South African MNEs Entry Strategies in Africa

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Abstract—This is a cross-cultural study that determines South African multinational enterprises (MNEs) entry strategies as they invest in Africa. An integrated theoretical framework comprising the transaction cost theory, Uppsala model, eclectic paradigm and the distance framework was adopted. A sample of 40 South African MNEs with 415 existing FDI entries in Africa was drawn. Using an ordered logistic regression model, the impact of culture on the choice of degree of control by South African MNEs in Africa was determined. Cultural distance was one of significant factors that influenced South African MNEs' choice of degree of control. Furthermore, South African MNEs are risk averse in all countries in Africa but minimize the risks differently across sectors. Service sectors chooses to own their subsidiaries 100% and avoid dealing with the locals while manufacturing, resources and construction choose to have a local partner to share the risk.

Keywords—Cross-cultural, emerging MNEs, entry strategies, internationalization.

I. INTRODUCTION

THE internationalisation path of MNEs from developed countries is well researched with theories such as the Uppsala and Eclectic paradigm developed as a result. However, little is known about strategies employed by emerging MNEs (EMNEs). According to UNCTAD [1], South African outward foreign direct investment (OFDI) into Africa was the highest among major developing economies in Africa, amounting to US$2.6 billion between 2006 and 2008.

The current study explores the internationalisation path and strategies followed by the South African MNEs in Africa in an attempt to close an existing gap in literature and provide some insights on intra-regional FDI dynamics amongst developing countries. In this regard, the study seeks to answer the following questions: Do South African MNEs follow a similar path adopted by other emerging MNEs as they internationalise? What firm specific variables are more pertinent for South African MNEs? Does culture play any role in determining the level of control that South African MNEs prefer in Africa?

II. LITERATURE REVIEW

A. Theoretical Literature Review

Several internationalisation theories explain why firms choose to internationalise. The transaction cost theory explains the existence of the firm. According to Coase [2] firms exist to avoid the costs of market transactions. Williamson [3] extended the theory and included avoiding

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opportunistic behaviour as one of the reasons for firms' existence while Cheung [4] added institutional costs. Also known as the OLI model, the eclectic paradigm is an extension of the transaction cost theory and was developed by Dunning [5]. The model argues that, for FDI to occur, an MNE must possess firm specific or ownership advantages (FSAs) such as trademarks, economies of scale, and technology amongst other things. The Scandinavian Model or Uppsala School explains how firms carry out their internationalisation process. Johanson and Wiedersheim-Paul [6] identified four stages of the internationalising firm as exports, licensing, joint venture (JV) and finally a wholly-owned subsidiary (WOS). Johanson and Vahlne [7] added that firms will start with markets with shorter psychic or cultural distance and then later on venture into culturally distant markets. Finally, the CAGE Distance Framework argues that even in the face of extensive globalisation, distance still matters. According to Ghemawat [8] distance between two countries can manifest itself along four major dimensions: cultural, administrative, geographic and economic distance (CAGE distance framework). The cultural distance (CD), which is the most overlooked by MNEs, can have an impact on how the firms' presence and products or services are accepted by the local market. Such differences will include religious beliefs, attitude towards time, relationship with the environment, social norms and language amongst others.

B. Empirical Literature Review

Empirical literature on FDI from developed countries is relatively abundant and covers all aspects of the FDI from choice of location, entry mode and degree of control to post investment performance as well as internationalisation strategies of MNEs. Li [9] analysed the internationalisation strategies of 180 services MNEs from US, Japan and the EU into the Asia-Pacific region between 1980 and 1986 and found no difference between the strategies employed by service and manufacturing firms located in the Pacific region. Barkema et al [10] found that the Uppsala model was preferred by the Dutch firms. However, the Spanish service MNEs preferred to frog-jump and entered through mergers and acquisitions (Alavarez-Gil et al [11]).

Similarly, cultural distance influenced MNEs from developed countries differently. Li [9] found that MNEs from US, EU and Japan preferred markets with a shorter CD from their home country. Cultural distance in Greece was found positively related to FDI performance (Kessapidou and Varsakelis [12]) in line with Morosini et al [13] findings for Italian MNEs. According to Quer et al [14] greater cultural distance reduced the likelihood of using higher commitment entry strategies (within that growing sequence: contractual

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agreement, shared-ownership FDI, full-ownership FDI) for the Spanish firms.

