Foreign Direct Investment Decision-Making Processes of Swiss Small and Medium Enterprises in China

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Christian-Otto Schmidli

from

Neuenkirch (Lucerne)

Approved on the application of

Prof. Dr. Li Choy Chong

and

Prof. Dr. Kuno Schedler

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Executive Summary

This dissertation explores foreign direct investment [FDI] decision-making processes of Swiss small and medium sized enterprises [SME] in the uncertain and foreign context of China. Unlike multinational enterprises [MNE], SMEs are smaller and often do not have sufficient resources to fully investigate a major FDI decision. If learning to gain contextual competence is necessary for successful FDI decision-making, how do these firms manage their learning and competencies to invest successfully in China? The main objective of this dissertation addresses the decision-making processes of SMEs for their FDI, how this takes place and how needed competencies are developed and managed.

Two main research questions, addressing areas of managerial interest, are investigated in-depth for China, namely: What is the decision-making process for foreign direct investment by SMEs? How do owners-managers of SMEs make such decisions? A multiple case study approach, based on eight cases studies with in-depth interviews, shows the decision-making process for foreign direct investment develops in phases. The findings support a decision-making model that proposes the decision process is divided into phases. These phases are of differing lengths and depths, largely depending on the type of management, and the decision-making speed can vary greatly between individual companies. The results indicate a distinction between SMEs managed directly by owners-managers and those managed by a board.

The findings show current foreign direct investment and decision-making theory is at a watershed. Previously well-established theories are challenged as emerging markets, such as China, require different approaches and market-entry must be considered as a developmental process, which is individual to a company. Overall the decision-making type can also vary within the same company and among decision-makers. Knowledge available builds, and influences, competencies and results in decision-making based on rationality or experience.

Key Words: Decision-Making, FDI, SME, China, Market-entry.

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Contents

Exhibits

Abbreviations

ABB	Asean Brown Boveri
AD	Anno Domini – of the Christian era
AG	Aktien Gesellschaft
ASEAN	Association of South-East Asian Nations
ASICO	Asia and Consulting
BtoB	Business to Business
BVI	British Virgin Island
CAFTA	China ASEAN Free Trade Agreement
CEO	Chief Executive Officer
CH	Switzerland
CHF	Swiss Franc
CN	China
DEZA	Direktion für Entwicklung und Zusammenarbeit
ENSR	European Network for SME Research
EU	European Union
FDI	Foreign Direct Investment
FPEI	Foreign Portfolio Equity Investment
FTA	Free Trade Agreement
GDP	Gross Domestic Product
GM	General Manager
HRM	Human Resource Management
IFC	International Finance Corporation
IMF	International Monetary Fund
IMS	International Market Selection
IP	Intellectual Property
IPR	Intellectual Property Rights

JV	Joint Venture
MAN	Maschinenfabrik Augsburg Nürnberg
MNE	Multinational Enterprise
MofCom	Ministry of Commerce
NZZ	Neue Zürcher Zeitung
OC	Organisational Capability
OECD	Organisation for Economic Co-operation and Development
Osec	Business Network Switzerland
OLI	Ownership, Location, Internalisation
PRC	People's Republic of China
R&D	Research and Development
RO	Representative Office
SCCC	Swiss Chinese Chamber of Commerce
SCS	Swiss China Survey
SECO	State Secretariat for Economic Affairs
SME	Small and Medium-Sized Enterprise
SSM	Schaerer Schweiter Mettler AG
TC	Tungsten Carbide
UNCTAD	United Nations Conference on Trade and Development
US$	United States Dollar
VAT	Value Added Tax
WTO	World Trade Organisation
WFOE	Wholly Foreign Owned Enterprise [subsidiary in which the investing company holds 100% ownership]

To my Family

LeNhi,
Celine-Bohai and Titus-Shanghai

Foreign Direct Investment Decision-Making Processes of Swiss Small and Medium Enterprises in China

SECTION 1

Chapter One ~ Introduction

1.1 Research Problem and Motivation

The globalisation of markets is taking place and business is increasingly becoming international. Organisations are faced with the influence of global markets, whether or not they sell or produce internationally. Emerging markets, such as China, have a considerable role in this change of environment and the Chinese mainland is expected to become the locomotive of the world economy.[1] China attracted US$ 70 billion foreign direct investment [FDI] in 2006,[2] and indications are that this will increase. The GDP development of China has been strong over recent years; between 7.1 % and 9.4 % growth over the last seven years, which elevates China as a leading force of global growth (World Market Analysis, 2006).

The significance of the Chinese market is also important for Swiss businesses – exports from Switzerland to China reached CHF 4.1 billion in 2006, an increase of more than 18 % over 2005, with an 11 % increase between 2004 and 2005. Confidence in the Chinese market is based on two main factors:

- With a population of over 1.3 billion, the emerging Chinese market has an extremely high potential for future expansion.
- China is believed to offer a low production cost structure in the longer term, particularly for labour costs due to the seemingly unlimited availability of labour.

These reasons have led to a concentration of production-focused investment in China since the 1980s (The Economist Intelligence Unit, 2004; Zheng, 2006), while the apparent success of some companies in this market has encouraged others to consider launching their own China activities. China today not only attracts large companies, but has also become a target for small and medium sized enterprises [SMEs] from Europe (Bülk, 1997; Haeusgen, 1997; Kleine, 2000). Kukovetz (2002) has shown that SMEs from Hong Kong and Taiwan can quickly and successfully enter the Chinese market and a recent survey shows SMEs from Switzerland are also attracted by the seemingly high potential of China (SCS [Swiss

[1] See United Nations (2005): China as the locomotive of the world economy.

[2] See UNCTAD (2006a): Foreign Direct Investment [FDI] inflow to China in 2006. See also www.unctad.org/fdistatistics [China fact sheet].

China Survey], 2006). For Swiss SMEs entering a new market, such as China, this often means expanding into a culturally new and unrelated country or market place, which has several consequences for a firm (Hofstede, 1980, 2001; Daniels and Radebaugh, 1998).

Most literature on the internationalisation of firms discusses the theoretical concepts of internationalisation that lead to a firm's FDI in a host country. Often the literature aligns itself with the internationalisation development of large firms, without explicitly relating to small firms. Various researchers contend that large firm experience in the internationalisation of business operations does not necessarily represent an easily transferable model for smaller firms (Coviello and McAuley, 1999; Brauchlin and Pichler, 2000; Dunning, 2002).

The complexity of different market-entry modes and inherent characteristics, and an SME's own characteristics, can increase management stress and confusion. Early research on German SMEs (Stahr, 1979) identifies a gap between theoretical and practical approaches to SME internationalisation, and, according to Stahr, '...the theoretical market selection approach appears to be complicated for the practitioner and seems to be too accurate'. A view which does not seem to have changed much, and, as a recent ENSR survey (2003) shows, although SMEs appear to be aware of strategic issues in the internationalisation process and the high importance of planning, in practice firms do not necessarily follow available knowledge during implementation.

Various definitions emphasise the importance of strategic and centralised decisions[3] and their relationship to the long-term focus of an organisation, often understood as a non-routine activity. While FDI is important, as are the resources it can utilise, FDI is not always a strategic process, accompanied by, or evolving from, a strategic decision-making process (Kukovetz, 2002: p3). FDI decisions are important to any size of company and can undoubtedly be strategic, which means the FDI decision-making process is important. This dissertation specifically analyses the FDI decision-making process that takes place in SMEs, and considers the decision-making processes of Swiss SMEs that have expanded into China.

1.2 Research Objectives and Relevance

There are numerous publications about China, and about market-entry into China. The pros and cons of different forms of FDI are often analysed and discussed, thereby expanding the internationalisation theory, especially in the case of China. Authors elaborate on the complexity of market-entry into China and highlight the obstacles to be met, but seldom is an in-depth analysis of different conditions made, or the development of an institutional framework discussed or how an individual firm finds its way through the maze. The

[3] Mintzberg *et al.* 1976: p246; Bower and Doz, 1979: p157; Ghemawat, 1991: p44; Pleitner *et al.* 1998: p46.

environment context is largely ignored and how a firm fits into this context, based on the individuality of the firm and its own investment decision-making processes for market-entry, is not given any attention, while major market-entry decisions are often generalised.[4]

The aim of this dissertation is exploratory in nature and provides a theoretical contribution to research on internationalisation and decision-making, underlined by two main assumptions:

- Current internationalisation theory can fail to explain the accelerated internationalisation processes of companies, especially for SMEs where firms do not have much international experience, yet directly engage in FDI activities.
- The decision-making process for market-entry into an emerging market deals with uncertainties.

The behavioural and organisational decision-making theories can benefit from the findings of this project on how small firms, and their owners-managers, make their decisions under uncertainty; possibly even a decision by a single person in a firm.
In this dissertation and in the decision-making model developed, individual and firm-level decision-making are integrated to include the entrepreneurial aspect of single managers or decision-makers that contribute to the market-entry of a company.

To this author's knowledge there is, as yet, no similar research on FDI decision-making processes in SMEs.[5] This dissertation supports the strategic decision-making theory on internationalisation, and this project not only has theoretical relevance but is also of practical value. It investigates the processes of market-entry into an emerging market, and its results can be applied in similar market places, while it also describes how individual decision-making can be developed.

1.3 Research Outline

The dissertation is divided into three main sections to guide the research process:

- **Section One**, in Chapter One gives the foundation for this project while Chapter Two reviews the multi-disciplinary literature on decision-making processes and foreign direct investment, concluding with a critical review.
- **Section Two** starts by defining the decision-making research framework in Chapter Three. This framework is based on the findings of the preliminary field study, the views of experts and the literature review. Subsequently, final research questions and

[4] See Lord and Ranft (2000: p574): It is suggested that as firms expand into new international markets, their organisational learning processes differ significantly. They are not smooth and seamless processes that are homogeneous across firms. Variations stem from both the nature of knowledge itself and from differences in firms' organisational structures.

[5] See Song *et al.* (2002): Managers from different nations may use different criteria to select a competitive strategy, because they use different 'mental models'. This presents the opportunity within this dissertation to conduct research amongst Swiss firms and their owners-managers.

propositions are formulated. Chapter Four discusses the research methodology for this dissertation.

- **Section Three** addresses the field study, with Chapter Five introducing the different case studies, followed by data analysis and its evaluation to confirm the research propositions. Chapter Six summarises the result of the study, addresses the research propositions and presents a model for SME decision-making for FDI, based on the findings. Chapter Seven addresses the overall conclusion of this dissertation. Exhibit 1 illustrates the structure of the research project.

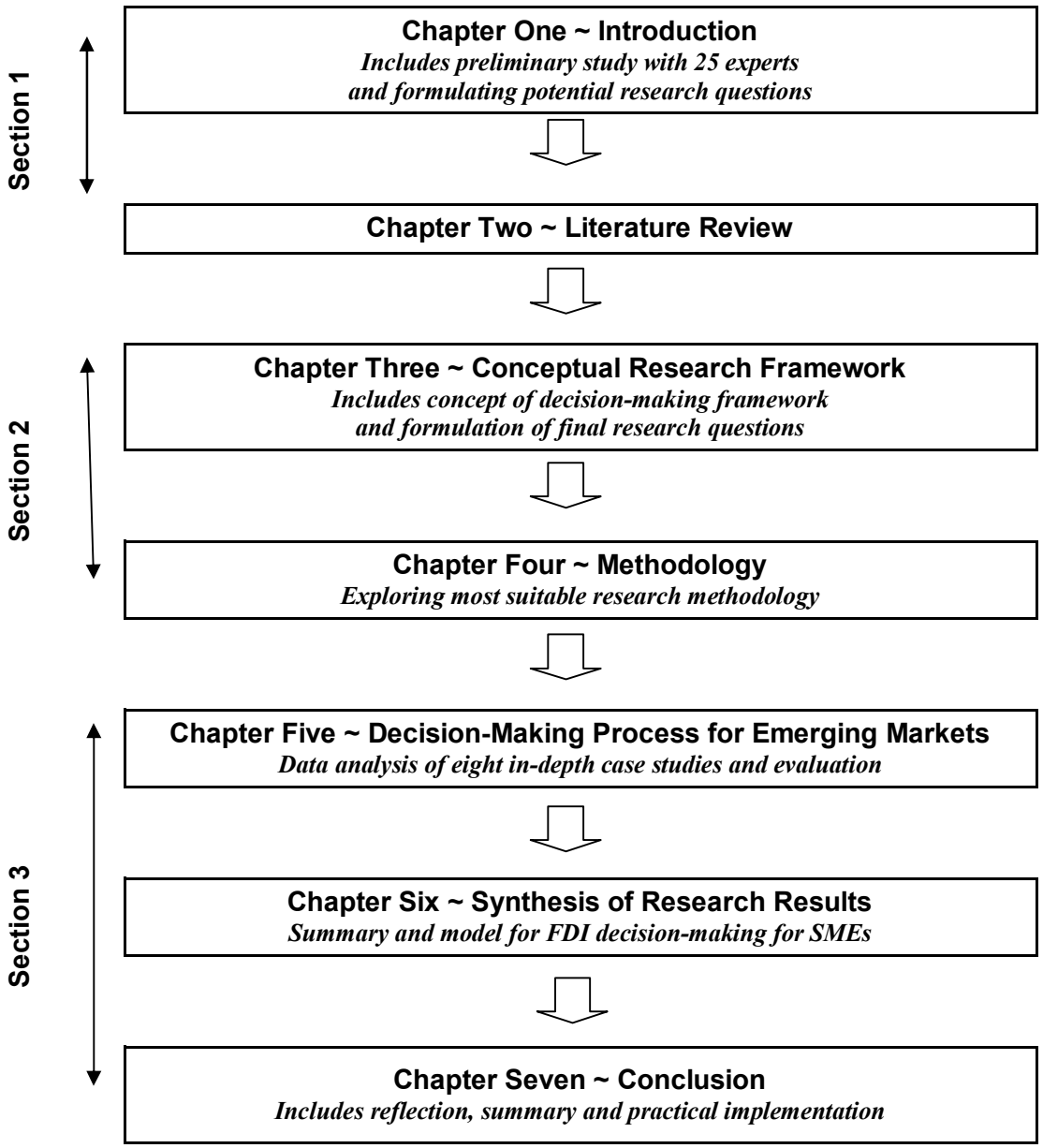

Exhibit 1: Structure of Research and Dissertation

(Author, 2007)

1.4 Emerging Markets and Swiss Firms

This section gives a brief overview of emerging markets, and, in particular, the case of China, followed by a discussion on the current situation of Swiss businesses in China. The section concludes with a preliminary research phase for this dissertation: a small-scale investigation amongst owners-managers of Swiss SMEs and China experts, conducted in the autumn of 2006. This preliminary evidence is used to draft potential research questions before the in-depth literature review is undertaken.

1.4.1 – Emerging Markets

Emerging economies fall into two groups: developing countries in Asia, Latin America, Africa and the Middle East and transitional economies, such as in the former Soviet Union and China (Hoskisson *et al*. 2000: p249; Gilpin, 2001: p333). One should be aware that there is no standard definition, or list, of countries agreed on as emerging economies, partly because the terminology itself is recent, and partly because the countries have had different starting points and arrived at different stages in the process (Hoskisson *et al*. 2000: p259; Hooke, 2001: p15). An emerging market is defined as a promising high growth market, with a high level of uncertainty, using economic liberalisation as a major driver of growth (Arnold and Quelch, 1998: p8).

Characteristics of emerging markets are introduced by Tudor (2000) with emerging markets more easily defined by what they 'are not', rather than by what they 'are' (Tudor, 2000: p7; Kolodko, 2003: p13). The phrase 'emerging market' was coined in the early 1980s by the International Finance Corporation [IFC], is understood differently in countries with highly-developed capitalist economies than in the countries to which it directly applies (Garten, 2000: p23). The IFC's definition is broad: 'The term emerging market can imply that a process of change is under way, with stock markets growing in size and sophistication, in contrast to markets that are small and stagnant'. The term can also refer to any market in a developing economy, with the implication that all have potential for development.

Some investors differentiate between fully-fledged emerging markets and frontier, pioneer or embryo markets, which are less developed, less liquid and riskier (Kolodko, 2003: p15). Hooke (2001: p15) considers emerging markets to be poor countries with a per capita income of less than US$ 9,000 per year. In the year 2001, 156 nations fitted this definition, encompassing 84 % of the world's population and 75 % of sovereign states. Other labels for these countries include developing nations, low-income countries and the Third World. Hooke describes how reality clashes with the developing nations' stated desire for foreign investments which can bring jobs, technology and progress. These countries want outside finance and technology, but only on their own terms, which may

be unrealistic from a Western point of view. Possible benefits of entering emerging markets are often offset by the perception of higher risks due to possible problems, such as political, macro-economic, currency and information disadvantages (Hooke, 2001: p98; Khanna *et al*. 2005: p63).

1.4.1.1 Business Strategies in Emerging Markets

The rapid and widespread adoption of market-based policies by emerging economy governments raises important issues for strategies adopted by private enterprises, both domestic and foreign (Hoskisson *et al*. 2000: p252). As domestic policies become more market-oriented, such governments are opening their countries to foreign markets and joining regional trading associations. New relationships between foreign and domestic enterprises are emerging as strategic alliances, and replace export processing zones and sub-contracting arrangements.

Enterprise strategies in emerging economies therefore face strong environmental pressure for change. Successful strategies for a firm's growth have to be formulated in the light of institutional frameworks[6] and constraints, which are different in emerging markets. It cannot be assumed that the transition path of emerging markets will necessarily lead to the same economic and social models existing in other countries (Peng, 2000: p46; Child and Tse, 2001: p5).

Khanna *et al*. (2005: p64) point out that successful companies develop strategies for doing business in emerging markets that are different from those they use at home and they often find novel ways of implementing these.[7] Western companies have access to advanced technology, cheap financing and sophisticated managerial know-how. In the absence of institutions providing these and other functions in emerging markets, diversification may be the best way to match competition (Khanna and Palepu, 1997: p51). As a consequence the development stage of an emerging market will largely determine an enterprise's strategy (Hoskisson *et al*. 2000).

As institutional forces affect an organisation's processes and decision-making Peng and Heath (1996: p521) argue that the internal growth of firms in transition economies is limited by institutional constraints, and, as a result, a network-based growth strategy is

[6] See Davis and Nort (1971: p6): An institutional framework is defined as a set of fundamental political, social and legal ground rules that establish the basis for production, exchange and distribution. See Peng (2000: p42): Firms also need to take into account broader influence from sources, such as the state, society and culture, when crafting and implementing their strategies. These influences are broadly considered as institutional frameworks.

[7] See Khanna *et al.* (2005: p64): One major set-back of emerging markets is that they lack skilled market intermediaries and have less effective legal systems. Because services by intermediaries are either not available in such markets, or are not sophisticated (Child and Tse, 2001: p7), firms cannot smoothly transfer the strategies they employ in their home markets.

expected to be more viable in emerging economies. Subsequently, as emerging markets develop, a trade-off between transaction costs associated with the market mode, a firm's need for control and the governance costs of the hierarchy can be dominant. Organisations as a governance structure will dominate markets in the presence of high uncertainty, large asset-specific investments and infrequent transactions among a small number of agents (Hoskisson *et al*. 2000: p254). The resource-based view draws on the issues of a firm's sustainable advantage and the ability to create, or develop, institutional capital to enhance the optimal use of resources. As resources are assumed to be context-based, depending on the characteristics of that context, a premature focus on the limits of resources could create strategic inflexibility and core rigidity for a firm, which would lead to negative returns (Leonard-Barton, 1992: p118).

1.4.1.2 Information Gathering and Risk

Many firms enter new markets simply because of senior managers' personal experiences and vision, family ties, gut feelings or anecdotal feelings (Shrader *et al*. 2000: p1244; Volery, 2003: p8; Acedo and Florin, 2006: p49). Sometimes firms follow key customers or rivals into emerging markets. Khanna *et al*. (2005: p64) note that firms often target the wrong countries or deploy inappropriate strategies for entry. Country portfolio analysis and political risk assessment, often used for new market assessment, chiefly focus on the potential of profits from business in developing countries, but leave out essential information on a possible soft infrastructure, or how to conduct business. Shrader *et al*. (2000: p1243) note that new ventures undertaking internationalisation in a single foreign country manage risks by determining trade-offs among three risk factors: economic and political risk in the host country, degree of commitment in the foreign location [indicated by the entry mode employed] and the percentage of foreign revenue exposure in that country.

The important role of intermediaries for reliable information gathering, as pointed out by Khanna *et al*. (2005: p64), underlines that poor information can result in the underestimation, or even neglect, of[8] accounting transparency, liquidity, corruption, volatility, governance, taxes and transaction costs (Bruner *et al*. 2002: p311). The valuation of future business partners in many markets relies on the availability of accurate reliable information that not only addresses current assets but also future prospects. Whereas reliable capital markets should give sound information about a partner firm, this may not be useful for smaller companies dealing with smaller firms in an emerging host country where a lack of transparency can be expected.

[8] See 'Risk management in Shanghai', Economist Corporate Network, Briefing Paper for presentation by Humphrey, P. [Price Waterhouse Coopers Investigations Asia Ltd.] and Sheng M. [Coface China] on 23 May 2002 in Shanghai.

Bruner *et al*. (2002: p319) argue that single institutional factors, as in emerging markets, do not justify decisions for investment as country factors and comparison alone lose significance[9] and an overall judgement is needed. Institutional capacity of a nation is however, and continues to be, the key for attracting inward FDI (Rondinelli, 1998: p9; Hoskisson *et al*. 2000: p252) and the level of development must be known to an investor. While information gathering about the institutional capacity of a particular country assists decision-making, the quality and volume of such information may still not be at the level used in the home country, and decision-making is thus based on less information (Hooke, 2001: p260). Perceived strategic uncertainty increases and risk trade-offs are found when internationalisation into emerging markets takes place (Shrader *et al*. 2000: p1244).

1.4.1.3 Perceived Strategic Uncertainty

For McGee and Sawyer (2003: p386) the external environment refers to relevant physical and social factors, outside the typical boundaries of an organisation, that influence managerial decision-making and can be classified into at least seven categories or sectors: technology, competitors/industry, customers/markets, suppliers, political/legal, economic and social cultural (Dill, 1958; Duncan, 1972). The initial four sectors are considered part of the immediate environment and tend to have a direct impact on the competitive situation of organisations. The remaining three sectors have a more indirect influence on individual organisations and are considered part of the remote environment.

The external environment is a primary source of uncertainty for managers responsible for identifying opportunities and threats facing their respective organisations (Duncan, 1972: p314) and small firms often lack sufficient internal resources to adequately scan the environment (Brush and Vanderwerf, 1992: p158; Brush, 1992: p50; Mohan-Neill, 1995: p12). Such firms must seek information outside their organisations (McGee and Sawyer, 2003: p395).

Duncan (1972: p325) proposes perceived uncertainty as comprised of a complexity dimension and a variability dimension. Complexity refers to the number of environmental elements and the level of interdependence among them, while variability refers to the rate of change in the environment, and Duncan argues that the variability aspect is more important for organisational adaptation.

Daft *et al*. (1988: p125) contend that perceived sector importance translates perceived environment uncertainty into strategic uncertainty. Strategic uncertainty thus reflects the strategic value of environmental information for organisational performance. Perceived

[9] See Bruner *et al.* (2002: p319): 'Some remaining questions and implications' as an outcome of the 'valuation in emerging markets' colloquium on 28/31 May 2002 at Darden Graduate Business School.

strategic uncertainty is the perceived absence of sufficient information about environmental events and activities, and the inability to predict external changes in strategically important sectors.

Concentration on the different environmental sectors rather than the environment as a whole emphasises the institutional framework[10] of a country that has to be analysed within its own sectors. This framework is made up of both formal and informal constraints around individual and organisational behaviour. Formal constraints include political rules, judicial decisions and economic contracts. Informal constraints include socially-sanctioned codes of conduct and norms of behaviour embedded in culture and ideology (North, 1990: p36; Child and Tse, 2001: p7). North suggests that in situations where formal constraints fail, informal constraints will come into play to reduce uncertainty and provide permanence to individuals and organisations (Peng, 2000: p43).

1.4.1.4 China

China's 'open-door policy' and its resultant business environment, at first glance, represents a radically new, ideologically paradoxical, phase in China's modern history. In 1978, China embarked on economic reforms aimed at moving away from state socialism and lifting its people from poverty to modernity (Shirk, 1993: p47; Peng, 2000: p26). A closer look at the business environment of China however reveals a long tradition of Sino-foreign cooperation. As early as the Tang Dynasty (618-907AD), Chinese trade crossed the vast Eurasian landmass via the Silk Road and maritime traffic moved through the ports of southern China.

China's politics, since 1949, have been shaped by a different inward and outward orientation of the nation (Lang, 1998: p45). This has resulted in some active relationships with the West, neighbours or other communist countries but, in other cases, has also led to isolation from the rest of the world.

Since the end of the 70's development has been characterised by the 'politics of small steps' which, with the integration of Hong Kong (1997) and Macao (1999), has resulted in further economic growth and development.[11] China aspires to maintain high economic growth, and the country continues to need resources and attract business from outside its

[10] Davis and Nort (1971: p6), An institutional framework is defined as a set of fundamental political, social and legal ground rules that establish the basis for production, exchange and distribution.

[11] See Lai (2006): Development since 1979 has not been even. There are three significant stages of development that have resulted in different performances: sustained high growth (1979-1996), growth slow down (1997-2002) and resumed growth increase (2003-present). Such uneven growth is reflected in an uneven inflation pattern during the same periods as China's inflation situation is quite unusual, and clearly has a connection with investment fluctuations, which, in turn, has partly to do with heavy government involvement in investment.

borders, as reflected in the 10th five year plan[12] and in the 11th five year plan[13] (Schüller, 2004: p44).

It is debatable if China can still be categorised as an emerging market, although it fulfils certain criteria that hold true for some supporting aspects such as large and geographically uneven GDP growth. Looking at the heterogeneity of the country, in terms of language diversity, cultures, infrastructure development and income disparity (Hooke, 2001; Kolodko, 2003; Davies and Nyland, 2004) China cannot be viewed as one homogenous body.[14] From this viewpoint there is indeed room for the assumption that the country is in a state of continuous transition. The oft-cited GDP growth[15] of China must not delude one into thinking this growth is uniformly distributed across the country.[16] Although the average annual growth of GDP has risen across all regions, the coastal provinces have tended to grow faster than the northern and western provinces[17] (Unel and Zebregs, 2006: p3). High GDP growth is not the only measure to indicate a nation's transition, and a misperception of this indicator is possible (Xu and Liu, 2005: p146).

Foreign investment in China has never been totally free of constraints, and foreign investors have been subjected to a series of stringent government controls as to where and how they can invest (Davies and Nyland, 2004: p186). Western companies must understand why and how China invites foreign companies to do business in China, and possible restrictions on such business. The lure of China's large potential market is used to direct technological transfer and finance into strategic sectors consistent with plan priorities (Folsom and Folsom, 1996: p22; Nolan, 2001: p45), which also extends to the transfer of management and marketing skills.

The Chinese government has however realised the need for a sound infrastructure and a comprehensive institutional framework to attract inward FDI, which, in their understanding, underscores the necessity for state intervention and fosters governmental influence (Davies and Nyland, 2004: p190). China is, in many ways, still centrally

[12] See Schüller (2004): 10th five year plan 2001 to 2005.

[13] Economic Report by Embassy of Switzerland (December, 2005): 11th five year plan 2006 to 2010.

[14] See China seminar on 2nd February 2006 at the University of Basel and statements by Dr. Weigui Fang - University of Trier. SCS (2006: p46): China's diversity is legendary in many aspects. In geographical terms, China is more a continent than a country, very much like Europe or India.

[15] See Lai (2006): There is a debate about the true growth of China's GDP. The debate began with a downward adjustment of the official GDP figure. This argument is based on apparent inconsistencies in official Chinese statistics (Rawski, 2001; Rawski and Xiao, 2001; Young, 2003).

[16] See SCS (2006: p55): The six economic regions and differences.

[17] See NZZ-Verlierer und Benachteiligte in China: 'China hat von der stürmischen Entwicklung seiner Wirtschaft enorm profitiert. Doch die eindrückliche Bilanz der letzten Jahrzehnte hat auch Schattenseiten. Nach Jahren des Wachstums um jeden Preis setzt die Regierung nun den Akzent auf eine sozial und regional ausgeglichenere Entwicklung. Wegen der Grösse der chinesischen Bevölkerung sind die Herausforderungen gewaltig' (NZZ, May 2004).

controlled and is a communist country despite its perceived openness. Some marginal changes may occur over time but this can only be considered a slow process.[18] The institutional context in China, its macro-economics and changes, must be understood by foreign companies, rather that market-entry being driven only by market potential or industry characteristics (Khanna *et al*. 2005: p67). More important, firms must learn how their own organisation can fit into this environment. Such consideration helps understand the different risks associated with doing business in China.[19] Companies can be quite perplexed[20] by circumstances they meet and the impact of the Chinese business environment. In reality, companies are often uneasy, as it takes time to establish a proper structure, logic or organisation to do business or handle regulations in China; an existing business model, or business idea, cannot just be transferred.

1.4.2 – Swiss Business and China

Switzerland, like many other countries in the world, is not untouched by the impact China exerts. Sino-Swiss relationships are not recent but as global markets have grown, and since the open-door policy was introduced, China has attracted more Swiss firms than ever. A number of Swiss institutions are involved in different areas of Swiss-Chinese relationships.[21] The utilisation of lessons learned by others and building on existing knowledge helps to understand the Chinese market place in the further development of Swiss firms. Exhibit 2 shows significant research on Swiss-Chinese business; no older than 10 years, and within the previous two five-years planning periods of China [1996-2000 and 2001-2005].

1.4.2.1 Relations and Trade between Switzerland and China

The first Swiss to go to China seem to have been Swiss Jesuit missionaries in the 16th Century. Swiss-Chinese economic co-operation has its origins in the mid to late Qing Dynasty (1644-1911) and in the 18th and 19th Century when Swiss business developed the export of watches. A number of Swiss trade firms eventually had branches in China by the end of the 19th Century.[22] In the mid-19th Century the manufacture of Swiss watches started in Shanghai and Tianjin. Expensive watches were imported from Switzerland and cheaper models produced locally (Roth, 2003: p206). Diplomatic relations with the old China basically started in the early part of the 20th Century, with the

[18] China seminar on 2nd February 2006 at the University of Basel and the statements by Walter Fust [Director of DEZA] and his remarks about the Swiss-Sino Centre at the University of St. Gallen [The Centre runs a long term programme on public management education for Chinese officials].

[19] See www.worldmarketanalysis.com and China – Country Risk Summary, for the division into different risk factors: political, economic, legal, tax, operational and security risks.

[20] China-Focus Seminar, April 2003 at Osec in Zurich.

[21] Activities of Osec, SCCC, University of St. Gallen and its Swiss-Sino Centre.

[22] See Swiss-Sino Trade – History, Embassy of Switzerland (March, 2006).

Treaty of Friendship and Trade concluded in Tokyo between representatives of Switzerland and the Northern Government of China (Sigerist, 1998).

Switzerland was one of first countries from Western Europe to establish official relations with the new China; on the 17th January, 1950, the Swiss Federal Council recognised the new government of the People's Republic of China, and on the 14th of September of the same year, China and Switzerland established diplomatic relations. Since establishing official relations and especially since the beginning of the reform policy in China, relationships between Switzerland and the Peoples Republic have steadily developed, and the Swiss and Chinese governments later agreed on mixed credits.[23]

When the open door policies were launched in late 1978, initial Swiss investments were in the elevator industry, the production of power generating equipment and a milk powder plant. Further projects soon followed, which reflects the increasingly prominent involvement of Switzerland's chemical, pharmaceutical, machine and instrument industries. The expansion of trade and direct investment activities between Switzerland and China has appreciably benefited from the support and facilities available from Swiss service industries, such as shipping, freight forwarding, banking, insurance and tourism. The bilateral agreement with China's WTO accession on 26th September 2000 made certain concessions for Switzerland's service industries.[24]

Resources and Research on Swiss–Sino Business Relations is given in Exhibit 2 overleaf.

[23] See Swiss Presence in China and history of Switzerland and China, Swiss Embassy in Beijing. 1st agreement - 80 m CHF (1984), 2nd agreement - 100 m CHF (1987),3rd agreement - 110 m CHF (1991), 4th agreement - 40 m CHF (1995). http://www.eda.admin.ch (2006).

[24] See Economy Report by Embassy of Switzerland (December 2005), The People's Republic agreed to make certain concessions for Switzerland in the fields of insurance licences, inspection services and the import of watches.

Researcher/Author/ Year/Title	Firm Size	Type of Research	Industry	Scope	Particulars
Nie, S. October 2006 Management localisation of Swiss companies in the Shanghai area	all	Quantitative among 27 Swiss firms in the greater Shanghai area	Not mentioned	Management localisation. Interaction between home and host countries/ entities	Focus on management behaviour and human resource management
SCS, 2006 China - Behind the China Kaleidoscope - A guide to China Entry and Operations	all	Quantitative and qualitative to 617 registered Swiss entities, return rate of 18 %	Chemical and pharmaceutical, services, manufacturing, machinery and equipment, consumer goods, construction, electronics engineering, IT and Telecom	Future outlook, analysis of Swiss firms in China	Guideline for market-entry for Swiss companies
SECO, November 2005	all	Quantitative, questionnaire to 230 Swiss companies, return rate 21.7 %	Production, pharmaceutical and chemical, services and insurances	Analysis of major framework conditions for commerce and FDI	- Access to the Chinese Market - Doing business in China
Roth, H. J. 2003, Erfolgskriterien der Führung von ausländischen Unternehmen in der Volksrepublik China	all	Qualitative interview, 40 managers, with 20 Swiss managers as well as Chinese managers that work for Swiss firms	Not mentioned	Research on leadership success factors	- Focus on problems of successful leadership in a culturally different work place - How to solve such problems - Which are the important requirements for successful management
Berger *et al.* 1998 Success Analysis of Swiss Direct Investments in the PRC	all	Quantitative, questionnaire to 281 companies with Swiss participation. 42 FDI and 56 representative offices answered	Consumer goods, Pharmaceutical & Health Care, Electronics/Electrical engineering, Construction, Chemicals, Mechanical Eng., Textiles, Services and Instrumentation	How success in China is achieved, conception of success factors	Advice for successful investors
Bülk, J.H., 1997 Markterschliess-ungsstrategien Deutscher und Schweizerischen Klein und Mittelunter-nehmen in der Volksrep. China	SMEs	Qualitative and quantitative questionnaire answered by 5 Swiss and 35 German firms	Mixed, research was done on firms that had already founded a WFOE or a JV	To show possible market-entry strategies to China	- Characteristics of SMEs in their internationalisation process - Chances and risks of market-entry to China for SMEs

Exhibit 2: Resources and Research on Swiss–Sino Business Relations

(Author, 2007)

1.4.2.2 Swiss Firms and China

By the end of 2005, some 230 Swiss firms, with 617 branches, were represented in China, employing almost 55,000 people.[25] Several types of legal entities are present, as in Exhibit 3, for the different Swiss entities active in different industries.[26] Swiss firms are mainly focused on sales and production in China, with purchasing activities less represented.[27]

	WFOE	Equity-JV	Contractual-JV	Rep. Office	Holding	Others
Number of Entities	205	103	21	265	11	12

Exhibit 3: Type and Number of Legal Swiss Entities

(SCS, 2006: p8)

Swiss firms, or branches, have mainly been established in the Beijing, Shanghai, Shandong and Jiangsu, Guangdong and Jianxi areas. As outlined by SCS (2006: p46) few Swiss companies settle in Chinese provinces away from the coast. Estimates put total direct investments at about five billion Swiss francs, making Switzerland the fifteenth most important national origin of FDI.[28] From indications by the Ministry of Commerce [MofCom], China granted 125 projects with Swiss participation in 2005 with a value of US$ 206 million.[29]

1.4.2.3 Relevance of Business Conditions for Swiss Companies

Swiss firms consider the Chinese market important, growing and becoming more and more attractive following perceived improvements and opportunities in the business environment [in particular for services].[30] In line with the perceived present and future importance of the Chinese market the priorities set by Swiss companies are: sales, marketing and brand management, distribution network and channels, market research, production management, general management, supply chain management, finance, administration, R&D and engineering.[31] The challenge China sets for foreign companies is that the overall climate is very competitive, many restrictions are found and market access can be difficult, with the regulatory environment complicated and costs in the

[25] See SECO survey (November, 2005).

[26] See SCS (2006: p67): Swiss presence in China is mainly in chemicals & pharmaceuticals, food/textiles and agriculture, banking & insurance, legal/audits & consulting, media & publishing, logistics, trading, manufacturing, machinery & equipment, medical, precision & optical instruments, watches, construction, civil engineering, environment protection, and information technology.

[27] See SCS (2006: p70): Reasons to be active in China are: (1) Only exporting to China, (2) Producing for the group, (3) Subsidiary producing and selling in China, (4) Producing, selling and purchasing, (5) Purchasing or trading.

[28] See Economy Report by Embassy of Switzerland (December, 2005), Bilateral investment flows. The precise amount of FDI is unknown. Enquiries by the Swiss Embassy in Beijing were largely ignored by enterprises, p7.

[29] See commercial report of Swiss Consulate in Shanghai (1/2006). http://www.sinoptic.ch/shanghaiflash/2006/200601.htm.

[30] See Handelszeitung (8th March 2006): China wird für Schweizer Firmen immer bedeutender: über 80 % der Schweizer Industriefirmen, 70 % der Pharma- und Chemieunternehmen und über 85 % der Dienstleistungsunternehmen, die schon in China tätig sind, wollen ihre Aktivitäten in China weiter ausbauen.

[31] See SCS (2006: p80): Activities of subsidiaries believed to strengthen the business in three years.

future thought to be on the increase.[32] There were also complaints from SMEs that their problems are not being taken seriously by the Chinese authorities, in particular on Intellectual Property Rights [IPR].[33]

Many companies see the East and South East Asia Region as an important market for goods produced in China, with significant potential, especially if China eases the logistics channels for exports.[34] But recent research by the SCS (2006), in the different geographical clusters of China, has shown that China cannot be characterised as one homogenous body, and a variety of difficulties are met across regions. Difficulties, as in Exhibit 4, are of different importance in each region and result in different approaches to setting up and operating a business.

Difficulties (1-least difficult, 9-most difficult)	**Beijing**	**Shanghai**	**Shandong & Jiangsu**	**Guangdong & Jianxi**
Changes in laws, regulations or policies after set-up	1	7	5	8
Major changes in market circumstances after set-up [e.g. smaller size, heavier competition, more difficulties, access to clients]	2	2	1	3
Lack of support and cooperation from authorities and bureaucracy [e.g. withholding of necessary licences]	3	4	7	7
Local human resources are not up to necessary standards	4	1	2	1
Corruption	5	9	8	5
Lack of understanding and/or support and/or commitment from the mother company [e.g. funding, sales, technical support]	6	6	6	9
Insufficient research and/or preparation leading to wrong evaluations and/or decisions [e.g. wrong cost, market or competition evaluation, unpublished laws and regulations]	7	3	3	6
Change in level of costs after set-up	8	8	9	4
Local materials/components/services are not up to necessary standards	9	5	4	2

Exhibit 4: Difficulties met across China

(SCS, 2006: p48)

1.4.2.4 Success Factors for Swiss Companies in China

More recent research on German (Parnell, 2002; Kaufmann *et al*. 2005) and Swiss SMEs (Berger and Partner, 1998; SECO, 2005; SCS, 2006) conducting business in China shows there is little difference between perceived success factors for firms. The research underlines

[32] See Handelszeitung (8th March 2006): Kritik von Firmen-Neueste Studie zeigt Mängel auf: Non-tariff barriers such as licences and expensive state constraints are considered hurdles for market-entry by Swiss firms. Easier market access, a free trade agreement and direct flight connections are required by Swiss companies.

[33] See SCS (2006: pxi): China presents considerable and growing opportunities for Swiss SMEs. The smaller the SME, the more timing is of the essence: small firms cannot afford to invest too early and wait for returns; neither can they invest sufficient resources if they start late and try to catch up.

[34] See Economy Report by Embassy of Switzerland (June, 2005), China-ASEAN Free Trade Agreement [CAFTA] planned to be implemented by 2010.

that most China entries, both from Germany and Switzerland, have, overall, achieved good business results and are intending to expand their China involvement in the near future.

Representative data on success rates for Swiss FDI are not easily available as some companies avoid disclosing such information. In their answers to the SECO survey by the Swiss Embassy in Beijing, in November 2005, more than half the Swiss companies doing business in China estimated the business climate is positive overall.[35] More than three-quarters of the firms in the SCS survey (2006: p73) stated they have recovered the amount of their investment with profit.[36] In contrast, a Taiwanese study states that 41.7 % of 1,644 Taiwanese businesses investing in China reported they had lost money or just broken even. Only 46.6 % of Taiwanese firms reported their investment in China as profitable.[37] The question remains why countries from culturally-unrelated countries, such as Switzerland, doing business in China, seem to be more successful in China compared to China's direct neighbours that do business in China but judge the overall business environment as difficult.

The SCS survey derives clusters of success, as shown in Exhibit 5, which allows elaboration on relevant Chinese factors. The categorisation distinguishes between different areas of importance while single sub-factors are relevant and influence each other. A, B and C clusters, as in Exhibit 5, are considered, by far, the most important categories by Swiss firms doing business in China.

