, near the place where they are provided, and are therefore associated with more local than international markets. We also control the propensity towards change of mode (number of changes) through the “NumChanges” variable in order to separate the effect of an individual change from the fact that a company is more or less accustomed to changing its method of operation abroad. The negative value of the coefficient and its significance enables us to conclude that companies which change their foreign investment strategy many times are not those that obtain the highest degree of internationality.

6. Managerial implications and conclusions

The present study reveals some important implications for executives in Spanish companies. First of all, the modes of entry into international markets that mean a reduction in the commitment of capital invested abroad are associated with greater internationality. On the current international scene, strong capital investments in international operations are not associated with the highest levels of internationality. Therefore, the formation of international alliances, which permit smaller capital investments, seem to be the best strategy to foster a high level of internationality, by making it possible to act in multiple markets with less direct investment than with wholly owned subsidiaries.

Specifically, the change from WOS to JV represents a strategy that ensures better results in terms of obtaining greater internationality of a company. The role of international alliances is thus key to strengthening and nurturing high levels of internationality, beyond establishing wholly owned subsidiaries. Our analysis indicates, therefore, that executives (or the TMT) should consider the use of international alliances with local partners as a very plausible option for entering international markets.

Furthermore, we can emphasize the role of size and previous experience with internationalization. Our study shows that the size of the company and the time it has been operating in international markets are not relevant factors to explain greater internationality. This reinforces in part the conclusion that it is not necessary to have a lot of resources, capital or human, to obtain a high degree of internationalization. The changes that have occurred in the area of new information and communication technologies as well as lower transport and transaction costs, can help explain these results. Obtaining a high level of internationality is no longer a prerogative linked essentially to large companies, and multinational companies today do not necessarily need to be linked to a large company.

Finally, we can indicate the importance for executives (or the TMT) to have the right attitude in terms of facilitating international success. Our study highlights the importance of the right attitude on the part of executives towards international business as a decisive factor to increase the internationality of their companies. A geocentric attitude/mentality is associated with greater levels of internationality. Each executive has his or her own attitude (mentality of centric profile) with regard to foreign cultures and markets. A

The change from WOS to JV represents a strategy that ensures better results in terms of obtaining greater internationality of a company

geocentric attitude considers that there are global similarities in terms of both cultures and markets. This attitude does not assume that either domestic (from the same country as the headquarters of the company engaging in internationalization) or local (from the new international market) practices or policies are any better or worse. This mentality is based on using those policies (in production, commercialization, finance, human resources, etc.) that manage to balance local and global practices: using the right policies and practices, regardless of the country or culture they come from. The geocentric mentality makes decisions that contemplate local responsibility and positive aspects of global coordination.

In conclusion, our work proposes a global international strategy for the international expansion of a company based on two pillars: maintaining an open mind towards foreign markets and cultures, and at the same time, limiting capital investment abroad through the use of international alliances as an ideal mechanism for achieving greater international expansion.

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