It has been established that emerging MNEs are increasingly becoming significant players in FDI (UNCTAD [1]). Emerging MNEs share some common features, that is, distance still matters. The distance framework by Ghemawat [8] is an important theoretical underpinning of the internationalisation strategies of EMNEs (Malhotra et al [15]; Sethi [16]). Also, the Uppsala model is not relevant of EMNEs as far as mode of entry is concerned as they tend to frog-jump into FDI (JVs or WOS) as was found to be the case for EMNEs from BRIC (Sethi [16]), and Turkey (Demirbag et al [17]). However, the Uppsala model is relevant for EMNEs in terms of location as FDI from EMNEs tend to be regional or bi-regional.

The impact of cultural distance is mixed. Lee et al [18] found that cultural distance was not a significant factor in determining the degree of control for Korean firms but found cultural distance to be significant for inward investment than outward investment. In the same vein, Malhotra et al [15] found that cultural distance has a significant, negative impact on the number of cross-border acquisitions (CBAs) by MNEs from developing countries. None of the studies examined here found country risk to be a significant factor on FDI from developing countries. Instead, Malhotra et al [15] found that market potential of the target country significantly moderates the relationship between the distance factors and the number of CBAs from developing countries.

The South African MNEs in Africa presents a mixture of success and failure as far as cultural considerations of the host country are concerned. In some cases they show sensitivities to the local culture and in other cases they are completely ignorant. Wöcke et al [19] examined the human resource (HR) strategies employed by four South African MNEs when dealing with the integration-differentiation dilemma and found that the four MNEs (telecommunication, fast food franchise, brewery MNE, and petro-chemical MNEs) differ largely in terms of recognizing the need to accommodate national culture in their HR practices. The finding was supported by Gomes et al [20] who found that a South African telecommunication MNE in the Democratic Republic of Congo (DRC) was completely ignorant of the local culture while Newenham-Kahindi [21] found that a South African Bank in Tanzania was more sensitive to the local culture.

C. Developing Hypothesis

1. Cultural Distance

Given that South Africans in general have a problem of trusting individuals from a culture different from their own (Finestone and Snyman [22]), the following hypothesis is made:

Hypothesis 1 : the probability of South African MNEs preferring WOS over any other form of control will be higher in all African countries.

2. Geographic Distance

Relatively speaking, since South Africa is geographically closer to the rest of Africa, the following hypothesis is made:

Hypothesis 2 : Geographic distance will only be significant relative to cultural distance. South African MNEs will prefer countries that are culturally close even if they are geographically far than those that are geographically close but culturally far.

3. Firm Specific Advantages

For South Africa, firms entered the global arena since 1992 following the end of apartheid, which meant that they had a lot of catching up to do with MNEs from both developing and developed countries. The following hypothesis in this regard is made:

Hypothesis 3a : Firm size will have a significant impact on the choice of Degree of Control with a high preference for WOS over JVs.

Hypothesis 3b : Type of industry, manufacturing versus services, and sub-sectors within services will determine the firm's preference for WOS or contract.

Hypothesis 3c : Firm experience will have an insignificant impact on the choice of Degree of Control.

4. Investment Potential

Malhotra et al [15] used market potential to moderate the impact of distance factors on market selection for FDI. FDI theory proposes that firms invest in foreign markets if the expected benefits, mostly through market size, from these investments will exceed the costs incurred in overcoming the difficulties related to entering new markets (Vernon [23]). Empirical evidence was provided by Ellis [24] who used both primary and secondary data to investigate the impact of market size on Chinese firms' entry into new markets. Therefore the following two hypotheses are made:

Hypothesis 4 : A higher investment potential of a country may results in South African MNEs considering other forms of control such as JVs.

Hypothesis 5 : A higher investment potential may increase the probability of South African MNEs locating in culturally and geographically distant market.

D. Methodology

1. Selecting the Theoretical Framework

The study will adopt an integrated approach that combines several frameworks as the basis of the study. These will include the transaction cost, the Uppsala model, the eclectic paradigm and the CAGE distance framework, all of which were discussed in detail in the literature review chapter.

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2. Selecting the Model: The Ordered Logistic Regression Model

The study of entry mode choice by Spanish firms is closely related to the current study with respect to the variables used. As a result, this study will use an ordered logistic regression model similar to Quer et al [14].

3. Theoretical Underpinning

Ordered Logistic Regression (OLR), is a statistical technique that can sometimes be used with an ordered (from low to high) dependent variable. The model has its origins in bio-statistics (Aitchison and Silvey, [25]) but was brought into the social sciences by two political scientists (McKelvey and Zavoina [26]). It is used in cases where the dependent variables are ordinal, but are not continuous in the sense that the metric used to code the variables is substantively meaningful.