Group	Cluster/Category
A	Human resource selection and management
B	Products
C	Knowledge of the local environment
D	Operations
E	Planning and preparation
F	Guanxi[38]
G	Selection of the location
H	Support from headquarters
I	Support from China-based institutions

Exhibit 5: Main Clusters of Importance for Successful Business in China

(SCS, 2006: p13)

[35] See SECO survey (2005: p18): The perceived business climate in China is challenging but overall positive. See also SCS (2006: pix): Over 50 % of respondents in China to the Swiss China Survey estimate China will be the most important economic area for businesses within the next five years.

[36] See SCS survey (2006: p73): 52 % of firms achieved, or expect to achieve, a payback of their investment in three years.

[37] See Economy Report by Embassy of Switzerland (December, 2005), Bilateral investment flows, only 46.6 % of Taiwanese businesses say they are successful in China.

[38] See Kleine (2000: p105): In China there is a tendency to personalise business relationships. The establishment of relations is an essential part of the Chinese way of doing business. These personalised relations result in networks. Companies and managers are woven into these networks. Guanxi can be understood as a relationship between individuals which is reciprocal, i.e. an informal relationship is sustained by recurring and mutual favours.

1.4.3 – Experts' Views

For this dissertation preliminary interviews with several experts were conducted during the autumn of 2006,[39] aimed at gaining a deeper understanding of the market-entry process and underlying decision-making for Swiss firms entering China. The objectives being to:

- Understand the state-of-the-art in this field.
- Set boundaries for the literature review.
- Gain a preliminary idea of the important features of the decision-making process for FDI and how to develop a possible research framework.
- Reach an observer position and understand the context of the research and boundaries.

This preliminary research stage helped develop a clear focus on the final research process.

1.4.3.1 Methodology for Experts' Views

The semi-structured interview method was selected to approach interviewees. The aim being to explore the topic in a narrative way, so interviewees would express their views, guided by several main questions. Interviews usually started with a broad entry question, such as 'Why do Swiss SMEs choose to enter China?' Subsequent questions followed, eventually leading to a core question, such as 'How can the decision-making process for internationalisation of Swiss SMEs into China be explained?' This approach held certain advantages. Firstly, the narrative approach allowed interviewees to tell their own story. Secondly, specific research questions are addressed based on the individual interviewee's own experience.

All selected experts were required to have a profound knowledge about China, to understand the circumstances of SMEs and further preference was given to experience in production in the industrial sector. The owners-managers had individual experience of either having gone through all the stages of establishing a company in China or were in the process of doing so. The consultants/advisors are mostly directly involved or supportive in an early phase of market-entry or decision-making, often when their clients have asked for initial advice.

1.4.3.2 Empirical Finding ~ Preliminary Research Phase

Reasons to enter China

Firms from Switzerland can enter China as their first ever market for sales and production, even without relevant experience. While not every market-entry is the result of stringent market research, Swiss firms normally try to be well prepared for market-

[39] See Appendix A for list of experts that supported this initial research phase. The list includes 13 owner-managers of Swiss firms and 12 experts/advisers and scholars.

entry. The positive attitude of Swiss firms in the preparation phase of market-entry shows owners and managers are very much committed when they take up their China venture. There are few 'trial and error' approaches and full commitment is recorded. Swiss SMEs do not necessarily enter China for the promising large customer base and the oft-mentioned high growth rate. They show a long-term view on how the business environment in China will develop positively for them. Swiss firms think they are quite knowledgeable about the pros and cons of business in China and do not overreact. Certain pull factors motivate Swiss firms into internationalisation into China, such as the entry by China into the WTO. Easy mobility of information, investment, staff and developments in telecommunication and transportation are believed to enhance the positive development of the business environment.

Seemingly attractive production incentives, such as low production costs, seem to attract Swiss firms. Cost incentives are however only one possible reason for entering China. Swiss firms see large developed areas/cities in China as trend-setting future markets. Swiss firms are aware of the changing environment in China and production cost issues are only secondary after positioning a firm in China, often considered one of the most important world economies. From the current geographic settlement of Swiss firms in China, mainly in the Southern and Eastern areas, it appears the future market potential will be very much in the Western region, which will attract additional market entries.

Developing Business in China

There is an overall understanding that entry into China needs a long-term focus and is not a short-term event. During actual market-entry there appears to be a rather short-term focus on targets with the long-term objectives taking on new dimensions, formulated as '…in any case the China venture will be successful for us'. As expressed by experienced owners-managers the development of firms in China can proceed in steps, often accompanied by 'fire fighting' as new situations are faced which could not have been foreseen. Operation management is often under pressure, and must be of the utmost flexibility. Strategic decisions for market-entry should consider operational decision-making processes during actual market-entry and implementation to determine if strategic targets are being met. It must be accepted that there will be situations that need ad hoc decisions, a need to understand the local situation and an intuitive way of making decisions. Necessary behaviour must be considered at the market-entry planning stage and room for flexibility included. The operational aspects of decision-making are significant and should feed back into the strategic, or overall, decision-making of the firm.

This flexibility has an overall implication on resource planning and underlines the significance of achieving short-term aims and not only long-term targets, to steer the firm in the right direction. Short-term planning is necessary to measure the actual situation and

control any gross departure from the plan, and to further motivate the stakeholders involved. From this perspective market-entry into China is little different from any other business development activity, but has to be adjusted to circumstances in China. There is a changing environment and changing competition, as always present in a nation under transformation, which highlights why market-entry into China must be process-oriented and not only rely on outcomes, to retain flexibility and continue the learning process.

The research basically found two different groups of views. The consultants/advisers underline the importance of good planning. Owners-managers mentioned the need for flexibility during implementation. This could indicate a shift of opinion once market-entry takes place when initial plans and actual management are found to be different. From the generally positive outcome of business results for established companies in China one explanation is that learning effects take place on the way forward and help managers to adjust their business attitude and be more positive.

Decision-Making Process

Swiss firms decide to enter China in different ways and there can be a great variation of entry mode selection. It is indicated that the type of decision-making processes to enter China depend very much on a firm's size and most likely on the people who make and support the decisions. This, in turn, can result in either a more rational approach or an intuitive approach. A distinction has to be made between the stage of the entry process and the kind of decision to be made, which will often influence the time needed for market-entry.

This investigation shows a generally positive attitude by Swiss firms interviewed and did not indicate any wrong decisions made on steps to enter China. Firms appear to decide on a certain type of market-entry to gain control over activities and to minimise their risks, while understanding the risks in China influences the entry mode decision. Overall market-entry into China is characterised as facing unknowns and uncertainty, and not everything can be planned in advance. From the investigation it is evident that Wholly Foreign Owned Enterprises [WFOEs] and representative offices, the latter as a means of soft entry, are the preferred market-entry option for Swiss firms. It cannot be confirmed if the decision for these modes is the result of detailed research or just results from the assumption that another mode is not suitable, for example, entry via a joint venture [JV]. As it is paramount for Swiss firms to have control over activities JVs are assumed to be less preferred.

Previous experience of China for a new market-entry is not necessarily a requirement if experience from other emerging markets is available. It is more important that decision-makers are open to exploration and have the ability to learn and establish a solid core of

knowledge about China. The available knowledge on China will then determine if decision-making for market-entry is rational or more intuitive. As learning takes place the actual decision-making processes are continuously adjusted. In the initial information gathering and research stage, prior to market-entry, information should be collected and analysed in a rational and focused manner. But a distinction between the decision-making processes for the initial or pre-entry [intended] phase and the developing and implementation phase [actual] must be made. The initial stage is more likely driven by rationality whereas intuition, or experience-based decision-making, takes on a greater role in the following stages. Overall the ability to decide rationally and intuitively is important for market-entry into China.

1.5 Potential Research Questions

From this preliminary exploration potential areas of interest on Swiss SMEs market development are deduced. As a result the primary objective of this dissertation is to investigate the FDI[40] decision-making processes of Swiss SMEs[41] in the emerging China market. The secondary purpose is to understand how owners-managers of SMEs undertake such decisions.

The literature review in Chapter 2 focuses on the areas of interest identified, which are relevant for the FDI decision-making process of an SME. The analysis guides an understanding of literature on the dissertation topic and final research questions are deduced.

[40] See UNCTAD (2006b): FDI refers to an investment made to acquire lasting interest in enterprises operating outside of the economy of the investor. In cases of FDI, the investors' purpose is to gain an effective voice in the management of the enterprise. The foreign entity or group of associated entities that makes the investment is termed the 'direct investor'. The unincorporated or incorporated enterprise – a branch or subsidiary, respectively, in which direct investment is made – is referred to as a 'direct investment enterprise'. Some degree of equity ownership is almost always considered to be associated with an effective voice in the management of an enterprise; a threshold of 10 % of equity ownership to qualify an investor as a foreign direct investor is suggested.

[41] See also http://www.kmu.admin.ch/kmu/index.html?land=de – SMEs as defined for statistical reasons in Switzerland are companies with less than 250 employees.

Chapter Two ~ Literature Review

2.1 Background

This dissertation analyses decision-making processes for Foreign Direct Investment [FDI] into China by Small and Medium-sized Enterprises [SMEs]. This resembles a firm's development into any new territory; in this case an emerging market that appears to be risky and uncertain due partly to its novelty. The aim of the literature review is to deepen the understanding of the decision-making processes for FDI, and, subsequently, to draft the final research questions for this dissertation. The literature review is also the basis for the development of a conceptual research framework, which is then used to analyse Swiss SMEs that have entered China *via* FDI.

In chronological order the first section discusses decision-making theories. The second section elaborates on investment theories, in particular those on FDI. As sub-groups the literature review discusses SMEs and environment factors met in the internationalisation process. In essence the literature review reflects the condition of entrepreneurial activities in the context of a firm's development.

2.2 Decision-Making Theory

Decision-making theory as an academic discipline is a relatively young field. It has attracted continuing interest in the literature on business and management. In earlier times business and management emphasised the rational processes of decision-making (Simon, 1957; March and Simon, 1958; Lindblom, 1959). The more or less formal economic decision-theory that forms the foundation of the firm, that is transaction cost or principal agent theory, inspired this development. The traditional decision-making perspectives maintain that uncertainty leads executives to search for additional relevant information to increase certainty[42] (George, 1980; Milliken, 1987; Simon, 1987; Eisenhardt, 1989a). As decision-making has more and more been seen as a central managerial activity, the centre of this activity is the problem of choosing a course of action under conditions of ambiguity and uncertainty[43] and in the process reducing these (Mintzberg *et al.* 1976; Janis and Mann, 1977; Gore *et al.* 1992).

[42] See Kedia *et al.* (2002: p41): Decreasing uncertainty is accomplished by scanning the environment for salient data, aggregating disparate internal and external data, and synthesising relevant information with which to make cogent decisions resulting in desired performance.

[43] See Simon (1947): Decision-making under uncertainty is seen to be far removed from utility maximisation because decision-makers do not posses enough information about final preferences and the means to reach them.

Cyert and March (1963) establish a strong link between the psychological theory of the decision-maker and the economic and organisational theories of how organisations, as opposed to individuals, learn and adapt to changing conditions. Behavioural sciences – sociology and psychology – contribute to this body of knowledge.[44] Further contributions come from philosophy and political theories. The different paradigms all make up decision-theory and there is no clear and distinct set of criteria that defines an overall theory (Harrison, 1987: p8; Brauchlin and Heene, 1995: p24; Butler, 1997: p308; Nilsson and Jiliberto, 2004: p27). The combination of the different theoretical contributions includes consideration of human nature and how people make choices, taking into account contextual setting (Mintzberg, 1975; Mintzberg *et al.* 1976; Hickson *et al.* 1986; Butler *et al.* 1993).

Such complexity gives rise to substantial implications on how managerial decision-making is characterised and how it can be developed. As noted by Bell *et al.* (1988), to prescribe procedures and rules to decision-making, in the interest of improving organisational decision-making,[45] one needs to simultaneously consider normative, descriptive and prescriptive aspects of decision-making (Nilsson and Jiliberto, 2004: p26). If decision-making is viewed from a 'procedural' aspect then automatically it becomes the notion of being normative and quantified; tending to be rather mathematical. The descriptive view attempts to explain how decisions are actually made in practice, which may substantially differ from the normative type. As a result behavioural decision-making can be grouped, according to different characteristics, into qualitative and quantitative approaches, noting that there are programmed, routine or more rational decisions and non-routine decisions.

Researchers have also challenged the traditional principles on the grounds that they fail to explain speed in decision-making (Eisenhardt, 1989a; Judge and Miller, 1991). It is argued that speed in decision-making is crucial and that the more successful companies are capable of making faster decisions in high-velocity environments. Such research results could not have been developed under consideration of purely rational decision-making models, as the traditional models consider the availability of unlimited time and emphasise the need to accumulate information and develop decision alternatives rather than limiting such necessities (Mintzberg, 1973; Nutt, 1976; Fredrickson and Mitchell, 1984). Similarly other researchers have criticised the fact that traditional decision

[44] See Heller *et al.* (1988: p11): In psychology the emphasis is on cognitive processes for solving problems or making judgements.

[45] See Butler (1997: p308): The dominant paradigm of organisational decision-making assumes decision-makers intend to be rational, but that rationality is 'bounded' by lack of knowledge about preferences and any associated instrumentalities.

principles do not explain performance and quality in decision-making processes[46] (Fredrickson and Mitchell, 1984; Dean and Sharfman, 1993; Majocchi and Zucchella, 2003), whereas it is seen as necessary to fully understand the decision problem and its context and formulation to materialise good decision-making (Caroll and Johnson, 1990: p19; Heller, 1992: p59).

2.2.1 – Decision-Making under Uncertainty and Risk

Uncertainty[47] affects motivation and to understand the full impact of uncertainty it is necessary to consider the concept of risk.[48] The decision-making behaviour of individuals in the presence of uncertainty is influenced by their attitude to risk. Risk and uncertainty are inherent in all decision-making (Radford, 1989; Caroll and Johnson, 1990; Hammond *et al.* 1999). These aspects have received considerable attention in academic decision-making literature (Knight, 1921, 1933; Arrow, 1953; Borsch and Mossin, 1968; Murtha, 1997; March, 1997; Atrill, 2000; Buckley, 2000). There is much confusion in decision-making literature over the definitions of risk and uncertainty (Davidson, 1982 and 1991; Murtha, 1997; Simpson *et al.* 1999 and 2000; Macmillan, 2000), and there is no conceptual basis for agreement on clear definitions of 'risk' and 'uncertainty'[49] (Brunsson, 2000; Dwyer and Minnegal, 2006). In management literature, many authors often use the terms risk and uncertainty interchangeably (Thurner, 2005: p41).

The empirical literature argues that investment decision-makers apply methods of decision-making that are affected by the decision-maker's own conceptualisation of risk and uncertainty (Grandori, 1984; Milliken, 1987; Butler, 1991; Lipshitz and Strauss, 1997). Such literature reflects the difficulties in explaining and separating the notions of risk and uncertainty, while the difficulties are seen as: (i) scale, (ii) the position of a particular player *vis-à-vis* particular situations and (iii) the problem of strategic

[46] See Nutt (1999:p75) and Fredrickson (1983: p573): Nutt notes that many decisions in organisations fail. Fredrickson argues the value of strategic process research will be realised only when it provides an understanding of important phenomena and helps improve organisational performance.

[47] See Butler (1997: p308): Coping with uncertainty forms the nub of decision-making. Without uncertainty as to which course of action to take there would be no decision to be made.

[48] See Harrison (1987: p52) and Gore *et al.* (1992: p7): The outcome predictability of alternatives is based on three possible states of nature: (i) certainty – it is assumed that there is complete and accurate knowledge of the consequences of each alternative, (ii) uncertainty – the consequences of each alternative cannot be defined even with a probabilistic framework, (iii) risk – it is assumed that accurate knowledge exists about the probability distribution of the consequences of each alternative. Ignorance occurs if possible outcomes are not known. Using this classification, information can be gathered to turn a situation of ignorance into one of uncertainty and then to one of risk.

[49] See Brunsson (2000: p43): Risk can be understood as the product of the uncertainty experienced by the individual and the stakes – or possible net losses – involved in the action. Since risk is defined as the product of those two, there can be no risk if either one of these is absent. Risk represents a greater threat to motivation than mere uncertainty.

interpretation. As a consequence the assignment of probabilities is difficult[50] (Douglas and Wildavsky, 1982).

2.2.1.1 Risk

Risk may be quantified – as opposed to uncertainty that cannot be quantified – and it applies to contexts in which players are able to assess the likelihood that events will occur.[51] In estimating risk, decision-makers typically attribute uncertainties about outcomes as a factor. For uncertainties thought to arise from inherently uncertain environment processes, decision-makers try to judge the likelihood of events. The estimation of risk is systematically biased by the experience decision-makers have in the organisation. Risk reduces the motivation for a given action by providing a 'contra-motivation', that is a motivation to not undertake the action (Brunsson, 2000: p43).

Individuals can be elevated to positions of decision-making authority by virtue of their past success (March, 1997: p15). As decision-makers have difficulty in recognising the successful role of luck in past incidents, current and future events often ignore risks encountered in previous decision situations (Langer, 1975; Taylor and Brown, 1988). Risk-averse decision-makers may thus actually be risk-seeking in behaviour (Keyes, 1985; March and Shapira, 1987; Kahneman and Lovallo, 1993).

The relationship between risk and return has received considerable attention from researchers (Fiegenbaum and Howard, 1988; March, 1988; March and Shapira, 1992; Shapira, 1995; Payne, 1997) and affects the market-entry mode into a new market.[52] It is argued that a firm's risk attitudes influence risk-return profiles,[53] and more troubled firms may take greater risks. Companies might be risk-seeking when they experience losses or are below targeted aspiration levels. Conversely, they will tend to be risk-averse following achievement of aspirations and targets (Payne *et al.* 1980 and 1981; Singh,

[50] See Cepa (2006): Some economists dispute the distinction between risk and uncertainty. The views reflect that the problem is the agent does not assign probabilities, and not that the agent actually cannot; the problem is really an epistemological and not an ontological problem, a problem of knowledge of the relevant probabilities, not of their existence.

[51] A view developed by Knight (1921 and 1933) which has caused some controversy, as Giddens (1999) proposes not to differentiate between risk and uncertainty but rather to distinguish between two different types of risks.

[52] See Shrader *et al.* (2000: p1227): Shrader investigates how the risk of accelerated internationalisation is managed by SMEs. The study is based on the assumption that trade-offs are required among multiple dimensions of international risk: (i) economic and political risk of the country entered, (ii) degree of commitment to the foreign location [indicated by the form of market-entry], and (iii) percentage of foreign revenue exposure in that country. As a consequence companies prevent risk by following a 'deep niche' strategy, thereby preventing, for example, the risk of imitation. Additional risk reducers are avoidance, flexibility, cooperation and control.

[53] See March (1997: p16) and Harrison (1987: p229): The level of risk taking observed in organisations is affected not only by estimates of risk but also by the propensity of a risk taker to seek or avoid a particular level of expected risk.

1986; Bromiley, 1991; March 1997). For an individual decision-maker it is shown that in practice most individuals exhibit a mixture of risk-seeking and risk-averse behaviour and that the sought level of return largely influences the amount of risk-taking.

The findings are not conclusive since variations in risk behaviour can be observed. It must be questioned how risk is conceptualised and in what organisational context decisions are made; whether based on individual or group decision-making.[54] However it can be deduced that the available resource level can lead to apparent and variable risk preferences and 'risk-shift' in a particular situation.[55] This is best illustrated in the case of market-entry, and the different stages of internationalisation a firm passes through, which highlights that an increasing international engagement shows an increased orientation to success[56] and can be related to learning effects (Johanson and Vahlne, 1977; Bamberger and Evers, 1994; Haeusgen, 1997; Shrader *et al.* 2000).

2.2.1.2 Uncertainty

Uncertainty is not necessarily a common phenomenon, even in organisations that operate in changing and complex environments.[57] When external observers or researchers feel uncertain while investigating such an environment and try to assess the possible future, this is not proof that organisational players, in themselves, feel uncertain. Uncertainty is a broad term and arises when one has incomplete or conflicting information about factors

[54] See Janis (1972: p4); Schweiger *et al.* (1986: p52); Caroll and Johnson (1990: p28); Eden and Ackermann (2000: p67): Group decision-making must also be viewed from the aspect of group cohesiveness, which can affect a decision either positively or negatively. In group decision-making a shift in emotional attitude to the problem situation can be expected as well as a cognitive shift. Changes of emotional attitude reflect, in part, the role of intuition and hunch, which leads to a feeling of comfort about the way forward. A phenomenon observed under experimental conditions in group decision-making is known as 'risk-shift'. This term refers to the fact that decisions made by groups are generally more risky than those that would be advocated by the individual member prior to a group discussion of the problem. Sharing of risk within a group contributes to a shift to alternatives that involve a higher risk (Radford, 1989: p116).

[55] See Payne (1997: p364): It is shown decision-makers show a shift of attention, greatly affected by their available resource levels. As the decision-maker's resource level increases he or she is more willing to take risks. Similarly if the decision-maker has or anticipates a resource level that places him or her below the target value, the person will take greater risks to have a chance to reach the target.

[56] See Bamberger and Evers (1994: p267): During the internationalisation process the orientation towards family tradition, change and home-market orientation decreases at the same time risk acceptance increases. Haeusgen (1997: p165) emphasises the significant role of owners-managers of SMEs and shows that German SMEs in the field of mechanical engineering and machinery are not necessarily risk-taking. However, increased risk-taking by the management is accepted when companies expand into emerging markets. Shrader *et al.* (2000: p1227) show that the attitude for risk acceptance of individual companies determines the internationalisation process and can be faster for those companies that can accept risk while perceived risk levels change over time.

[57] A differentiation has to be made between different kinds, and levels, of uncertainty, not only in the external but also in a company's internal environment (Miller, 1992: p312; Geissbauer, 1998: p81; Yang and Lee, 2002: p99). Companies can underestimate overall uncertainty as a new external environment can result in internal uncertainties. Uncertainty is fundamental in emerging markets, as there are unknowns on the outcome of each decision, and reference values seldom exist. This makes a company's internal and external uncertainty analyses necessary and uncertainty avoidance must be regarded as an objective, and as part of the decision-making process (Yip *et al.* 2000: p10).

involved in decision situations, as influenced by ambiguity (Morgan and Henrion, 1990: p47; Butler, 1997; p315; March, 1997: p5). Recall Knight's definition of uncertainty; Uncertainty refers to situations when this randomness cannot be expressed in terms of specific mathematical probabilities, whereas risk refers to situations where the decision-maker can assign mathematical probabilities to the randomness being faced (Knight, 1921 and 1933). As authors use the terms risk and uncertainty interchangeably and often conceptualise risk as downside uncertainty or chance of loss, it is often the case of missing the recognition of the positive side of uncertainty and risk, and its potential upside (Thurner, 2005: p41; Dwyer and Minnegal, 2006: p3).

The classical approach to decision-making in the face of uncertainty relies on the paradigm of expected utility theory, and therefore on an approach by rational decision-making processes (Hüllermeier, 2001: p3; Cepa, 2006: p3). By incorporating the effects of utility as a result of ambiguity on the input level, different outcomes of decision processes are likely since many different real world scenarios are found[58] (Hogarth and Kunreuther, 1992: p209). The imperfection of knowledge about the external environment of a company is greatly responsible for this ambiguity[59] on the input side of the decision-making process.

Two main aspects of uncertainty can be considered; the source and the degree of uncertainty (Thurner, 2005: p42). The degree of uncertainty can be reflected in four different levels of uncertainty: clear enough future, alternative futures, range of potential futures and true ambiguity,[60] whereas the source of uncertainty may broadly be classified into internal and external factors for an organisation (Duncan, 1972: p315; Wernerfelt and Karnani 1987: p189; Friend, 1989: p147; Miller, 1992: p314; Fischer, 2002: p82).

Broadly speaking uncertainty on the prospects of a certain enterprise is ultimately a combined effect, composed of a number of often inexplicably interwoven sources (Thurner, 2005: p45). Measurements often concern uncertainty on specific variables, but different tasks or actions can also generate varying amounts of uncertainty within organisations, giving rise to pull and push effects (Harrison, 1987: p152; Brunsson, 2000: p39). Exhibit 6 overleaf highlights the complexity a company meets when entering a new market, such as an emerging market. It is argued by Delios and Henisz (2003: p240) that

[58] See Cepa (2006: p3): Expected utility approach is *via* objective probability (Von Neumann and Morgenstern, 1944) and subjective probability (Savage, 1954). Assigned probabilities are merely expressions of what is ultimately amorphous belief and thus may seem more uncertain.

[59] See Nisbett and Ross (1980: p150) and Sproull (1981: p9): There are studies on individuals that suggest people are overconfident. Beliefs in organisations are often much stronger than seem justified even when organisations are exposed to new and contradictory information.

[60] True ambiguity: where a number of dimensions of uncertainty interact to create an environment that is virtually impossible to predict.

firms, within their investment strategies, concurrently reflect on the market and cultural environment, as well as on the policy environment of their host country.

Uncertainty can be classified either into the exogenous variety, in the context that it can be randomly resolved by Mother Nature over time and not by the firm, or an endogenous[61] variety, in that it is resolved by actions chosen by other decision-makers (Folta, 1998: p1010). Such a distinction is important and even more fundamental for decision-making processes, such as in the case of an emerging market[62] where it can be assumed that certain inputs to a decision problem are beyond any influence from the decision-maker. The nature of the uncertainties involved will, and ought to, affect the way the decision-maker perceives and analyses the decision situation.

General Environment Uncertainty	Political	Terrorism, war, changes in government
	Government Policy	Fiscal and monetary policies, trade restrictions, regulations affecting the business sector, tax policy
	Macro-economic	Exchange rates, interest rates, inflation, terms of trade
	Social	Social unrest, shift in social concerns
	Natural	Variations in weather, natural disasters
Industry-Specific Uncertainty	Input market	Quality of inputs, supply relative to industry demand
	Product market	Consumer preferences, market demand, availability of substitutes and complements
	Competition	Pricing and other forms of rivalry, new entrants, product and process innovations, technological uncertainty
Firm-Specific Uncertainty	Operations	Labour relations, availability of inputs, production variability and downtime
	Liability	Product liability, emission of pollutants
	R&D	R and D activities, regulatory approval of new products
	Credit and Fraud	Problems with collectibles, fraudulent behaviour of employees
	Cultural	Cultural friction

Exhibit 6: Uncertainty and its Components

(Miller, 1992: p314)

The concept of uncertainty becomes an issue of describing the environment, such as variability or complexity,[63] but is also used to describe a psychological state of the

[61] See Thurner (2005: p45): Endogenous uncertainty can be resolved by action. It involves learning and provides the opportunity to stop investing if the value of the project falls due to new insights or an exogenous shock. It is caused by lack of knowledge about the environment, and impedes the ability to recognise the true, exogenous uncertainty. Endogenous uncertainty can be narrowed through learning and experience up to a certain level, which represents the boundary between endogenous and exogenous uncertainty. Endogenous uncertainty is based on changing environment factors and can never be fully eliminated.

[62] A crucial factor in defining rationality in decision situations with exogenous uncertainty are the beliefs of the player about the relative likelihoods of the states of nature, where true state is determined in a purely random manner by Mother Nature. A main new element in decision situations with endogenous uncertainty is that the state of nature is now determined 'strategically' by some other players, because the state is actually now a strategy choice of some other player.

[63] See Thurner (2005: p42): Uncertainty has to be distinguished from complexity, as uncertainty is future-oriented while complexity is more of a present phenomenon.

decision-maker (Downey and Slocum, 1975: p562; Brunsson, 2000: p37). Downey and Slocum propose the definition that uncertainty exists when individuals define themselves as engaged in behaviour-based thinking; on less than complete knowledge of existing and future relations between the individual and environment and how these are causally related to each other.

Knowledge and information can be re-defined as correct knowledge and information. If this definition is accepted, then it is natural to describe uncertainty simply as a lack of information. If information is defined as correct information it is, by definition, impossible to obtain any information about the future and, strictly speaking, anyone who sees future events as an important factor in determining present action is going to constantly be uncertain (Brunsson, 2000: p38; Thurner, 2005: p41). As hints, guesses and forecasts are also information, uncertainty can be related to incorrect information as well as to incompleteness.

Two underlying reasons confirm the need to reduce uncertainty. Firstly there can be many sources of uncertainty that can be potentially devastating, and overall environmental changes may render long-range planning by individuals and companies obsolete; as a result failure to perform transactions, as spelled out in contracts, may result in economic loss. Secondly, when confronting uncertainty, individuals prefer to have better control over their actions, and organisations such as business firms prefer to minimise surprises in their transactions with other parties (Pfeffer *et al.* 1976: p228; Peng, 2000: p43).

Considering the particular issue of market-entry into an emerging market, such as China, recent management literature reflects the difficulties in conceptualising the different sources and degrees of uncertainty and thus the measurement thereof. At the same time there is, to this author's knowledge, little research investigating the impact of uncertainty on a firm's internal environment and decision-making processes.

2.2.2 – Behavioural and Organisational Decision-Making

Contributions to decision-making theory come from philosophy, economics, political theory, sociology and psychology disciplines (Dunn, 1994; Keeney and Raiffa, 1993; Sexton *et al.* 1999; Nilsson and Jiliberto, 2004). Behavioural decision-making[64] is to understand how decision-makers, individual or unit, make decisions in an uncertain environment and how they can make the decision-making process more effective and efficient. Behavioural theories focus on the assumed behaviour of the decision-maker in an organisational context, and originate from the organisational theory of Weber and findings

[64] Following Nilsson and Jiliberto (2004: p26) the systematic study of decision-making processes is a relatively new discipline, usually named decision science, decision-making theory, decision analysis or behavioural decision research.

of behavioural decision theory by Simon (Weber, 1947; Simon, 1957). The development of heuristics and bias paradigms in the study of judgement under uncertainty and pursuit of prospect theory and framing in individual choice behaviour greatly contributes to the development of behavioural decision-making theory (Kahneman *et al.* 1982; Kahneman and Tversky, 1984; Kahneman, 1991).

Individual and organisational decision-making overlap greatly because many decisions in organisations[65] are made by individual managers. In this sense, the reference is to decisions made in organisational contexts. Behavioural decision theory, by contrast, deals primarily with judgement and decision processes of individuals, but not in an organisational or other context (Shapira, 1995: p4). Researchers of organisation theory question the validity and relevance of behavioural decision theory to real life situations. As managers are not immune to judgemental biases and cognitive implications of organisational behaviour this is relevant to strategic decision-making (Schwenk, 1984; Zajac and Bazerman, 1991; Bazerman, 1994).

Paramount is the recognition that rational decision-making models alone cannot explain the decision-making processes of a firm. It is more and more accepted that both qualitative and quantitative viewpoints enhance a stronger foundation for better decisions (Gregory, 2000). As a consequence both theory frameworks are important to this dissertation as they deal with the decision-making process of SMEs and where individuals, most likely the owner-manager, can make isolated decisions, but also where the wider context of the organisation is apparent.

2.2.3 – Taxonomy of Decision-Making Models

Many theorists see the analysis of the decision-making process as the key to understanding how organisations function.[66] From strategy literature, strategy is characterised by long-term planning and an integrative pattern of decisions. Various analytical frameworks have been developed that describe decision-making as rational or sequential, while others describe it as random and anarchical (Eisenhardt and Zbaracki, 1992: p17; Butler, 1997: p313; Nilsson and Jiliberto, 2004: p28).

[65] See Shapira (1995: p5): Characteristics that differentiate between organisational and individual decision-making are: (i) ambiguity is pervasive in organisations, (ii) decision-making in organisations is embedded in longitudinal context, it is an ongoing sequential process, (iii) incentives/penalties and impact play a role in organisations connected to long-term impact, (iv) repeated decisions are based on rules rather than on information processing, learning effects can be impaired, (v) conflict is pervasive in organisational decision-making. Hierarchical systems, authority and political system relations may have a large impact on the way decisions are made.

[66] See Simon (1947): According to Simon, the decision-making process is the core of all administration and organisation theory.

A focus on human problem solving, such as rationality and its different degrees, is found. Butler *et al.* (1993) argue that those decisions which manage to achieve an interaction between computation, bargaining, judgement and inspiration are the most effective in terms of objectives attainment and learning. This dissertation focuses on SMEs market-entry to China and the decision-making processes for FDI; the processes which must include consideration of human nature and how people make choices in different context settings. This is even more relevant in the particular situation of small firms when considering the development of organisations and the incidence of single decision-makers, in contrast to organisations where decisions can be made by a group of people.

2.2.3.1 Rationality

Organisational theory is a departure point for rationality theory and the basic principles of decision-making can be derived from utilitarian principles (Gore *et al.* 1992: p4; Nilsson and Jiliberto, 2004: p29). Rooted in historical development the literature has a strong normative or quantitative orientation. Therein decision-making is accompanied by strong goal orientation and justification of the aims (Harrison, 1987; Dean and Sharfman, 1993; Brauchlin and Heene, 1995; Nilsson and Jiliberto, 2004). The decision-maker is assumed to have:

(i) a fixed and unambiguous objective or set of values which are logically consistent,
(ii) almost unlimited time and money to spend on search and evaluation activities,
(iii) virtually perfect information on the probability of alternative outcomes, and
(iv) inexhaustible cognitive powers for comprehending, assimilating and retaining an infinite number of variables.

This translates into a common model of rational action as an extensive search procedure to explore all possible options and where, after application of the appropriate algorithms, an optimal choice can be made (Simon, 1957 and 1965; Lindblom, 1959; Cyert and March, 1963; Allison, 1971; Eisenhardt and Zbaracki, 1992). Significant value can be seen if a decision situation can be approached from a stance of how decisions can be made more rationally, which gives the baseline for establishing sound information to increase values, utility and quality in decision-making. Actions undertaken will, as a result, satisfy the decision-maker's preference hierarchy (Zey, 1998). A considerable danger is seen in breaking up the strategic question into components and losing an overview of the problem.[67] This touches on the scope of the rational player model in

[67] See Radford (1977: p17): Decision-makers usually desire to make a rational choice or to make one that will be judged to have been rational in the light of future events. However it has been observed that those dealing with complex problems consciously, or subconsciously, abandon an approach involving comprehensive models and the goal of a uniquely optimum solution. Instead, they adopt procedures they consider rational in the face of the complex decision problems encountered.

analysing managerial behaviour, as it is believed rational action[68] implies managers do not make mistakes and have power and wisdom (Etzioni, 1989: p123).

Limitations

It is virtually impossible for a manager to orchestrate all internal decisions, external environment events, behavioural and power relationships, technical and informational needs as well as the actions of intelligent opponents, as these do not come together at a precise moment (Fredrickson and Mitchell, 1984: p419; Dean and Sharfman, 1993: p589).

Rational decision-making needs to meet conditions that consider the decision-maker and the environment in which the decision takes place.[69] If this cannot be met, a departure from pure rational decision-making is possible, which may indicate the limits of a simplistic model of decision-making resting on economic theory only, but which also has to consider social and psychological science.

Often managers face situations that need continual modification of objectives without the necessary information. Control of variables might not always be possible[70] and, as a consequence, it is not feasible to attempt a search for each alternative (Simon, 1947: p75; Harrison, 1987: p77).

Several empirical studies reveal the cognitive limitations of decision-makers (Cyert and March, 1963; Pinfield, 1986; Janis, 1989; Jones *et al.* 1992; Snyman and Drew, 2003). It is observed that decision-makers, to avoid high risk, often select alternatives that even they do not expect will solve the problem and do not follow the norms of rational behaviour. Instead of a rational goal definition, followed by generation of alternatives and choice, the discovery of goals and choices through social processes is observed (Anderson, 1983).

Scholars have developed some constructs of rationality. These constructs approximate the rational model of decision-making. Decision-makers are understood to be rational to the limits of their own capabilities, that is bounded rationality, which stems from cognitive

[68] See Dean and Sharfman (1993: p588): Rationality is a fundamental assumption about individual behaviour used in building economic theory. Economists equate rationality with utility maximisation, a particularly stringent form of rationality where individuals seek to maximise their expected utility.

[69] Following Gore *et al.* (1992: p5) seven conditions have to be met for rational decision-making: (i) an economic objective, (ii) transitive and consistent preferences, (iii) unlimited information processing abilities, (iv) well defined mutually exclusive alternatives, (v) estimates of outcomes and values of each alternative, (vi) selection of alternative that maximises expected utility, (vii) unlimited information without time and cost constraints. The first three conditions refer to the individual decision-maker and the remainder are features of the decision environment.

[70] Following Nilsson and Jiliberto (2004: p32) rationality is also constrained by institutional norms such as laws, policies and codes of conduct.

and political realities.[71] Given these limitations, decision-makers aim to achieve objectives which are 'good enough' rather than the 'best' (Eisenhardt, 1997: p1; Elbanna, 2006: p3).

The relationship between rational decision-making and comprehensiveness[72] and organisational outcomes and effectiveness, especially performance, is widely discussed. There is no consensus among researchers since outcomes are often controversial, but, often, depending on the contextual environment, decisions are taking place (Fredrickson and Mitchell, 1984; Jones *et al.* 1992; Khatri, 1994; Goll and Rasheed, 1997). A positive relationship between rationality and performance, in a stable environment, is found by Fredrickson (1984), whereas Dean and Sharfman (1996) argue that the relationship between procedural rationality and decision effectiveness will be stronger in unstable environments than in stable ones.

Environment setting can limit rational action. The most prevalent argument is that more complex or turbulent environments require less rationality. Less rational behaviour however should not automatically mean an irrational decision-making process.[73] Strategic decision processes based on rational models should be accepted as having limitations and to only be appropriate for some environments. The question arises as to where the optimal point on the continuum is, or the degree of rational and intuitive inputs[74] (Fredrickson and Mitchell, 1984: p419; Eisenhardt and Zbaracki, 1992: p22; Dean and Sharfman, 1993: p587; Khatri and Ng, 2000: p78; Mintzberg and Westley, 2001: p93).

2.2.3.2 Bounded Rationality

More complex or turbulent environments can still be effectively dealt with by rational decision-making processes (Eisenhardt and Zbaracki, 1992: p21; Sinclair and Ashkanasy, 2005: p353), but it is proposed that new conceptual frameworks are needed.

Bounded rationality implies that a rational decision-making process takes place within the boundaries of the limited ability of human beings to be entirely value free and objective

[71] Following Elbanna (2006: p4) the complexity of the problem and the conflict among decision-makers often influence the shape of the decision process.

[72] See Fredrickson and Mitchell (1984: p399): Comprehensiveness is a measure of rationality and is defined as the extent to which organisations attempt to be exhaustive or inclusive in making and integrating strategic decisions.

[73] See Simon (1987: p57): The value of the economic model of rationality however must not be disproved. Sometimes the term rational, or logical, is applied to decision-making that is consciously analytic. The term non-rational is applied to decision-making that is intuitive and judgemental, and the term irrational to decision-making and behaviour that responds to emotions, or deviates from rationally chosen action.

[74] See Mintzberg and Westley (2001: p91): They make a distinction between decision-making processes into: thinking first, seeing first and doing first. The first is applicable in a more structured world and the last in a new unknown world. Strategies that assess weaknesses and strengths or rely on a firm's core competencies can go wrong as it is difficult to distinguish weaknesses and strengths in a new sphere.

(Nilsson and Jiliberto, 2004: p32). It also embraces limitations in information processing,[75] imperfect information, time and cost constraints, perception, memory and judgement (Simon, 1955; Harrison, 1987). Analysis may thus be limited to a minimum of alternatives, and decisions often reflect the use of standard operating procedures rather than systematic analysis (Eisenhardt and Zbaracki, 1992: p20). Theories based on organisational or behavioural studies concentrate on the ability to influence or control the decision-making process rather than the outcome, or the ability to act to ensure goals can be reached. These models are all satisficing[76] models because of bounded rationality and information limitations, which differ from maximisation.

As outlined by Eisenhardt and Zbaracki (1992: p21) the debate over whether decision-makers are rational or bounded rational is no longer very controversial (Elbanna, 2006: p3) as limitations to the rational paradigm can be explained. Researchers acknowledge that decision processes are often bounded rational and seek to improve rationality. Rationality and bounded rationality can even be seen as a continuum (Cosier, 1981; Janis, 1982, 1989; Nutt, 1989; Schweiger *et al.* 1986 and 1989, Cosier and Schwenk, 1990; Harrison and Phillips, 1991).

2.2.3.3 Intuition

Researchers present a fairly common view on intuition and intuitive events that originate beyond consciousness. Holistic and automated information processing takes place and intuitive perceptions are frequently accompanied by emotion (Parikh *et al.* 1994; Shapiro and Spence, 1997; Ben-Ze've, 2000; Miller and Ireland, 2005). However, there is little research on intuition[77] in strategic decision-making processes, and only recently has it been taken up by researchers (Simon, 1987; Parikh *et al.* 1994; Epstein *et al.* 1996; Khatri and Ng, 2000; Kukovetz, 2002; Klein, 2003; Sinclair and Ashkanasy, 2005). The current level of research shows some confusion on the conceptualisation, and, as a result, the measurement of intuition, while there are substantial differences between research approaches (Khatri and Ng, 2000; Sinclair and Ashkanasy, 2005). The earlier research

[75] See Simon (1955): Simon's critique on the maximisation principle is based on two issues. First, to maximise one has to have all relevant information. Second, people are limited in their ability to process information; hence, the chance people would be able to maximise is rather small.