III. THE DEPENDANT VARIABLE: DEGREE OF CONTROL

The ordered logistic regression model will be used in this study with Degree of Control as the dependent variable with three possible outcomes: wholly owned (WOS) taking the value of 1; joint venture (JV) taking the value of 2; and license taking the value of 3. Quer et al [14] followed a similar approach and used degree of commitment as the dependent variable. The variable was also split into three likely outcomes although they ranked from lowest (1) to highest (3) commitment, which is the opposite in this study where 1 represents that highest commitment.

IV. THE INDEPENDENT VARIABLES

A total of 7 independent variables will be used, which are a mix of continuous and dichotomous variables.

A. Cultural Distance

This study will use the Kogut and Singh formula to calculate a CD score from South Africa obtained using Hofstede's and GLOBE's cultural dimensions. Other similar studies have done likewise (Kogut and Singh [27]; Barkema et al [10]; Kessapidou and Varsakelis [12]; and Malhotra et al [15]). Quer et al [14] created three dichotomous variables (Europe, Latin America and Rest of the World) to measure the cultural distance between Spain and the rest of the world.

B. Location

Although location is included in the model as an independent variable designed to capture country-specific characteristics, it is also closely related to Quer et al [14] variable that measured cultural distance. In this study, location is a four dichotomous variable (Anglophone, Francophone, Lusophone, and Arabophone).

C. Geographic Distance

Other studies that included geographic distance as an independent variable have expressed it as a logarithm of the actual distance in kilometres between the major cities of the acquiring and the target country (Buckley et al [28]; Ojala and Tyrvainen [29]; and Malhotra et al [15]). In this study, however, geographic distance will be expressed as the direct flight time (in minutes) between Johannesburg and the main airports in the relevant target countries as estimated by the Travel Distance Calculator.

D. Industry

Similar to Quer et al [14] who created five dichotomous variables to capture the effect of different sectors on the choice of mode of entry, five dichotomous variables were also created (Services, Manufacturing, Retail, Resource and Construction) as necessitated by the sample composition.

E. Firm Size

Most studies have included firm size as an independent variable; however they differed in how they expressed the variable. Kogut and Singh [27] expressed firm size by the asset size of the foreign firm while later Kessapidou and Varsakelis [12] used two variables to capture firm size: logarithm of the number of employees and logarithm of the capital owned by the foreign subsidiary. Quer et al [14] used sales volumes to measure firm size. Demirbag et al [17] on the other hand used number of employees in an ordinal form including 7 categories. This study will use the actual number of employees as a measure for firm size.

F. Firm Experience

Firm experience has been included by many studies as an independent variable but expressed differently. Kogut and Singh [27] expressed the variable as the actual number of countries that a firm has foreign operations while Barkema et al [10] expressed it as a logarithm of all foreign expansions that the firm had undertaken. Kessapidou and Varsakelis [12] expressed it as the number of years a firm had operated in Greece (the target country). This study will express firm experience as the number of continents that a company has FDI operations.

G. The Moderating Variable

Demirbag et al [17] included country risk as measured by the Corruption Perception Index as a moderating variable in their study while Malhotra et al [15] used market potential as measured by the GDP of the target country similar to previous studies (Davidson [30]; Terpstra and Yu [31]; and Mitra and Golder, [32]). Earlier, Quer et al [14] used country risk as a moderating variable and measured it by the risk ratings provided by the Spanish Export Credit Insurance Company. This study will also include a moderating variable, investment potential of the target country, as measured by the Investment Potential Index of 2006 (latest available).

Table I summarizes the expected signs between the dependant variable and the independent variables

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TABLE I
SUMMARY OF EXPECTED SIGNS

Independent Variable	Expected Results
Cultural Distance	Significant (-)
Geographic Distance	Insignificant (-)
Firm Size	Significant (-)
Firm Experience	Significant (-)
Investment Potential	Significant (+)
Industry	
– **Services**	Significant (-)
– **Manufacturing**	Significant (-)
– **Retail**	Significant (-)
– **Resource**	Significant (-)
– **Construction**	Significant (+)
Location	
– **Anglophone**	Significant (+)
– **Francophone**	Significant (-)
– **Lusophone**	Significant (-)
– **Arabophone**	Significant (-)
	Significant (-)

V. SAMPLE AND DATA

A sample of 40 South African MNEs was drawn from a list of foreign companies abroad compiled by the Departments of Trade and Industry (the **dti**) and International Relations and Cooperation (DIRCO) as well as Business Unity South Africa (BUSA). The criteria used for selection was for any South African company that had current FDI transactions (10% and more) in at least 3 or more African countries. For retail and services companies, FDI in a country was counted once as opposed to the number of stores or braches in a given country. The 40 companies together possess 415 FDI entries in Africa that will be used as observations for the regression analysis.