[76] See Harrison (1987: p122): Satisficing means finding a satisfactory, rather than an optimum, course of action. The satisficing decision-maker differs from the maximising decision-maker in that constraints, both internal and external, limit global rationality, and consequently behaviour depends on certain attributes of the decision-maker – for example, desire to achieve, level of aspiration, persistence and perceptions.

[77] Some definitions of intuition: Parikh *et al*. (1994: p57) conclude that intuition is something of an antithesis to logic and reasoning, gut feeling, sixth sense and subconscious process. Klein (2003: p4) defines intuition as the way we translate our experience into action. Sinclair and Ashkanasy (2005: p353) emphasise the non-sequential information-processing mode, which comprises both cognitive and affective elements and results in knowing without use of conscious reasoning. Sinclair and Ashkanasy (2005: p355) argue there is a lack of agreement on what constitutes intuition, accentuated by sparse terminology, which results in a profusion of inconsistent or even contradictory definitions.

was conducted with a qualitative orientation (Landry, 1991; Little, 1991; Ferguson, 1999; Petitmengin-Peugeot, 1999) and later approaches began to take on an exploratory approach in quantitative form[78] (Parikh *et al.* 1994; Burke and Miller, 1999).

Khatri and Ng (2000) show various relationships between the use of intuition[79] in decision-making and organisational performance. Remarkably their research, to this author's knowledge, is the first that differentiates between stable and unstable environments, within different industries, and between financial and non-financial performance outcomes.[80] Other research shows that intuition is positively associated with faster decisions and managers who react more quickly (Eisenhardt, 1989a; Wally and Baum, 1994).

Management scientists more often adopt the psychological model of intuition and primarily deal with the aspects of process, experience and prerequisites for intuitive information processing. But field research in a management context is basically non-existent, albeit intuitive synthesis is assumed an important strategic process factor which managers often use in strategic decision-making.[81] Some researchers consider the theory of strategic decision-making has to take both rational and intuitive processes into account[82] (Pondy, 1983; Simon, 1987; Kukovetz, 2002). Advances in cognitive science and artificial intelligence support the value of intuition and note that intuitive processes stem from long experience and learning,[83] and the mass of facts, patterns, concepts, techniques, abstractions and what can be called formal knowledge or beliefs, which are impressed on our minds (Prietula and Simon, 1989; Agor, 1990; Harung, 1993; Seebo, 1993; Khatri and Ng, 2000; Hüllermeier, 2001).

Although there are some contradictory research results, which make it difficult to compare and replicate findings, intuition appears to have substantial face validity and can be considered relevant for strategic decision-making and solving ill-defined problems

[78] See Wozniak (2006: p8) and Sinclair and Ashkanasy (2005: p363), Measurements aiming at assessment of intuition are: Myer-Briggs Type Inventory (Myers, 1962), Test of Intuitive Ability (Westcott, 1968), Intuitive Management Survey-AIM (Agor, 1989), Intuitive Profile-IQ2 (Cappon, 1993), International Survey on Intuition-ISI (Parikh *et al.* 1994), Intuitive Cognitive Style Index-CSI (Allinson and Hayes, 1996), Faith in Intuition (Epstein *et al.* 1996).

[79] Intuition is conceptualised within judgement, experience and gut feeling.

[80] The analysis was carried out among 221 firms in the banking, computer and utility sectors. It is noted that only three industries were selected and the limited number of participating firms does not allow generalisation. Furthermore the self-reporting of measures within research on intuition has to be considered. Personal bias, values and misperceptions can influence responses.

[81] See Khatri and Ng (2000: p77): In their research two variables to measure intuitive synthesis, namely experience and judgement, are used extensively in strategic decision-making.

[82] Following Mintzberg (1994) it is argued that the term 'strategic planning' is an oxymoron. Mintzberg argues that strategy cannot be planned as planning is about analysis and strategy is about synthesis.

[83] See Khatri and Ng (2000: p58): Often researchers develop the view that intuitive processes fall into the realm of the irrational or paranormal.

(Parikh *et al*. 1994: p60; Kukovetz, 2002: p213; Sinclair and Ashkanasy, 2005: p354; Miller and Ireland, 2005: p29). Intuition in this respect can be interpreted as experience-based decision-making,[84] applicable within more complex decision situations (Parikh *et al.* 1994).

2.2.4 – Strategic Decision-Making Processes

There is a wide debate in economic and management research if, and how, strategic decisions differ from ordinary decisions (Nippa, 2001). For the main categories of strategic research a differentiation into context, content and process of strategy is made (Ketchen *et al.* 1996; De Witt and Meyer, 1999; Elbanna, 2006). Strategic decisions have attracted considerable research attention and different models of decision-making have developed (Ireland and Miller, 2004). The earlier models tend to be normative and prescriptive.

Normative theories of decision-making, such as classical economic theory, propose that decision-makers follow a highly hierarchical and rational procedure for making decisions distinguished by different levels[85] of decision-making (Von Neumann and Morgenstern, 1944; Hofer and Schendel, 1978; Higgins, 1982; Pettigrew 1990; Schneider and De Meyer, 1991; Rajagopalan, *et al.* 1997). The normative models of management science have a significant influence on the routine work of the lower and middle levels of organisations and almost no influence on the higher levels. On the premise that a model links the theoretical world of our minds with the empirical world of our senses, different decision-making models have developed. They are the result of differing perceptions and of the application of these perceptions to diverse decision situations. The later models of decision-making are of a descriptive nature and characterise levels of decision-making as more closely related to each other[86] claiming rationality cannot be assumed in every decision-making situation. Thus a generic view of the decision-making process has developed an understanding that strategic decision-making processes are not necessarily deterministic or programmable as a whole and take place in distinctive phases or intervals (Witte, 1972: p180; Mintzberg *et al.* 1976: p274; Gore *et al.* 1992: p14; Nippa, 2001: p15).

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[84] See Simon (1987: p61) and Kukovetz (2002: p144): Quick decisions can be less rational and less order in sequential analysis is applied. Experience-based intuition allows the decision-maker to decide faster with a given accuracy of the decision outcome, as well as a more accurate decision for a given decision-making speed. Thus no matter what combination of speed and accuracy a company targets in its decision-making process, experience-based intuition will allow it to be more efficient.

[85] In practice the total decision space can be divided into three categories: strategic, administrative and operating decisions. Strategic decisions are primarily concerned with establishing a match between the firm and its environment and specifically with the selection of the product-market combination. These strategic decisions are made at the upper end of the organisation and have relevance for the continuity of the organisation (Ansoff, 1965; Heller, 1992: p59; Gore *et al.* 1992: p4).

[86] Lower-level decisions affect higher-level decisions (Simon, 1960; Drucker, 1967b).

Strategic decisions have the notion of being at the discretion of top management, often with a long-term effect, affecting the application of the firm's resources to secure the survival of the firm. Strategic decisions reflect the interaction between an organisation and its environment,[87] often with a high level of uncertainty, and show how an organisation manages this relationship (Mintzberg *et al.* 1976; Ginsberg, 1988; Pettigrew, 1992; Dean and Sharfman, 1996, Nippa, 2001; Wilson, 2003). Elaborating on the notion of uncertainty Harrison (1987: p20) argues that strategic decision-making is not text book decision-making under uncertainty where alternatives are given even if their consequences are not, but decision-making under ambiguity where almost nothing is given or easily determined.[88]

The current level of investigation bears relevance for this study project taking into account:

(i) the characteristics of strategic management strongly relate to decisions by groups of people; although the aspect of individual decision-making is being discussed, many different individuals or groups can be involved or influence strategic decision-making,[89]

(ii) the particularities of SMEs have not been the broad focus of past investigation, where levels of management may not even exist. Sometimes there is only one decision-maker,[90] the owner or manager, and firms might be limited in their diverse resources,

(iii) there is practically no literature available that looks at performance in decision-making and thus a particular decision-making process,[91]

(iv) strategic decisions and processes, compared to regular decisions, need to consider the aspect of time and the variability of influencing factors needs to be

[87] Following Pettigrew (1992) strategic decisions are embedded in both inner context [psychological, structural, cultural and political factors] and outer context of the organisation [competitive factors].

[88] Strategic decisions, according to Harrison (1987) and Schwenk (1988) are complex and grouped into (i) classification – non-programmable and non-routine, unique, creative, innovative, (ii) structure – novel, un- or ill structured, uncertain cause/effect relationships, decision criteria may be unknown, outcome preferences may be certain or uncertain, (iii) strategy – reliance on judgment, intuition, creativity and heuristic problem-solving techniques.

[89] See Papadakis *et al.* (1998: p133) and Hambrick and Snow (1977: p112): Strategic decision-making has to be considered within the interplay of decision-specific management, environment and organisational factors, where the decision-specific characteristics have a dominant role in determining a decision process. Decision-specific characteristics moreover contain generic attributes [perceived magnitude of impact, frequency/familiarity, uncertainty, threat/crisis, significance/influence of the decision-making process] used in objective categorisation by the decision-maker.

[90] Strategic decisions are seldom made by chief executives acting alone – they are usually the product of the dominant coalition, the most influential members of the top management group (Hambrick and Snow, 1977; Hill and Wright, 2001; Etemad, 2004).

[91] See Drucker (1967a: p96); Brunsson (2000: p31); Elbanna (2006: p12): To complete the model of strategic decision-making and success, one needs to include how well decisions are implemented because of the potentially significant impact of implementation on strategic decision success. An organisation's main problem is not choosing; it is taking organised action and implementation.

considered.[92] Elbanna (2006: p12) argues that strategic decisions by companies are not entirely based on one process, but may arise from a number of processes.

Researchers consider that in firms, and this was specifically underlined for SMEs, the decision-maker's characteristics, such as knowledge, past experience, attitudes and motivation, play a key role in the internationalisation decision of the firm (Cavusgil, 1984: p19; Bloodgood *et al.* 1996: p64; Papadakis *et al.* 1998: p134; Evangelista, 2005: p184). It is argued that attitudes of decision-makers in SMEs, rather than environment factors, can propel them into internationalisation (Welch and Luostarinen, 1988: p34; Calof and Beamish, 1995: p116; Papadakis *et al.* 1998: p133; Holbrook *et al.* 2000: p1038). To attain international success, a firm not only has to have the appropriate product and strategy, but its decision-makers must also have appropriate attitudes. It is these attitudes that determine how decision-makers perceive the benefits, costs and risks of internationalisation[93] (Chetty and Campell, 2003: p801). International strategy, and thus its process, rests heavily on leadership styles and their understanding of decision-making theories (Kedia *et al.* 2002: p49).

2.2.5 – Conclusion on Decision-Making

As various decision models have developed, knowing their differences is important when analysing new decision problems; decision problems in environments shaped by uncertainty. The selection of an appropriate decision strategy is important and such selection must not detach the decision problem from the later process. It is argued that strategic decisions by companies are not normally only based on one process, but can depend on a number of processes. Normative, descriptive and prescriptive aspects of decision-making are simultaneously relevant within a decision process.

Mintzberg *et al's.* (1976) strategic decision-making process, sub-divided into identification, development and selection phases, shows the process contains rational as well as less rational elements. Explicitly the model includes feedback loops based on learning by doing, building an increasing stock of inherent knowledge and assisting a possible rational approach to decision-making. Implicitly the model shows the decision process is an evolvement over time built on information needs. In earlier times explicit formulation of information under time constraints was not common. Rather strategic behaviour was shaped by rational approaches and based on unlimited resources such as information and time. The continuous appreciation of new information in the decision

[92] See Nippa (2001: p16): A strategic decision process depends on rich and intensive information and communication, and qualitative and quantitative data. The time frame and variability of influencing factors frequently make it possible for decision-makers to manipulate risk and outcomes of strategic decisions.

[93] Following Haeusgen (1997: p165) a company's internal culture able to accept risk, moves faster through an internationalisation process. Such companies, as a result, are more likely to be inclined to undertake equity investment.

process is crucial to revalidate the process on the way forward. This helps measure the decision-making performance while an incremental development allows corrections to the process.

The implementation of final decisions has been largely ignored in most decision models, but decisions have a significant implementation phase over time, which touches on the point that authorisation, modelled after Mintzberg *et al.* (1976), and implementation must not be detached from the decision process. The context in which the decision process takes place, such as in a dynamic environment of an emerging market, must be considered and only proof that a decision taken is accepted by its agents, and is workable, renders the process acceptable. Most decision models are thus static and rather descriptive in nature, and fail to explain how decision processes are performing. These findings bear relevance for further research.

The characteristics of strategic management relate strongly to decisions by groups of people, and although the aspect of individual decision-making is discussed, many different individuals or groups are actively involved in, or influence, strategic decision-making. SMEs in particular, where levels of management may not even exist, sometimes with only one decision-maker, who is the owner/manager, and where firms might have limited resources, have not been the broad focus of investigation. Pertinent characteristics of SMEs must be considered in further research. The decision-maker's characteristics, including past experience, knowledge, attitude, motivation and cognitive ability, play a key role in internationalisation decisions of a firm. The attitudes of owner-managers in SMEs, rather than environment factors only, propel them into internationalisation.

To attain international success, a firm must not only have the appropriate product and strategy, but its decision-makers must also have appropriate attitudes. These attitudes determine how decision-makers perceive benefits, costs and risks of internationalisation. International strategy, and thus its process, rests heavily on leadership styles and understanding of decision-making theories.

It is recommended that a holistic analysis model for decision-making processes, especially for SMEs, must be developed. The model must be applicable from several viewpoints, for example, dynamic and unstable environments, small firms and their resources, owner-manager characteristics and learning ability. The model must consider that the decision process can have an incremental development. The wider context should include the decision pre-phase and implementation phase, and a decision process must have the capability of evolving, with learning and cognition taking place, to develop an effective decision process.

A decision process should be acknowledged as open-ended, and not be limited to the immediate debate on whether the decision-making process is more rational or more intuitive. More importantly it must incorporate the different strands of theories without limiting itself to only a few concepts.

2.3 Foreign Direct Investment

Globalisation increases cross-border commercial activities, with these activities encompassing investment, international trade, capital flows and the migration of labour (Nicholas and Maitland, 2002: p7; Jones and Wren, 2006: p19). Consequently the worldwide flow of FDI has increased tremendously,[94] with the largest part of FDI into developing economies.

Foreign investments, according to the International Monetary Fund [IMF], are divided into Foreign Direct Investment [FDI] and Foreign Portfolio Equity Investment [FPEI]. Until the 1960's economic theory did not differentiate much between FDI and FPEI and considered international companies as mere arbitrageurs of capital seeking to maximise their returns internationally (Ronge, 2001; p13). Then a new point of view developed based on Hymer's findings (Hymer, 1960) that asserted Multinational Enterprises [MNE] transferred an entire bundle of resources across borders rather than just capital, which can only be explained by considering firm-specific characteristics. As a consequence today the internationalisation process of firms is mostly explained in terms of economics (Buckley, 1996: p24). If the current OECD's definition for FDI[95] is considered it is understood that the target of the investor is to gain part or all of control in the invested company in the host country. Hence the OECD's definition is synonymous with Hymer's definition (Hymer, 1960).

As the FDI process reflects the strategic direction of the firm, an understanding of FDI must pre-suppose an understanding of internationalisation as a strategic process (Edwards, 2002: p41; Kukovetz, 2002: p24) and thus how to place a firm in its host environment. It is thus appropriate to consider FDI on a macro-economic and micro-economic level.[96]

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[94] See UNCTAD (2006a). Worldwide Foreign Direct Investment [FDI] and FDI inflow to China in 2005. See also www.unctad.org/fdistatistics. The yearly world FDI inflow increased from US$ 618b (2002) to US$ 916b (2005). It was on a yearly average of US$ 495b between 1990 and 2000.

[95] See UNCTAD (2006b): FDI refers to an investment made to acquire a lasting interest in enterprises operating outside the economy of the investor. In cases of FDI, the investors' purpose is to gain an effective voice in the management of the enterprise. The foreign entity or group of associated entities that make the investment is termed a 'direct investor'. The unincorporated or incorporated enterprise – a branch or subsidiary, respectively, in which direct investment is made – is referred to as a 'direct investment enterprise'. Some degree of equity ownership is almost always considered to be associated with an effective voice in the management of an enterprise; a threshold of 10 % of equity ownership is suggested to qualify an investor as a foreign direct investor.

[96] See Hymer (1960): Hymer criticises the macro-level FDI theory for being too general. It does not account for the anomalies associated with a bird's eye view of a situation. Details cannot be seen and are

2.3.1 – The Nature of FDI

The extant literature on reasons *why* FDI occurs is explanatory in nature, and takes a macro-economic view when the impact of FDI is explained, with FDI attributed to several factors:

- Increased levels and changes in technology,
- Greater liberalisation of trade and changing trade flows,
- Effects of exchange rates and taxes,
- Investment,
- Ownership and de-regulation, and
- Privatisation of markets in many countries (Strange, 1997: p24; Blonigen, 2005: p2).

Yet internationalisation of a firm, which can lead to equity participation in a foreign country, is a process of increased involvement in international operations; which requires adapting a firm's strategy, resources, structure and organisation to an international environment[97] (Graham, 1978; Welch and Luostarinen, 1988; Calof and Beamish, 1995; Dunning, 2002). Early international business scholars argued that international diversification for firms is important because it is based on exploiting foreign market opportunities;[98] internationalisation increases the firm's competitive position (Ansoff, 1965; Rugman, 1979; Mintzberg, 1987) and expands a firm's development beyond its local boundaries.

These factors have led to increased competition between firms; in turn leading to cross-border mergers and acquisitions, joint agreements and establishment of new companies as firms seek to reduce costs and increase competitiveness in the global economy. This has supported the phenomenon of internationally-active companies, with the term multinational enterprise [MNE] traditionally used to describe larger companies or other entities established in more than one country, and so linked that they can co-ordinate their operations in various ways (OECD, 2000: p17; Dunning, 2002: p2; Bora, 2002: p8). Although MNE is a commonly accepted term to describe larger firms, it is not explicitly related to the effective size of a company, albeit some scholars treat multinational

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thus not accounted for. According to the macro-level theory of FDI, industries in capital-intensive countries will invest in capital-poor, but labour-intensive countries to maximise profits. Hymer offers an alternative, a micro-level theory, which is firm-specific, rather than country-specific. Note: Hymer's theory was written in 1960 but not published prior to 1976.

[97] See Jones and Wren (2006: p39): The notable feature of the strategic approach to FDI is that it believes an initial inflow of FDI into a country will produce a reaction from local producers in that country, so FDI is a dynamic process. Firms engage in strategic activity not only to gain extra market share directly, but to threaten potential entrants and other firms from expanding.

[98] See Strange (1997: p21): Strange divides FDI into seven types: (i) to gain access to specific factors of production [resources, technical know-how, patents, brand names], (ii) to gain access to cheaper production factors, (iii) for mutual investment, also with competitors, to gain access to each other's production ranges, (iv) to secure access to customers in host-country, (v) to facilitate tariff-jumping, ease of import into host-country, (vi) to access future markets and (vii) to establish protective barriers.

enterprises and foreign direct investment, related to larger firms, as one and the same thing (Dunning and Pearce, 1995; John *et al.* 1997).

A significant stream of research on macro-level FDI focuses on host and home country impact and country development, and on institutional development of the countries involved[99] (Peng, 2000; Child and Tse, 2001; Meyer, 2001; Xu and Shenkar, 2002; Trevino and Mixon, 2004). Topics on technology transfer and impact, development of legal systems, trade and employment and effects on industrialisation are widely discussed. A common belief is that the attraction and settlement of foreign companies in host countries brings an increase in capital income and skilled labour, higher technology and greater productivity (Hanson, 2001). At the same time productivity and market-access 'spill-over' can take place[100] (Markusen, 1998). Such a spill-over has a positive impact on the host economy and should be taken into account during investment decisions (Gorg and Greenway, 2004). Recent research on spill-over effects is not conclusive as it is more and more evident that negative spill-over, or reverse spill-over, surfaces, as in the case of 'technology sourcing' of foreign firms in a host country (Jones and Wren, 2006: p89).

FDI brings dynamic institutional framework conditions that may be acceptable to larger and stronger firms, but may have a bigger, less acceptable, impact on smaller firms.[101] The phenomenon of *why* FDI occurs is of significance for the individual firm and for environment development in the host country. It is imperative this be considered in the environment analysis of any firm and its influence on the decision-making process.

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[99] See Busenitz *et al.* (2000: p995): The three pillars of institutions are distinct, a division that has been validated empirically: (i) the regulative pillar rests on the setting, monitoring and enforcement of rules based on instrumental logic and uses legal sanctioning as the basis of legitimacy, (ii) the normative pillar prescribes desirable goals and the appropriate means of attaining these; legitimacy is rooted in societal beliefs and norms, (iii) the cognitive pillar highlights internal representation of the environment by players; legitimacy is anchored in cultural orthodoxy. Xu and Shenkar (2002) suggest each of the pillars produces its own measure of institutional distance and these measures vary in terms of their implications for a company's behaviour, while pillars can also interact. Rather than explaining competitiveness by economic theories it is also explained by national differences in organisational principles and societal institutions, which coincide with the internationalisation process model, viewed as a series of incremental adjustments to changes in the firm and its environment. Thus Kostova (1999: p316) proposes that the larger the institutional distance, the more difficult it is for the company to establish legitimacy in the host country and to transfer strategic routines to foreign subsidiaries.

[100] See Jones and Wren (2006: p72): Productivity spill-over takes place when domestic companies increase their productivity in the wake of settlement by a foreign company. Market-access spill-over takes place when domestic companies are able to gain knowledge on markets foreign firms are active in, such as distribution networks or export markets, and use this information to their own advantage.

[101] See Wang (2002: p52) and Dunning (2002: p62 and p182): Wang in research on Western SMEs doing business with China establishes a framework of success and risk factors that distinguishes between market competitiveness, human resource management, entry-dependent, strategic and operational management, cultural understanding and network-related factors. The framework explicitly indicates external factors, such as country and policy change risks, beyond the control of SMEs. Dunning argues that organisation theory has generally neglected government-related and other exogenous variables in the examination of decision-making practices of firms. This is especially of relevance as more and more SMEs participate in FDI decisions and consider host-country conditions.

2.3.2 – FDI Theory

Hymer (1960) claims the expansion of a firm beyond its boundaries and into a new country does result in internal movement of finance and resources, specifically from the mother company to its new subsidiary; which was not considered in earlier theories. FDI is where the investor wishes to gain control over the production activities of the foreign enterprise, which is the basis of Hymer's theory. A stronger focus on organisational theory and a firm's development must be considered on the micro-economic level. Since earlier FDI concepts stem from a macro-economic view this is the initial position the following sections are based on, with a subsequent shift into discussing the micro-economic level of FDI.

2.3.2.1 Macro-economic FDI

The macro-economic aspects of FDI motivated various researchers into understanding the Export-FDI relationship (Kojima, 1975; Markusen, 1995; Egger and Pfaffermayr, 2000; Markusen, 2002; Helpman, 2006). The inter-relation between FDI and trade,[102] and, as a consequence, the change of trade flow patterns is an early objective of research on the macro-level of FDI. Depending on individual country characteristics FDI can support, or even substitute, trade. Initially a country focuses on its comparative cost advantages. But these factors do not stay constant over time, influenced by transfer of capital, technology and management resources (Kojima, 1975). Establishing international divisions gives rise to patterns of international 'trade flow' (Daniels and Radebaugh, 1998; Heiduk and Prinz, 1999).

The product cycle of international trade (Vernon, 1966) combines the view of how products mature with the evolution in a firm's international activities,[103] and shows patterns of trade and investment change over time. This explains *why* macro-level FDI and host country production is established as lower factor costs can be utilised, for example, in developing countries. Vernon's life cycle theory helps one understand the different stages a product occupies and, as such, indicates when production in another location is less costly. Vernon's product cycle theory, similar to the Uppsala model, seeks to focus on the long-term development of the firm and its environment.

[102] See Heiduk and Prinz (1999: p31): The impact of FDI on trade is analysed according the Heckscher-Ohlin model.

[103] See Jones and Wren (2006: p30): The distinctive stages are: (i) product development or innovation phase [needs to be close to the innovator, producer and market], (ii) maturing products [increased standardisation can lead to economy of scale] can give incentive to produce abroad, (iii) standardised products; competition will grow and cost reduction is necessary. The theory looks at FDI as a dynamic process in terms of why, when and where it occurs.

The chain of establishment,[104] or Uppsala model, is one of the earlier schools of thoughts and draws on the assumption that market-entry into new markets is the result of a series of incremental decisions.[105] It theorises the staged development from sales and export, to subsidiary, and into production/manufacturing plants (Johanson and Wiedersheim, 1975; Johanson and Vahlne, 1977). The Uppsala model is mainly characterised as a firm's development over time from one phase into another, with progression through the stages driven by experiential knowledge accumulation.[106] It explains *why* FDI happens as a logical development for the firm in incremental steps and as complementary to export. It has been argued that if the chain of establishment is not too deterministic its own logic leads to incorrect predictions of the firm's development.

Three exceptions to the incremental process (Johanson and Vahlne, 1990; Andersen, 1993) are:

(i) Large firms can take bigger internationalisation steps,
(ii) When markets are stable, knowledge can be gained in ways other than through experience,
(iii) Experience in similar markets may allow a firm to generalise this experience.

More recently the model has been challenged when firm's started to leapfrog certain stages of the internationalisation chain and showed an accelerated internationalisation process (Rennie, 1993; Oviatt and McDougall, 1994; Madsen and Servais, 1997; Shrader *et al.* 2000; Andersson and Wictor, 2003). Under these circumstances FDI need not necessarily be viewed as complementary but can rather be considered as a substitute for export.

2.3.2.2 Micro-economic FDI

Internalisation Theory

The internalisation theory of FDI is based on Coase's theory of the firm (Coase, 1937), which examines the role transaction costs[107] play in the formation of organisations and

[104] Although listed here under the macro-level heading the Uppsala model is considered a micro-level economic model.

[105] See Cavusgil (1980): A distinction between the so-called Uppsala [U-model] and innovation related model [I-model] is made where a linking effect of learning is sought. It has been generally criticised that the time effect on the step-wise development of the firm is neglected (Ayal and Raban, 1987; Turnbull, 1987; Millington and Bayliss, 1990; Andersen, 1993). Rennie (1993: p45) shows a tendency for increased internationalisation speed with the 'leapfrog' of some stages.

[106] See Edwards (2002: p30): The Uppsala model has a second strand which asserts that the location pattern of FDI is determined by 'psychic distance', defined as the cost of acquiring and internalising relevant information about business conditions in other countries, the perception of risk and uncertainty involved in foreign operations, and the resources required to gain access to foreign networks. The model asserts that the costs involved in overcoming psychic distance decline over time as a function of the experience gained by the firm in each market.

[107] See Casson (1979): Casson shows an overview of transaction costs. The most important transaction costs are: costs for information, negotiation and enforcement of contracts.

which have to be optimised due to market imperfections. Specific assets, the frequency of economic exchange and uncertainty surrounding the exchange of resources, represent the core dimensions of the transactions. The composition of these dimensions is decisive for the way in which cost efficient governance modes are assigned to the transaction (Andersen, 1997: p33; Coviello and McAuley, 1999: p226; Dunning, 2002: p162) and, more importantly, how they can create a competitive advantage.

The process of internalisation is developed to explain international production and FDI (Buckley and Casson, 1976; Hennart, 1982; Dunning, 1988; Ietto-Gillies, 2005). Buckley and Casson take the approach that the subsidiary of the mother company takes on two roles: i) the production of goods and services, and ii) the activities of marketing, training, research and development, management techniques and involvement with financial markets. These activities are independent and connected by intermediate products, taking the form of material, products or knowledge and expertise. If the markets for the intermediary products are imperfect an incentive arises for the firm to internalise these, provided the benefits exceed the costs. When it occurs across national boundaries of a company FDI most likely occurs.

According to Caves (1971), who made the link between industrial organisation theory and Hymer's theory, a distinction between horizontal and vertical FDI has to be made:[108]

- Horizontal FDI takes place when the firm possesses unique or intangible assets which others do not have, such as superior knowledge or information about its products and its markets. But horizontal FDI also takes place when profits in the host country depend on successful local production. Horizontal integration can be understood as substituting export into local production and explains international development over stages (Johanson and Vahlne, 1977; Kamm, 2001).
- Vertical FDI occurs at different stages of production within the same industry and results in a high dependency between stages, often at high investment costs. Such dependency can be for technological and quality reasons, but is also influenced by cost reasons; such as transfer pricing or general factor costs (Bora, 2002; Jones and Wren, 2006). The existence of vertical FDI can be explained by the integration of intangible assets and imperfections of the market. Additional safeguarding is needed to secure such vertical integration over time.[109]

[108] See Markusen and Maskus (2001) and Dunning (2002): The choice between vertical and horizontal production structures depends on country characteristics, such as relative size and relative environment differences, as well as trade and investment cost. Other reasons are economy of sale, different consumer needs and tastes, mix of natural resources and capabilities and factor costs.

[109] A typical approach to vertical FDI is where firms keep management and strategy related factors such as R&D in the home country, and low cost production in a foreign place, in common parlance called 'outsourcing'.

Research into the differences between horizontal and vertical FDI is not yet conclusive (Bora, 2002) but an understanding of the differences is of great importance since it is also thought to be a matter of available resources.

Dunning's Eclectic Paradigm

Critics consider Hymer focuses too much on the market-power approach – control over activities – and ignores Coase's transaction costs and *how* a firm operates efficiently in other countries (Dunning and Rugman, 1985; Yamin, 2000; Cantwell, 2000). Hymer elaborates on large companies and the main goal of achieving profits through expansion and gaining size, rather than through ownership advantages. But today not only oligopolist firms invest abroad and increasingly SMEs are entering the international arena. It is thought that scale, or market power, as the objective for strategy is outdated and ownership advantages are keys to the creation of successful MNEs.

Dunning (1979; 1980), influenced by the theories of Coase, Hymer and Vernon, proposes the eclectic paradigm of FDI. The proposal integrates several strands of cross-border business activities with international trade theory, with a resource-based view and the transaction cost theory as its main pillars. The resulting eclectic theory, or OLI paradigm,[110] can be considered as a bridge to the macro-level view on ownership advantages:[111]

- (O) addresses *why* companies go abroad; the ownership advantages,
- (L) *where* to go and the micro-level view of internalisation advantages, and
- (I) addresses *how* FDI is being carried out.

Dunning's eclectic paradigm of FDI states that a firm will only directly invest in a foreign country if it fulfils the three OLI conditions.[112] The eclectic paradigm poses a holistic

[110] See Dunning (1979; 1980) and Fasano (1999): Enterprises engage in overseas production when they possess net competitive advantages over firms of other nationalities, which can best be exploited by foreign rather than domestic production, and which are more profitable to internationalise than to sell or lease to other enterprises. It is possible to identify these advantages and disadvantages, all of which arise from imperfections in product or factor markets, or physical or psychic distance between countries or government. Three elements determine a multinational enterprise's international competitiveness, the geographical configuration of its asset base and its organisational structure. The three elements are: (O) Ownership specific advantages, (L) Location/host-country specific factors and (I) Internalisation advantages, commonly expressed as OLI.

[111] See Fasano (1999: p23) and Jones and Wren (2006: p36): Within the internalisation theories and paradigms, only Dunning explicitly mentions size as a particular asset of a company. Dunning elaborates on 'which' companies decide to produce in a foreign country.

[112] See Dunning (1979; 1981; 1988) and Jones and Wren (2006) for detailed OLI advantages related to country characteristics. FDI is undertaken if three conditions [hypotheses] are met: (i) enterprises must possess net ownership advantages compared to companies of other countries in their markets, (ii) internalising the use of resources in which they have an advantage is more profitable than selling them on external markets, (iii) if the first two requirements are fulfilled, the host country must offer special location advantages which, in conjunction with those derived from ownership and internalisation, are more than exporting to that country from a home production base.

framework to explain export and FDI behaviour.[113] Its strengths, compared to other theories, are in looking at the specific location, host country and factors of the FDI. Dunning and others have continuously refined the eclectic paradigm over recent years and more recently expanded it with a cultural component and strategy considerations (Woodcock *et al.* 1994*;* Jones, 1996; Dunning and Bansal, 1997).

The strengths of the eclectic paradigm is characterised by its richness[114] and creativity. The strengths also, however, represent potential weaknesses since the basic theories can provide complementary but also overlapping explanations. It can be argued that a focus on internalisation and location factors only can be sufficient. Ownership advantages are derived from the possession of intangible assets and from internalisation itself (Itaki, 1991). For Casson (1987: p32) the possession of intangible assets is not a necessary condition while the second type of advantage, as an ownership advantage, is tautological.

The creation of core competencies requires a focus on ownership advantages as a key element of competitive success (Cantwell, 2000: p44). A narrow concentration on single advantages, for example, on firm-specific advantages, seen as the most important requirement to be successful in a foreign country, can prevent trade-offs between other location factors. This can result in a situation where a less appropriate market-entry mode will be selected.[115] As a consequence the eclectic paradigm, to be fully utilised, means careful consideration of all the OLI factors, which increases the complexity of the analysis.

Organisational Capability

The organisational capability [OC] perspective is based on the notions of bounded rationality and the resource-based theory (Penrose, 1959; Andersen, 1997). According to Madhok (1997), the OC perspective perceives the firm as a bundle of relatively static and transferable resources, which are the basis for competition (Prahalad and Hamel, 1990;

[113] See Kamm (2001: p43): The eclectic paradigm also explains market-entry through licensing which is not further elaborated on here.

[114] See Kamm (2001: p47): Several input factors have to be considered: Market position and size, transportation and communication costs, exchange risks, trade barriers, protectionism, influence of taxes etc. It is however not clear how they interact with each other and what the conditions are where each parameter is (i) significant and (ii) at the level where it triggers internationalisation. As a consequence the location advantage is difficult to measure.

[115] See Andersen (1997: p35): The concept of location advantage is also likely to have a direct influence on international market selection [IMS]. The interrelationship between choice of entry mode and IMS has been recognised by other authors but one still does not know the nature of this interrelationship. Most entry mode literature assumes the entering firm has the option to choose an entry mode in a given country. The assumption that the choice of entry mode and IMS can be regarded as independent decision processes may not be true. For instance, do firms select a country where the location advantages are perceived to be great [e.g. high market potential, low production costs] but where government restrictions narrow the feasible set of entry modes.

Cantwell, 1991) and development of a firm's capabilities.[116] As a result individual skills, organisation and technology are inextricably woven together in considering the overall value of the firm and not only the factor of costs[117] (Nelson and Winter, 1982; Amit and Schoemaker, 1993; D'Aveni, 1994; Madhok, 1997).

Attention is shifted from the characteristics of the transaction to the capabilities of the firm.[118] The OC contrasts with the internalisation perspective. Where the latter focuses solely on market failure and the transaction cost involved, OC looks at the limits of a firm's capabilities and the boundaries of the firm. The internalisation approach focuses on exploitation of advantages whereas OC looks at the development of such advantages. The key distinction between the attributes of cost and value is emphasised and the consequence of applying different management approaches.[119] As a result, a broader approach for the management of a firm's capabilities, and how new capabilities could be created while exploiting existing capabilities in a competitive external environment, is suggested (Itami and Roehl, 1987).

Information management to broaden the firm's knowledge is the key to the OC approach. Understanding this can bring constraints when entering new and unfamiliar markets at a great distance from the firm. In such situations, an alternative is to supplement the firm's resources by acquiring know-how from others and subsequent integration into a firm's knowledge base. In terms of foreign market-entry the ratio between embedded [more specific] and generic [general] know-how determines if an individual firm has a preference for internalisation or for collaboration (Madhok, 1997). It is proposed that in the event of exploitation of an existing advantage of a firm, where the potential for erosion in the value of a firm's know-how due to ownership effect is greater than that due to the location effect, there will be a greater preference for internalisation. Conversely, if the potential for erosion in the value of a firm's know-how due to the location effect is greater than that due to the ownership effect, there will be a greater preference for collaboration[120] (Madhok 1997: p49; Solberg *et al.* 2002: p4).

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[116] See Madhok (1997): This line of argument is theoretically and intellectually rooted in behavioural theory (Cyert and March, 1963) and the evolutionary theory of the firm (Nelson and Winter, 1982).

[117] See Peteraf (1993) and Madhok (1996): Due to the idiosyncratic nature of firm-specific resources and capabilities, these resources are specialised to a particular firm. Specialised resources bear more value for a particular firm than any other.

[118] See Teece (1982): Teece argues that the source of a firm's advantages is better understood in terms of capabilities rather than products.

[119] See Bartlett *et al.* (1991): An emphasis on development rather than exploitation is given and a balance sought. In comparison the transaction cost approach may not result in optimal FDI ownership form viewed from an organisational point of view. The OC approach emphasises a fit between the requirements of the particular product-market strategy and the firm's existing stock of knowledge in determining the appropriateness of a particular ownership form.

[120] See Madhok (1996): Due to lack of experience in a new sphere of activity, a firm incurs substantially higher costs for information acquisition, interpretation, evaluation, absorption and diffusion. Even if it could develop a particular set of capabilities, this may not be competitively relative to those already present in a

Network Approach to Internationalisation

The network approach has its roots in the early findings of Johanson and Vahlne (1992: p12) and their Uppsala model. It is argued that networking under consideration of internationalisation, has not yet been a core focus for research. Johanson and Vahlne argue that internationalisation is related to the exchange within networks, and foreign market-entry is a gradual process utilising such networks. Later Johanson and Vahlne (2003) developed their model in emphasising that networks and resulting relationships are core to the internationalisation process and need to develop over time.

As more recent internationalisation research takes on alternative views and focuses on non-hierarchical systems,[121] where firms invest to strengthen and monitor their position in international networks,[122] the paradigm gives a more profound understanding of internationalisation process development (Hood and Vahlne, 1988; Axelsson and Easton, 1992; Sharma, 1992). This school of research draws on the theories of social exchange and resource dependency. The focus is on firms' behaviour, inter-organisational and interpersonal relationships. Organisational boundaries incorporate both formal business and informal social relationships (Coviello and McAuley, 1999: p227; Dunning, 2002: p62).

The network perspective makes the assumption that single firms and markets are not the only ways of organising production. Co-operative agreements[123] between firms can provide an alternative, both to the firm as a co-ordinated system, and to the market through the ability to compensate for market failures (Mariti and Smiley, 1983).

The most significant acknowledgment within the network approach is the acceptance of externalisation, in contrast to the internalisation theory. The firm-specific advantages are second to network relationships. The network perspective offers a complementary view to FDI theory, given that FDI does not account for the role and influence of social

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more experienced firm. Organisational capabilities, therefore, behave both as a source of competitive advantage as well as a constraint.

[121] See Chandler (1977, 1980): Chandler is concerned to explain the development of large corporations administered by a hierarchy of salaried professional managers. Chandler suggests modern business emerged when administrative coordination did better than market mechanisms in enhancing productivity and lowering costs. A managerial hierarchy is a prerequisite for realising the advantages of coordinating multiple units within a single enterprise. The growing volume of economic activities makes administrative coordination more efficient than market coordination.

[122] See Coviello and McAuley (1999: p232): A cross-examination of 16 empirical studies on SME market-entry shows there is strong empirical evidence that SMEs are using, at least partially, a network approach for internationalisation.

[123] See Fruin (1992), Kleine (2000) and Dunning (2002): Fruin refers to Keiretsu, or vertical groupings of successively smaller companies dominated by major firms at the top of an industry. Kleine refers to German company pools for successful market-entry to China. Kleine emphasises the network approach does have a learning effect for the individual participating firm, which they would otherwise not experience with a market-entry on their own, as the companies are building up personal expertise. Dunning proposes network building through technology, i.e. R&D activities.

relationships within business transactions. It is suggested conceptual development should incorporate concepts associated with FDI, together with those from the stage models and the network perspective. Notably, internationalisation decision-making and activities in the network perspective emerge as patterns of behaviour influenced by the various network members, whilst traditional FDI theory assumes rational strategic decision-making (Granovetter, 1985: p481; Coviello and McAuley, 1999: p227).

2.3.3 – Strategic Approach and Type of FDI

There are two broad issues of relevance in foreign market-entry decisions:

1. The motivation for firms, or *why* enter a foreign market, i.e. the entry decision itself. Broadly speaking, entry into a particular product-market is to either exploit an advantage a firm possesses; to strengthen an existing product-market; or to develop a new, though normally related, product-market.[124]
2. The means by which firms choose to participate in the particular product-market, or *how* to enter a foreign market, i.e. the decision regarding the mode of entry.

Theoretical contributions are more advanced in the area of foreign entry mode than in other topics on a firm's internationalisation process (Kim and Hwang, 1992: p33; Andersen, 1997: p28; Kumar and Subramaniam, 1997: p59; Bradley, 1995: p59). The choice of entry mode is a key strategic decision in a firm's internationalisation process. Using a seemingly safe, or convenient, way of market development will not automatically be the most suitable strategy (Root, 1994: p181). As entry mode is a core component of the internationalisation concept; the choice of the correct entry mode for a particular foreign market is a critical decision for firms. Not surprisingly there has been considerable research into the patterns and determinants of foreign market-entry. Some researchers have focused on ownership and control issues, implied by various modes of entry (Davidson and McFetridge, 1984, 1985; Gomes-Casseres, 1989; Contractor, 1990; Agarwal and Ramaswami, 1992, Hennart and Park, 1993; Hennart and Reddy, 1997; Chang and Rosenzweig, 2001). An extensive stream of research has included cultural (Kogut and Singh, 1988; Gatignon and Anderson, 1988; Cho and Radmanabhan, 1995; Ghemawat, 2001) and performance aspects (Ghoshal, 1987; Kogut, 1989; Arni, 2003; Ruigrok and Wagner, 2003). The entry mode choice is contextual in the sense that the intention to enter a given host country can already limit the choice of the entry mode. Restrictions can apply in terms of the size of equity and the industrial field, whereas the two can also be in combination.[125]

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[124] See Li and Clarke-Hill (2004), UNCTAD (1998) and Dunning (1993, 2001): Motivations for foreign market-entry are market-seeking, efficiency-seeking, knowledge-seeking and risk-reduction seeking.

[125] See Zhao and Levary (2002: p2) and Wezel (2004: p3): The most severe restriction possible on FDI is to not allow foreign entry into the entire economy or certain sectors of strategic importance at all, which a sovereign state has the absolute right to do under international law. More commonly investors are granted freedom to establish operations in emerging markets subject to certain equity participation limits, i.e.

UNCTAD (1998) sets out three broad categories of factors on the host country determinants of FDI, namely i) policies of host countries, ii) proactive measures countries adopt to promote and facilitate investment, and iii) the characteristics of their economies. To find certain host-country criteria, and the characteristics of the host-country economy, Dunning (1993, 2001) identifies four main strategic types of FDIs for firms, namely: market-seeking, efficiency-seeking, knowledge-seeking and risk-reduction seeking.

The policy framework of the host-country will offer different types of equity entities for FDI to the investing firm, and, as a consequence, the foreign company is often limited in its choice. Considering such framework conditions several studies have taken on a particular country focus on FDI entry mode selection, such as for China. For China an extensive stream of research on Joint Ventures [JV] and Wholly Foreign Owned Enterprises [WFOE] can be identified. A major research stream covers the choice of entry mode (Tse *et al.* 1997; Vanhonacker, 1997; Pan and Tse, 2000; Chen and Hu; 2002) whereas another stream of research looks at operational and performance factors for such equity entry (Beamish, 1988; Yan and Warner, 2001; Yang and Lee, 2002).

It is concluded that the decision on the type of entry mode, in particular for China, is a decision that must not be made in isolation. For such a strategic decision an overall alignment with the firm's strategy is necessary[126] (Tahir and Larimo, 2005). These insights help support further research as they give the necessary information for understanding the vehicles for FDI in China. Although this is not the core of this dissertation, since the intention is to show the decision-making process of Small and Medium Sized Enterprises [SME], the research mentioned on China entry modes supports this study project.

2.3.4 – SMEs Market-Entry and FDI

The dynamics of today's markets and the trade/FDI balance shows FDI is of increasing interest to firms. The theory for FDI developed from the viewpoint that larger firms with extensive resources participate in international markets. Historically these industries were largely characterised as being oligopolistic in nature. For SMEs and their entrepreneurial and environment embedment, as well as today's fragmentation of markets, expressed in product and market characteristics, the condition of oligopoly can no longer be supported. Various researchers contend that large firm experience on the internationalisation of business operations does not necessarily represent an easily transferable model for the

prohibition on wholly foreign owned affiliates or the forced taking of stakes by local firms (UNCTAD 2001: p56; 2003: p102).

[126] See Madhok (1996: p588): The choice of market-entry mode can intrinsically have an impact on quality and/or price. This links the governance choice with strategy, which has traditionally been interested in the choices firms make on quality and price.

small firm (Tse *et al.* 1997; Karagozoglu and Lindell, 1998; Coviello and McAuley, 1999; Brauchlin and Pichler, 2000; Dunning, 2002). Specific research on FDI by SMEs is limited, but confirms that approaches by larger firms cannot readily be transferred to SMEs (Oviatt and McDougall, 1995; Kohn, 1997; Apfelthaler, 2000; Lu and Beamish, 2006).

SMEs internationalisation research has concentrated on management characteristics, such as knowledge, attitudes and motivation[127] (Cavusgil, 1984; Bloodgood *et al.* 1996; Chetty, 1999), and underlines the importance of the past experience of managers for successful internationalisation (Welch and Luostarinen, 1988; Zahra *et al.* 2000; Holbrook *et al.* 2000). Another stream of research investigates the decision-making processes for the internationalisation of SMEs. The findings emphasise the difficulties of compiling and analysing data from host countries and indicates a concentration on decision-making ability of managers, sometimes characterised by limited cognitive abilities[128] (Luostarinen, 1979; Coviello and McAuley, 1999; Chetty and Campbell, 2003; Collinson and Houlden, 2005).

Two streams of research explain more recent internationalisation patterns for SMEs, namely organisational (Itami and Roehl, 1987; Peteraf, 1993; Madhok, 1997) and network capabilities of the firm (Axelsson and Easton, 1992; Sharma, 1992; Coviello and McAuley, 1999; Dunning, 2002). Both these research streams identify that foreign direct investment decisions of small firms cannot be explained in economic terms only but are rather based on available resources, and, as a result, organisational capabilities and internal and external network capabilities. This is strongly supported by findings on the significance of the preparation phase for internationalisation and the handling of experiential learning-commitment mechanisms on markets and relationships (Knight, 2000; Yip *et al.* 2000; Johanson and Vahlne, 2003).

There is little research on SMEs and their struggle to overcome a lack of resources and finance (Woodcock *et al*. 1994; Yeoh and Jeong, 1995; Coviello and McAuley, 1999; Bell *et al.* 2003). This bears some relevance since the resourcefulness of large firms, in contrast to small firms, has been widely discussed as having an influence on market-entry

[127] See Cavusgil and Nevin (1981) and Calof and Beamish (1995): The most prominent findings describe two internal determinants important for propelling SMEs into internationalisation: (i) management's expectations of a significant impact on the growth of the firm through internationalisation, and (ii) a high degree of commitment to internationalisation. It is the overall attitude of the decision-makers in SMEs, rather than environment factors, which propel them into internationalisation.

[128] While learning and accumulation of knowledge over time is seen as important for the internationalisation process, to match international resources and competencies (Eriksson *et al.* 1997; Zahra *et al.* 2000), the notion of time needs consideration for several reasons. Luostarinen (1979) recognises the potential of decision delay due to limited perception, restrictive reaction, selective search and confined choice, while other researchers note the potential destabilisation of decision-making forced by a lack of time and internationalisation that is too fast (Chetty and Campell, 2003).

mode decisions. It is shown that large firms can, by themselves, have an environmental impact, which smaller firms often do not have, which, in turn, influences the acceptance of investment risks (Calof, 1993; Westhead, 1995; Shrader *et al.* 2000).

2.3.5 – Conclusions on FDI

Studies on the international activities of firms tend to concentrate on the internationalisation process (Barringer and Greening, 1998; Oviatt and McDougall, 1997; Wolff and Pett, 2000). Internationalisation of a firm, that can finally lead to equity participation in a foreign country, has been argued by some researchers to be a process of incremental, increasing involvement in international operations (Johanson and Vahlne, 1977 and 1990; Root, 1994; Kumar and Subramaniam, 1997). This tendency is reflected in the underlying FDI and capital investment decision-making models, which largely indicate a linear pattern over time that shows risk minimisation characteristics accompanied by learning effects (Aharoni, 1966; Bower, 1972; King, 1975; Wei and Christodoulou, 1997; Sykianakis and Bellas, 2005).

Some researchers challenge the incremental development of internationalisation, and the evolvement of a new research stream focuses on 'born globals', where accelerated internationalisation of firms has been found. It is shown firms can quickly and successfully enter international markets by taking on an equity form of foreign market involvement, even at an early stage of the firm; often driven by the entrepreneurial spirit of decision-makers (Rennie, 1993; Oviatt and McDougall, 1994; Madsen and Servais, 1997; Shrader *et al*. 2000; Andersson and Wictor, 2003; Bell *et al.* 2003; Evangelista, 2005).

Despite the environment constraints any firm can meet on its way forward and the importance of today's investment activities, FDI decision processes have attracted considerably less attention from researchers than have domestic investments (Boddewyn, 1983; Wilson, 1990; Larimo, 1995; Sykianakis and Bellas, 2005). This comes as a surprise as empirical studies have revealed a gap between capital investment theory and the understanding of practice (Northcott, 1992; Pike, 1996; Arnold and Hatzopoulos, 2000; Sofian *et al*. 2004). Knowledge-intensive firms can ignore home markets altogether (Bell, 1995; Boter and Holmquist, 1996; Coviello and Munro, 1997; Madsen and Servais, 1997) and 'leap-frog' certain stages of the internationalisation process, which may indicate a missing, but important knowledge element. Internationalisation theory needs a broader base and trends show a recognition of this aspect.

One prominent approach to FDI, the OLI paradigm, criticised by some for its richness, is able to conceptualise different and relevant aspects. The OLI approach elaborates on different advantages, but the negative side is that 'disadvantages' are noted to a lesser degree. The concentration on advantages can be questioned as the OLI approach

elaborates on the exploitation of advantages – a characteristic of the transaction cost approach – rather than on developing competencies. The focus on firm-specific advantages must be broadened to conceptualise the relevant competencies of the firm for internationalisation.

While FDI approaches *via* organisational capabilities, collaboration building and networks shed new light on the internationalisation processes of firms, and give the opportunity to include organisational behaviour and social theories, they must not neglect the negative sides of these paradigms. Increased complexity of information finding, dealing with intangible assets, an understanding of values and not explicitly of costs, means the decision process can be lengthened. Overlapping issues can arise and, as a consequence, result in more confusion than anticipated. A general drawback in FDI theories is that they do not, as yet, explicitly conceptualise the factors of distance and country. An understanding of the concept of institutional distance between different companies and countries will help develop needed competencies. As noted by Johanson and Vahlne (2003: p98) the notion of distance can change due to experiential learning and trust building.

A strong resemblance between the development of FDI theory and SME market development is noted. Both need the acknowledgment of organisational behaviour theory required for further research on decision-making for the internationalisation of firms.

2.4 Summary of Literature Review

Only a small number of researchers focus on the foreign investment decision-making process for small firms. SME decision-making processes for foreign direct investment need to be carefully analysed and it is not appropriate to adapt the decision models of large firms.

Earlier researchers argue certain factors in the FDI decision-making process, rather than the decision-making process itself, are important (Aharoni, 1966; Pike and Dobbins, 1981), and emphasis must be laid on strategic analysis rather than following a normative and linear model of decision-making. This underlines the importance of the behavioural approach to decision-making (Aharoni, 1966; Larimo, 1995; Wei and Christodoulou, 1997; Kukovetz, 2002).

Both the factors and the process of decision-making are important:

- Firstly, because of the nature of the decision problem,
- Secondly from the uniqueness of SMEs compared to their large counterparts, and
- Thirdly the influence of the decision-making environment, which in the case of emerging markets, has many uncertainties as it evolves.

In contrast to normative decision-making models that see goal formulation and implementation as being outside the decision-making process (Hofer and Schendel, 1978) it is argued that any dichotomy between decision-making process formulation and implementation is a false one (Sykianakis and Bellas, 2005; Elbanna, 2006).

There is compelling evidence that the decision-making process for market-entry by SMEs must be more holistically analysed. Traditional theories of trade, investment and internalisation are of great value to explain the mechanisms that determine, and trigger, international business activities, but they fail to explain *how* to enter international markets. They list reasons *why* firms eventually develop beyond their boundaries, with approaches which are normally quite rational. The author argues that although traditional models capture the dynamics of the markets they are rather static in acceptance of a firm's internationalisation processes. Organisational behaviour and social aspects are issues that have not been fully considered within traditional internationalisation theories but are of increasing relevance for SMEs. It must be assumed that recognition of this will allow the consideration of less rational approaches to FDI and advance the decision-making theory.

The inherent characteristics of SMEs, such as the owners-managers contexts, and network and organisational capabilities, have to be considered. Such characteristics are fundamental for an analysis as some researchers, specifically in the China context, show extremely successful and rapid cross-border venturing by local companies. Rapid strategy adjustment, as the outcome of a series of small decisions in response to external motivations and environment changes, is fundamental for successful market-entry (Mintzberg, 1987; Huy and Mintzberg, 2003; Sykianakis and Bellas, 2005). The presumable ease Hong Kong or Taiwanese SMEs show in entering China may not be replicated by every firm (Wei and Christodoulou, 1997; Kukovetz, 2002), but the same unstructured external environment of China can be used to analyse and compare the decision-making processes of Swiss SMEs, and their decision behaviour for market-entry.

SECTION 2

Chapter Three ~ Conceptual Research Framework

3.1 Background

The core of the strategic decision process can be described in terms of Mintzberg *et al.*'s (1976) proposal where the iterative nature of the decision process is emphasised, as in Exhibit 7.

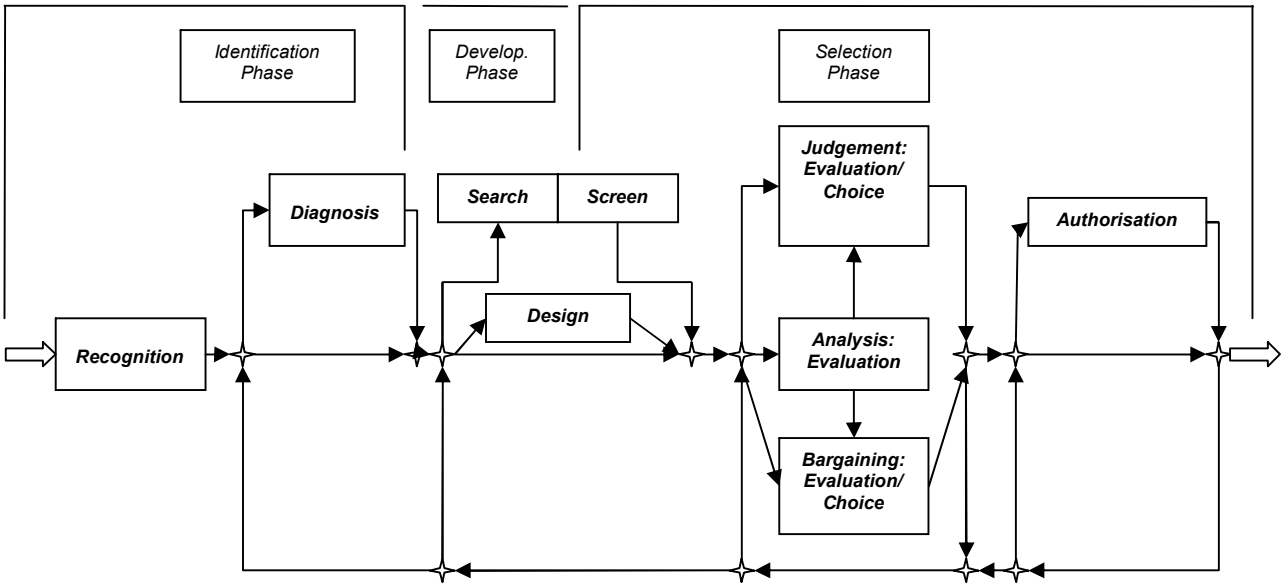

Exhibit 7: Model of Strategic Decision Processes

(Mintzberg *et al.* 1976: p266)

It is argued by researchers that there is a lack of knowledge about strategic decision-making processes, their efficiency and how they increase organisational performance (Eisenhardt, 1989a; Dean and Sharfman, 1996; Knight, 2000). This supports the findings of Luostarinen (1979) who argues that limited perception in the preparation phase greatly influences a time delay in the decision-making process.

Because of shortcomings the process must consider the nature of the decision problem and goal formulation in the preparation phase, and again later in the implementation phase. This is in contrast to normative models of decision-making, such as described by Hofer and Schendel (1978), and allows the identification of the specific firm's characteristics and influences from the environment on the decision-making process.

Mintzberg *et al.*'s (1976) decision framework is thus extended for the purpose of this research and can broadly be divided into three sections which overlap:

1. Perceiving and learning phase, characterised by learning,
2. Recognition and development phase, which may trigger a decision, and
3. Selection and implementation phase of the decision-making process, which is characterised by the operationalisation of a decision.

Such a categorisation, as in Exhibit 8, which consists of sub-groups, best considers the efficiency of a decision-making process when feedback loops can be applied.

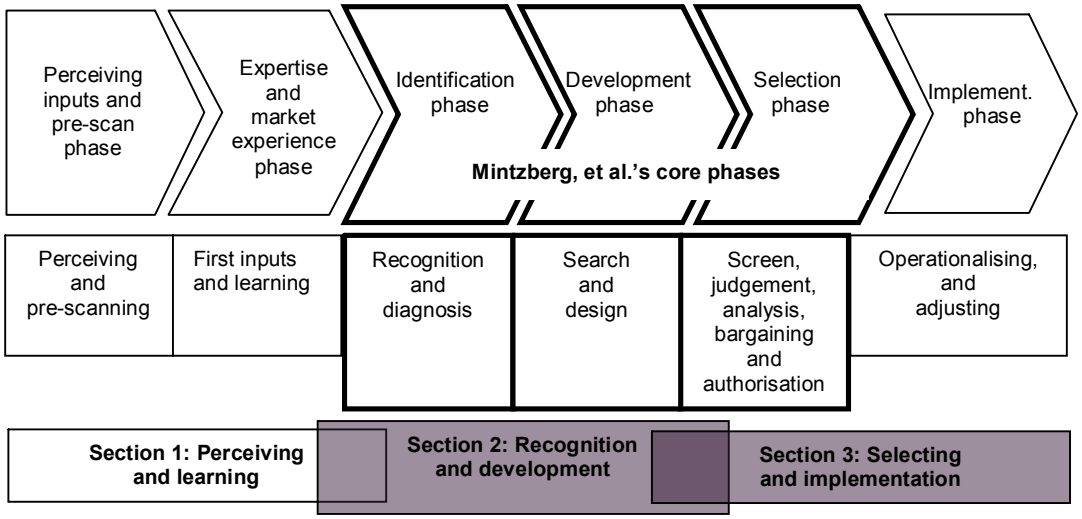

Exhibit 8: Extended Decision-Making Model

(adapted from Mintzberg *et al.* 1976: p266)

3.2 Main Sections of Framework

3.2.1 – Perceiving and Learning

Small firms can lack strategic orientation and only subsequently develop strategic thinking (Haugh, 1997; Julien *et al*. 1997). In the perceiving and learning phase the decision is taken as to whether the firm understands market indications and if involvement in a foreign market is important to the firm. This should consist of serious incremental inputs to avoid a 'first time' lag in the later decision-making process (Luostarinen, 1979). Larimo (1995) notes the stimulus in FDI is usually an opportunity arising in a foreign country, rather than a problem requiring change. Initial triggering can originate within the firm itself and not only from external conditions. This initial phase can be part of identification, or stimuli, and part of information collection, which can by no means yet indicate if and how the company will enter a foreign market (Larimo, 1995; Wei and Christodoulou, 1997). Within this phase a discrete and rational choice can be made as to location or market being entered (Benito and Gripsrud, 1992: p474).

Kukovetz (2002) notes it is quite difficult to determine an exact trigger point for a market-entry decision, as there is an informal phase in information gathering. Kukovetz found this initial phase depends on the characteristics of the managers involved and their experience stemming from similar market environments. Within this phase, and depending on available knowledge, learning is important. This generating of experience has more recently been seen as being absent – or at least partially absent – in firms that show an accelerated internationalisation process. More often this period is expressed as a period of increasing involvement in a foreign market, sometimes opportunistic, and characterised by risk minimisation, such as export or sourcing activities (Dembinski and Schönenberger, 1994). It is not clear however if the exporting company is interested in a deeper involvement or just stays at the export stage (ENSR, 2003). Firm size has been shown by ENSR to influence export behaviour but small size does not necessarily prevent exporting (Calof, 1993; Westhead, 1995; ENSR, 2003).

It is noted that human and financial resources available to small firms can act as a considerable constraint on developing an international orientation, as in:

- Lack of finance may hinder the firm's ability to identify opportunities,
- Inadequate financial resources may restrict the exploitation of opportunities already identified (Smallbone and Wyer, 1995; Kalantaridis, 2004),
- Limited management competencies (Bell *et al*. 2003), and
- As a consequence of these, time stretching and delay may occur.

Awareness of potential investment opportunities may thus be lacking, or opportunities cannot be further developed.

It is recognised that internal and external networks are important for the internationalisation process (Coviello and Martin, 1999; Jocumsen, 2004). As shown by McGee and Sawyer (2003) there is evidence that owner-managers of small firms rely more heavily on internal sources of information than on external sources. Higher internal locus of control, less willingness to accept outside advice, lack of organisational structure and processes for effective environment scanning, and a limited number of external linkages or boundary scanning opportunities are reasons for reliance on informal and internal information (Lang *et al*. 1997; Pineda, *et al*. 1998). Network capabilities are relevant in the initial phase of information gathering and learning, with both formal and informal networks advantageous. Strategic alliances with other companies, also in target countries, can support and enhance learning within relationships (Kohn, 1997; Johanson and Vahlne, 2003).

3.2.2 – Recognition and Development

Mintzberg *et al.*'s framework (1976) for unstructured strategic decisions builds the core of this dissertation and the research project framework. It reflects the need of an analysis tool for the FDI decision-making process for SMEs in the context of emerging markets, such as China. As outlined in the literature review researchers argue for the importance of certain

factors in the FDI decision-making process rather than the decision-making process itself (Aharoni, 1966; Pike and Dobbins, 1981). This is considered at the very initial stage of the decision-making process, by stretching Mintzberg's model and considering this within the perceiving and learning phase. The decision problem in this way is profoundly considered and not isolated from the decision-making process. Problem content and environment context are not separated. However only the recognition stage, and its consequent diagnosis, should be considered as the trigger point for an FDI decision. The outcome of the earlier phase is not always clear, nor has it yet focussed on a specific country. At the recognition stage the firm has accumulated a considerable commitment and in SMEs it must be ensured that owners-managers have created the necessary initiative to enter a specific market via a FDI (Kukovetz, 2002). At this stage timing for FDI market-entry is drafted.

The diagnosis of the decision problem may still be novel to the company and the firm can face difficulties in finding reference values, especially relevant in SMEs where an equity market-entry via a JV or WFOE is not an often, or a repeated, occasion. As noted by Sykianakis and Bellas (2005) this is the process stage where the firm shapes its initial ideas and the search for information in the market is focused on political, economic, demographic and other issues. It shows existing knowledge may not be sufficient, as previous similar decisions cannot act as an appropriate base, and a ready-made solution may not be available, thus a departure from a rational diagnosis is possible.

As emphasised by Mintzberg *et al*. (1976) intense decision problems, and presumably FDI decisions for SMEs can be categorised as such, can cause time and cognitive pressures that discourage formal diagnoses of the problem. This stage can result in loss of momentum and initiative. Where the firm has already become partially involved in a foreign market, on a low risk side, such as export or sourcing, and experiences some success, it can enter a stage of 'productive leisure'; a situation where current, although small, success can make the firm reluctant to enter a deeper involvement in the foreign market (Reinmoeller and Chong, 2000).

The development phase is characterised by following a route of search or design (Mintzberg *et al*. 1976). According to Kukovetz (2002) large firms search for, design and develop investment alternatives. As SMEs differ from larger firms, do smaller firms have the capacity of concurrently developing different alternatives? This process phase is shown to result in flexible strategies firms develop in emerging markets. It is concluded that firms are still at a stage of acquiring market knowledge, intending to be flexible, and abstain from making large investment at this stage. This has some similarities to the real option theories, where firms look to make small investments on initial market-entry with the flexibility of exercising larger investments after market knowledge has been obtained (Thurner, 2005;

Fisch, 2006), which largely depends on perceived uncertainties that are met, such as in an emerging market.

According to Mintzberg *et al*. (1976) this is the phase where most resources are used and the empirical findings show search activities are rather hierarchical, developing from memory and from familiar sources into patterns of active search for alternatives. At this stage it is important whether or not the firm is able to acquire a supportive network. If such a search is not successful the design route is then taken, and custom-made or modified solutions sought. Custom-made solutions are rather expensive and time consuming and companies, especially with lesser resources, may be reluctant to spend resources on more than one alternative.

3.2.3 – Selection and Implementation

The selection phase is core to the decision-making process since here the actual decisions are made. This depends on the decision-making abilities of the owner-managers of SMEs and possible cognitive limitations, either through information overload or unintended and intended biases. This phase, according to Mintzberg *et al*. (1976), is shaped by an evaluation-choice routine that consists of screening, analysis, bargaining and judgement. At this stage a decision-maker needs to consider the consequences of the solution. Mintzberg finds that this phase follows a multi-stage, iterative process and reflects decision-making in the environment of emerging markets with uncertainties about a decision's outcome.

Although people strive for good decisions and often have a high opinion of their own decision-making ability, research repeatedly shows that decision-makers often do not understand their own implicit decision rules and are systematically overconfident about the quality of their judgements and decisions (Nisbett and Ross, 1980; Caroll and Johnson, 1990). This process is less analytical, especially in emerging markets which are characterised by uncertainties. Utility functions do not play a major role in this phase which will propose how decision-makers can deal with risks. Within this phase the evaluation of contextual criteria, often soft facts, pose some difficulties and tension for the decision-maker. Kukovetz (2002) argues that the evaluation method within this phase is either intuition-based or accompanied by extensive research, which largely influences the time needed to reach a decision.

Mintzberg *et al*.'s (1976) model underlines the role of decision-making authorisation. This must be seen from a different angle in the case of SMEs as smaller firms can have a different construct of management levels. In the most extreme case there is only a single decision-maker in the company which calls into focus the owner-manager's role (Hill and Wright, 2001; Etemad, 2004). In other cases the solution has to be approved, and can well be rejected resulting in abandonment or the need for further development. Such authorisation can have a controlling effect and in the extreme case of a SME

internationalisation may not take place at all. In SMEs decision solutions may not be exposed to an approval process, as possibly met in larger firms (Eisenhardt, 1989a; Eisenhardt and Zbaracki, 1992). Kukovetz (2002) argues that delegation of decision-making authority can benefit the making of better decisions, specifically when closer to the market. Delegation of decision-making may however be difficult in small firms where resources are limited. Owners-managers in SMEs may not delegate decision-making, which can influence the speed of the decision-making process.

This is the stage where the firm has to make a real commitment, and inadequate financial resources may restrict the exploitation of opportunities already identified (Smallbone and Wyer, 1995; Kalantaridis, 2004).

The decision-making process, its outcome, and implementation must not be separated (Mintzberg, 1978). Kukovetz (2002) argues that the market-entry of successful SMEs from Hong Kong is characterised by a process of an initial slow learning phase – maximising organisational learning by trial and error – followed by a fast growth phase. Initial investments are small and considered at the early entry stage, combined with intuitive decision-making capabilities for further decision stages. The timing of entry is adjusted according to the learning capabilities of the firm. This outlines the importance of the implementation phase of the process, for continuous learning and for processes that will occur after the selection phase. Initial and growing local market knowledge is therefore crucial and empirical studies on the internationalisation of companies show a positive relationship between a company's specific and learned attributes and success (Kogut and Singh, 1988; Yip *et al*. 2000). As a consequence the way forward should always consider the effects of learning (Pleitner *et al*. 1998). Experience and cross-cultural learning are key elements and fill the gap between expectations after the selection phase and experience (Yamazaki and Kayes, 2004).

Mintzberg *et al*. (1976) argue that missing knowledge about the decision process flow and structure can be pervasive throughout the process and finally reach the point where effective implementation is heavily impaired. As a consequence it is questioned how a decision can effectively reach the operational level. The ENSR survey (2003) shows that although companies appear to be aware of strategic issues in the internationalisation process and the major importance of planning, in practice, firms do not necessarily follow these during implementation. Early research on German SMEs (Stahr, 1979) identifies a gap between theoretical and practical approaches to internationalisation, and, according to Stahr: 'The theoretical market selection approach appears to be complicated for the practitioner and seems to be too accurate'.

In the literature review it is clear that decision style, cognition, uncertainty and risk taking[129] and the entrepreneurial orientation of decision-makers involved in the internationalisation process[130] must be considered when drafting an appropriate final research framework for this dissertation, in which the dominant role of environment factors on internationalisation[131] organisational factors[132] and networks[133] are considered, as in Exhibit 9.

Considering these aspects, the extended decision-making model of Mintzberg *et al*. (1976), [here after referred to as Mintzberg *et al*. (1976) or Mintzberg's model], for unstructured decision-making processes, has been further amended. Emphasis is given to its three main sections and underlines the fact that such decision-making processes take place in an uncertain environment of an emerging market, as is demonstrated in this dissertation.

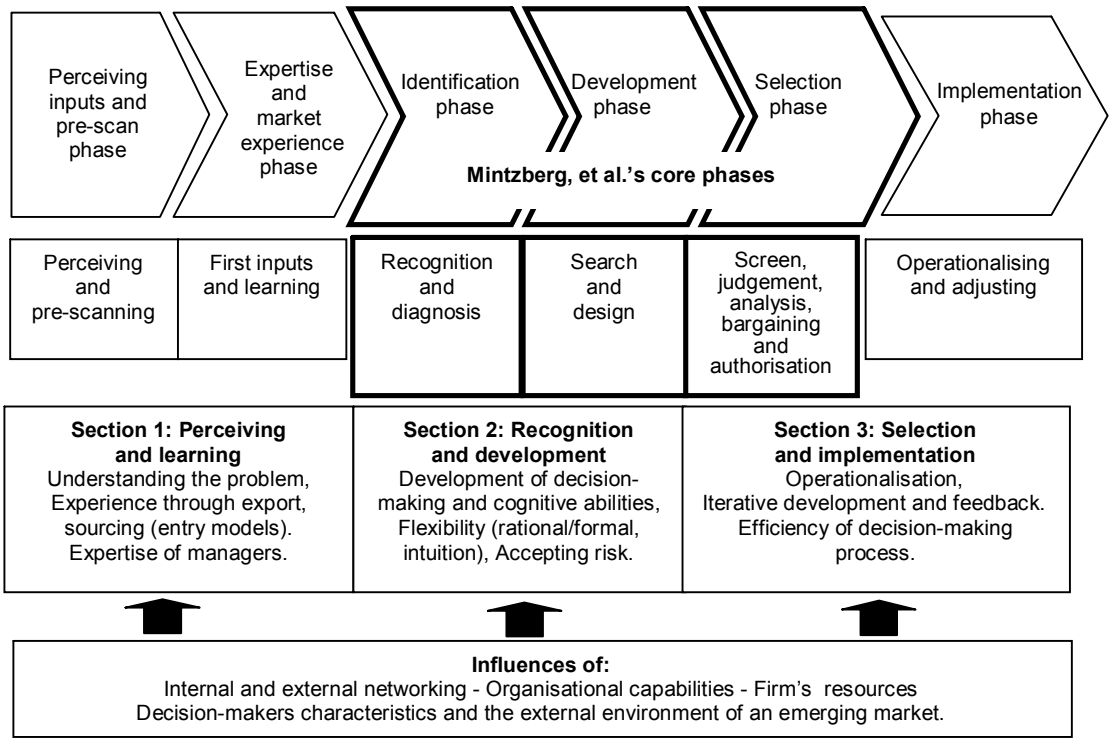

Exhibit 9: Proposed Conceptual Research Framework

(adapted from Mintzberg *et al.* 1976: p266)

This extension of Mintzberg's framework has several advantages. Firstly, at this stage it does not reject the original framework. Secondly, the initial phase of the decision-making process and the implementation phase can give insights into the efficiency of the process

[129] Eisenhardt, 1989a; Yip *et al.* 2000; Sinclair and Ashkanasy, 2005; Xuemin, 2005.

[130] Bloodgood *et al.* 1996; Knight, 2000; Lu and Beamish, 2001; Mazzarol and Reboud, 2006.

[131] Hambrick and Snow, 1977; Kathri and Ng, 2000; Lyon *et al.* 2000; Sykianakis and Bellas, 2005.

[132] Lyon *et al.* 2000; Xuemin, 2005.

[133] Wei and Christodoulou, 1997; Coviello and Martin, 1999; Jocumsen, 2004; Collinson and Houldon, 2005.

and the model profoundly captures the timely development of the decision-making process. Thirdly, further research in this dissertation is not limited to set paradigms.

3.3 Final Research Questions

The preliminary field study and the literature review show an early decision-making stage, where the formulation of the decision problem and the implementation stage must be considered in the decision-making process, and a modified decision model is consequently drafted, based on Mintzberg *et al.*'s (1976) decision model for unstructured decision-making.

Based on the empirical findings of the preliminary field study and the literature review in this Chapter the following research questions are defined:

1. What is the decision-making process for foreign direct investment by SMEs?
2. How do owners-managers of SMEs make decisions on foreign direct investment?

These research questions are further defined in several propositions as follows:
Research Question 1 ~ Research propositions are:

1. Small businesses undertake a series of well-defined decisions for FDI in sequential steps; accompanied by learning and feedback.
2. The decision-making process depends on diverse process factors: the ability to utilise internal and external networks, learning and building of organisational capabilities, ownership characteristics.
3. The decision-making process shows some flexibility and considers operational aspects.

Research Question 2 ~ Research propositions are:

4. The owner/manager of a SME has an influential decision-making role and available and accumulated knowledge at each step of decision-making builds competence.
5. Small business owners-managers are well prepared for FDI decision-making and show a high commitment in launching a FDI process.
6. The decision-making process is characterised by numerous external uncertainties and owners-managers apply a mix of rational and intuitive approaches to decision-making.

Based on these questions the most suitable research methodology is next deduced for the core research of this dissertation where the study investigates the proposed decision model and how it can be applied.

Chapter Four ~ Methodology

4.1 Background

This dissertation has two major objectives:

- To compare Swiss SMEs market-entries into an emerging market; in particular their Foreign Direct Investment [FDI] decision-making processes in the case of China.
- To support and develop the decision-making process model [Exhibit 9] that led to such FDI.

The research context is based on two main premises:

(i) Emerging markets are those where few outside companies have as yet entered, and available information is often random, unstructured or scarce; such an environment is complex and with a high degree of actuality, and

(ii) SMEs, that are often private companies, are reluctant to release data and information.

In addressing these premises, the results need to be described in words rather than figures to answer the stated theoretical propositions. As the subject of this dissertation is novel, exploratory and explanatory in nature it makes a qualitative rather than a quantitative research method more appropriate. Miles and Huberman (1994) consider qualitative data is likely to produce serendipitous findings and new integrations, by forcing the researcher to go beyond preconceptions. Qualitative data are not only a source of well-grounded, abundant descriptions and narratives; they may also be used as a means to determine which events have led to specific consequences and to derive plausible explanations.

The case study approach for gathering qualitative data forms the general framework for this study, and an open approach is used as the method for collecting and analysing the data, with findings used to detect patterns across the cases. According to Yin (1998) the case study approach has major advantages:

- It deals with contextual situations, and the reality of many social and contemporary phenomena is that phenomena and context are not precisely distinguishable.
- A pure quantitative method requires a larger sample size if statistical interpretation is sought.[134]

[134] This supports the application of a qualitative research methodology. As there are, as yet, only a few hundred Swiss SMEs in China, the number of foreign direct investments by these firms is even smaller. Existing surveys on the topic of Swiss firms and their China activities have shown the limited number of Swiss firms that have entered China. These surveys have not necessarily distinguished between small

- There is widespread acknowledgement of the qualitative method as a valuable and valid research approach (Eisenhardt, 1989b; Cassell and Redman, 2001; Weber, 2004; Cepeda and Martin, 2005).

In the first part of this Chapter the open approach to data collection is described followed by a discussion on the case study approach. The research cycle is discussed in a separate section, and emphasis is given to case study analysis, limitations and quality of research.

4.2 Open Approach to Research

Qualitative social research is not based on broad hypotheses deduced from theory but rather begins with data. It is conceptualised as an inductive process. Ideally the researcher should not have preconceived ideas on the research problem or have previous knowledge of the theory. These principles are based on the initial monograph of Glaser and Strauss (1967) who consider researchers must not impose theoretical concepts on data as theoretical concepts must emerge. One main reason to select an open approach in this project is that the method can deal with large volumes of qualitative data, and is a method that supports the generation or discovery of new insights and theory (Cresswell, 1998: p56). Such insights and theory are derived from systematic gathering and analysis of data throughout the whole research process. Data collection, analysis and theorising stand in close relationship to one another and the final theory or insights developed are solidly grounded in the data.

Glaser and Strauss (1967) argue that the researcher should approach data with as little existing theory as possible in mind, later somewhat moderated by Strauss and Corbin (1990) in that it is recognised that existing theories must not be disregarded and can guide the research and data collection (Laudan, 1977; Kelle and Kluge, 1999). It is also debated whether empirical data can be the base for scientific recognition, as theories cannot simply consider the collection of data, but should rather offer an explanation of data. Empirical observations and methods are always embedded in a theoretical context. Logical consequences that lead to the formulation of new insights are therefore not solely inductive or deductive in nature.

New scientific knowledge evolves from a combination of old and new experiences (Anderson, 1987: p47). Within this dissertation the position is taken that the existing theories are important and act as useful guides. The real strength of using an open approach however, and the main reason it is chosen, is the fact that large volumes of

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and large firms (Bülk, 1997; Berger *et al.* 1998; Roth, 2003; Seco, 2005; SCS, 2006; Nie, 2006). The quantitative results of these surveys are mostly shown as descriptive statistics. The number of Swiss firms contacted and return rates, denoted as research/number/return rate, were: SCS, 617, 18 %; Seco, 230, 21.7 %; Berger *et al.* 281, 30 %, which indicate the relatively small number of Swiss firms active in China.

qualitative data can be analysed. The rigour of collecting and examining data, analysing its meaning and coding helps detect relevant concepts, their properties and dimensions (Urwyler, 2006: p29). Theory building is not the intention in this dissertation, and the open approach must not be misinterpreted as a method of grounded theory.

4.3 The Case Study Approach

The case study approach is recognised as a valuable research strategy in small business and entrepreneurship research (Chetty, 1996; Hitt *et al.* 1999; Cope and Watts, 2000; Perren and Ram, 2004). This research strategy is preferred to answering *how* and *why* type research questions where the research problem is of an explanatory nature. The case study method is a comprehensive research strategy that relies on a multiplicity of data sources as an evidence collection method. Data need to corroborate other data by triangulation and combining different data collection methods, such as archival research, interviews, questionnaires, document scanning and observations (Yin, 1994; Zheng, 2006).

Such research situations deal with operational links that need to be traced over time, rather than mere frequencies or incidences. A relevant aspect in favour of the case study in the context of this dissertation is that the method is especially pertinent to investigate exploratory types of *what* questions, where the purpose is to develop hypotheses or propositions for further probing[135] (Yin, 1994; Maugain, 2003). The possibility of generating novel theory is supported, with high testability and strong empirical evidence underlined; advantages of the case study method (Eisenhardt, 1989b).

Case study research is argued to be particularly appropriate for research questions in which the research problem and theory are at their early, formative stages, often contemporary events, where the experiences of the players are important but there is little or no control over behavioural events (Roethlisberger, 1977; Yin, 1981, 1994; Bonoma, 1983; Benbasat *et al.* 1987; Eisenhardt, 1989b).

Based on current definitions of the concept of 'case study' a fuzzy and blurred perception among researchers exists on what can be defined as a case study, although there is some consensus on the following:

- Firstly, the case study can be used as a pedagogic device for illustration,
- Secondly, the case study can develop a framework for the collection of evidence, and
- Finally it can be used as a research tactic (Remenyi *et al.* 1998: p163).

[135] See Eisenhardt (1989b: p535): Case studies can be used for various aims; to provide description, test theory or generate theory.

4.3.1 – Case Study and Evidence Collection

Within this dissertation the case study strategy is primarily used for evidence collection and not as narratives of cases. There is some agreement that a case and its study has a generic nature, and that there is no distinct separation between what is being analysed and its environment. The holistic dimensions of this approach are underlined (Winegardner, 1998: p1; Remenyi *et al.* 1998: p164; Grünbaum, 2007: p82). Great care is taken to identify the unit of analysis and set the boundaries of the study; to ensure the quality and focus of the qualitative research (Miles and Huberman, 1994; Perren and Ram, 2004). Tight heuristic boundaries do not support the emergence of categories and concepts and the construction of theories and new insights is limited.

An initial theoretical perspective helps focus on relevant data[136] and it is this theoretical sensibility that enables one to reflect empirical data on the theory (Glaser and Strauss, 1975). As outlined by Yin (1998: p239) in an example on decision-making, the contextual conditions of the case, that is time, space and process, influence the *when*, *where* and *how* of the decision-making process and the holistic approach to the case is emphasised. According to Yin, the main advantage of the case study method is that it allows one to start an investigation without precisely knowing the boundaries of the case, and even to discover insights into the way decisions are made, because initial contextual conditions may turn out to be key parts of the decision-making process and may later become part of the case.

Some researchers argue that the case study approach can oversimplify a case. In particular case study researchers can face difficulties when studying poorly understood situations, and as a consequence have the risk of improper or subjective interpretation, and a high probability of researcher bias has to be considered[137] (Gable, 1994; Winegardner, 1998; Remenyi *et al.* 1998; Cepeda and Martin, 2005). As argued by Winegardner (1998: p5) a researcher's epistemological assumptions are thus central when classifying and approaching case studies.

As a consequence a distinction between positivism and interpretivism case study approaches can be made. In the interpretivism approach researchers can find themselves in a central role in the research process due to their interpretation, based on their experience of the research objective.[138] The researcher's role must be clear in the research process, and this dissertation takes the research position that the investigator has little or

[136] See Glaser and Strauss (1975): They consider theoretical sensibility is needed in research.