A South African company is defined as any company originating and incorporated in South Africa with a listing in the Johannesburg Stock Exchange. In this regard, a foreign subsidiary incorporated in South Africa was excluded while South African companies listed elsewhere in the world in addition to Johannesburg were included. Finally, only holding companies as opposed to individual enterprises were included.

Data about firm characteristics such age, number of foreign operations, number of employees and so on were obtained from latest annual reports downloaded from companies' websites between December 2010 and January 2011.

VI. RESULTS AND ANALYSIS

A. Descriptive Results

1. Industry

The independent variable industry was divided into five sectors. The sectoral composition of the sample is given by Fig 1. According to the figure, more than half of the sample of South African MNEs currently investing in Africa comes from the services sector (61% for services and retail combined) with manufacturing as the next biggest sector at 18%. Only 13% are in resources while 8% comes from construction.
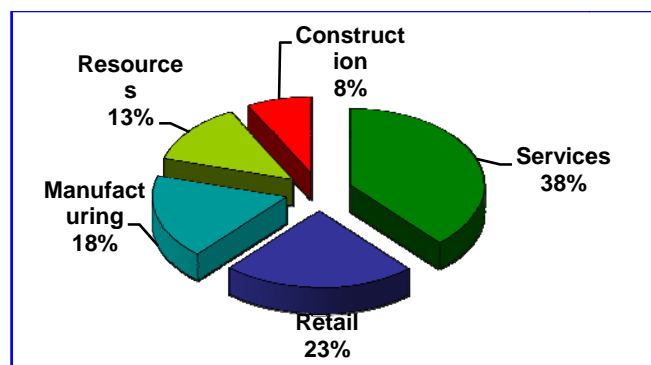

Fig. 1 Sectoral Breakdown of the Sample

B. Firm Variables: Age, Size and Experience

The variables relating to firm specific advantages was made up of firm size, age and experience. Firm size was measured by number of employees; firm age was given by the number of years a firm has been in operation; and firm experience was given by the geographic spread (number of continents that a firm has FDI operations). Table II gives a summary of the three variables.

TABLE II
SUMMARY OF FIRM VARIABLES

Variable	Obs.	Mean	Std. Dev.	Min	Max
Firm age	416	72.63462	40.50859	9	172
Firm exp	416	3.65625	1.96833	1	6
Firm size	416	27815.09	23393.11	100	75000

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C. Regression Results

TABLE III
ORDERED LOGISTIC RESULTS GLOBE PRACTICE

Dependent Variable: Degree of Control	Coefficient	Standard Error	Z Value	P>|z|	95% Conf.	Interval
Services	-.8221677	.2468014	-3.33	0.001***	-1.30589	-.3384459
manufacturing	-.30119	.2930738	-1.03	0.304	-.8756041	.2732241
Retail	-1.497766	.3417046	-4.38	0.000***	-2.167495	-.8280375
Firm Experience	-.2244302	.0549653	-4.08	0.000***	-.3321603	-.1167001
GLOBEP	1.414748	.8156908	1.73	0.083***	-.1839769	3.013472
Investment potential	.0042356	.0020459	2.07	0.038***	.0002257	.0082456

LR Chi2(6) = 39.75 Log Likelihood = -434.53939   Prob. > Chi2 = 0.0000
No of observations = 415   Pseudo R2 = 0.0437

Results are presented in both correlations and regression analysis. The correlation table looked at the relationship between the dependant variable (degree of control) with all independent variables using one of the four sets of data (GLOBE practice) since they are all similar. Significant correlations were observed on the following variables: francophone, services, construction and firm experience, all at 1% significant level. All but construction are negatively correlated with degree of control.

Geographic distance was not significantly correlated to degree of control but had a negative sign, which implies that the further away a country is from South Africa, South African MNEs will prefer wholly owned subsidiaries as opposed to joint ventures or contract. Furthermore, geographic distance was positively correlated to cultural distance but not significantly. Hypothesis 2 (*Hypothesis 2: Geographic distance will only be significant relative to cultural distance. South African MNEs will prefer countries that are culturally close even if they are geographically far than those that are geographically close but culturally far*) is partly confirmed by the correlation results.

The correlation results for the location variable should be interpreted to mean that South African firms have a strong preference for the highest level of commitment (wholly owned) when they invest in a Francophone country compared to an Anglophone, Lusophone or Arabophone, but only Francophone is significant. However, this result confirms hypothesis 1b (*Hypothesis 1b: the probability of South African MNEs preferring WOS over any other form of control will be higher in all African countries*).