[137] See Maugain (2003: p173): Great care must be taken to prevent bias in case study research where the researcher not only retrieves the data, but also codes, processes and interprets it.

[138] See Cepeda and Martin (2005): Person (researcher) and reality are inseparable (real-world) in an interpretivism approach, whereas person (researcher) and reality are separate in a positive approach.

no control over the cases and is in an observer position, and thus has a positivism case study approach.

4.3.2 – Generalisations from Case Studies

A single case study may enable generalisation to other case studies that represent similar theoretical conditions[139] (Yin, 1994: p36; Yin, 1998: p239). Although critics typically state that single cases offer a poor basis for generalisation, a single case study could offer multiple levels of analysis (Yin, 1998). An embedded case study design can help overcome limitations within the single case study approach.

For SMEs this is a feasible approach as it is assumed SMEs might not always offer a study of multiple subjects within one single setting (Maugain, 2003). Generalisation from case studies is not a matter of statistical generalisation but a matter of analytical generalisation; using single or multiple cases to illustrate, represent or generalise a theory. Often the sample size is too small and the split between the subject of investigation and context does not allow for statistical generalisation (Yin, 1998; Geib, 2006; Zheng, 2006).

However, analytical generalisation is not automatic. A theory must be tested through circles of replications of the findings in a second or even third context, where the theory specifies the same results should occur. Analytical generalisation can be strengthened by the application of a multiple case study approach. Different cases are treated similarly as a series of independent experiments to confirm emerging conceptual insights (Brown and Eisenhardt, 1997). The method of pattern matching is used to compare patterns of research results with theoretical predictions (Eisenhardt, 1989b; Miles and Huberman, 1994; Stake, 1995).

The multiple case approach is designed to replicate cases, producing evidence from two or more cases, designated as literal replication. Or generalisation may be broadened as the multiple cases are designed to cover different theoretical conditions, producing contrasting results designated as theoretical replication (Yin, 1998: p240). An appropriate multiple case study design can do both. The number of case replications however, both literal and theoretical, is a matter of discretionary and judgemental choice and is determined by certainty on the multiple case results needed. Case study evidence collection follows the logic of an experiment rather than the logic of a survey, and it is unnecessary to replicate a case study many times[140] (Yin, 1998; Remenyi *et al.* 1998).

[139] See Yin (1998:p239): Classic single case studies are, in part, classic because of their broad implications or generalisation ability – even though only a single case was the subject of study.

[140] Kukovetz (2002: p63): Initial bulk of variables are found early during research on a few companies.

4.3.3 – The Interview Process

This research project is mostly of an explorative nature, whereas some elements have an explanatory base, especially where causal relations are investigated. Six sources of evidence are offered for data collection[141] (Yin, 1994: p80). It was perceived that SMEs are not too exposed to public interest and that outside information might be scarce.[142] The interview method was thus selected as the main data collection technique. Saunders *et al.* (2007: p312) distinguish between structured, semi-structured and unstructured interviews, as in Exhibit 10.

	Procedure	Research Category
Structured Interviews	-use questionnaires -based on predetermined and standardised questions -collect quantifiable data	Descriptive, more frequent Explanatory, less frequent
Semi-structured Interviews	-use list of themes and questions that can vary from interview to interview and organisation -understand relationships -non-standardised	Explanatory, more frequent Exploratory, less frequent
Unstructured Interviews	-in-depth interview -explore an area of interest -no predetermined list of questions	Exploratory, more frequent

Exhibit 10: Forms and Types of Interviews

Saunders (2007: p314)

Semi-structured and unstructured interviews provide the opportunity to probe answers, where interviewees explain or the interviewer wants to build on responses. Most suitable is where the interviewee becomes an informant without undue interaction from the researcher. The in-depth survey through interviews aims to obtain detailed and rich evidence, usually from a relatively small sample size (Remenyi *et al.* 1998). The open-ended character of in-depth interviews is preferred in a study that includes exploratory elements, as they give ground for new insights and challenge the preconceptions of the researcher. Opportunity is given for immediate response from the researcher (May, 1997: p112; Robson, 2002: p59), while additional questions can be asked and doubts clarified (Emory and Cooper, 1991; Kukovetz, 2002).

In this study the unit of analysis is the decision-making process of the firm. Different interviewees that participate in the actual decision-making process can have various experiences, due to their managerial level or job function, but all contribute to the decision-making process. As a consequence there can be variations on how individual

[141] See Yin, 1994: p80; Remenyi *et al.*, 1998: p175: Sources of evidence are documentation, archival records, interviews, direct observations, participant observations and physical artefacts.

[142] SMEs may not have strong exposure to the public. Especially when companies are not stock listed and do not publish reports and other documents are mostly dedicated to immediate stakeholders.

interviews are conducted. The interview process must therefore have some flexibility and questions must be adjusted to each contextual setting.

Evidence collecting can incorporate more than one type of interview within one single case study. Whereas the overall aim is to use in-depth interviews to explore a theme and find common patterns, semi-structured interviews can be considered, especially in situations where it is the aim to explain patterns that have emerged (Wass and Wells, 1994; Healey and Rawlinson, 1994; Yin, 1998). The combination of the in-depth and semi-structured interview methods utilises the advantages of both methods.

4.4 The Research Cycle

A theoretical understanding of the decision-making process for FDI, and in the particular case of SMEs, has been established during the literature review. Further understanding will be accumulated through the cycles of research. These research cycles, according to Cepeda and Martin (2005: p858) consist of four stages, namely planning, data collection, analysis and reflection, while the stages can also overlap.

4.4.1 – Planning and Case Selection

The research framework, the basis for the field research on decision-making processes, is developed to broadly set the unit of analysis, and the research method chosen is the holistic multiple case study design construct.[143] This design allows several cases, the decision-making processes of different Swiss SMEs, to be included in the research where each individual case study consists of a whole study (Yin, 1994: p49). The rationale behind this is to obtain more robust findings, replication logic, literal and theoretical, and external validity.

Care has been taken in selecting the single cases so they either predict similar results to the other cases, which is literal replication, or they, for predictable reasons, produce constraining results, as a theoretical replication. As noted by Eisenhardt (1989b: p537) and Yin (1994: p45) the cases are chosen, for theoretical not statistical reasons, to replicate previous cases and extend emerging theory, or are chosen to complete theoretical categories and provide samples for polar types. The limited number of cases that can, in such a way, be studied directs the research strategy to select cases that are categorised as extreme situations or polar types in which the process of interest under review is transparently observable (Pettigrew, 1988).

[143] See Yin (1994: p39): Four basic types of designs for case studies are: holistic-single case (type 1), embedded-single case (type 2), holistic-multiple case (type 3) and embedded-multiple case (type 4).

The number of case replications, both literal and theoretical, is a matter of discretionary and judgemental choice and is determined by the certainty about the multiple case results needed. An important step in all these replication procedures is the development of a rich, theoretical framework. This framework needs to state the conditions under which a particular phenomenon is likely to be found as well as conditions when it is not likely to be found. The theoretical framework later becomes the vehicle for generalising to new cases (Yin, 1994: p46). Different sizes of SMEs can be taken to distinguish between polar types of cases. The research opportunity is taken to contrast smaller or micro firms, presumably mostly entrepreneurial companies, and larger SMEs. From the reasons for firms to be active in China it was decided on a sample focus on firms that have established a production platform in China. From this perspective the sample selection, although opportunistic,[144] is limited to eight cases that are: (i) producing/manufacturing Swiss SMEs, and are (ii) of different sizes. Bear in mind the selected companies are chosen on their ability to contribute to evolving insights (Creswell, 1998: p118; Kukovetz, 2002: p48).

4.4.2 – Data Collection and Analysis

Data collection and analysis in qualitative research are closely interrelated, and may be viewed as overlapping (Eisenhardt, 1989b: p533; Maxwell, 1998: p89). Data collection should be flexible and opportunistic, which opens up new areas for exploration and incorporates issues that emerge during the research process. Adjustments are encouraged because inductive theory is built on deep understanding, rather than statistical comparisons between data collected through standardised protocols (Cepeda and Martin, 2005: p859). Although data collection and analysis may overlap the two must at a later stage clearly be separated to realise when data collection has ceased and to understand that data analysing is the heart of theory building (Eisenhardt, 1989b: p539).

A broad categorisation into reasoning (Toulmin, 1988) or coding (Miles and Huberman, 1994) of the data can help categorise the data. It must be ensured that each single case is understood as a stand-alone entity and familiarisation with each case is obtained. The research framework supports categorisation, as data can be judged according to their face validity and soundness within a specific field or context, and in being linked to the research objectives. Categorisation or coding of elements helps identify phenomenon within the data (Creswell, 1998; Strauss and Corbin, 1998).

[144] See Cresswell (1998: p118): The purposeful selection of companies included in the field research sample represents a key decision point in any qualitative study.

4.4.2.1 Open Coding

There is no standardised approach to the analysis of qualitative data (Saunders *et al.* 2007: p478). According to Tesch (1990) strategies to deal with collected data include understanding the characteristics of language, discovering regularities, comprehending the meaning of text or action, and reflection. Categorisation or coding[145] describes the analytical process through which data or text segments are broken down, conceptualised and integrated in theoretical statements, models or frameworks. They provide an emergent structure to organise and analyse data that is relevant to the research project. The identification of categories is guided by the purpose of this research.

Dey (1993: p93) considers categories must cover two aspects; an internal aspect, which must be meaningful in relation to the data – and an external aspect which must be meaningful in relation to the other categories. In the later process the categorisation of data helps identify causalities and inter-relationships between the category findings and a deeper understanding of the situation results. Analysis, similar to data collection, is not a one-off activity but an on-going iterative task. A frequent review of transcripts and notes is necessary to deepen knowledge and enhance further data collection and exploration of data (Hirschheim *et al.* 1995; Cepeda and Martin, 2005), and new categories of data can result. The analytical process of open coding is a selective process, guided by the purpose of the research, which has the effect of reducing and rearranging the data into a more manageable and comprehensible form, called data reduction (Miles and Huberman, 1994; Saunders *et al.* 2007). Over time a sharper focus on the research question will result (Strauss and Corbin, 1998).

4.4.2.2 Axial and Selective Coding

The main purpose of this dissertation is to explore the decision-making process and the main objective is to compare empirically-based patterns with predicted patterns. Axial and selective coding is most important for theory building, and used here to explain relationships between categories of data that have emerged from open coding.

In axial coding relationships between categories are developed. Data have to be carefully selected and organised within the categories to develop themes. The objective is to carry out a synoptic and interpretative analysis. Aspects of newly coded parts have to be compared to previously processed passages. With such a procedure the characteristics of the category is developed and relationships between categories are recognised. Categories are rearranged into hierarchical form, with the emergence of sub-categories (Kelle and

[145] See Maxwell (1998: p89): The goal of coding is to fracture the data and rearrange it into categories that facilitate comparison between things in the same category and between categories. These categories may be derived from existing theory or inductively generated during the research.

Kluge, 1999: p57; Strauss and Corbin, 1998: p111; Saunders *et al.* 2007: p501). The essence of this approach is to explore and explain a phenomenon.

In selective coding the objective is to identify one of the principal data categories and related sub-categories, which becomes the core or central category for relating the other categories. The central phenomenon is thus systematically related to the remaining categories. In this stage the emphasis is placed on recognising and developing the relationships between the principal categories that emerged from the grounded approach to aid the development of an explanatory theory or insight (Strauss and Corbin, 1990; Creswell, 1998).

4.4.3 – Cross Case Patterns and Reflection

Every company first has to be analysed independently from the others, followed by a cross case analysis. Cross case pattern analysis offers a way to strengthen the internal validity of the case study. To apply good cross case comparison it is proposed to look at the data in different divergent ways. The previous and foregoing analysis and coding is an important step for further cross case pattern identification (Trochim, 1989). Bourgeois and Eisenhardt (1988) propose different tactics for looking for cross case patterns, namely to select categories or dimensions, and then look for similarities within groups coupled with inter-group differences. Another tactic is to select pairs of cases and then list similarities and differences, where incremental differences can often break simplistic frames. Most important is to apply a creative pattern search and force investigators to go beyond initial impressions and ideas, to review data and use diverse lenses for analysis. One objective is to detect possible social structures revealed within the groups being compared (Kelle and Kluge, 1999: p91).

Pattern-matching, described by Campell (1975), is where several pieces of information from the same case may be related to a theoretical proposition, as a way of relating the data to the propositions, even though the entire study consists of only a single case. As noted by Eisenhardt (1989b: p542), qualitative data are particularly useful for understanding emergent relationships. When a relationship is supported, the qualitative data often provide a good understanding of the dynamics underlying the relationship; the *why* of what is happening. The case study method is shown in Exhibit 11 overleaf, which underlines the single steps in the case study design.

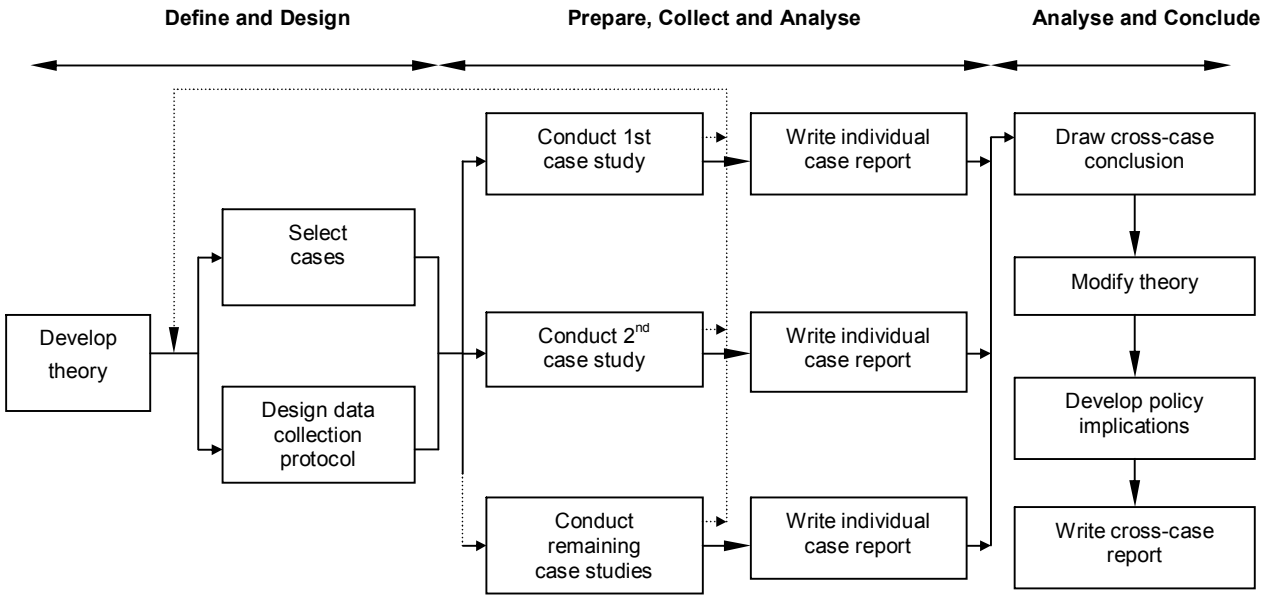

Exhibit 11: Case Study Method

(Yin, 1994: p49)

4.4.4 – Quality of Research Design and Validity of Finding

A number of criteria have to be fulfilled for the chosen research methodology to be proven appropriate but also to ensure the ongoing research process quality. Design tests proposed by several authors constitute a classical quality criterion in positivist research (Lincoln and Guba; 1985; Denzin and Lincoln, 1994; Miles and Huberman, 1994; Hirschheim, *et al.* 1995; Yin, 1998; Robson, 2002). The design tests in positivist case studies are construct validity, internal validity, external validity and reliability. These tests are recommended as means to improve and evaluate validity and reliability in case study research (Riege, 2003; Cepeda and Martin, 2005), as in Exhibit 12. Adherence to these criteria is necessary not only in the design stage but also as controlling mechanisms throughout the research process (Yin, 1994).

The benefits in utilising different sources of evidence can be maximised if three principles are followed, namely multiple sources of evidence, creating a case study database and maintaining a chain of evidence. The first has to do with the research design; the others with the process and the rigour of management of the research process. Case studies can, for example, be entirely based on interviews[146] (Yin, 1994: p91).

[146] See Yin (1998: p247): Most commonly, case study interviews are of an open-ended nature.

	Test	Tactic
Construct Validity	Establish correct operational measures for the concepts to be studied and question if the instrument measures what is supposed to be measured.	- Use multiple sources of evidence - Establish chain of evidence - Have key informants review draft case study report
Internal Validity	[For explanatory or causal studies.] Establishing a causal relationship, whereby certain conditions are shown to lead to other conditions, as distinguished from spurious relationships.	- Execute pattern matching - Execute explanation building - Execute time series analysis
External Validity	Establishing the domain to which a study's findings can be generalised.	- Use replication logic in multiple case studies
Reliability	Demonstrating that the operations of a study - such as data collection procedures can be repeated, with the same results.	- Use case study protocol - Develop case study database

Exhibit 12: Case Study Tests and Tactics

(Kidder and Judd, 1986: p26; Yin, 1994: p33, 1998: p243)

Only the use of multiple sources of evidence can challenge the real strength of the case study research methodology, namely a combination of different data sources and the development of converging lines of inquiry; a process of data triangulation. With triangulation[147] potential problems of construct validity and reliability can be addressed. The grounded approach for evaluation of data, and especially the coding process, helps revisit the source of data and question the findings; in doing so the emergence of a new category of data can be continuously monitored and judged whether of significance to the study. The limits of doing research in the field of SMEs, and, most of the time, non-public companies, must be addressed as the collection of any information can pose a major problem for an investigator. The analytical strategy of this dissertation considers these quality criteria.

4.4.5 – Limitations of Research Methodology

Lack of rigour is a constraint to case study research. The researcher may allow equivocal statements due to a biased view or analysis and, as a result, influence the direction of research and, most importantly, the conclusions (Yin 1994: p21; Gibbert: 2003: p166). According to Yin (1994: p65) all other research skills are of limited value if the researcher seeks to substantiate a preconceived position. The proposed research framework can pose an additional boundary to the research process if the data collection is too narrow. An objective approach to the investigation may blind the researcher to nuances and other explanations outside the organisational and conceptual framework. Consequently the analysis of the case should allow a balance between the objective and subjective

[147] See Patton (1987): Patton discusses four types of triangulation: of data sources, among different evaluators, of perspectives on the same data set and of methods.

perspectives[148] (Miles and Huberman, 1994: p25; Stake 1995: p2; Grünbaum, 2007: p83), although the unit of analysis is set, namely the decision-making processes of SMEs.

This dissertation investigates organisations, and in particular SMEs. The owners-managers' characteristics must be included, as often in small firms there is only one decision-maker in contrast to decision-making by several people in larger firms. It is debated if false conclusions about organisations can be made when information is based on a single individual (Yin, 1994: p72; Perren and Ram, 2004: p91). Eisenhardt (1989b) argues that people are notoriously poor processors of information, and as a market-entry process is often recalled from the memory of the interviewee, this must be considered. Over time, incidents, or pieces of information, have perhaps found a different level of importance, even being entirely forgotten. Past incidents and facts may be judged differently and the researcher, as a result, can reach premature and even false conclusions. Only a true longitudinal study can however overcome such difficulties. This weakness has been considered in this study and has been moderated by using a multiple case study approach in which two rounds of interviews with the same companies have been carried out. Special consideration was given to those companies that were in the decision-making process during the first series of interviews, with a time break of six to eight months between the interviews and after they materialised or implemented their FDI.

4.5 Summary

The rationale is developed as to why a qualitative research methodology, in the form of a multiple case study approach, is adopted in this dissertation. It is concluded that the case study approach is most appropriate to deal with the contemporary phenomenon of decision-making processes for market-entry of SMEs into an emerging market. The process an individual company experiences conceptualises a phenomenon that underlines the need for longitudinal research, where quantitative research approaches are less suitable.

The case study design includes a conceptual framework, research questions and propositions, and the selection of appropriate cases. These cases determine the unit of analysis, the logic linking the data to the propositions and the criteria for interpreting the findings, leading to exploration and inductive reasoning. Great care must be taken that the unit of analysis is clear throughout the process; which in this study is the decision-making process. The analysis of the data involves the ongoing iterative processing of transcripts and data, reviewing the whole process and the conceptual framework, to establish patterns within these data and as a base for identifying opportunities and finding new insights on

[148] See Perren and Ram, (2004): The nature of the social world can be portrayed as the dichotomy between objective and subjective perspectives. Those with a subjective view are interested in understanding the way in which the individual creates, modifies and interprets the world, and those with an objective perspective see the social world as if it were a hard, external objective reality.

the decision-making process. The explorative nature of this study yields the grounded approach as an ideal method for data collection and evaluation.

The selection of different and contrasting cases allows for challenging the propositions and is only possible when using a holistic multiple case study approach. The application of such a holistic multiple case study approach does not only help foster external validity, most prominently replication logic, but also to overcome the overall problem of obtaining a suitable database. The main case study approach strength is the likelihood of generating novel and testable theories or insights, with the resultant theory likely to be empirically valid. The main weakness is that intensive use of empirical evidence can yield theory which is overly complex and which tries to capture everything. But the overall advantage of the qualitative approach, and a major contribution to this dissertation, is that it does not lack sample representation and the resulting danger of reductionism (Collis and Hussey, 2003).

SECTION 3

Chapter Five ~ Decision-Making Process for Emerging Markets

5.1 Background

Eight Swiss SMEs were analysed and a total of 18 interviews conducted. The open interview technique accumulated an appreciable volume of data, and the requirement of at least two in-depth interviews for each company was fulfilled. There are several advantages in having at least two interviews, sometimes three, for each company:

1. Duties are often shared between different managers in one company, allowing the explanation of a situation from different viewpoints.
2. Interviews within one company mostly had a time gap between each interview, giving the opportunity to adjust probing questions and search for new insights after the initial analysis and clustering was completed.

All interviews were fully recorded and then transcribed, with the data collection filling some 300 A4 pages. The transcribed interviews were handed to the interview partner for any necessary clarification and follow-up interviews were undertaken for clarification. At an early stage of the interview phase and consequent analysis, it became clear that the data could be broadly categorised into main clusters.

After discussing the data collection method with various experts and colleagues from the University of St. Gallen, it was decided to utilise data analysis software for processing the large volume of qualitative data, and MAXQDA software was chosen for this aspect. The use of analysis software was justified for several reasons:

1. Initial main clusters and raw screening can continuously be refined.
2. An ever increasing volume of data needs good filing and quick availability.
3. The *in-vivo* coding allows scanning of the text and generation of new coding.
4. Ability to continuously revisit the cases and reflect new findings.
5. Full transparency and replication of data.

The iterative process, characterised by several rounds of review, based on time-delayed interviews, allowed the generation of new data clusters that would not have been obvious at an early stage. Such data clusters, in the analysis phase, were individually re-analysed, compared and combined. The final analysis resulted in some 60 different main and sub-clusters containing some 2,500 text passages.

5.2 Introduction of Cases

Eight Swiss SMEs which had all started a Wholly Foreign Owned Enterprise [WFOE] were analysed in the field study. The main requirement was that the cases be about companies that had concluded the founding process of such a WFOE, exclusively in the production sector, and at the time of the interviews were fully operational, or had just begun to operate. The selection of these cases allows comparison amongst similar SMEs with the same type of equity investment. The most obvious distinction amongst these firms was their individual size. The companies are listed in Exhibit 13 and are introduced in the following sections in alphabetical order.

Company Detail	Core Business
Asico AG (3, 70, 1998)	Manufacture of hard metal steel balls for ball pens
Frutiger AG (21, 3, 2007)	Manufacture of heavy duty wheel washing and scrape dozer equipment
Metar SA (25,9, 2006)	Manufacture of winding machines for electrical capacitors
Plaston AG (130, 130, 2004)	Manufacture of plastic casings and air treatment systems
Proftech International GmbH (3, 5, 2006)	Manufacture of stainless steel components and consultancy, and management services
Schaerer Schweiter Mettler AG Textile Division (220, 50, 2003)	Manufacture of yarn winding machines for the textile industry
Stopinc AG (60, 7, 2005)	Manufacture of slide valves for the steel making process and engineering solutions for steel production processes
Wolfensberger AG (240, 23, 2006)	Manufacture of casting components and engineering solutions for casting processes

Note: Details in first column are: Name, Staff [Switzerland] in 07, Staff [China] in 07, Date founded in PRC

Exhibit 13: Selected Case Studies

(Author, 2007)

5.2.1 – ASICO AG

ASICO AG [ASICO] built up a production company near Shanghai without previous sourcing activities in China. It is an entrepreneurial company where the owner is the decision-maker and acts as the central person both in Switzerland and China.

ASICO was founded in 1986 and registered in Zug, Switzerland. Based on the professional background of the founders, ASICO is a specialised technical consultant in the area of manufacturing ballpoint pens. Design of production lines, installation of machinery and instruction of personnel are the main activities. Developing Asia was the target market [Asia + Consulting = ASICO].

A trading activity soon grew out of the initial activity to supply Swiss machinery to Asian customers and import Asian pen components into Europe. ASICO began to supply high precision TC [Tungsten Carbide] miniature balls to the highly specialised market niche of ballpoint pen tip manufacturers. The production of these TC balls was outsourced to a factory in China, where a highly developed production facility was built. ASICO had exclusive distribution rights for all of Europe. By 1994 ASICO had reached a significant market share in the specialised industry, especially in Italy, Germany and Switzerland where the main players in this business are located. Evolution of the industry in low labour cost markets, especially India, placed increasing pressure on European manufacturers. These, in turn, were obliged to look for alternative supplies of material and components to save on costs.

New developments in communication and the arrival of the Internet made easy and direct contact between manufacturers and users possible and promised price reductions. The exclusivity privileges of traders were increasingly put under pressure from both sides. The time was ripe for ASICO to become a manufacturer itself to defend its market position and its business margins. In 1998 ASICO's own manufacturing plant in Shanghai – SINTERBAL TUNGSTEN CARBIDE MFG. CO. LTD. – was founded, which has today become one of the leading manufacturers of TC balls for the pen industry.

All ASICO competitors now manufacture in China. The continuing battle for a higher market share and lower cost is now fought by restructuring production technology, increasing output quantities and thereby improving cost efficiency.

During 2006 Sinterbal moved into their new factory building. The increased production capability will make further steps in this direction possible. Sinterbal also plans to develop a second product range in TC powder metal technology to support development in the future. Sinterbal will increasingly become independent from ASICO as the manufacture of industrial products moves away from Europe into lower labour cost countries, and closer to China.

5.2.2 – Frutiger AG

Frutiger is a Swiss SME domiciled in Winterthur Hegi near Zurich. Founded in 1957 by Edwin Frutiger the company is today managed by the second generation, one of the sons.

Frutiger was originally a trading company for the import of German-made construction machines. The second generation, after 1994, developed the company into a world-wide company. Today the Frutiger group is an organisation with companies and sales offices in

eleven countries, with Germany and the USA the most important markets. Frutiger employs a staff of 21 people in Switzerland.

Frutiger is active in a niche market and had an early focus on two core products; scrape dozers and wheel-washing systems. Scrape dozers for the excavation, stowing, transportation and discharge of soil and wheel washing machines for cleaning truck wheels when leaving a construction site. For these niche products Frutiger has established a full value chain; the products are developed, produced, sold and serviced by the company.

The main focus of the headquarters in Switzerland is research and development, sales and servicing and the coordination of the world-wide activities of the group. In 2000 Frutiger established a production site in the Czech Republic. Frutiger has continuously developed and refined its core products and is today considered a leader in its field, with a commitment to become the world leader. In 2006 the firm received a European innovation prize for its newly developed wheel washing equipment, the Moby Dick Dragon [Dragon]. The Dragon extends the existing product portfolio of Frutiger in that it offers a high quality brand product at a somewhat lower cost in a market area that cannot be entered by low cost producers.

Part of the Dragon concept includes a production facility in China. But China was not only the focus for possible low cost production. Frutiger management predicted in 2004 that China will offer a large sales market for its products, especially in the area of wheel washing machines. Frutiger carried out market research and found an increasing demand for its equipment as China is becoming aware of environment protection issues that include road cleanliness. Preliminary production cost estimates showed local production in China was feasible at comparable low cost and an acceptable quality level. After founding a representative office, for the sales of Frutiger products, at the start of 2006 it was decided at the end of 2006 that a production facility should be established in China. In the spring of 2007 Frutiger received its business licence in Changsha, China for the production of its equipment. Frutiger intends to build up its production capacity to achieve an equal share of locally sold and export products by the year 2008, when they hope to sell 50 machines in China and intend to export 50 machines.

5.2.3 – METAR SA

METAR SA [METAR] has, since 1968, developed and manufactured machines and equipment for the production of electric capacitors and batteries. The firm operates from Matran in Switzerland, and at its peak the firm had 150 staff, establishing strong roots in the Matran area. The firm developed strong expertise and knowledge in designing,

manufacturing and developing its machines – mostly winding machines for capacitors; today considered niche products.

METAR's winding machines are state-of-the-art. Its technical level is well-known in different industries and often taken as a technical standard for setting required quality levels of end products. The company is not a producer of capacitors or batteries but its machines are used within the electrical and electronic industries to produce high quality end products. The producers of such end products have within the last number of years shifted their activities, and more importantly their production, to Asia. Markets did develop in the USA, followed by Japan and Korea, but currently producers are establishing themselves in China or are in the process. The shift of these markets resulted in a situation where winding machines have to be sold world-wide. METAR reacted to this tendency and in the early 80's had already opened up a sales office in Beijing. The tendency of shifting markets enhanced competition and local markets in Korea, Japan and Taiwan, and motivated competitors to develop their products.

From its early beginning METAR focused on high quality Swiss-made products, producing high value machines at rather high price levels. In the early 2000s METAR realised the high quality of its products no longer justified its prices. Competitors' products now reached a high quality level but at much lower prices. METAR's products still distinguish themselves as they can span a variety of different applications, but are often perceived as too flexible with unnecessary features. Such features are often not needed in the Chinese market where, although producers of capacitors do need several machines, they are simple and needed only for the purpose of producing a few types of capacitors. METAR realised its machines were not suitable for this market and they could lose their share of the market. The emergence of China as a manufacturing country motivated Chinese competitors to develop their own winding machines which fit their clients' demands. METAR had to face the situation that they could soon be out of business if they were not able to react to these forces.

In 2004 METAR decided to launch a new business model. At that time the company had already drastically downsized and employed a staff of 25. Activities concentrated mainly on design, development and assembly of machines. Most of the components were outsourced to different sub-suppliers. The company did not see a potential to downsize further in Switzerland. At this stage the decision was taken to establish a new company in China; a company that focused on assembly and sourced components from different suppliers in China. At the time a new winding machine was developed that would suit conditions in China; had fewer features, but was still built to a high quality. METAR thought such a business model would guarantee the survival of the company in Switzerland and retain its employees.

In early 2005 the decision was taken to enter China in the form of an investment. At this early stage METAR decided to found a new company in the form of a wholly foreign owned enterprise [WFOE]. The reason was mainly to gain full control over their future activities in China so they could retain their knowledge acquired over the years. Around one year later, in early 2006, METAR obtained its business licence, started up assembly, and in early 2007 completed its third China-produced winding machine.

5.2.4 – Plaston AG

A Swiss entrepreneur founded Plaston AG [Plaston] in 1956, and took the opportunity of entering, at that time, a new business field for the production of plastic products. The company developed its expertise in plastic injection moulding and mainly produced products for the household. In 1970 it became the supplier of plastic cases for Hilti. The following 20 years, until the early 90's, saw investment into large production machinery, and new products were developed, such as air treatment systems. Today Plaston is a world-wide supplier of industrial plastic and air treatment systems, and employs 130 people in Switzerland. Core activities in Switzerland are production of plastic packaging, development and engineering, tooling development and procurement, marketing, sales and supply chain management.

In the early 1990's Plaston's management realised international markets were gaining significance and that foreign production, sales and marketing would support the company's growth. This provided the initiative to found production companies in China and the Czech Republic as well as a sales and marketing company in the USA.

In 1993/1994 setting up production in the Czech Republic was decided, which helped gain early international experience for the company; characterised by extensive decision-making processes. The new plant started production in early 1996. Shortly after the decision to enter the Czech Republic it was decided to start operations in China and in 1996 Plaston entered an initial joint venture with a Chinese partner. The set up in China was planned to become the second foreign production facility. Holding 90 % ownership, Plaston was the major partner in this joint venture, with a 10 % minority share taken by its Chinese partner. This joint venture did not develop according to Plaston's expectations and despite owning the major share of the venture Plaston was not able to fully execute their ownership rights. Towards the end of the 1990's it was decided to abandon this less successful joint venture; a decision which coincided with the development of the Asian crisis.

In early 2000 it was realised that many of Plaston's key customers were moving to China to set up local business activities. As Plaston's business mainly takes place in a business to business [BtoB] fashion, it was realised that Plaston could sooner or later lose key customers without a production facility in China. It was decided at the end of 2003 that

Plaston must be active in China with its own production facility, and the decision was taken to set up a new factory in China. At this time the option of entering *via* a wholly foreign owned enterprise [WFOE] was being developed. In October 2004 Plaston started production in Jiaxing, China and is today the supplier of plastic packaging systems for Bosch, Hilti and Metabo in China. Plaston was also able to develop their air treatment business in China, an opportunity not foreseen at the outset for the new China activities. Plaston has not only started a production plant in China but has also developed marketing and sales know-how that has led to new business opportunities.

5.2.5 – Proftech International GmbH

Proftech International GmbH [Proftech] is a company founded by a Swiss entrepreneur who worked in China and learned of the business potential in China. Proftech was founded in 2000 as a BVI [British Virgin Island] company and in the same year opened a branch office in Shanghai. In 2003 it was registered in Switzerland and now operates under Swiss laws.

The company evolved out of experience in shipbuilding project management in China, where several shipbuilding projects have been undertaken. Know-how on project and quality management, contracting, design, procurement and supply chain management was acquired. The shipbuilding projects are for European ship owners, who utilise the lower cost structure in China, as an alternative to Europe, Korea and Japan. For Proftech, when the company started out, this resulted in a good network that has been the basis for further development. The initial business of Proftech was limited to ship-building services. Foreign ship-owners meet little known challenges when undertaking projects in China, and Proftech was of assistance in successfully implementing and supporting such projects. The experience showed that each shipbuilding project had similar challenges to meet the final quality and delivery time for a vessel. These two objectives are the most important criteria for an individual ship owner and Proftech felt a sound process of shipbuilding could better fulfil the owner's objectives.

In 2003 Proftech Switzerland was founded from where it now operates in St. Gallen, Switzerland. From this rather isolated location shipbuilding project management could not remain the core business activity of Proftech. The founding of Proftech Switzerland and start of operations from Switzerland helped detect a new market niche. With knowledge from ship-building in China it was realised there was a small Swiss marine supply community that had no common activities and which was very much fragmented. Over time Proftech identified some 220 Swiss firms that had some activity in ship-building, at least as a by-product, or had the potential to be active in this industry, which initiated support for the Swiss marine industry and the opportunity to market the industry with a

special focus on China and Asia. From this position relevant China consultancy know-how has been continuously developed.

Since establishment in Switzerland a different business potential has arisen, and, over time, different industrial projects [non ship-building] have appeared. Several consultancy projects for China materialised, which took the form of market research, sourcing of components, IP [Intellectual Property] questions, building of agency networks and initial positioning of firms in China. At the end of 2004 Proftech joined a Chinese partner to set up a joint venture for the production of machined and welded steel components. The partners operated a small workshop near Shanghai but had to give it up after a half year of operation when the local government decided to turn the location into a residential area. This experience and several other consultancy projects showed Swiss firms often need initial support to enter the Chinese market, although the degree of such support can vary considerably. One of these projects in particular provided the initiative for a drastic change in Proftech's engagement in China.

In 2005 a sourcing project for semi-finished stainless steel components for a large Swiss company began. It was the intention to find Chinese firms that could consistently deliver stainless steel products at an agreed quality and quantity. The company agreed to buy components from a selected Chinese SME, but during further proceedings it was realised the Chinese SME had large fluctuations in quality, while the business understanding was not always clear. Proftech was asked for a solution, which resulted in Proftech taking over the part of the Chinese supplier in China, thus becoming part of the supply chain and taking over quality control and certain financial risks.

At the same time Proftech became part of a third Swiss firm near Shanghai, where Proftech rents factory space and does light machining, quality control and the dispatch of goods to Switzerland. Proftech thus extended its services and took the initiative of becoming a manufacturer to serve its own customers in Switzerland with mechanical products. In mid-2006 Proftech started on its own to strengthen its presence in China. Reasons were for better control over employees, a better relationship with its suppliers in China and a business-like approach in the market and to its customers. Early in 2007 Proftech negotiated a contractual joint venture with a known servicing firm in China, which came into force in July 2007.

5.2.6 – Schaerer Schweiter Mettler AG

Schaerer Schweiter Mettler AG [SSM], with its textile division, and head office in Horgen, Switzerland is a designer and producer of yarn winding/processing machines. SSM has production plants in Switzerland, Germany, Italy and the Czech Republic. For many years SSM operated a marketing and sales office from Hong Kong. The

management of SSM realised in the early 2000s, that in the low-end winding machine segment, different competitors were increasingly attacking the market position of SSM. Competitors mainly came from India, China, Korea and Taiwan. Since these low-end winding machine producers did not offer extensive functions and options on their machines, they were able to offer low cost machines, spare parts and services to their clients. The management of SSM decided to take counter-measures and agreed on establishing a production company in China for the production of cost effective machines.

In May 2003 it was decided to enter the Chinese market in the form of a wholly foreign owned enterprise for the assembly of low-end textile machines and sub-assemblies for high-end yarn processing machines. Further objectives were to establish a repair centre with a local after-sales service. At the start of planning it was clear to SSM that machines should be produced for both local and export markets and machinery had to fulfil Swiss quality standards.

The management of SSM had a very proactive approach to the planned market-entry. To develop quickly the management decided to employ an experienced project manager who had a proven record of establishing and managing a company in China. They favoured hiring an experienced person, rather than taking on consultancy services or following a path of time-consuming self-learning.

One of the first tasks of the project manager, together with the management of SSM, was to select and decide on an appropriate location that had to satisfy multiple objectives; to be close to existing and potential clients, assure the quality of the industrial zone and other firms in the zone, ensure protection of SSM's knowledge, have the possibility of obtaining and retaining suitable staff, and provide favourable tax and sound import/export conditions. After close evaluation of several industrial zones the company decided to settle in the Torch Hi-Tech Industrial Development Zone in Zhongshan, which is in the Guangdong Province, in the south of China and close to Hong Kong. To start the project, the administration office of the industrial zone offered an office for the project manager and his future team.

In September of 2003, four months after deciding to enter China and after evaluation of different sites in China, SSM had worked out its business plan and obtained the business licence necessary to be fully operative in Zhongshan. At this stage SSM-Zhongshan started to employ key Chinese staff, realising that the future success of the company would rest heavily on their capabilities and performance, but, more importantly, on how they could integrate into a Swiss company and share its philosophy. For this task the headquarters of SSM deployed key personnel from Switzerland to China to support Chinese staff in this critical planning and start-up phase. Several challenges had to be

faced to build a functional production plant. In mid-October 2003, the final plans for the Zhongshan factory – layout, work and material flows – were presented to and approved by SSM headquarters. In January 2004 SSM-Zhongshan was able to start assembly.

The implementation phase showed problems that had not been considered during the previous stages. It was realised that the long years of experience, and embedded expertise, in producing textile machinery could not just be transferred to China. Technical drawings had to be revised and translated into Chinese. It had to be accepted that local production standards were not necessarily equal to those in Europe. This was even more important since the SSM-Zhongshan's business concept foresaw SSM in China merely operating as an assembly plant with several suppliers. SSM's operation in China included starting an assembly plant and obtaining the approval of key suppliers. SSM's objectives included sourcing 70 % of needed components in China to meet cost targets drafted in the business plan. The selection, approval and continuous coaching of SSM's suppliers are some of the biggest challenges the new company faces. In May 2005 SSM-Zhongshan delivered the first machine to a local customer.

5.2.7 – Stopinc AG

Stopinc AG [Stopinc] is a medium-sized Swiss firm with sales to China. Chinese customers and the expanding Chinese market required local production, while cost pressures and closeness to customers brought the launch of an assembly firm in cooperation with local Chinese suppliers. Stopinc, with its headquarters in Hünenberg, Switzerland is the founder of INTERSTOP flow control technology that sets market standards for the control of molten metal in steel plants and foundries and is also used in non-ferrous applications. The company, founded in 1966, employs 100 people world-wide.

The INTERSTOP slide gate system is used in more than 71 countries. Stopinc's R&D efforts are driven by a team of highly knowledgeable engineers working in Switzerland and in the USA. China is an important market for Stopinc; its office in Shanghai was established several years ago and transformed into a WFOE in 2005. The Chinese steel industry is currently undergoing tremendous changes, reflected in the modernisation and optimisation of steel plants; further motivated by promising forecasts for steel consumption. Local steel production has to become more efficient, and smaller steel plants have to optimise their processes to be competitive, Stopinc`s customer base will undoubtedly expand further.

To meet low market prices in China and to overcome the problem of high import duties and taxes, the management decided to look into the possibility of producing valves, or parts, in China, and, at the end of 2002, it was decided to start production in China.

Stopinc realised that cultural differences, language and distances would make it difficult to start production on their own, and they employed a consultant to study this task. Initially ten Chinese casting shops and machining companies were evaluated. To prevent copying, the valve is divided into components, which are then produced separately in cooperation with selected suppliers at different locations; with a maximum of two in one place. It was felt agreements with local Chinese partners would not sufficiently secure the intellectual property rights – hence the splitting of production among independent suppliers and components would be more suitable in China. Today it is realised that splitting up the manufacture of components will not protect intellectual property in the long term. Contracts with suppliers will have to take account of this in future.

Three sites were selected, including Chinese companies with, or without, export experience and one Swiss-Chinese joint venture – the production of components started with these three suppliers. All three sites had a different understanding of the production process, with the language problem one of the biggest hurdles in negotiations. Feedback was useful for Swiss engineers with little experience in producing the parts apart from designing them.

Fachhochschule Brugg-Windisch [The University of Applied Science of Brugg-Windisch] in Switzerland became involved to deliver their know-how on ferrous/non-ferrous materials, and all material was tested in Switzerland. It was recognised the Chinese material was equal qualitatively to the European-sourced material and it was decided to use heat-treated cast iron that, in future, would be used in the Chinese products for an extended life for the valves.

To start, a small series of 50 valves was produced in China and assembled in an independent workshop. The second step was the development and procurement of the main parts in China and selling them to new steel plants allowing them access to Western technology at reasonable costs.

Stopinc realised that the technology transfer in a culturally-unrelated country was difficult and it took them a year to obtain acceptable results. The quality consistency was, and still is, partly a problem. Stopinc's own R&D department learned from the individual casting companies as R&D partners and eventually improved the product, but the ongoing survey of quality and tolerances was a key factor for success.

Stopinc at an early stage built its manufacturing capacity in China by selecting suitable suppliers, transferring technology and having an independent assembly plant. Only after this was established was the representative office changed into a WFOE.

5.2.8 – Wolfensberger AG

The company was founded in 1924 in Bauma, Switzerland, and is still today a family-owned company. Currently it employs 250 staff. Traditionally all the activities of the company have been conducted from Bauma with a very strong commitment to this location. Wolfensberger today is a company that offers a variety of casting solutions to its clients. But the company also acts as a general contractor that includes product development, casting and machining. Wolfensberger opened a new machining shop in Bauma in 2003 after years of continuous growth, and, in the same year, started to export products to Japan.

Since the founding of the company a strong focus has been on the ongoing development of casting techniques, materials and processes. Initially only nodular cast iron was processed. Over time the company developed their expertise into processing and casting of various types of steel and nickel-based materials. Subsequently the casting technology was developed from sand-casting to ceramic precision casting and today Wolfensberger is a company that is not only a producer of components but also a high technology company that continuously refines and develops casting processes. This innovative character of the company resulted in excellent business relations with well-known clients, such as ABB, Andritz, Alstom, Bühler, MAN, Siemens, Voith and many others, practically all of whom are world-wide companies, while Wolfensberger often acts as a strategic supplier.

In 2003 Wolfensberger was asked by one of its clients, ABB Turbo Systems, to become active in China and to operate and manage a foundry. Previously Wolfensberger had no relevant experience in China, nor any business relations there. ABB Turbo Systems on their globalisation course, and in a negotiation to enter a joint venture with a Chinese partner, felt they had to secure the local supply of high quality castings in China. Under this premise their intention was to engage Wolfensberger as their local supplier in China. Part of the concept was that Wolfensberger would enter a joint venture with a casting company owned by a future joint venture partner of ABB Turbo Systems. After a year of analysing and evaluation Wolfensberger however decided not to engage in any such cooperation. The management board of Wolfensberger came to the conclusion that the risk of engaging with a Chinese partner, and thereby as a minority shareholder, was far too high. This decision was supported on the grounds that ABB Turbo Systems did not want to engage in the casting business on their own and thus wanted this separate business entity.

In early 2005 Wolfensberger was contacted by one of its key clients and asked if they would be interested in offering their casting expertise in China. Andritz, an Austrian producer of industrial goods in China, with whom Wolfensberger had previously developed a new technology of producing pump wheels, urgently needed technical

support in China. Andritz's current Chinese casting partners could hardly supply the needed quality and it was felt they had to integrate a new and reliable casting supplier to secure their future supplies. The plan was to establish a new casting company in China jointly owned by Andritz, Wolfensberger and a Chinese partner. From previous experience and accumulated China knowledge, the board of management of Wolfensberger was keen to develop this new opportunity. The initial concept changed however and after the Chinese partner decided not to participate in this new venture, Andritz and Wolfensberger in early 2006 decided to set up a jointly owned WFOE. Half a year later the new company was founded in Foshan near Guangzhou. After building a factory the new casting plant started operation in the spring of 2007.

5.3 Case Study Comparison

Whilst focusing in this dissertation on the decision-making processes that finally resulted in an FDI by a SME it is important to understand the reasons why firms enter an emerging market such as China. All the interviews during the field study opened with an introductory question to explore the reasons why companies enter China. This question helped interviewees recall the early stages of planning and helped set the scene for further questions. The cases were analysed in this initial phase on international experience and SME characteristics that are relevant in founding a wholly foreign owned enterprise [WFOE]. Setting the scene in this way helps underline the early impact China had on interviewees and their firms, which triggered their future development.

To disguise the exact identities of companies referred to in the dissertation each has been allocated a Greek letter for identification in the further discussions.

5.3.1 – Reasons for Entering China

China was in all cases identified as an important business place that could no longer be ignored. Large business potential for foreign firms will grow over time, as China will continue to develop not only at present growth points, but also in areas away from the coastline. Each company had already started a WFOE at the time of the interviews, which was preceded either by many years of business relationships in China, or by previous knowledge of owners-managers. Falling markets in the rest of the world is one reason; markets that have shifted to Asia and, in particular, to China. Market-entry to China is seen as an investment for the future. In one interview this was expressed as: '*…we cannot anymore afford not to be present in China*' and in another, '*...China is our only option, otherwise we are near to closing down our Swiss company*'.

Motivations for establishing a company in China are of differing natures. One reason is for production or sourcing only, with the intention to tap a presumably low-cost

production structure; but also in combination with sales, as it is considered a great advantage to have one's own production site closer to local Chinese clients. For Companies Digamma and Eta it was actually European clients who showed a strong demand for companies to join them in China so as to offer their products and services locally. Although not explicitly expressed by all companies interviewed, this showed a type of dual strategy, a combination of production and sales, is currently, or in the future, attractive for a company. Export sales from China to the rest of Asia and the rest of the world are seen as an important opportunity. A local presence will also allow the supply of products to future clients who will become aware of local production; a product supply can be more cost effective if locally-made or delivered from a local warehouse. Companies Gamma, Delta and Zeta, producing complete machines, consider it an asset that Swiss quality products are manufactured in China.

All companies agree that sales in China can only be effective if one has a local production. Several reasons support this, such as China's demand for quality locally-made products, availability of low production costs and qualified staff. China offers a good production platform for larger volumes, and for this reason export sales from China are attractive. In Companies Delta and Gamma it was explicitly indicated that it is attractive for Chinese clients to buy locally-produced Swiss products which are then advertised throughout the world. Swiss products are often used by Chinese manufacturers to process end goods, which again have a high quality requirement, and are often products intended for export from China.

The pressure on price margins and production costs is not seen as the only reason to start activities in China, but low production costs, driven by a low cost structure and, in particular, a low cost for labour, is seen as an outstanding advantage in China. It was emphasised that low cost manufacturing in combination with high product quality is essential. As noted in the three cases of Companies Delta, Gamma and Zeta, it is a false assumption that production in China must lead to lower quality levels when compared to Swiss-made products. Such an approach – planned or unplanned – will lead, sooner or later, to confusion within the company and its clients and a two-quality strategy will not be appreciated by world-wide clients, who will expect the same product quality level at all times.

5.3.1.1 Technology

High-end production equipment is needed in China to produce export products. High technology and quality machines, as produced in Switzerland, are comparably more expensive than machines that can be called 'fit for purpose', as produced by Chinese competitors. End users need to reduce production costs, and this margin pressure is transferred to the maker of production equipment. In case studies Delta and Epsilon

Chinese end users of products – in one case a whole production machine and in another case a key process component – have shown great interest in the production technology of the products, and have even requested the Swiss companies undertake a technology transfer to China and start local production.

For the Gamma Company lower production costs in China, and a lower equipment price, have shown that higher and more expensive technology equipment can be offered to clients originally positioned in a lower price segment. By sharing part of the profit margin, a lower market segment where clients usually use cheaper equipment can be entered, but incorporating characteristics of quality and technology.

The Zeta Company, a manufacturer of niche production equipment, states that local production in China is attractive for more than just direct cost reasons. An additional advantage is that the overall price level in China is kept low. With the assumption that technology is expensive, the Chinese are believed to be less interested in investing in new technology, and basic purchase prices are kept low. If a foreign company can strengthen its name locally, although initially selling lower technology, customer relationships can be fostered over time. At a later stage higher technology products can be sold within an established customer relationship.

Company Eta identifies that the overall lower production costs in China, compared to equal production parameters in Switzerland, enables the use of higher technology process equipment in China. Such process equipment results in higher quality end products. Awareness of the possibility of purchasing a higher level of technology in China, at lower costs, has resulted in a reverse technology transfer to Switzerland. The company is capable of developing its traditional production processes in Switzerland by utilising technology from China.

Companies Alpha and Beta use production in China for the export of semi-finished goods to Switzerland. These production facilities are also aimed at potential future sales markets in China. Company Alpha noted it was attractive for the company to source raw material that could not be exported directly without initial processing and machining in China. The export of semi-finished products allows companies to carry out cost intensive work and pre-qualification of the raw material and products in China before sending to Switzerland for further processing. This inherently results in safeguarding a company's technology and standards, as critical production steps are not carried out in China, while purchase and control of raw material at an early stage is a significant quality approval step.

Companies Delta and Zeta have developed their own product development divisions in China. Foreign companies can be handicapped if they plan to sell ready-made Western

designed machines into the Chinese market as such designs often do not meet the requirements of Chinese clients. Swiss machines can have unnecessary surplus features and as a consequence are too expensive. To counter this companies have started to develop and design locally with the support of Chinese engineers and as close to the market as possible. Local engineering capabilities can help overcome difficulties in technology transfer, especially production know-how, which is often rooted in information which is not always clear on technical drawings and which requires additional explanation.

Half of the companies in the study state they are active in niche markets. It is an aim of these companies to distinguish their firms *via* their product portfolio and quality, realising that differentiation by price has become more and more difficult over time. In one market Chinese manufacturers have reached a high quality level and consequently a higher price by a Swiss company is no longer justified, which has led to the decision for local production in China. The companies analysed firmly believe they will succeed in their fields by incorporating their own China production platform into their business concept. However the companies which claim to be active in a niche market are concerned that technology and production know-how can be lost in China. These companies expressed their concern at a very early stage of market-entry and intend to look for rigorous control of their production and suppliers, so as not to lose their technology and production know-how.

5.3.1.2 Competition

Companies can be 'forced' to enter China, once they learn that not only their clients but also their competitors are taking up activities in China. Other foreign companies, including a number from Asia, have started production in China. For Company Epsilon this resulted in a world-wide price war after one competitor began to export from China. Western competitors, Chinese firms and other Asian companies compete against Swiss companies in China. In more recent times Chinese companies and their machines have developed significantly, thus building stronger competition and narrowing the technical gap between competitors. This leaves Swiss producers in a less favourable competitive position, mainly due to overall cost structures.

As Chinese-made products can these days have a good quality level at a comparably lower price, a subsidiary local manufacturing company is seen as essential to improve a company's competitive position. Within this concept a Swiss firm can offer a full range of machines, from low to high specifications. As remarked in one case '*…our Swiss company has to become a local Chinese company to produce low-end machines locally*'. Manufacturing in China improves one's position *vis-à-vis* competitors.

It is noted that some Swiss firms have been indirectly compelled to take up production in China. High import duties, taxes and complicated import procedures made the sale of Swiss-made products difficult. Transportation issues, such as additional freight costs, potential risk of delay and a time span that could, at least partly, be utilised for manufacture, complicate matters. Generally importing goods to China means Swiss products are less competitive.

If a foreign company takes up local manufacturing in China, it is often forced to accept payment in the local currency. There are differing opinions on this aspect in the Swiss companies interviewed. In one situation this was said to be a real disadvantage as there were difficulties in maintaining profit margins**.** For Company Zeta this was seen as an advantage, as new Chinese clients can be found, who previously, due to restrictions, had no foreign currency available, but now can purchase local Swiss products. Company Epsilon only sees import restrictions as pressure to force a company to begin local production and support technology transfer to China.

To contend with growing competition Companies Alpha, Beta and Epsilon, initially active as traders, started their own production in order to be more attractive for clients in Switzerland. It was thought that as business gets more and more direct and tends to take place directly between businesses, traders would become largely redundant. Subsidiary production in China can thus be seen as a step in business development.

5.3.1.3 Reputation

The cases studied reveal that setting-up production in China can have a significant impact on a company, especially where such a company can appear more attractive to others. Chinese clients much appreciate cooperation with an international company with activities in China. This is expressed in closeness to clients and direct service without distance delays, understanding the needs of clients and showing quick reaction times, support on daily issues, the chance to justify one's locally-made product against imported goods and being able to optimise.

There is also a positive impact on the home activities of a Swiss company. Many world-wide clients appreciate cooperation with a company that has activities in China. Such a company is accepted as a global company and shows commitment to others. Swiss clients that have moved or intend to move to China see it as an additional asset to cooperate with such a partner. Such clients can also speed up their own market-entry if they are aware of key network partners. In case study Digamma the company reduced its risk of a product shortage in Switzerland by its own supply source in China; a supply source that produces Swiss quality products in China.

Overall there is consideration of one's activities in China strengthening activities in Switzerland. In most cases China activities have resulted in a better internal company climate and staff is motivated by employment in an international company. Company Eta, with no significant direct international activities before starting up in China, stated that the China engagement has resulted in a new company era, and this traditional and strongly-rooted Swiss company has started to achieve a more open internal business climate. Only in Company Epsilon did management report resistance from staff, mostly mid-level management, who did not fully support the China engagement of the company. Opposing voices in this company felt the China venture would result in lower product quality that could damage the company's reputation.

5.3.1.4 Against Market-Entry into China

The interviewees were asked for reasons why their companies should perhaps not take up production in China. Personal opinions of some of the interviewees on the strategy of their companies revealed some common worries about market-entry, but also some valuable inputs which should be taken care of during market-entry. The most cited arguments against China were worries about losing technology and production know-how and not having control over activities in China; besides worries about losing jobs in Switzerland.

All agreed that even though China is distant, such a distance is not too difficult, and is even seen as a challenge. China is distant, not only in terms of physical distance but also in terms of language and culture. There are initial worries that the staff in Switzerland would be against foreign production as they are worried about losing their jobs. As a consequence, staff responsible for the operational aspects of running the new business could, perhaps, not be flexible enough and oppose market-entry development. Swiss-made products are well-known and the company could lose their reputation if production is not properly managed and results in low quality production.

Worries were expressed that the development in China, and its stability cannot be predicted, but can only be assumed. Forecasts for China are thought to be too optimistic and future development in China unpredictable. A possible development in China is that high initial and sunk costs of establishing production need time to be recovered and if stability is not present such costs may not be paid back or could even be lost.

The smaller firms in this investigation worried that small size could be a limiting factor for several reasons, including difficulties in raising project finance in China, the company not being attractive enough to find suitable staff and talents, dealing with government agencies and related offices could be a disadvantage, small initial business and market volume make one dependent on a few key customers.

5.3.2 – International Experience

In addition to the initial introductory question some relevant information about the companies was collected. International experience of the firms was found to be divided into two main groups although these depend on each other. The main groups are: relevant international experience of the company and individual experience of owners-managers of the companies. In small companies, there can be a close owner-manager relationship, which could even be the same person, while it is indicated that a distinction between the entity of the firm and the owner-manager is reducing.

5.3.2.1 International Experience of a Company

Three companies, case studies Digamma, Gamma and Zeta previously set up production platforms in the Czech Republic, had other world-wide production sites and are internationally active in sales. Production start-up within Europe is quite manageable from Swiss headquarters resulting in more support and control or the independent operation of the sites. These companies' business successes are based on international activities and it is noted that in these three cases a very open company atmosphere has been created over time. The foreign production platforms helped shift focus within the Swiss headquarters, which started to pay more attention to business process optimisation, product quality and research and development [R&D] activities.

In three other cases the companies had no international experience at all before starting-up in China. In Companies Alpha and Beta market-entry was driven by owners who themselves had international sales and project experience. One 'inexperienced' company, Eta, the largest of the cases analysed only had international experience through indirect export activities before the decision was taken to enter China and take up production.

Overall most companies – as a company or through their staff – had China experience before setting-up current production in China. The experience was mainly in terms of sales and some sourcing activities. In the most prominent case business relations went back some 40 years which has resulted in long-term business ties and an extensive client base. Companies Beta and Digamma initially entered joint ventures [JVs] with Chinese companies, but these had to be closed, as there were different business interests between the shareholders. In case study Delta the Company intended to enter the Chinese market *via* a Taiwanese JV. However this was not successful, as Taiwan-made products are difficult to sell in China; while the planned dual quality strategy was not practical as Taiwanese products are perceived to be of lower quality and not accepted in the marketplace. The Swiss staff also did not fully support the concept of a JV. In two other

cases, Companies Delta and Eta had in the past briefly looked into market-entry with a Chinese JV partner, but neither had materialised after analysing the given circumstances.

5.3.2.2 International Experience of Owners-Managers

Strong motivation for market-entry to China stems from the people involved, especially from the owners and managers of the companies. In cases where the owners are also the managers of the companies it was noted during the interviews that such people are strong drivers of the entry process into China. These persons mostly have an open mind; claimed to be necessary if one intends to enter a market such as China. As noted by one owner '*The cultural experience and understanding in being active in those markets, and especially the experience from Asia, has helped us a lot to enter and develop our activities in China. There are small but important things such as having meals and sitting together, the social aspects in general are important. If a company such as ours adapts and is open within these aspects it will greatly help to develop future business. Such openness is a pre-requisite for success*'.

In case studies Alpha and Beta production in China was started after the owners realised the business potential in China from previous engagements and both had relevant international and China experience. In Company Beta the founder had worked previously for several companies in Korea and China. His China experience was characterised by placing and carrying out large-scale projects, sourcing and manufacturing products through a sound relationship network. China involvement has also led to experience in remote places in China, and projects have been carried out where few foreign companies have yet undertaken projects. An understanding of how to deal and cooperate with the Chinese, and learning the basics of the language helped to develop projects. The other co-owner, who is an ethnic Chinese but lived for a long time in Switzerland, strengthened the development of the China business through his language skills, thus building a bridge between Switzerland and China. It was underlined that problems in China can be solved *via* this bridge; problems that mainly originate from language difficulties, cultural issues and misunderstandings. It was also underlined that the development of business in China needs familiarisation with the environment and an ample time horizon.

There is some variation in opinions about the experience a manager should have for market-entry to China. It was noted in case studies Eta and Zeta that those initiating and driving the market-entry had no relevant China experience, but developed the process successfully until its implementation phase. In Company Eta the implementation stage was then managed by an internationally experienced manager, whilst in the other case implementation was being managed by an experienced China manager; both selected for the particular task of implementation. In the first case the implementation manager needed strong technical process know-how, whereas in the second case the manager needed a

relevant China business background but less technical experience.

In all companies analysed it was stated that although the international experience of a manager is important, this need not necessarily be China experience. China business was said to differ greatly within China. It is thought that one can have sound previous China experience, but each case of starting a China venture is still based on different premises. New knowledge must be acquired for each individual case. More important than China experience is the ability to be open-minded and adaptable, whereas previous China experience could sometimes be a hurdle against flexibility.

5.3.3 – Size Issues

Two major concerns on company size were mentioned. The first was the worry that it can be difficult for a SME to raise market-entry finance to China. Market-entry is likely to be connected to a considerable sunk cost, and return on investment will take some time. The second concern was about the management of China entry. All cases had in common the fact that they felt limited in human resources and a China entry process could only be shared by one or a few people within the company. Even in the largest company it was commented that few people acquired much China knowledge in an initial phase.

It was underlined that China activities should be managed by top managers or owners mainly by simply spending more time over and above daily business activities. This is seen as an advantage as a strong focus on necessary issues is given, such as full commitment needed, serious information processing, careful time management and only concentrating on relevant issues. The identification of the owners-managers and staff with the company, and their strong involvement with the China business is seen as an asset in developing the business.

In case studies Delta, Digamma, Gamma and Zeta the companies needed to acquire relevant China knowledge. This was obtained through consultants or hiring general managers that would implement the projects in China. In Company Delta it was realised that the implementation phase of market-entry would utilise more human resources and manpower than available in the company. Here it was estimated that the opportunity costs of sending a Swiss manager to China would exceed the available budget by far and consultancy services from China would be used to implement the venture.

Some of the interviewees tried making comparisons with larger firms and their market-entry to China. Whereas they assumed that in larger firms teams of market-entry specialists would be formed to develop the market-entry, it was a belief that their own SME entry would follow a different route. It was a common assumption that in larger companies market-entry would follow a formal analysis, based on strategic decisions and

where many aspects can be researched and prepared. In SMEs this would be too expensive as high opportunity costs are faced. The philosophy in SMEs is to grow as much as possible with one's own staff, and develop their own expertise, despite worries that in SMEs it was assumed the company size was too small to attract suitable staff and talent in China.

5.3.4 – Role of the Entrepreneur

It is noted owner and manager positions in small firms can greatly overlap. In the cases analysed there were firms where the owners, or part owners, are also the managers. Managers had a large influence on the non-executive board of companies, while often a manager was also part of such a board. The power for decision-making is reflected in smaller firms where even the owner, in the role of the manager, will make all the decisions without other authorisation. In the cases where a non-executive board must be consulted, in case studies Delta, Digamma, Epsilon, Eta and Zeta, managers are mostly those within the company who designed the proposal and implementation plan for market-entry to China. Each stakeholder, and owners and managers in this research, regardless of the size of the company, have taken on an entrepreneurial position for market-entry to China. This position is believed to be necessary for successful entry to China as there are no ready-made market-entry solutions to China.

In small companies, such as Companies Alpha, Beta and Gamma, where the owners are operationally active themselves, and in the larger firms where owners are more likely to be represented on the board, owners have shown a strong commitment to enter China and believe they will be successful. Owners and board members have to show continuous support and involvement during implementation to motivate all the managers and staff involved. At the same time it is underlined that trust must be given to those people implementing the market-entry decision so they can act as entrepreneurs – as owners – themselves.

Overall it is shown by the companies analysed that entering China is not only a spoken commitment but is also reflected in finance, time and manpower investment. It is emphasised that the managers involved see themselves as pioneers – and in some cases characterised as risk takers – and practically all were fully convinced that their market-entry to China will, in the long run, be successful. As indicated by all the companies financial risks taken would not really question the survival of the firm – apart from case study Delta where it was reported that China was the only option for the survival of the company – and would have a significant impact on the company as lost investment would be missed for other ventures.

The entrepreneurial character of owners-managers has been markedly noted during this

research. One owner stated '*For me there is no difference between running a business in China or Switzerland. Starting up in China is not different to other places. There are risks but I want to be operative in my company and take these risks*'.

5.3.5 – Conclusion on Case Comparison

This initial comparison of the eight cases has shown there are common aspects but also differences when comparing the individual cases. The situation before entering the Chinese market in the form of a WFOE, does greatly vary between the cases. The major differences are the physical size, owner-manager situation and constitution, international and China experience and planned activities in China. Despite appreciable differences all the companies have established a production platform and these, at the time of the interviews, were all successfully in operation.

The interviewees expressed, on several occasions, their belief that there was no ready-made entry plan or solution they could use for their own market-entry to China. Reflecting on two extreme cases – the company driven by its single owner, with a strong entrepreneurial spirit, who has been active for about ten years as a WFOE in China, and another case where the company is of a fair size with a non-executive board and a first experience of a failed joint venture with a Chinese partner – the market-entry process varies greatly between companies and an analysis of the decision-making process that led to the WFOE is justified.

Please refer to Exhibit 14 for a summary of major findings on the Case Comparison.

Reasons to enter China	- Demand from European clients to produce/service locally in China - To offer Swiss quality products made in China - Cost pressures and utilisation of lower overall cost structure
Technology	- Adjust to Chinese requirements and offer products that are 'fit for purpose' - Chinese clients may ask for technology transfer before asking for local production - Low cost structure allows sale of higher technology at equal price level - Semi-finished products for export can safeguard end-product technology - Use local talent to develop 'fit for purpose' products - Local talent allows better understanding of local production circumstances - Concern that technology might be lost if production process is not fully controlled
Competition	- Competitors have moved to China and company is forced to take up activities there - Chinese made products are increasingly improving and becoming more competitive - Import of products is less profitable and causes logistical time delays - Traders are being phased out. Take up own production to be more competitive
Reputation	- Company more international and attractive - Risk is spread amongst several international locations - Products are available in multiple locations - Employees appreciate working for an international company
International Experience	- Previous international experience helps develop China business - Firms without China experience can also be successful - Firms with little International experience can enter China quite quickly - Firms can have several decades of trade experience without making an investment - Previous failure in China does not necessarily stop firms from re-entering China

	- Entry scenarios cannot be copied from other markets. Individual development is needed
Management	- Market entry to China depends heavily on owners-managers whose experience varies - An open mind by owners-managers is important for market-entry - Fully committed owners-managers are the actual drivers of market-entry - Trust in the people who develop market-entry is most important - Delay of market-entry may occur when owners-managers have to report to a board - Swiss firms whole-heartedly develop their market-entry to China - Full commitment from owners and board must be given; reflected in financial support
Reasons Against Entering China	- Loss of technology and loss of reputation - Staff might oppose China business due mainly to worries about losing their jobs - China's development is unsure and worry of losing investment - Size of company may prevent entry and company development - Lack of finance and fear that firm cannot attract suitable staff - Staff may not have sufficient China knowledge; such knowledge is expensive to develop

Exhibit 14: Major Findings on Case Comparison

5.4 Different Phases of Market-entry

The following Sections show the different phases of the decision-making process for market-entry progress to China. The progress is divided into three sections:

1. Perceiving and learning,
2. Recognition and development,
3. Selection and implementation.

Refer to Exhibit 9 and the decision model for market-entry.

5.4.1 – Perceiving and Learning Phase

Analysis of the early stages of founding a WFOE, is presented in Exhibit 15.

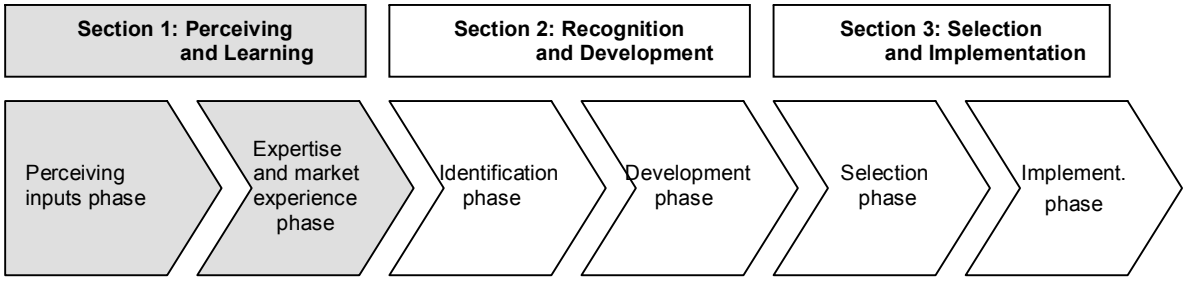

Exhibit 15: Decision-Making Process ~ Perceiving and Learning

(Author, 2007)

Most cases analysed show extensive international experience before China became of interest. Participation and business in an international environment is understood to be the first step; to be open for new, far distant and possibly exotic markets such as China. In case studies Digamma, Gamma and Zeta it was firmly emphasized that an early and open company atmosphere resulted in international networks for sales and production, which

made China entry much easier for the companies; especially important is acceptance and support by staff. An international focus helped develop products needed in international markets and has continuously supported product development and quality improvements. In another company, case study Beta, the founders of the company, which has operated for several years in China, established the company specifically for the purpose of doing business between Switzerland and China. The many inputs received from China melded together and were turned into a business concept that eventually led to the production of mechanical components in China.

5.4.1.1 Shifting Markets

The companies analysed in the case studies can be described as victims of shifting markets; shifting markets of a different nature – clients moving to China, a low production cost structure in China, Chinese manufacturers increasing their production capacity and growing export markets from China. The companies analysed did not all look directly for new markets but were influenced by these market movements into starting production in China. This research shows that the growth taking place in China, perceived in startling growth rates, does not always result in complete optimism, and in the interviews the growth rates in China are also seen as dangerous; being too fast, uneven and not really controllable.

In case studies Digamma, Gamma and Zeta, an outsourcing philosophy and strategy started prior to the China entry, with China seen as a furthering of this tendency. In Company Alpha it was realised clients were searching for direct business relationships and Western clients were looking for direct contacts with producers in China. This was a strong incentive to start company production in China to reduce trade risks.

In case study Eta, the company did not intend to move to China, but enquiries from Swiss-based key clients that already had activities in China were serious and could not be overlooked. An initial inquiry by a Swiss MNE enterprise went back several years before a second inquiry resulted in the founding of a WFOE, together with a European MNE. Although the first inquiry did not end in a market-entry it resulted in the acknowledgment that China is a potential market and that Swiss customers have increasing business activities there.

Company Digamma learned that their clients had started, or were close to taking up, production in China. The company began to indirectly export its products to China, within the scope of delivery to their clients. However, it was soon realised this process was not efficient and was too costly. It was felt that neglecting this business opportunity gave local Chinese manufacturers the chance to develop their products and obtain the status of a key supplier to these clients. The company took up activities in China, but the Asian

crises showed how vulnerable a company is if dependent on key clients, and they have started to reduce their business activities in China.

The direct impact China has on the companies analysed is emphasised. In case studies Delta, Epsilon and Zeta, the companies had several years of trading experience in China and learned that Chinese end-users are increasingly asking for higher quality and high technology products, aiming at achieving international standards. These companies explicitly underline the dominance and power of the Chinese market, and have direct experience, not through a third party. As the products of these companies are considered niche products, high-end production machines and one key component in raw material processing, it is felt that such products must, intentionally or not, be increasingly locally-produced for sales to Chinese clients.

5.4.1.2 Developing Expertise

Early exposure to China is important. Previous sales and marketing experience resulted in a sound understanding of China business. In three cases, Companies Delta, Epsilon and Zeta, interviewees felt they had acquired sound relationships in China, particularly *via* their representative offices in Beijing, Shanghai and Hong Kong, which resulted in related business networks. An active presence in China helped to realise that more and more competitors from Asia are entering the Chinese market and that competition has started to develop from more than one direction.

Locally-represented companies can develop their experience, beyond sales and marketing, into client support, servicing and maintenance tasks. As such the companies learned of local cost structures for such services and also for production, and comparisons with their own cost structure could be made. Closeness to the market has helped, in case studies Delta and Zeta, with the realisation that local engineering capacity must be utilised to develop machines focusing on the needs of the Chinese market, rather than only on importing from Switzerland.

Companies Beta and Digamma entered joint ventures [JVs] with Chinese partners at an earlier stage. Both were unsuccessful.

- In case study Digamma the Swiss company held an ownership share of 90 %. Although holding such a high ownership share the company perceived it impossible to exert any control over the activities of the JV.
- In the other case the JV was equally shared between the Swiss and Chinese partners, but the JV was closed down following a legal problem. The JV operated a workshop producing mechanical components, but the workshop was built in a location not meant to accommodate any industrial type of work and had to be closed. The sunk

costs for founding the company could not been fully recovered and the financial loss resulted in the closing down of the company.

Company Eta, requested by a Swiss MNE client to join them in China, was asked to enter a JV with an old Chinese state-owned enterprise to locally supply the Swiss MNE. In this instance the Swiss company was faced for the first time with the environment of China and undertook an analysis of the situation. Within the analysis the company learned that it could be very burdensome to collect information about a company in China and as a result many assumptions had to be made, assumptions which, due to the company's lack of experience and reference values in China, were less qualified. The management of the company decided to only enter a business relationship with a Chinese partner if the Swiss partner could exert full control within the new venture, but they felt this would be difficult with the potential partner. The company reached the conclusion they had insufficient China experience to enter this JV and would not be able to acquire the necessary expertise within a reasonable time span. The company felt their core competencies were related to technology and less to business in China and it would be too complicated for the company to deal with Chinese authorities and agencies. As a result it was decided that a future market-entry would only be undertaken with a Western partner; a partner that, through experience, knew the business environment and how to start a business in China.

In case study Delta the Swiss company that planned to enter China via a JV from Taiwan, was also unsuccessful. It was learned that Chinese clients who might purchase the Swiss-Taiwanese products did not appreciate the quality level of the products. In the process the Swiss company also learned how important it is to involve all the staff in Switzerland. When the company took a management decision to found the JV without involving staff, the staff, at a later stage, did not fully support the JV proceedings. Decisions of this type have to be fully communicated and supported by staff of the company.

It was noted that China has a strong media presence that cannot be ignored, especially not by businesses involved in cross-border business transactions. Companies Alpha, Delta, Eta and Zeta said listening to numerous sources of information, such as other business owners and managers, consultants and in seminars, could result in developing a limited and single-minded picture of China. The companies in the study noted that the difficulties of doing business in China are often over-emphasised by others. Such input can create an early opinion of China that makes one overly cautious on market-entry, especially when lacking experience. Although valuable, such information must be questioned to decide if it is relevant to one's own case.

The shifting of markets and the development of expertise go hand in hand. Awareness of the business potential in China has taught companies that there are sound business

opportunities, but also a threat of Chinese competitors. Only when a company fully understands China and market-entry does it realise the real potential, and appreciate China's size and possible threats, which cannot just be acquired from third parties.

5.4.1.3 Early Market Exposure

Serving clients via a representative office, in case studies Delta, Gamma and Epsilon, developed the concept of setting up a production platform in China. Representation in China acted as a door opener, often through Chinese staff, and helped gain an understanding of how competitors in China are active. This led to a positive feeling about being present in China and helped clarify the need for starting local production. However in Company Epsilon such representation helped postpone the necessity of local production. The particular company was, for a long time, content to import products from Switzerland. However, reluctance to enter the market and a delay in taking up activities in China could lead to a situation where a company could be too late with their market-entry. It was noted in case studies Delta and Digamma that competition in China expands quickly, as competitors quickly achieve a good technology level and good quality products. Competitors can thus reach a significant production position, or become a supplier to clients that have moved from Switzerland to China. Such competitors can develop as exporters and start to feed back products to Switzerland.

The companies interviewed mostly considered delay a disadvantage while a proactive position to market-entry could be an advantage. In some areas the business potential was lost to competitors during a phase when the Chinese subsidiary was stable and doing well, without an apparent need to develop. The particular case of Company Delta, previously an industrial leader in its field and one that had set industrial standards, showed that Chinese competitors could develop their products to a degree which became a threat to the Swiss company. By taking up production in China earlier, this threat could have been avoided.

As a supplier with very high standards of intermediate products to its clients, Company Eta was asked by a client to start production in China, a step that was not initially planned. Today the company is able to supply Swiss quality China-made products to its clients, mostly European, which use the components for world-wide applications. But the growing emergence of China and increased interest by the company management in China triggered a process of entry, neither forced, nor really needed by all accounts. However it was felt that market-entry without pressure is much appreciated and more easily tackled now, rather than being pushed to enter China later.

5.4.1.4 Perceiving and Learning Conclusion

The perceiving and learning phase differs across the cases. The main difference is the length an individual firm has been exposed to China and the depth of such exposure. The time span ranges basically from zero, where a company was founded for the specific purpose of doing business in China, up to 40 years where China was originally served *via* a representative office. In one of the cases, with 80 years of company history, China was basically the company's first international expansion. In some cases the first China engagement was in the form of unsuccessful JVs.

It is common to all of the companies that there was a point in time when someone in the company decided to found a WFOE. The decision to enter China did not follow a gradual expansion process or accord with an internationalisation path that followed an incremental development. In almost all cases the common basis was that either the companies or their owners-managers had substantial trade and business experience in China or clients had asked the company to enter China. In each case involvement with China was taken very seriously and was dealt with directly by top management or the owners. But up to that moment business development was based more on opportunities – in the cases of representative offices the focus was on sales. Environment fact finding and information gathering in China was not necessarily focused, and information was mainly obtained through learning by doing and informal networks rather than through a structured information search.

Please refer to Exhibit 16 overleaf for major findings on the Perceiving and Learning Phase.

Case Study	Experience through unsuccessful earlier partnerships with Chinese partners	Media presence from China. Companies are increasingly receiving inputs and attending seminars. Negative views and perception can occur as difficulties in China are overemphasised by others	Companies experience the shifting of markets and see China as a production platform	An open company atmosphere, for new developments and international business, fosters interest in China. Understanding that markets are moving/shifting has developed	Observes that more and more Swiss clients are moving to China and increasingly are asking for locally-made products	Considerable trading experience in China results in an understanding that Chinese clients are becoming more and more demanding. Chinese clients must be better served	Representative office helps develop network in China. Competitors' positions are more closely observed and understood	Local presence helps understand products must be tailored to local needs and engineered accordingly	**Perceiving and Learning Phase**
Alpha		X	X						BtoB markets forces the company to become a producer to prevent clients looking for direct business in China. Previously the company was only a trading company
Beta	X		X						Company originally founded to offer services in China for Swiss companies. One consultancy project resulted in taking up production on behalf of a client
Delta	X		X			X	X	X	Waiting too long to establish production in China resulted in a loss of market share
Digamma	X		X	X	X				First operated in a JV with a Chinese partner. Although a 90 % ownership was held, the initial partnership was not successful and a separate WFOE was developed. The JV experience was very negative, and the company had no intention to re-enter China at first
Epsilon			X			X			Competitors started price war by producing in China and exporting from China
Eta		X	X		X				Company was never under pressure to start production in China, but increasingly understood clients are setting up production in China. Initially considered a potential Chinese partner but came to the conclusion the company did not have sufficient China experience at that time. Only later developed market-entry to China when a new partner approached them
Gamma			X	X			X		The company was contacted by a Chinese competitor during an exhibition for purchase of a machine, and started to be more involved and interested in China
Zeta		X	X	X		X	X	X	Company had long trading history with China before starting up own production. Company followed an out-sourcing culture In Switzerland, but decided in China it would operate an in-sourcing type manufacture

Exhibit 16: Major Findings and Similarities in Perceiving and Learning Phase

5.4.2 – Recognition and Development Phase

This phase is considered the core-phase of the decision-making process, as in Exhibit 17, and within this phase it is decided if a China involvement will be undertaken in more depth. Within this section the triggering of further China involvement takes place. The accumulation of inputs during the previous section has reached a level where the companies in our sample have explicitly formulated their wish to start a production facility in China. This seems to follow a structure, but it must be noted that each of the cases showed a different development in terms of the time taken. Some differences can be explained by length of previous China experience, depth of knowledge, local networks and sales activities in China.

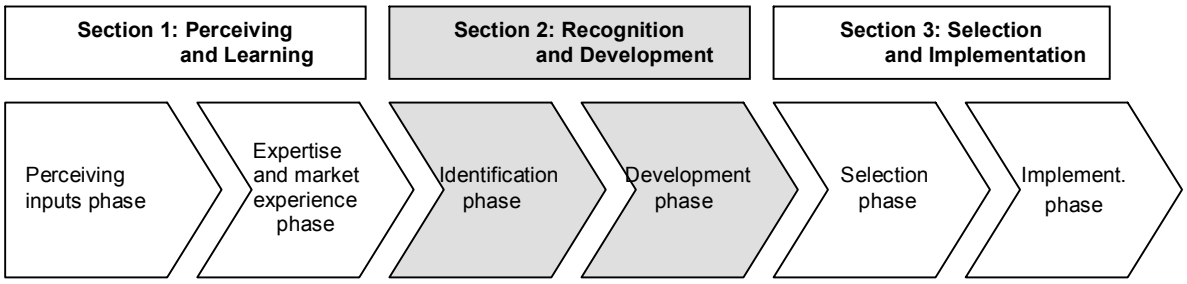

Exhibit 17: Decision-Making Process ~ Recognition and Development
(Author, 2007)

5.4.2.1 Identification Phase

Three of the companies intended to start with a small production facility in China to only operate locally as a small organisation.

- Company Gamma had in mind to start a production facility as it was thought local sales could only be achieved if local production was available. It took the company about three years from the first inputs until this stage.
- In case study Epsilon, in addition to a small production platform planned, the company had had sales in China for many years and from the founding of its representative office it took about six years until production was undertaken.
- In case study Zeta, with about 40 years experience of sales in China, the company decided to set up a production platform in China. The management explicitly wanted a low risk and limited entry to China since they had heard of failed companies and wished to be cautious about their entry.