The variable 'firm size' was the least correlated and the results cannot validate hypothesis 3a (*Hypothesis 3a: Firm size will have a significant impact on the choice of Degree of Control with a high preference for WOS over JVs*). However, the positive sign implies that larger firms prefer wholly-owned subsidiaries over contracts or joint ventures. The fact that almost all firms were relatively large (more than 10 000 employees) may have rendered this variable redundant.

The variable 'industry' was significant for two of the five sectors, which are construction and services. The South African construction, manufacturing and resources firms strongly prefer contracts followed by joint ventures when they go into Africa while the services and retail firms strongly prefer wholly owned subsidiaries when they invest in Africa.

This is consistent with high risk aversion for all sectors but they adopt different risk minimization strategies. For the construction, manufacturing and resources firms, risk is minimized by bringing local partners into the transaction mostly because the investment requires a lot of capital on the ground and is more vulnerable to expropriation. The services and retail firms on the other hand minimize risks by full control and avoid post-merger challenges of cultural assimilation. Hypothesis 3b (*Hypothesis 3b: Type of industry, manufacturing versus services, and sub-sectors within services will determine the firm's preference for WOS or contract*) is affirmed.

The variable 'firm experience' turned out to be very significant. The result should be interpreted to mean that South African firms that are in more than one continent strongly prefers wholly owned subsidiaries when they invest in Africa compared to firms that are still regional or bi-regional. The result for this variable did not validate hypothesis 3c (*Hypothesis 3c: Firm experience will have an insignificant impact on the Choice of Degree of Control*).

Investment potential is not significantly correlated with either degree of control or cultural distance; however, it is

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significantly correlated with geographic distance with a negative sign. The two hypotheses relating to investment potential cannot be confirmed by the correlation results.

Hypothesis 4 : A higher investment potential of a country may results in South African MNEs considering other forms of control Such as JVs.

Hypothesis 5 : A higher investment potential may increase the probability of South African MNEs locating in culturally and geographically distant market.

In terms of regression results given by Table III, the GLOBE cultural dimensions by House et al [33] proved more relevant for South Africa than the Hofstede dimensions for both the 1980 [34] and 2006 [35] scores as replicated by Oshlyansky et al [36]. Using the GLOBE value CD scores, four out of six variables were significant at 95% confidence level, namely, services, retail, firm experience and cultural distance. Only investment potential and manufacturing were not significant. For the GLOBE practice CD scores, the same four variables were significant with investment potential also significant. Only manufacturing was not significant.

According to GLOBE regression results, cultural distance is a significant factor that determines the location of South African FDI in Africa. The more culturally distant a country is from South Africa, the probability of South African MNEs choosing WOS is high. This result is similar to the correlation outcome even though it was not significant.

Investment potential was also significant on GLOBE practice and positive, implying that the probability of South African firms choosing lower forms of control such as contract and joint venture increased in countries that have higher investment potential than otherwise. Investment potential plays a moderating role in this regard and validates hypothesis 4 and 5 above, which could not be affirmed by correlation results. The other three variables were significant and negative for the regression results using all four data sets; GLOBE practice, GLOBE value, Hofstede [34] and Oshlyansky [36]. In terms of this, the probability of South African MNEs in services and retail choosing WOS is higher than joint ventures or contract while more experienced firms will most probably choose WOS over joint ventures and licensing.

VII. CONCLUSION

South African MNEs, on the other hand, are neither similar to other emerging MNEs nor MNEs from developed countries. In terms of geographic spread, save for India, EMNEs are mostly regional or biregional; South African MNEs by contrast are relatively distributed across the six continents. The Uppsala model, which applies to most developed MNEs do not apply to South African MNEs as they tend to frog jump into FDI and choose the highest form of control, wholly-owned (WOS) the first time and most of the time. Furthermore, South African MNEs are risk averse in all countries in Africa but minimize the risks differently across sectors. Service sectors chooses to own their subsidiaries

100% and avoid dealing with the locals while manufacturing, resources and construction choose to have a local partner to share the risk. South African MNEs can improve their geographic and cultural spread in Africa into areas other than Anglophones by increasing their willingness to understand other cultures different from their own; the domestic market is good practice ground for that. A willingness to consider joint ventures with local partners in Africa will go a long way in this regardA conclusion section is not required. Although a conclusion may review the main points of the paper, do not replicate the abstract as the conclusion. A conclusion might elaborate on the importance of the work or suggest applications and extensions.

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