Companies Digamma and Eta were faced with a situation where their clients started to 'demand' they move to China. In a first stage this was understood as an option but then developed into a situation where clients would look for alternative sources. Both companies felt this to be a unique chance, which would possibly not re-occur. Both these companies had previous joint venture [JV] experience. In one case the company had, about three years previously, only analysed a potential Chinese JV partner, but in the

other case the company was still engaged in an unsuccessful JV that had already been going for about six years. The significant customer demand was, for both companies, the trigger for developing ideas on production in China.

Company Delta had been well represented in China for some 25 years before plans for production were developed, and was well established with its niche products in China. But substantial business loss over the past few years, plus growing competition in China, was a decision point for a revised strategy. At that time all equipment was made in Switzerland but it was realised only local R&D activities in China, together with production, could meet the current and future demands of Chinese clients. The management of the company felt so threatened by the situation they felt they would have to close the Swiss company if they did not start up in China and become more competitive. This company strongly emphasised that in China competition developed quickly and created a situation threatening the company.

The remaining cases did not have such experiences but felt that production in China would bring them closer to their clients, improve their overall competitive position and make them more international.

In this research project, the two smallest companies, case studies Alpha and Beta, driven by their owners, had a somewhat different approach. Both cases intended initially to establish production for export only. In one case the owner had engaged for many years in trading his product and wanted to strengthen his position when he realised clients were showing a tendency to not rely on traders. It was his express intention to lower the overall trade risks by starting production. In the second case production was started when a client wanted to source semi-finished products in China. The company undertook a consultancy project for the client to find suitable suppliers in China. After the suppliers were found the client could not develop the project smoothly. The company took over the project and started production to deliver the goods to the client. These two cases show an opposing tendency. In the first case the agent felt he would be bypassed and over time become redundant and in the second case an agent took over the production role in China to ensure the business could be developed. In the first case the owner had some 20 years of experience in China whereas in the second case the client, a MNE from Switzerland, did not have the required know-how on China. For this company, to extend their production to China, it was more convenient to utilise the consultant who, as a result, founded a production plant for this purpose.

5.4.2.2 Search, Design and Screening

Prominent literature about international market-entry mainly suggests two types of equity ventures; the joint venture [JV] and the wholly foreign owned enterprise [WFOE]. All the

companies interviewed expressed their preference to only enter China in the form of a WFOE. Some companies had earlier experience in China of JVs which had been closed down. All the companies expressed their intention to look for control over their activities in China; control that was mainly understood to be only possible through full ownership. Only Company Eta started with a slightly different approach, and entered China through a joint venture. The JV partner was also a foreign company, which had already set-up manufacturing in China some years previously. Interviewees stated they considered their financial investment in China could only be safeguarded if materialised as a WFOE. Lack of finance was not considered a reason to found a joint venture but a main reason could be a lack of China experience in making a foreign direct investment [FDI].

This phase of market-entry was characterised by looking for information about the different types of market-entry, in-depth information about the business environment in China, increased network activities, potential locations and overall fact finding in China. Overall an increased activity of information collection characterises this phase. This phase differentiates between two groups of companies. The first group is looking for as much information as possible on China to obtain, in their opinion, a broad picture about market-entry. These companies take a position of not neglecting anything important and supporting decision-making with facts; often having to justify their information gathering. The second group has not really engaged in an extensive information search, but is prepared to address new situations as they appear. In this analysis the second group consisted mainly of those companies where the owners are directly the drivers of market-entry to China.

The two cases with relevant JV experience noted that only a WFOE would allow sufficient management control for a venture into China. Any share of equity in a JV, even as high as possible, was not believed to offer sufficient control authority. This was similar to the opinion expressed in the oldest WFOE, founded about ten years ago. Its owner said there was always only one option for him to enter China, which was in the form of a WFOE. Although only a WFOE appears to offer full control over investments, control must be carefully considered as a foreign business owner in China will always need Chinese associate(s) to manage the business and control can take on a different form. The term control should therefore be relative and narrowed down. Although a company might wish to have full control over all business processes, control over finance is indicated as being crucial.

Two of the companies initially sought to enter China with a JV partner. In case study Delta this resulted in a steep learning curve about China but did not materialise in a JV, whereas Company Eta initially foresaw the founding of a new entity between a Chinese and another foreign partner, in total three partners. The Chinese partner decided not to

join the venture and the company was founded between the two Western partners. In case studies Delta and Gamma the companies actively searched for a suitable Chinese partner with experience in the production of the kind of machines they intended to build in China. During the search it became apparent that the wrong partner could easily be selected. As a result the strategy was changed and the search focused only on Chinese companies that could produce complementary components, but the search was unsuccessful. Although there were potential Chinese companies available there were obvious reasons not to join up, including technical standards too difficult to upgrade, threat of losing technology and production know-how and lack of control. In both cases the idea of founding a JV or cooperation was dropped from an overall fear that a Swiss company could have a problem with selected Chinese partners.

Companies Beta, Delta and Gamma did not completely reject the concept of establishing JVs in China, but it was clearly stated that such JVs would only be considered after the firms had settled down in China and after their first market-entry. Future JVs are seen as possible business development in China and could be started once the local market is much better known.

In this phase companies not only draft their opinion about their possible type of market-entry, but also start to consider a potential location for their FDI and whether they intend to build or lease a factory. In Companies Beta and Eta, one of the smallest and the largest company, it was clear within this phase that future production sites could be established at favoured locations. In the first case the opportunity of renting space was offered within an existing WFOE and in the larger company the foreign partner was already established and it was decided to build an additional production plant close by.

5.4.2.3 Conclusion on Recognition and Development

The recognition and development phase includes the company decision towards an in-depth involvement in China. There appears to be a trigger point, where initial experience becomes the initiation of a focused approach to establish an equity venture in China. In the first instance the individual owners-managers are responsible for transferring inputs into the concept of starting a venture, up to a point where the concept takes on its own momentum and the whole organisation agrees on developing a market-entry strategy.

In all cases in the sample of companies sound China knowledge was available. Although such knowledge was of differing and varying natures the companies all drafted the conclusion that any market-entry should only result in a WFOE. This underlines the strong impact the previous phase – the perceiving and learning phase – had on the companies. Although thought to be a period of ‘early market exposure’ there are many perceived inputs that draft possible future entry scenarios. It cannot be claimed within this

analysis that development into an equity venture will be *via* a representative office, nor can the premises to draft a decision that leads to a JV entry be illustrated.

The smaller firms, compared to larger SMEs, are equally eager to develop into an emerging market such as China. They do not seem to be limited by possible size disadvantages. The classification of the cases within this sample shows that the owners-managers situation of a company must be considered while the entrepreneurial circumstances strongly influence the decision-making process. The owners-managers situation also influences the information collection approach. Larger firms, where managers have to address a non-executive board, appear to go through several rounds of information gathering and refinement to establish a broad information base. Such an information base is primarily claimed to support an analytical decision-making process. Whereas in firms where owners are directly involved in the market-entry the information collection is less formal and focuses on what is believed to be essential.

Please refer to Exhibit 18 overleaf for findings on the Recognition and Development Phase.

Case Study	Actual need of products by clients in China and these clients starting to look for alternative sources increasingly influence the company	Realising a set-up in China will strengthen relations with clients	Companies initially foresee only export	Further development of business concept rests on founding of a WFOE. Stories of failed market-entries have a strong influence	A JV in China can be a future option	A favoured location for a FDI surfaces	Worries wrong partners in China are selected and partner evaluation is exercised	Increased period of information gathering about environment and WFOE founding	Key local Chinese person speeds up process	**Recognition and Development Phase**
Alpha			X	X		X		X	X	Chinese trading partner and its network take an important role in developing future WFOE
Beta			X	X	X			X		Previous failed JV helps develop new market-entry as a WFOE
Delta		X		X	X	X	X	X		Initially thought a Chinese competitor could be persuaded to found a JV. The company increasingly worries such a relationship is only to the benefit of the Chinese partner and it would be easier for the company to start from scratch
Digamma	X	X		X		X		X		Company developed its current WFOE although the failed JV still existed. Closing of the JV was not easy and was costly
Epsilon		X		X		X		X		The company analysed a Chinese company with the intention of buying it, but it was more attractive to develop own activities. The concept of several independent suppliers developed and the company only carries out management, logistics and quality control
Eta	X	X		X	X					Company realised they had insufficient China knowledge to start on their own as they are very much focused on technology. The market entry to China was only possible by teaming up with another foreign company that already had experience
Gamma		X		X	X	X	X	X	X	Local representative, working for Chinese competitor, becomes a key employee
Zeta		X		X		X	X	X		In contrast to previous outsourcing projects in Europe the company realised it has to control the whole production process in China

Exhibit 18: Major Findings and Similarities in the Recognition and Development Phase

5.4.3 – Selection and Implementation Phase

This phase is considered an advanced stage of the decision-making process, as in Exhibit 19, and within this phase it is decided how further China involvement develops, with a distinction between a selection and an implementation phase being made.

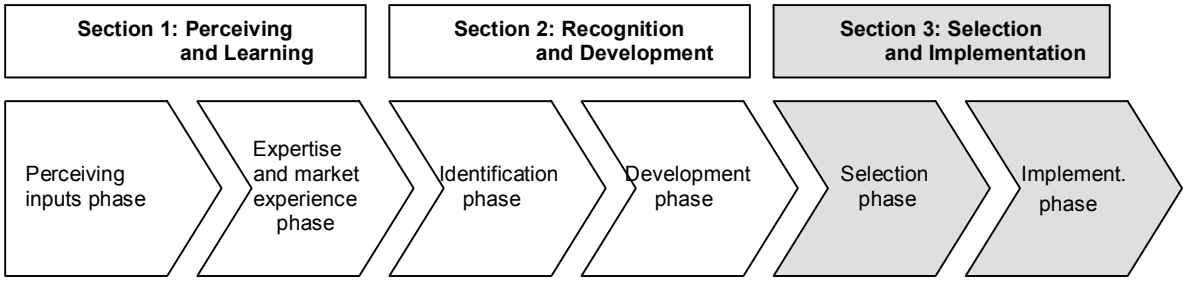

Exhibit 19: Decision-Making Process ~ Selection and Implementation

(Author, 2007)

5.4.3.1 Judgement, Analysing and Bargaining

Within this phase companies take the actual decisions for the type of entry. In the analysed cases it is more a justification of previous intentions to enter as a WFOE and deciding geographical location. Here it is also decided how and where to deal with third parties. Such third parties can be a local government administration and industrial zone and its management, but also key suppliers and partner companies. None of the cases showed a relationship between the type of business, the type of entry form and the selection of a WFOE location. In the analysed companies, there are no restrictions on establishing a WFOE. Earlier regulations might have directed Swiss companies to accepting a less preferable equity form and location.

5.4.3.1.1 Strong Commitment for WFOEs

Five out of eight cases were very clear at this stage that they would only materialise their foreign direct investment [FDI] in the form of a WFOE.

The other three cases were slightly different, but in each case the Swiss company intended to retain major control over its future activities.

- Company Delta actively started to look for a Chinese JV partner as it was explicitly required that a WFOE should not be the only alternative for market-entry to China and a second option must be presented. As the firm did not find a suitable partner, it gave up its JV plans.
- Company Zeta went through an analysis phase including speaking to different Swiss companies and lawyers in China. It reached a decision against a JV after obtaining inputs against a JV from its future local general manager; a senior Swiss manager hired at this stage to implement the company's entry in China.

- Company Eta entered a JV with a Western company, thereby founding a WFOE between the two Western companies.

All eight cases confirmed their wish to enter China with control over their investment, although there were differing circumstances, whereas in four companies, in case studies Delta, Epsilon, Gamma and Zeta, it was primarily related to safeguarding technology and production know-how, in the remaining four cases it had to do with the control of production and product quality, but less about the protection of product know-how or technology.

The aspect of control was mentioned a number of times and further probing showed control was understood to have different dimensions, such as control over finance, staff management, quality, know-how and technology issues. It was further assumed that the values of firms and their intentions are more likely to be transferred within a WFOE. It was also noted that a WFOE allows more flexibility during operations, without the need to report to, or consult, another party as well as others not having insights into business processes. Not only is control over production sought, but the retention of clients through a WFOE is equally important, clients that can be dealt with directly and not through others. A WFOE is believed to prove the commitment of Swiss companies to their clients, not only by being represented in China but also in making the customer relationships much stronger through production. This is seen as especially important where both sales and production are in China.

On several occasions it was mentioned in the interviews that only the implementation phase will prove how much control is, in fact, possible in China after some management experience has been gained. As expressed in one interview, with the company with the longest experience as a WFOE, '*...Also within the concept of a WFOE one needs a Chinese partner who will guide one around*'. A WFOE is seen as creating the only base for control at this stage of market-entry.

5.4.3.1.2 Designing the Business Concept

The companies are sensitive about their technology and would only decide on a market-entry concept that, in their opinion, protected their technology and production know-how. The type of entry – the WFOE – is part of this concept. In case study Zeta it was planned to set up a 'Black-Box' concept in China, thereby creating full control over their supply chain. This Black-Box, in contrast to out-sourcing, enables the companies to in-source components and parts, with the Swiss company operating or co-ordinating the different steps of assembly, quality control and testing. The aim is basically to have independent suppliers that cannot cooperate and communicate with each other and have no influence on the sales of components and equipment, and no contact with end users. This system is considered to protect overall technology and allows for stringent quality control. It will

also allow building R&D capacity to develop local products, and provide an additional opportunity to develop customer relationships in China.

In this stage companies are actively looking for suppliers to form part of their business concept. Such suppliers must be managed in future for consistent quality, timely delivery and consistent prices. Practically all the cases were confronted by this issue, regardless of whether raw material, semi-finished goods or components are being sourced from third parties. It was noted that these interfaces require a lot of management attention in building up the company and need much support during the implementation phase.

Within this stage it was realised by most of the companies, and especially those that rely on their supply chain in China, that they could face difficulties in future if processes cannot be managed properly. It was recognized that a known business concept from Switzerland cannot just be transferred to China. The company must be flexible in adjusting existing procedures and systems to the conditions in China. As the aim of the companies is to deliver good quality products, and in some cases to protect the company technology, it was realised, above all, that operational problems can surface within the implementation phase of market-entry. It was further realised that it is just not possible to analyse the entire environment in a rational manner to look into every aspect, eventuality and risk.

5.4.3.1.3 Analysing and Selection

The firms with previous JV experience, including the one that attempted to enter China *via* its Taiwanese JV, elaborated that the selection of the right form of entry is most important as closing down an existing entry-form is troublesome and time consuming. The firms mostly made an in-depth analysis between the option of a JV or a WFOE, and it became obvious that managers can have a strong pre-conceived idea of their planned market-entry, influenced through networking, media and seminars, and often confirmation of the pre-conceived concept is sought. It was noted on several occasions that one heard of unsuccessful or unpractical JVs that influenced one's own decision-making, whereas a WFOE type of entry was thought to be less risky.

Although there appeared to be strong feelings against JVs it is not *per se* the JV which is the hurdle, Swiss firms and their managers indeed appear to be friendly and open to co-operation. It showed there was a fear of having less or loose control over such co-operations; co-operation that takes place far from home where the Swiss firm could lose its investment and, or its technology, as explicitly shown in three cases in this research:

- In case study Beta the firm had just entered JV negotiations during the research, although this company has been active as a WFOE for about one year.
- In case study Delta the company did not completely reject the opportunity to enter a JV with a Chinese partner after WFOE experience had been collected.

- And finally Company Eta explicitly considered a JV would be a reasonable option, as long as the company had control over activities.

The preferences shown for WFOEs within this research are clear. This is underlined by one manager's statement that only a WFOE stands for a real commitment: '*...A JV has the taste of not having full commitment for a venture that will be given up even before the investment is made*'. A WFOE is thus seen as a strong platform that is culturally homogenous in itself, which a JV most likely will never be. As a result, in three cases, Companies Delta, Gamma and Zeta, the final concept was based on the aforesaid 'Black-Box' that, in contrast to out-sourcing, considers the in-sourcing of products.

5.4.3.1.4 Location

Apart from Company Epsilon it was reported that the companies intended to settle down in an industrial zone; most preferred one with experience of other foreign companies. The main reasons mentioned: a preference for working with people with relevant experience of helping to settle a foreign company, who are able to communicate in English; a developed infrastructure for transportation, power and communication, and an overall transparent cost structure. Other reasons recalled were assumptions on availability and attraction of suitable loyal staff, closeness to competitors, technology protection, distance to harbours and airports and general logistics.

The selection process for the location was shown to be very individual and differed greatly from company to company. A preferred location that, one way or another, appeared in an early China involvement is shown to be the most favoured one. It was commonly acknowledged that the selection of the location must be carefully done to prevent relocation and losing established networks. In case studies Delta and Gamma it was explicitly stated that companies had to set priorities and settle in areas where the most suitable staff and talent are available, often in areas where competitors could already have settled. It was noted in case studies Beta and Zeta that one should locate a company where there is, as yet, less development and staff issues are not yet fully developed, to train people for the company's own purpose and obtain less expensive staff. The staff and general human resource management [HRM] issues are said to be one of the most important issues influencing the location decision for a company in China. It is acknowledged that staff in China can be flexible and move around to find the most attractive job position in terms of salary level and position. Staff and HRM issues have in all cases surfaced at an early stage of decisions on market-entry. Some companies with extensive experience said staff and HRM issues can create continuous problems and often need costly solutions.

The decision on the location appears not to be difficult, and can be based on hard facts. There are many alternatives available in China and many industrial zones trying to attract foreign investors. These industrial zones are fairly well developed, are in competition with each other and are well aware of how to attract a client's attention. In most cases analysed it was underlined that it was quite convenient to collect information needed on the different localities and companies could establish lists of criteria they wanted fulfilled as a basis for further analysis.

In case studies Digamma and Eta the location selection was primarily based on closeness to the company's clients. In the six remaining cases the selection for the location was mainly based on the preference of the local representative or leading manager, or in possible combination with previous business or personal contacts.

Companies Alpha and Eta, the smallest and the largest companies, decided to build their own production facilities whereas in the remaining cases it was mostly planned to rent production facilities, including Company Digamma which decided to build and then lease the factory space. The two companies that built their own factories, and remained in ownership, were of the opinion that only full ownership prevented an on-going rental increase. Reasons against building or buying production space in the other cases were: too high an initial investment, availability or overcapacity of suitable floor space and uncertain development in China. In Companies Digamma and Eta it was found difficult to understand that the legal situation in China only allows leasing of land and that 'ownership' by the companies is so not considered real ownership. It was said that investing in factory space on leased land is considered an unsafe practice.

In the following sections, the eight cases are analysed for the implementation phase and the operationalisation and adjustment of the companies.

5.4.3.2 Implementation

Basically two groups of firms and approach to the founding process of the venture are identified:

- The first group consists of companies that did the application by themselves or through close associates.
- The second group of companies utilised the services of a third party, either a consultant or an agency.

The first group included those cases where the owners were directly involved in the operational side of the business, namely Companies Alpha, Beta and Gamma, and expressed their intention to manage the market-entry as far as possible by themselves. In addition it contained one case where the company hired an experienced Swiss general

manager with experience of founding a company in China, and who is described as having a strong entrepreneurial spirit.

The utilisation of a third party service – consultant service, agency or in case study Eta delegated to a partner company – depended on the available resources and knowledge of the companies. In case study Epsilon the company wanted to undertake the founding process on its own but was hindered in the process. They felt the process was too complicated, full of surprises and they could not cope with the paperwork requested. This company finally used a Chinese consultancy service in founding the company. Company Eta noted their strong technical abilities but felt it did not have the necessary business background needed to establish a company in China. This company relied on its JV partner, another foreign company, which had already set up a business in China. Companies Delta and Digamma used the services of different local Swiss consultancy companies. Both these consultancy companies have shown their experience in placing companies in China. In one company management estimated the opportunity costs would be too high if they managed the founding by themselves. All cases that relied on a third party service reported that the application for the business licence went rather well.

In the cases where the owners themselves developed the market-entry it was claimed that one must be able to delegate some of the process to local associates and that full trust must be given. These frontline people appear to deal locally with the market-entry in a very direct way which could not be managed from Switzerland. There are situations met in industrial zones and in agencies that need immediate explanations and clarifications. As explained '*...there were grey areas met during the application process that the management of our industrial zone had not faced before. As a result favourable conditions resulted for both parties*'. In those companies where the owners relied on Chinese associates it was reported that the 'no-problem' attitude of their trusted people must be carefully considered. Often there are issues that need further clarification, or where the local administration asks for more detail or an explanation. In such situations the Chinese associates may not always appear transparent and may not transfer all requests. This interrupts the application process, which can then be time-consuming. In the cases of Companies Digamma and Gamma the process was stretched out and took longer than planned, so the two companies started production, *via* selected suppliers, before the business licence was obtained. In all cases the application and issue of the business licence was reported, on the whole, to be a smooth process after the mechanism was understood or a third party used. More concerns were expressed in the implementation phase which followed.

5.4.3.2.1 Operationalisation

This phase is considered a milestone in the process of market-entry. The previous and more formal process now turns into a phase where a company's own experience is created. Companies Alpha, Beta, Digamma, Epsilon and Zeta reported that they considered themselves fully operative at the time of this research. These companies have already entered a stage were substantial experience has been obtained, and have even realised which of their initial plans were correct and where adjustments were needed. The remaining three companies have just entered the first year of operation and are optimistic that their market-entry can develop as planned. In all the cases the implementation time appears to take longer than planned; not because of administrative issues or the actual founding of the company, but in achieving stable working conditions and quality. As noted in one case '*...Our positive approach we had at market-entry faded away. Now we realise that we were too optimistic at the beginning. We underestimated the time needed to implement our project*'.

It was reported in all cases that running a company in China needs flexibility as it is not possible to control the China venture from Switzerland or through a Swiss management system. A degree of autonomy is needed. The planned business processes or concepts used elsewhere cannot just be transferred to China. One has to adapt the venture to the Chinese working mentality and business environment.

Practically all companies emphasized that if a company cannot quickly adapt to the business environment in China it may fail. The faster the adjustments are made the more efficient the company will be and the quicker positive business results can be expected. As expressed during one of the interviews '*…Our Company wants to settle down in China. We do have to adjust ourselves to the local circumstances, not the Chinese to ours. It is not possible to change China for the benefit of oneself and to insist on our own Swiss way of thinking*'.

Problems that arise during implementation are of a different nature with the major problems in factory construction issues, HRM and staff situation, product quality, intellectual property, management and business processes.

5.4.3.2.2 Building or Renting Factory Space

Companies that built their own production facilities faced difficulties during construction:

- In case study Alpha, where it was decided to build production facilities, the building was appreciably delayed due to an incorrect cost estimate and the bankruptcy of the construction company. The company initially rented other premises and were able to produce there, but the move to the new facility was delayed for over a year.

- In case study Digamma the construction process suddenly stopped after the central government released a note that there were too many new production buildings and the building boom had to be stopped. As it turned out the construction had started without obtaining the building licence, but the building was be finished after a month's delay and after intervention by the industrial zone's management. The same company had to pay particular attention to the construction of the building's ground floors. The firm's heavy and high precision production equipment needed a high quality foundation, which in the initial stage was not guaranteed by the construction company.
- In case study Eta the company was awarded a piece of land within the selected industrial zone. Shortly before construction began a visiting Swiss manager found the land was heavily polluted, caused by a neighbouring company. The management of the industrial zone offered a replacement. In a later stage of building the budget was greatly overstretched as more costly work for the foundation had to be done.

In all cases one must be involved in every aspect of the construction work and keep an eye on progress. Delays and higher costs are too easily incurred.

In Companies Alpha, Delta and Zeta it was reported that soon after the implementation-operationalisation phase was reached it was found that the initial market-entry factory plans were too small, or space owned or rented was not large enough. In these three cases it was said the companies should have planned for larger development. The potential for growth soon showed more production capacity would be needed. In three cases, Companies Beta, Delta and Gamma, it was reported that new business opportunities materialised that would also result in further growth for the company, which was not considered in the planning stage.

5.4.3.2.3 HRM and Staff Issues

Overall the human resource management [HRM] situation was appreciably underestimated and initial worries were confirmed. As noted in one case '…*One may assume or have heard about the HRM situation in China but one only really gets to know about it after one experiences it. It is really very difficult to deal with HRM issues in China*'.

In Companies Eta and Gamma where activities in China had just started when this research was carried out, the people responsible – in the first case the owner, in the second case the manager hired for the local management of the company – said they were very optimistic for their future HRM. In the first company, the owner has set up several international entities and had sound HRM experience. He was strongly of the opinion that one has to select one local key person, a person that could be trusted, who will develop the local business on behalf of the owner and the company. He had previously met the person who had been trained in Switzerland. In the second case, the company founded its first ever company outside of Switzerland.

The more seasoned companies all consider the HRM situation to be very difficult in China. There were claims from Company Digamma, a company operating under Swiss management in China, that staff fluctuations could be high, whereas in the oldest Swiss WFOE, namely Company Alpha, it was said that they had barely any staff fluctuation. In the latter case the local general manager is a Chinese. The two companies are both close to Shanghai and one appears to have a high fluctuation rate, the other not, so it is difficult to relate this to location influence. On several occasions in the research it was mentioned that Chinese people are highly mobile and can quickly move from one work place to another. It was reported that staff fluctuations might be related to the place a company locates. In one case the company settled in south China and one selection criterion was the assumption that staff movement in south China was lower.

The work mentality of the Chinese people appears to be different to that of people in Switzerland. In case studies Alpha and Delta it was learned that it is difficult to create teams and team spirit, with one person in a group speaking up and showing responsibility. It was understood that people highly value seniority or hierarchical systems and support close relationships. To build functional working groups, as a consequence, is seen to be very difficult as a leader must be fully accepted by team members. As found in Company Delta, a Chinese general manager asked to be downgraded to being a team member, as he was not able to handle his staff and was simply not respected by them.

HRM issues appear to give rise to higher costs than planned. It appears that Swiss operations must extensively support local culture. In case study Digamma the company said they had started to use external consultancy services to find solutions for this increasingly significant and costly problem. They understand that it is necessary to create more job value and opportunities for the Chinese staff to identify with the company and thereby to retain them. Company Zeta found they had to change their staff hiring method, because an initial approach, as taken in Switzerland, did not give the required results. In China a more pragmatic way seems to be more practical; that is to confront the potential job candidate with real tasks so as to give practical experience and an understanding of how one approaches specified tasks.

The implementation phase clearly shows the disadvantages experienced if the Chinese language cannot be spoken or understood. With one exception, case Beta, all the companies and managers needed translation services or communication through their closest associates and staff. It is commonly agreed that the content of conversations, meanings and information gets distorted. If one has to rely on third party translations direct communication is greatly impaired.

5.4.3.2.4 Quality

In cases, such as in Companies Alpha, Beta and Eta, where production depends mainly on the company's own activities, without major inputs from third companies, quality management has worked rather well. Although the work mentality is different the resulting product quality is, in most cases, acceptable. However uncertain consistency of quality is a major issue for those companies depending on suppliers. The management of the interface to the suppliers appears to be a real challenge. Each supplier needs support, which can be a handicap as support often needs to be *via* Chinese intermediaries. Often the Chinese staff member is not flexible enough and not used to working as an all-rounder.

Overall the emphasis on quality transfer to the Chinese suppliers is not smooth and needs continuous support. Language barriers greatly interfere with technology transfer. Drawings and technical content are often understood differently when compared to Europe where production know-how is also different. This results in situations where material specifications, technical drawings and production technology must be adjusted to local conditions for a product to meet final specifications. The local sourcing activities must be supported from the home operation, often an underestimated task, utilising a fair amount of resources.

The management of suppliers and control of product quality is a continuous task. As noted in Company Epsilon, where production started around four years ago, '*…We face continuous problems to keep the consistency of quality. Initially it was fine but later products turned out to be of lower quality. We now receive complaints from our clients and that product quality is sometimes not given anymore. We realise that we need more local quality control*'. In this case the whole China venture is currently being questioned. It now appears that assumed low production costs in China are not really correct, and additional support and management fees have to be considered. Over the four years of operation, indirect costs for support and quality reasons, have accumulated and make the overall product costs higher than estimated. The company realises that support to its China production must be improved to meet the required quality level. As a consequence local production costs have greatly increased.

5.4.3.2.5 Management and Adjustments

The companies with longer experience in China were strongly of the opinion that the entity in China must be regarded as an independent company, running and managed on its own, with extensive autonomy. While there is need of initial and strong support from headquarters it also must be accepted that the local Chinese facility needs some independence. Surprises are common in China and one has to learn to deal with the unexpected. Local management may just work differently and if this is not fully understood in Switzerland it can cause

misunderstandings. It is important to have an open mind, to not overreact and to solve problems as they arise.

As noted in one case '*…There are always things that one never knows on why or how they are in China. Probably one never really finds out. There are situations where we just have to accept the Chinese way, but others must really go the European way of doing things. It is important that we have influence over the processes and know what is going on. Often we have to accept a middle way of doing things and to compromise. Above all, the commitment is important and we will do things here in China and not give up*'.

As an example reported in Company Zeta, IT management systems in particular, procurement and accounting cannot just be transferred to China. Such systems may not be approved in China at all and the Chinese could meet language problems. In addition such systems need much support and maintenance, which for small firms can be a very heavy burden. As an investor this may be very hard to accept as they are part of a control system, and this interface can cause much friction.

It is reported that there are always daily problems to be solved in China that cannot be dealt with from Switzerland. The problem can be small, but needs immediate attention to keep the organisation going. In Company Digamma it was discovered that the import of certain goods and raw materials – foreseen to be duty free – were suddenly required to be taxed. A situation that questioned the whole production cost structure. In another case study, Company Beta, the export regulations suddenly changed in such a way that the value added tax [VAT] was no longer fully returned to the seller, which indirectly made the products more expensive. Again this questioned the whole production cost structure which was the basis of the initial business plan. It is said that laws and regulations can change in China at very short notice. Even the Chinese themselves can be surprised by new conditions.

It was mentioned several times during interviews that local management needs flexibility and the ability to react to upcoming issues. Two local general managers said they considered their positions to be rather like fire-fighters having to solve problems *ad hoc* and watch the daily business so it does not move in the wrong direction. In case study Alpha the Swiss owner said one should set certain guidelines and everything between those guidelines should be accepted as long it goes in the right direction. The strategy must be flexible enough to tolerate small deviations. However it was also said that this aspect also had positive sides especially in that one can accept local conditions which can give rise to new opportunities.

Most of the companies appreciate that their local presence allows the utilisation of

advisory services, for example, from the industrial zones or local consultants as there are often situations that need an intermediary who can deal with new situations. Especially valuable are the services of the management of industrial zones and in such cases a continuous good relationship must be maintained.

5.4.3.2.6 Learning Effects

The cases studied confirm that not everything in the implementation phase can be planned in advance. An analysis within the core decision-making phase and prior to the actual entry decision cannot cover all the aspects that will be faced later during implementation. A company must be prepared to face unexpected situations and be able to show flexibility in tackling *ad hoc* situations, rather than try to consider every eventuality in the preparation phase of the market-entry. As one interviewee said '*…A company should be able to apply practical risk management and consider certain safety aspects – but not overreact, to start to read between the lines – and accept the way of doing things as the Chinese solve problems. Step by step developing and financing helps to lower risks and small step planning seems to be safer. Losses can thus be tolerated*'.

As expressed in this research project by the oldest WFOE, Company Alpha, '*…A company may finally be controlled only via accounting. After the financial year the figures have to be judged and one has to decide if it is a worthwhile business at all. So the given direction of the firm – the initial strategy and its given guidelines – must be reviewed to see if the current business is still within its limits, accepting its dynamics and flexibility but not beyond*'.

It was mentioned that during implementation the company must set reasonable short-term targets, needed for control and which help for orientation. Chinese employees need such short-term targets. This also allows for immediate problem solving as problems arise. In China planning appears to be different and strategic planning even more so. As problems arise they have to be solved *ad hoc*, an emergency plan in China does not work, as it would have to been planned, and planning in such circumstances is difficult. Professional planning is only believed possible after a new generation of Chinese, who understand the western way of thinking, emerge. Long-term planning is fine at the start of market-entry. But during the actual implementation phase it is important to establish short-term objectives and reflect on new inputs. It is believed the strategy must come from Swiss management but the operational management from the Chinese side.

When this project was carried out the firms analysed had started thinking of the optimisation of their processes. In the more seasoned cases it was reported that market-entry had now reached a stage beyond pioneering. It has developed more and more into a situation of administration and stabilisation.

5.4.3.3 Conclusion on Selection and Implementation

The cases analysed have shown that size and owner-manager differences influence the way decisions are made. Whereas it is shown that all SMEs analysed already had a strong intention to found a WFOE there was no one case that purposely made a direct comparison between the option of a JV and a WFOE. In all cases the owners-managers already had in mind to introduce a WFOE for the further development of their business. But the selection phase within this section indicated that firms do reconsider their thoughts to justify a WFOE as a feasible option.

Differences in information handling between the smaller and larger SMEs were observed. Whilst the smaller firms in this sample were managed by their owners it was found a rather informal information search and analysis took place, whereas the larger SMEs have followed a route of establishing a broad information base for further decisions. Although in both groups companies had already opted for WFOEs, in the selection phase the final decision on location was made.

The location selection appears to be somewhat different between the smaller and larger SMEs in this sample. In the owner driven companies there can also be a preconceived idea about the future location; an intention that could be drafted through personal likings and relationships that had been established earlier. The selection phase shows that where managers have to address their non-executive board, in the sample for this analysis the larger SMEs, a more formal decision-making takes place.

This section of the decision-making process shows not only confirmation for founding a WFOE and the location, but that the firms also decide on their future business model and how to control their activities. The WFOE is understood to be the foundation of control on which the business concept can be placed. Regardless of the different sizes of firms analysed in all cases risk minimisation is pursued and thus required control of the new venture. The phase reveals that some firms carry out the business application process by themselves, while others use the services of experienced consultants or agencies. In the latter group it is claimed specialised companies are more efficient for this task whereas opportunity costs could be too high.

The operationalisation stage of this section has shown that the experiences of firms are rather different. In the more recent history of the cases analysed, the operationalisation stage varies between one year and ten years in the individual firms, which has resulted in different experiences and recollection of memories. In all cases it was found the operationalisation stage needs considerable support and, at the same time, acceptance that the China ventures must receive some autonomy.

As the companies have different business concepts they cannot be directly compared. In more technology-oriented companies the management becomes more complex and there are more interfaces with Chinese stakeholders who have to be included in the venture management. The transfer of quality and technology aspects needs a lot of attention, which can stretch a firm. Those firms with fewer technology aspects or which produce single components indicate they face fewer problems. The situation is attributed to the complexity of the business concept in combination with the HRM situation in China. As HRM issues are now experienced directly this is the biggest uncertainty Swiss firms meet during their market-entry to China and will decide what management adjustment is needed.

The operationalisation stage has shown a company needs to be rather flexible, and capable of reconsidering earlier decisions in a pragmatic way. The quicker the company is able to adjust the more efficient it will be.

Please refer to Exhibit 20 overleaf for findings on the Selection and Implementation Phase.

Case Study	Developed market-entry on their own	Realise WFOE is a viable market-entry option	Control over own technology is major reason for setting up a WFOE. Decision for a 'black-box' concept is confirmed	Control of production and product quality are major reasons for setting up a WFOE	Of opinion type of final entry-mode is an important decision rather than just a convenient entry-mode	Settling down in an industrial zone is preferred to cooperate with experienced partners that can support the entry process	Prefer to settle where talented staff is found	Prefer to settle where less developed; to develop staff and own ideas	Rent production space rather than build factory	Realises initial planning was limited and larger initial investment should have taken place	New business potential has developed	Local management considers company works best if it has certain autonomy from home operations; to retain flexibility in new situations	HRM is a major challenge during implementation of the business	**Selection and Implementation Phase**
Alpha	X	X		X		X				X		X	X	Company first rented factory space and then built own production facilities; to expand and be freer in further layout. Owner considers accounting and financial control probably the only controls to understand how company performs
Beta	X			X	X	X		X	X		X		X	A Swiss management system cannot just be transferred to China. As one owner is Chinese an understanding of local business behaviour is found. Company tries to develop sustainable business in less developed areas
Delta		X	X		X	X	X		X	X	X		X	Local operations took on a momentum that was unexpected in Switzerland and management underestimated development speed. Home operations were not ready for this speed
Digamma				X	X	X					X	X	X	The final location is selected to be close to clients and company has arranged a 'build to lease' factory concept
Epsilon		X	X										X	The company came to the conclusion the initial expectations to enter China were too large. It turned out that the need for management support from Switzerland is far higher than expected and also more costly than planned
Eta				X		X								The only company in this research that has entered as a JV (with another European company that is also its client). To be close to this client the company decided to build its own manufacturing plant next door
Gamma	X	X	X			X	X		X		X			As one of the smaller companies in this research the owner thinks the business can only be developed by hiring trusted staff in China
Zeta			X			X		X	X	X		X	X	Company made an in-depth analysis for type of market-entry and options

Exhibit 20: Major Findings and Similarities in the Selection and Implementation Phase

5.4.4 – Timely Development of the Market-Entry Process

The overview on the timely development of market-entry progress does show that individual firms can have a long history of business in China, up to the point where a WFOE is established; one company going back more than 30 years. Comparing the individual cases, there does not appear to be any significant relationship between the period of development, incremental development from export or sourcing, local representation, foreign direct investment and the size of a company. As shown in Exhibit 21 there are some companies with substantial trade experience in China before the decision was made to start up production.

Company Name and Data [Summer 2007]	**Development in China**
Asico AG 1) 1998 2) Nanhui 3) 70 4) 3	- trading between CH and China prior to 1994 - 1994 to 1997 increased thoughts about production in China - 1997 decision to found the company in China, renting production space - early 1998 obtaining business licence - 2004 start construction of own factory building - 2006 transfer to new factory
Proftech International 1) 2006 2) Nanhui 3) 5 4) 3	- 2002 representation in China - 2004 failed JV with Chinese partner - 2005 sourcing project for large Swiss customer - end of 2005 decision to be active as an own entity in China for sourcing - April 2006 being operative
Frutiger AG 1) 2007 2) Changsha 3) 3 4) 21	- 2003 first contacts with Chinese during exhibition in Germany. Future GM met - 2004 visiting exhibition in China and decision to have own exhibit in 2006 - 2005 product development for China market - 2006 founding of RO, sales market analysis - 2006 display of products at exhibition in China - Early 2007 decision to found production - Mid-2007 obtain business licence
Metar SA 1) 2006 2) Shanghai 3) 9 4) 25	- 1985 RO in China - early 90's JV with Taiwanese company for export to China - 2004 first thoughts about production in China - January 2005 decision to found production - April 2006 registering the company
Stopinc AG 1) 2005 2) Shanghai 3) 7 4) 60	- since 1992/3 export to China - 1996 founding of RO - 2000 analysed local company that could be bought for production, not bought - 2002 assembly and production via 3rd party - April 2004 decision to found WFOE - November 2004 received business licence
Plaston AG 1) 1996/2004 2) Jiaxing 3) 130 4) 130	- 1996 founding of JV - 1996-2000 fluctuation of activities and relation to JV partner not good - 2000 own clients from Switzerland go to China - 2001 and 2002 plans to found a WFOE - March 2003 Evaluation in China - November 2003 Decision to found WFOE - until April 2004 Evaluation of locations and factory building [build to lease) - April 2004 received business licence - October 2004 start of production
SSM – Schaerer Schweiter Mettler AG Textile Division 1) 2003 2) Zhongshan 3) 50 4) 220	- prior 30 years of sales experience via Hong Kong office and import to China - 2002 realising that production in China is needed, start of research - May 2003 hired Swiss GM to develop China production, evaluation of locations - April 2003 finishing business plan - May 2003 obtaining business licence - May 2004 delivery of first machine
Wolfensberger AG 1) 2006 2) Foshan 3) 23 4) 240	- 2003 evaluation of JV with Chinese State Owned Enterprise, did not materialise - February 2005 contact with partner, a foreign company, to start production - June 2005 evaluation in China and first business plan - September 2005 agreement for cooperation between partners, the foreign company and own company, to found WFOE - January 2006 cooperation contract - May 2006 obtaining business licence - July 2006 start of factory construction - February 2007 start of production

Notes: 1) Established in China 2) Location in China 3) Staff in China 4) Staff in Switzerland

Exhibit 21: Development of Individual Market-Entry

(Author, 2007)

In a cluster of three cases, those of Companies Beta, Eta and Gamma, there was no such experience and the WFOEs were basically started based on client demand. This cluster includes both one of the smallest and the biggest companies researched, which did not have a representative office prior to start of production. Common to all the companies is the relative short time span for implementation of the WFOE after the decision to make the investment. Once the commitment was in place and the business application process started it took the companies between three and six months to receive their business licences. In four of the cases the production of components had even indirectly started, through sub-contractors, before the actual business licence was obtained.

Preparation to apply for the business licence is important and if this preparation work is done properly the later process will proceed more smoothly. All companies commented that the founding process went well once the process was fully understood. It was indicated that nowadays such processes follow a given and known path in China. The information gathering is also not difficult and a relevant information base can be obtained. The case studies show that once the business licence was obtained the firms quickly moved to the stage where the first products were manufactured. In Company Zeta, where a complex textile machine is produced, it took no longer than one year from writing the business plan and founding the company to delivery of the first machine.

The interviewees in all the cases reported they were satisfied overall with the timely development of registering their companies and taking up production in China. Considering the circumstances in China the registration of a company went quite quickly, although some thought that the duration of the actual process was unnecessarily lengthy. But only two of the analysed cases, Companies Delta and Epsilon, complained the business application process was either too long or had unnecessary bureaucratic steps and harassments. In retrospect they did remark registration was nevertheless not too difficult.

All the cases reflected on strong market knowledge and networks being established prior to the founding of the WFOE. The suppliers and partners needed were partly known and already evaluated, and the founding process was understood to be a formal process. The production of complex textile machines mentioned earlier underlines how fast such a development can take place if people are entrusted with implementing such a project and have previous experience. The particular company employed an experienced Swiss manager for this task.

The implementation phase and operationalisation of the company is a process that cannot be fully commented on for all the cases researched. It is an ongoing process that will need adjustments over time, possibly years, as shown in those cases where production started in, or before, 2004. Only in one case, the oldest WFOE, had a return on investment been

reached at the time of this research. The indications in all cases are that the companies are prepared for implementation as being a long process. A comment from one company: '*…Considering the differences of the Swiss and Chinese systems, mainly trade and fiscal related, and the need to adapt one's business to these circumstances it can be said that a quick company establishment is difficult to achieve in a short time in China. The quicker it takes place the more problems will surface*'.

5.5 Influences on the Market-Entry Process

The previous part of this analysis focuses on the reasons why firms enter China, the relevant firms' background, the entry process and its timely development. In the following sections how information gathering takes place, the environment impact of China on firms and the significance of relevant networks are analysed.

5.5.1 – Information Gathering

All participants in this research project noted that once they were actively looking for information on establishing a WFOE such information was readily and easily obtained. The interviewees thought the collected information was reliable. In most cases no initial reference values were available, and companies often collected information from different sources to cross-check if information could be trusted.

Early information gathering often started through attending seminars in Switzerland and talking to experienced owners-managers of Swiss companies that have set up operations in China. But seminars and first hand experience often resulted in a rather one-sided picture about market-entry to China. Experienced owners-managers often talk about difficulties of setting up a China venture, but it must be considered that not everyone openly discusses their own way of success. Listening to others can possibly result in a misconception about China; can distract from one's own needs and false barriers could be established. Although the companies analysed had differing experiences and histories in China, including staff with different experiences, the companies were capable of acquiring information through both formal and informal networks.

5.5.1.1 Stages of Information Gathering

The companies were generally looking for three types of information.

- In the first round they were looking for market potential and, or production costs as well as business set up information. In practically all the cases the companies operated through a representative office [RO] or otherwise possessed extensive China experience. The early stage of information gathering was perceived as an informal data collection or verification phase. Within this stage it was an aim of the companies to understand the cost structure for production and to see if their venture could be competitive. Within this round it was shown to be an aim of proving if a

production set up in China was justified. This early information gathering stage took place during the first two phases of market-entry development: the perceiving and learning phase and partly within the subsequent recognition and development phase of the process.

- Although connected to the early information needs, in the second round the companies looked at process and product quality issues compared to their own ventures, and, in cases of co-operating with suppliers, the establishment of continuous processes and quality. It was underlined that companies within this phase are more demanding in their information needs, ask for verification of first round information, and already enter a stage of selection. Certain preferences for future suppliers, location and staff are drafted.
- The third aspect of information needs was about founding a company in China. This stage was perceived as quite simple since plenty of support can be obtained from official agencies, lawyers, consultants and similar sources, and also from other Swiss companies. In two cases it was explicitly noted that one must distinguish between average China knowledge and particular knowledge needed for an individual company, as well as relevant detailed issues on market-entry. Company Digamma had the experience in founding their business that procedures and the staff situation varied greatly between the Shanghai area and a location about 50 kilometres away from Shanghai. After a company has acquired a strong base of information it must elaborate on this information and confirm if it fits the particular business case.

5.5.1.2 Reliability of Information

The tendency indicated is that Swiss firms, after an initial informal round of information gathering is concluded, are going to enter an in-depth information collection phase. In five Companies, case studies Delta, Digamma, Epsilon, Eta and Zeta, this resulted in an extensive local information search in China. Those companies that already had a RO partly used their representatives to help look for information. The other three cases, Alpha, Beta and Gamma, are companies where the owners-managers had extensive China experience either from trade or project management. In China information gathering was considered fast and direct. It was noted that agencies in China and in the industrial zones want to attract foreign investors and cooperate very professionally with companies. Potential co-operation partners, needed for future production, are reported as very keen to develop business relationships. Information from official sources was said to be trusted. However it was mentioned on several occasions that information from potential Chinese partner companies, suppliers, or even collected from close Chinese associates must be questioned and correctly interpreted. Often such information can have uncertainties from being non-fact based, due to less experience or guesses, contextual settings not known, no

direct source available or source unknown. It was noted that information from Chinese informants could be over-optimistic – often based on emotion – and temporary in nature.

In one of the cases it was mentioned '*…Information gathering in China is done much more carefully than in Switzerland and companies are looking more for hard facts. In Switzerland one can rely more on soft facts and one is able to make more assumptions about situations or business partners since all are in the same system that is known to everyone, everything goes according to the same norms*'. It was found that unspoken information in China can also be important and one has to learn to understand and judge situations; to read between the lines. Information should be gathered in a consistent manner, and should not be ignored if required information is absent. Alternative and creative ways should be applied to obtain needed information. In several interviews it was said Chinese people would not give all available information unless specifically requested as they may think such information is not of concern or relevance. Generally all the companies noted that, during the information gathering phase, it was difficult to sum up information on HRM and the staff situation as needed for a particular company case, as the collected inputs and experiences were too different.

5.5.2 – Business Environment Impact

The interviewees said the Chinese business environment had a great impact on them. The analysis shows specific China factors are of concern to a firm and for its business development.

5.5.2.1 Language

All interviewees commented that knowing the local language is the key to success in China. At an early stage of market-entry companies already face situations where trusted translations are needed, often beginning when a company searches for early market information. Language is considered a major problem to be overcome in China; an issue persisting throughout, from first contacts until management of fully operational production.

This major problem in China is that foreigners often cannot directly communicate with the Chinese people. Even in larger organisations there may only be a few Chinese people that can speak and understand the English language. It was found younger people are more often conversant in a foreign language, whereas, in many cases, the older Chinese never had the motivation to learn another language, as the internal markets in China in which they are active are large enough without the need to communicate in English. Younger people, who speak English, will not speak up or explain situations to their senior managers due to their lower hierarchical position. This was a substantial hurdle when one

of the analysed companies was trying to address seniors in a company to line up direct business relationships but could not reach them due to language difficulties.

Language, combined with knowledge of the Chinese culture is an even better key for success. Often one cannot be completely sure translations are done correctly. It was sometimes thought that even if a Chinese person translates that something is possible it could already mean 'no'. The proper translation of such statements may only be possible if the context is fully understood. The correct translation is not limited to the spoken but is also important in the written language. As expressed by one interviewee '…*We were told never to sign any document that was written in Chinese. There must always be a written translation to it and both documents must be considered equally in front of any authority*'.

Company Beta is in a comfortable situation where one of its owners knows the Chinese language. It was noted it is a great advantage if translators are not needed, as it prevents many misunderstandings, mistakes and time loss, caused by lengthy or wrong misinterpretations. Language sends out signals of respect in China, and business partners are much more careful about what is being said or not being said.

Knowing the Chinese language is considered even more important after the local business develops. In several cases it is explicitly said that the local business can only be managed and developed if the local language is known. In case study Delta the Swiss management of the company, for this reason, said the local manager must be a Chinese as often Western managers are not capable of acquiring sufficient Chinese language skills. In Companies Alpha and Digamma it was considered important that the Chinese language be fully accepted as there are often no alternatives and not everything can be translated – it is just not possible to follow up everything in English. A strategy of trust and acceptance must be developed, though control as in Switzerland is not always possible. Companies Alpha and Gamma noted they had built up much trust in their local Chinese general managers and utilised their language skills without depending entirely on translators. They believe that only trust brings these managers closer to the Swiss operations.

5.5.2.2 Culture

Culture can have many inputs and extensive definitions which go beyond the scope of this dissertation.[149] A specific definition of culture was accepted and the interviewees indicated from this the differences between China and Switzerland. During the interviews two different phases of cultural understanding were met: the first during the original

[149] See Hofstede (1984): Culture is the collective programming of the mind which distinguishes the members of one category of people from another. Damen (1987): Culture is learned and shared human patterns or models for living; day-to-day living patterns. These patterns and models pervade all aspects of human social interaction. Culture is mankind's primary adaptive mechanism.

involvement in China up to the point where firms started to consider taking up production; the second after the firms had actively taken up the decision phase and implementation of the project, and after more experience on China's environment had been accumulated and owners-managers were more acquainted with the environment in China.

5.5.2.2.1 Culture ~ The First Experience

It was generally agreed that China is very different from what people are used to in Switzerland. One interviewee expressed his experience of having the feeling that one is stuck in a situation in China and that there is no escape. In such situations it becomes clear that one depends very much on other people in China and one needs support from Chinese middle-men. Some situations in China cannot be explained and just have to be accepted; one has to go through this in a pragmatic way. In case studies Alpha, Beta and Gamma the business environment in China was judged to be different to that in Switzerland but not too difficult to deal with. It was said China is not that difficult in a cultural sense and the Chinese are pragmatic in their dealings. In China there is a certain pragmatism reflected in the materialistic behaviour of the Chinese people. These three cases are companies where the owners have broad experience in the Far East and were the drivers of market-entry.

On several occasions it was mentioned that it was not always easy to understand situations where Chinese people would agree to something because they are afraid to say 'no'. 'Yes' and 'No' must be related to the context and, if in any doubt, questioned as to their real meaning. In Company Zeta it was felt that in larger organisations the Chinese are often disinclined to make agreements or commitments in front of others. However in smaller Chinese firms people are capable of making fast decisions and can quickly say 'yes' or 'no' to a situation. On several occasions during the interviews it was mentioned that it appears that Chinese people do not seem to like to take responsibility.

In case study Epsilon it was judged that the aptitude and mentality of the Chinese were largely underestimated in business planning and that the Chinese appear to be very complicated and very different to deal with. It was considered that one has to adjust to local cultural circumstances but still keep one's own values. Culture should neither be given up nor copied in an effort to gain business opportunities. The Chinese are very pragmatic in establishing and maintaining their business relationships. If a company or a person is interesting to do business with, the relationship is kept alive; if not it will wither. It is considered crucial that one is able to socialise. Business is largely influenced by social contacts or goes hand in hand, which is not much different to Switzerland. Relations between people are most important. For most of the interviewees China was not something completely unknown to them, so the difference in culture did not come as a

total surprise. It was agreed that if one can overcome cultural barriers one can achieve success in doing business in China.

5.5.2.2.2 The Impact of Culture

Culture was observed to be deeply rooted in China and the interviewees expressed the feeling that the behaviour of people cannot be easily, or quickly, changed. In most cases it was agreed situations, as met in China, must be accepted as they appear and that it will take some time, even generations, until Chinese people are able to adjust and get used to Western behaviour. It was agreed amongst the interviewees that, for the time being, foreign companies must take the lead in approaching cultural understanding and showing flexibility in their business behaviour. As said in one instance '*…we are only guests in China. We have to adjust ourselves to the local circumstances*'.

It is claimed an understanding of cultural issues and way of thinking in China must be developed, and it must be accepted there are more cultural differences between Switzerland and China as compared to other countries. As understanding often starts with language it can be a handicap for foreigners who have difficulties learning the Chinese language. One has to be prepared for problems to surface due to this fact, but such difficulties can barely be quantified and have to be faced as they appear.

It was said by interviewees that the Chinese have their own point of view about matters, and will not necessarily reveal everything about an issue, may even think it is not of concern. One has to ask several times and may even never receive all the answers needed. This can create situations on unspoken issues, issues that may later appear in a process. There are situations where a company has to accept the Chinese way of doing things even if one is not capable of understanding the logic. The Chinese often have a different point of view on how to make something in terms of the process and with whom.

Different ways of approaching a target should be tolerated, which should be accepted if the target is reached. It was basically expressed in all the case studies that Swiss managers had to learn how to make compromises. Such situations often cannot be understood by management in Switzerland which has no exposure to the context of the situation. There are also occasions when both views – the Chinese and the Western – must be accepted and which ideally support each other. But the most difficult situations are said to be met when the Swiss way of doing things must be accepted by the Chinese without any compromise.

In case studies Delta and Zeta it was said that during their business application processes these companies had to accept and understand the local culture and take a position that the Chinese administration also faces a new era, and needs to adjust. In accepting this, a foreign company can understand a business application process may not run smoothly.

One has to learn to do what is needed in China and not what one wants to do, and not think one's application process is not dealt with seriously. Similarly during the founding of the company one has to adjust to the needs of the management of the industrial zone and not *vice versa*. If this is understood things can develop well in China. Misunderstandings have to be cleared at an early stage so all involved understand the meaning, otherwise there will be moments when unsolved issues will come up again and again.

In Company Zeta it was noted in China one is more careful in analysing or judging potential partners or situations. There is a tendency to question more to find out what is available and to question from different angles. In Switzerland there are approximately equal values amongst people; values that do not need an in-depth questioning of a situation. But this was not felt to be the case in China, where a stringent analysis is required.

During this research it became obvious that there are major cultural differences between Switzerland and China, emphasising the great impact China has on the companies. It was confirmed that to run a successful business in China people are needed who know both cultures and who are capable of communicating between the cultures. Although such people are rare they can prevent many misunderstandings, often believed to be a reason for problems within a company's HRM.

5.5.2.3 HRM and Staff Issues

Most of the companies had relevant China experience prior to the decision to start production in China. Experience with HRM and staff situations was of a different nature between the cases and ranged from employment of RO staff, JV management, trade and project management. All interviewees remarked that during the development of the market-entry one of the biggest unknowns was the future situation on the employment of people. The firms were prepared to offer considerable support for HRM from Switzerland. The manager of one of the smaller firms remarked: '…*We were afraid that we could not attract suitable staff and talent. We thought that our company might lack attractiveness for Chinese staff*'.

It was broadly agreed by the companies that expectations on future staff and its management could not be related to Swiss conditions. The experience and training in China – for example, no apprenticeship system in China – obviously differs from Switzerland, but it is recognised that well-educated staff is available in China, or people that are eager to learn and develop themselves. Chinese people can have a very good education and experience, sometimes through training in foreign firms. The cases analysed showed Swiss management was often afraid the Chinese staff would have an attitude of continuously changing their jobs. Lack of loyalty from Chinese employees was listed as a worry for Swiss firms in China.

It was remarked that the staff experience available to the firms might not be sufficient for the founding of a WFOE. Companies Delta and Epsilon, which had operated for many years through a RO in China, faced the situation that their own RO staff could not help them with the business application process. Both Companies hired an external consultancy service for this task. In the first case the company simply had no experience in its own staff suitable to found and implement the WFOE. In the second case the company management was of the opinion their local Chinese general manager showed little interest in developing the new venture.

In two other case studies, Companies Alpha and Gamma, the owners-managers were strongly of the opinion that only the previous selection of the most suitable local associates – in their particular cases the selection of Chinese managers – helped them reach their current success. In case studies Digamma, Eta and Zeta it was reported that the future implementation phase of the companies could only be successful if their general managers had relevant international experience. For this reason general managers were hired especially for the implementation phase, and, in two of these cases, even within the business planning phase.

5.5.2.4 Technology Aspect

Four of the researched companies, case studies Delta, Epsilon, Gamma and Zeta, started production in China for products that needed technology protection. The business environment in China was perceived as such that technology and production know-how could be lost if no safeguards were established. In the Epsilon case it was reported that the Company felt the Chinese government indirectly forces Western companies to transfer technology to China and the Chinese laws are perceived as not really protecting foreign technology. This particular company came to the conclusion that only older technology products should be produced in China which are least vulnerable for copying by others, or alternatively that not all technology is revealed in China, for example, in the form of key components, drawings and processes. As a consequence production in China may not necessarily be for all components or products. In the remaining four cases it was reported the products and processes are not that critical and do not need any special technology protection.

In all the interviews it was learned that the meaning of technology can be very differently understood in China and a Swiss company cannot just transfer *technology* to China. In particular misunderstood product and manufacturing technology can result in a different end product. In addition Swiss and Chinese quality standards – especially the understanding of quality – can greatly differ between China and Switzerland. Technology transfer can, as a result, be very complex and early compromises on single aspects can turn a final product into a non-acceptable product. For this reason the overall product, its

manufacturing and materials must be completely understood and, perhaps, eventually adjusted to local conditions.

Within the core decision phase, when companies have already clarified the feasibility of their project, produced sample components or selected suppliers, a time-delay period can occur until final product quality is reached. The language barriers mentioned earlier can make technology transfer even more difficult and it was commonly understood the build up of production needs considerable support and ample time. Starting production in China is not only about copying products. The full manufacturing processes and the understanding of components must be transferred to conditions in China. In several cases this was largely underestimated and needed extensive and continuous support from Switzerland.

But the difficulties in the transfer of technology, and understanding the production and technology level in China also has some advantages for the cases analysed for two reasons. The situation should not only be regarded a threat, as:

- First, in a broader understanding China was learning to be a technology partner. For Companies Delta, Gamma and Zeta it was explicitly reported that utilisation of local products and production know-how helps the companies locally develop products that could not have been developed from Switzerland. Especially when Chinese engineers were employed who had R&D capabilities. The companies have learned during their early exposure and within the evaluation phase of market-entry that local know-how can be acquired and business potential in the local market can be developed.
- Secondly, the perceived lower production technology in China has indirectly proven to the companies that competitors cannot just copy their products. If the Swiss company initially is able to sell less complex products in China – that are difficult for production by Chinese companies – but, at the same time, develop more sophisticated products, a competitive advantage can be established. Chinese clients, possibly new clients, can be convinced to buy existing technology and a customer relationship is established and maintained, with such clients purchasing more sophisticated products in the future.

The technology aspect must be considered from different angles that finally result in control over activities, including technology management. In all cases it was stressed that the companies are looking for as much control as possible. In cases where know-how protection is sought it is believed this can be done *via* a platform that is described as a ‘Black-Box’.

The Black-Box concept is believed to safeguard against copying and includes stringent quality management of components and suppliers. The principles are that individual suppliers know only their designated products – single components or sub-assemblies – and do not know other suppliers or the whole manufacturing process. Key components can be imported or made locally by the company, and technology sensitive parts are not necessarily produced in China or are, at least, shielded from others. Management of drawings and the overall coordination of activities are done by the company. Leaving the protection of know-how aside this helps the company take a focused approach on component supply *via* its suppliers and supports them in a most efficient way. This concept indirectly means that only a WFOE is suitable for this type of management as a JV would not have the strengths to do so.

5.5.2.5 Legal Issues and Dealing with Officials

Several times in the interviews it was mentioned that the business environment in China is perceived as different from what companies are used to in Switzerland. It is noted companies can feel their cases are dealt with in a very bureaucratic way after they apply for business licences. However Companies Beta and Digamma have previous JV experience and in the past had already gone through a business application process, and together with the oldest WFOE, they confirmed that within the last ten years dealings with officials and business application processes have largely improved. The more seasoned companies in this research noted that the laws and regulations in China have greatly changed over time, and a foreign investor gets the feeling that dealing with officials is getting less complicated, and that there is improved security for a company's investment in China.

Those companies that have just completed their business application process expressed the feeling that a business application is a complicated process in China and not really transparent. In case studies Delta, Epsilon and Eta the companies made the decision to carry out the application process through a third party; specialised consultancy companies. It was felt the Chinese officials that dealt with their cases were either not competent or the Chinese law-makers make the processes too complicated, often asking for the same information twice. In contrast to these are the cases that have, from the beginning, looked for the contact to industrial zones in the belief that the management of such zones will guide them through the application processes, and will, additionally, support them when the company becomes operational. The different approaches all explicitly emphasise companies looked for local support to manage their business establishment in China.

In retrospect the companies perceive their market-entry as smooth and relatively short, but comment that the business entry process needs an ample time span and one should not get

frustrated about seemingly repeated questions or re-submitting papers and certificates. It was commonly agreed that it was not difficult to obtain information on how to establish a company in China but it was the actual process of how the application is processed that raised some concerns and which was shown to be handled individually from case to case. From a more time-distant point of view – after some time had passed since the application process was done – it was said on several occasions that companies face the dynamics of changing laws and regulations in China after they take up activities in China, and that the exact meaning of laws and regulations are only understood after activities have started and the company faces the impacts. The margin of interpretation of laws and regulations is assumed to be rather wide in China. This can have advantages but also disadvantages if the law-makers insist on their interpretation, as indirectly shown in the case of Company Beta that had to close down its previous JV factory. It was claimed by the local authority that the factory was not allowed to operate within a particular area. The office that issued the licence held the opinion that in the designated area the operation of this type of factory was allowed, whereas the higher authorities judged the case differently.

Laws and regulations in China have been reported to change with short notice and new legal issues appear, and sometimes even the Chinese themselves are surprised. Although laws and regulations are developed for the better, sudden changes can upset business processes. As an example it was reported that import laws suddenly changed which made the import of production machines needed more costly, or in another case that export products were suddenly taxed differently, which, as a result, made products more expensive. The understanding of laws and regulations and their interpretation is an ongoing process in China and the full extent can often only be experienced once operationalisation of a company has taken place.

5.5.2.6 Future Development in China

Within the pre-entry phase the interviewees had a variety of thoughts on how China will develop in the future. The companies interviewed dealt very differently with their own outlook about China and how safe they perceive their investment. It was commonly agreed that an extended outlook would be very difficult, which, as a consequence made long-term planning even more difficult. The interviewees agreed, in general, that current development in China is not homogenous across the country and that, in their opinion, China has to further develop for the whole country to reach an equally developed state. The opinion was shared that this is also the general strategy of the Chinese government and, as such, gives a strong base for justifying a company's investment in China.

The laws and regulations are also perceived to have developed in a way that makes investors feel more secure about their investments with the laws showing a tendency to develop greater liberalisation. This was especially noted in the more seasoned cases. Still

for SMEs the market-entry is planned in such a way that a loss in China due to unforeseen reasons would not result in a collapse of the whole organisation. Indicated in several cases investment in China is done in a way that either no large investment is done, e.g. by leasing rather than building factory space, or investment is in small and thoughtful steps so the risk of investment is not too high.

5.5.3 – Networks

In the analysis it is shown that the companies researched had different China experiences before the decision to found a WFOE was made. The different experiences resulted in different networks and relationships in which an individual company is embedded. Such networks can be more, or less, formal and at the same time be more externally, or internally, oriented.

5.5.3.1 External Networks

Most companies started by contacting other Swiss firms, with relevant China experience, to learn about China. The companies looked for first hand information in seminars and from firms that have direct experience. Over time seminars about China lose their significance, and are believed to be important at a very early stage of market-entry, or thereafter if they are on specific topics of doing business in China.

Other Swiss firms are contacted in Switzerland or during visits to China. As noted earlier the contacts in these firms and information obtained have to be treated carefully as often firms only underline their difficulties in China, or even say market-entry would not have been done if all the difficulties had been known in advance.

In three case studies, Companies Delta, Gamma and Epsilon, the Swiss Business Network [Osec] was consulted for advice on market-entry to China. Osec has, through its business hubs in Beijing, Shanghai and South of China, relevant networks that can support Swiss firms in their market-entry to China. Osec supported the Epsilon Company in a very early stage of market-entry and later, through its business hub in Shanghai, when the business application process did not develop smoothly. In the advanced progress of market-entry the companies appreciated the services of industrial zones where they intended to settle. After the business licence was obtained the management of these industrial zones also greatly supported companies to solve daily and upcoming problems.

Information from interviewees indicated that a local external network in China is also needed for the development of the market-entry process. These networks can include Chinese and also Western consultants with sufficient experience who all have their relevant networks. Chinese people are especially favoured as they speak the language and can deal with tasks and problems in a direct way. In case studies Delta and Digamma the

companies used external Swiss consultancy services, both of which have businesses in China with relevant China experience and staff. In cases Alpha and Gamma, the companies employed Chinese consultants who later became employees of the company and are now acting as general managers in China. The external network is most important during the first concepts of building a WFOE and during the business application process. Then the external networks appear to become more informal with less external advice sought and after substantial experience by the individual companies has been made.

External networks have not been of too much relevance for two of the companies analysed in case studies Alpha and Beta. The two companies claim business development was carried out by the owners of the company. These owners have extensive relationships from earlier activities in China and one owner speaks the Chinese language, as she is an ethnic Chinese.

5.5.3.2 Internal Networks

Companies Digamma, Gamma and Zeta had previously established production platforms in the Czech Republic. All had relevant China experience, either through sales activities or JVs. In cases Alpha and Beta the companies have extensive previous China experience. The remaining three companies either had no direct international experience or were initially too small to build relevant international experiences that could be reflected in an internal network. In case studies Delta and Epsilon it is stressed how important the internal network can be in setting up a WFOE. For Company Delta an early JV with a Taiwanese company failed, as, it was believed, little support was given by staff. In Company Epsilon, in the operation phase of the company, the staff did not support the China venture and the process was only supported by the management of the firm.

Internal networks are important to successfully develop the China venture. The cases in which production platforms in the Czech Republic have been established show company staff contributes much to the development of the firm. The contribution can be of two kinds:

- First, it can be moral support where the staff appreciates working in a global company and cooperating with entities away from Switzerland.
- Secondly, there can be managers with relevant international or China experience that can contribute directly to the establishment of the venture in China.

It has also been shown in the larger of the companies, where the non-executive board had some influence in developing the China business, individual experiences of board members can contribute largely to the entry process. Such board members can not only contribute through their own experience but also question information and process steps in a constructive way.

It is reflected in the research that internal network contributions increase over time and external inputs decrease during the market-entry process. The company's own staff become accustomed, and can contribute, to the process. New experienced staff may join the company and an external network or available know-how becomes part of the firm's capabilities. This took place in five of the companies: in case studies Alpha and Gamma, Chinese externals were hired, at a later stage, to be the companies' designated local general managers; in case studies Eta and Zeta, internationally experienced managers, one with previous China experience, were recruited to develop the ventures; and, in the case of Company Digamma, one of the Chinese advisors was appointed to the non-executive board of the new venture.

For the companies with insufficient China experience, the employment of experienced staff is an efficient way to obtain suitable China experience towards quickly developing the WFOE. China experience, as commented on, on several occasions, must be available in-house and not depend on externals. The value of external networks had been much appreciated but it appeared unanimous that the companies analysed firmly intended to generate their own expertise and be less dependable on external networks. The common opinion was that a company must make its own experience and decisions, and apply learning by doing.

5.5.3.3 Relationships

In China personal relationships are very important. The interviewees reported that the people who make the business contacts are the most important in the first place and not the company. A company and its employees must ensure that they can establish good relations in China which can help to develop the business. However this must also be approached with an open mind and one should not allow one's self or the company to be taken advantage at in the first place.

It was learned in the case studies of Alpha, Beta and Gamma that a company and its managers should accept local circumstances and make every effort to integrate and to socialise. Chinese people appear to be very emotional in their interactions with others so it is important that people are close and support each other. However, as foreigners face the difficulties of language barriers, Chinese people are often needed to act as a direct bridge. It was seen as a major advantage in the smaller companies where either the owner, as an ethnic Chinese, knew the value of establishing good relationships but also knew the language, or Chinese people became close associates in China and helped establish and maintain the necessary relationships.

Company Zeta hired a Swiss general manager who had previously established a WFOE in the same industrial zone. The management of the company was strongly of the opinion

that the previous interaction of their general manager with the industrial zone helped develop relationships, which later were to the advantage of their own company. In case study Eta the Swiss company relied entirely on its JV partner – also a foreign company with many years' experience in the appointed industrial zone – to apply and implement the WFOE. The management there was of the opinion that the established relationships must be utilised for the company's benefit, as it would take them too long to establish the necessary relationships.

In all cases it was reported that as the business develops, more and more daily issues and problems must be handled directly and locally. Regardless of whether the local management is Chinese or from Switzerland, it must find ways to access the relevant key people in China who can help develop the business and solve problems. Relationships must thus be maintained locally to manage the company. Those companies with substantial investment or those that are a significant local employer report that good relationships with local government are more and more important. In turn, local governments are very much interested in good relationships with their investors, which is very helpful if conflicts of any kind have to be settled.

5.5.4 – Conclusion on Environment Influences

There are numerous influences on the decision-making process. The analysis has shown these influences change over time. They can become more significant or even disappear and surface again at a later stage. One must never forget that in an emerging market like China business conditions can change, often influenced by the central government.

The most prominent factor is the location of China, a country far away from Switzerland and culturally unrelated. Companies have shown that, prior to the decision to enter China as a WFOE, information collection is less formal. A *laissez-faire* approach to China changes into a situation where thoughts about China's environment are considered. It is confirmed that the companies adopt a global view of China and are rather looking for risk minimisation approaches for their later engagement. It is realised that SMEs do not have the strength to alter the external environment, and there are closer environment issues which are confronted directly by the companies, such as language, culture, HRM and technology. These are issues that for the companies analysed are manageable during market-entry. It is believed, by the Swiss SMEs analysed, that these issues are less of a threat as these firms are of the opinion that their individual approach is suitable, and they look for controlling power over these issues.

Formal and informal networks take on an important role in managing the market-entry. Whereas external advice is first sought, the companies are at the same time developing their own expertise in addition to their earlier China experiences. An external network can

be internalised at a later stage, and it is noted that Swiss SMEs also employ experienced China managers. The companies have learned how important good relationships are in China to develop a business. To manage relationships in China it is understood that foreign companies need close local Chinese associates that can convey the interests of the Swiss firm.

Please refer to Exhibit 22 overleaf for Influences on the Market-Entry Process.

Case Study	Previous failure, understood as learning, is not stopping company re-entering China	Company has international production experience from Eastern Europe	Managers need China/international experience	Board inputs supportive for entry process	Owners-managers use China/international experience for quick decisions	Own staff not all supportive in developing FDI	Information gathering mostly dependent on owners and their China experience	After initial information gathering an in-depth second round of gathering information	Information for market-entry is collected more randomly; only what is thought important	Chinese environment is different from Swiss patterns but not too difficult	Technical understanding in China is different. Transfer of technology can be complex	Knowing local language is key to success	Underlines business in China is between people. Can be emotional	Right local relationships most important to develop business in China	External network important for entry support	External network becomes internal over time	Company feels dealings with officials and application processes have greatly improved	**Market-Entry Process**
Alpha					X		X		X	X	X	X	X	X	X	X	X	Market-entry into China should not be considered too different from other market-entries. Most important to be open-minded
Beta	X				X		X		X	X	X	X	X	X			X	Major advantage that one owner speaks local language
Delta	X	X		X		X		X			X	X		X	X			Considers company can only develop through local management
Digamma	X	X	X	X				X				X		X	X	X	X	One should not withdraw from seemingly unsolvable situations. Step back and look at situations from a different angle. Often unconventional solutions will appear
Epsilon						X		X	X		X	X		X	X			The intelligence of the Chinese people should not be underestimated. China wants foreign companies to found FDI to obtain technology. Company only started to transfer older technology to China. Internal network not supportive of Chinese venture
Eta			X	X				X			X	X		X		X		Company can learn from China and optimise production processes in China. Can acquire process technology in China that is more expensive in Europe
Gamma					X		X		X	X	X	X	X	X	X	X		The owner is of the opinion that successful market-entry can only be done if one selects a trusted local person to assist
Zeta		X	X	X				X			X	X	X	X		X		Business analysis for China is carried out more stringently. Focuses on hard facts

Exhibit 22: Influences on Market-Entry Process

5.6 Decision-Making

The previous sections analyse the different phases of the decision-making process to enter the Chinese market and environment influences. This section discusses the decision-making type and style of the cases analysed. The companies underline that the market-entry decision processes show different characteristics; characteristics that can vary within one particular case and in the context that it takes place. It was noted during the interviews that individuals can judge the type of decision-making quite differently, even on the same case. From the interviews it is concluded that there are rational as well as intuitive aspects in a decision process where intuition is often strongly rooted in earlier experience.

5.6.1 – Decision-Making Type

The section on reasons to enter China and its sub-sections shows all companies in the study have considerable previous experience in China. Firms passed through a development phase in China and reflected on China relevant issues prior to the founding of a WFOE.

5.6.1.1 Strategic Decision to Enter China

The companies analysed show their China commitment is long-term. Those cases with a long history of trade or even having previously entered China *via* a JV have shown a strong commitment to develop their presence in China, despite, in some instances, previous failure. Considering this prior engagement in the decision to found a WFOE was of a trial and error nature, it was agreed by all interviewees that the decision to found a WFOE is clearly of a strategic nature.

Elaborating on this has shown that in the companies where there is a strong influence on decisions from a non-executive board, there is a clear distinction between strategic targets and operational targets, whereas in the smaller firms strategic targets are clearly interwoven with operational aspects. The three smaller firms within this research, Companies Alpha, Beta and Gamma show that the owner-manager role largely determines the development of the venture in China. Although it was claimed WFOE decisions are of a strategic and long term nature operational aspects must be considered.

Eventually entry decisions can emerge through less structured ways where it is mentioned that *ad hoc* inputs received resulted in decisions to found a WFOE. In the larger firms the operative management of the companies took the initiative and introduced the concept of production in China to the non-executive boards. In return the non-executive boards were keen on these proposals. Where the non-executive boards in companies Delta, Digamma, Epsilon, Eta and Zeta had a general liking of the idea – some of its members have their own

activities in China – this contributed to the acceptance of the concept of market-entry to China. In all cases the non-executive boards required a structured information base for making further decisions.

The analysis further shows that in the cases where CEOs are also members of the non-executive boards they were partly emotionally involved in the idea of setting up a WFOE in China. These CEOs had strong intentions to establish the companies in China. In the smallest three companies, case studies Alpha, Beta and Gamma, and the biggest company, case study Eta, it is shown that the roles of owners – or part owners – who are, at the same time, managers of the companies, largely influence the strategic decisions of the companies and are strong drivers of market-entry.

5.6.1.2 Basis for Decision-Making and Planning

In a previous section it is shown there are a variety of reasons to start a production facility in China. The design of an entry strategy to China was said to be carefully and well prepared. It was underlined in the cases of the failed JVs, where the interviewees were strongly of the opinion that any entry strategy must be very well prepared. Experiencing a wrong entry strategy can be very troublesome and in their particular cases resulted in disbandment of the ventures. The non-executive boards of the cases that had negative JV experiences were very sensitive about a repeat failure. It was reported these boards had to be thoroughly convinced through several rounds of consultancy on the new attempts through the operative managers. Finally the boards were very supportive of new attempts to re-enter China.

Hard facts are primarily the basis for decision-making on market-entry. Such facts include low production and labour costs, closeness to clients and current and potential market share. In addition the firms established milestones on delivery of first components or machines and in terms of required quality, product turnover and break-even for investment. Presentation of a business plan is a requirement in the larger firms but is handled less formally in smaller firms.

In four of the larger companies it was admitted final business plan targets were not met in all cases after operationalisation started. In Company Eta the investment costs for building the production plant were much higher than expected. In Company Epsilon the support costs for the Chinese venture were largely underestimated and the time horizon to establish the business was not met. Companies Delta and Digamma did not meet their expected return on investments on time as a result of higher management costs and delays of the business start.

Although the business plans were not always met, the companies underlined that they were on the right track, but had to find ways to optimise their operations. In two of these cases, Companies Delta and Digamma, it was mentioned that not meeting the business plan was also due to the unexpected development of new business opportunities in China, business that was not under consideration when the initial business plan was drafted. The smallest three firms – driven by the owners of the companies – claimed their ventures developed according to their expectations. These firms had a very informal way of developing their market entries, without extensive business planning and analysis.

Generally all firms consider that although a long-term business focus is necessary, long-term business planning is difficult in China. Only the implementation stage will indicate if sufficient parameters have been considered during the planning stage.

Smaller firms had a more pragmatic approach to market-entry. Whilst not setting too many barriers during the initial strategy design, operational aspects were seen as being of more importance. As a result the planning of the market-entry explicitly considers high flexibility in decision-making during implementation. As a consequence for the smaller firms short-term targets have been more significant. As claimed by the owner of one of the smaller companies '*…Strategic planning is difficult in China, everything changes quickly in China, such as laws, export regulations, taxes which influence the business results. Not everything can be quantified at an early entry decision. Thus short term planning is more important than long term planning*'. But the larger firms also meet this problem, as shown in case study Eta, the biggest Company, which had just entered the operationalisation stage of the venture during the analysis. It was reported in this case that increasing support from Switzerland is given during the current implementation phase. Problems have to be solved as they can appear on a daily basis but were never thought of during the planning stage of the venture.

5.6.1.2.1 Decision Speed

In all the cases the period from the decision to found a WFOE until operationalisation of the new venture was reasonably short. In the fastest case of Company Zeta it took only three months to obtain the business licence – this company had the longest history of trade with China. In the Gamma case study it was reported all the relevant information for the entry decision was collected during a three day visit to the location where the company finally founded the new enterprise. It was confirmed in all the case studies that once the decision for the establishment of a WFOE took place there was a strong commitment to implement the decision. Up to this point the companies individually established their relevant information base, accepting that information in a market like China can be quickly outdated and might only be valid for a specific case.

It is assumed that long years of previous experience of companies or managers in China can assist to the extent that an actual market-entry decision in the form of a WFOE can materialise quickly. This shows the decision style is often experienced-based with a quick decision made.

As the circumstances of doing business in China are thus basically known through learning-by-doing the firms are well prepared to enter a stage of formal information collection – or justifying existing know-how – in a speedy way. The focused information collection allowed companies to make fast decisions within the core phase of the market-entry – the recognition and development phase. Increased experience and determination allowed the firms, either directly or indirectly *via* their associates in China, to increase the knowledge base especially when a company has entered the stage of selecting a suitable location. In this stage the companies had already committed themselves to China and most probably had a preferred location in mind where information support is given through industrial zones and other direct sources.

The speed of decision-making was clearly shown to depend on the decision-makers authority. In the cases where the owners have management power, mainly in the smaller firms, the decision speed was rather fast and direct. In these cases it was not necessary to obtain authorisation from a non-executive board or indirectly from the owners of the companies. At the same time the analyses of the decision situations were less formal and, as claimed, '*from the gut*'. The larger of the cases analysed, where a non-executive board had to be addressed have shown that such a decision-making process goes through several rounds of presentation and authorisation. Such rounds are characterised by refining the subsequent information search and individual comments from the board members. Overall the market-entries to China were in none of the cases heavily questioned and all were finally supported.

In those cases where a firm had experienced a previous JV failure the non-executive board wanted to see strong arguments for re-entering China, a risk analysis and ways to reduce risk before agreeing on a new market-entry attempt. The major discussion points were about budget control and timing but less about the details of market-entry. The non-executive boards wanted to be involved but delegated most decision authority to those people that made the proposals for such market-entry.

A comparison between smaller and larger firms shows – with a distinct difference between companies that have a strong influence from a non-executive board and those that do not have such an influence – there is a tendency for decisions in larger firms to take longer. A smaller firm may have a smaller span of control and can make decisions in an informal way.

5.6.1.2.2 Dealing with Risks

The decision environment in China is perceived as not being as transparent as in Switzerland. The stance is taken that although market-entry to China is risky such a market-entry to China should be at the least possible risk. As a consequence companies make an effort to analyse the different risks to market-entry. This approach to an analysis is often more thorough than it would be in Europe. The analysis shows that in the cases of non-executive boards personnel concerned are requested to develop a risk analysis. In the analysed cases different types of risk were apparent, which were mostly relevant for an individual case. Matter-of-fact risk clusters were loss of investment and technology, not finding the right staff and management, risk due to small company size, how China will develop and loss of control.

It was indicated during the interviews that there was not a real differentiation between risks and uncertainties and that the terms were used interchangeably. Within the analysis it is clear that risks were attributed to situations faced during the first information gathering stage which were perceived as difficult but not impossible for management by the company. The interviewees were the opinion that such risks could mostly be quantified and alternative ways developed to face them. The decision to found a WFOE, rather than another entry-form, is probably the most prominent example. In all cases the risks for a joint venture [JV] – in particular the risks of little control, losing technology and limited culture or mentality transfer – were seen to be too high. In four of the cases – the larger of the firms – the management established a broad information base and has made efforts to quantify the perceived risks to understand their individual needs on information and risk. Each of the cases, at a very early stage of the decision-making process, came to the conclusion that only a WFOE would be a feasible and acceptable risk.

Swiss firms feel there are few uncertainties in market-entry to China. Uncertainties and unknowns were approached by talking to other more experienced Swiss companies and studying different market-entry cases as well as attending seminars. Firm-specific uncertainties such as HRM, product quality, costs and cultural issues were the most prominent worries in this study. These worries were issues continuously addressed by other Swiss companies consulted and worries that have turned out to be points of conflict in the cases analysed during their own operationalisation stages.

All the firms claimed they had, as far as possible, made determined efforts to collect information suitable for their individual cases to justify their own decisions to found a WFOE. At the same time it was understood that the larger firms were asked for a broader information base, and therefore fuller collection of information, to apply more analytical decision-making. The smaller firms carried out a more random information collection –

concentrating on what was thought to be important issues and on the assumption that not every aspect can initially be clarified – largely under the view that a company has to undergo its own experiences.

Based on the risk or uncertainty analysis the companies tailored their own market-entry scenarios. All cases claim that a failure of market-entry to China would not endanger the survival of the whole company. It was generally decided to make small step by step investments and advancements, as an example, not to build or own a factory at all, and to only enter *via* a WFOE, building firewalls to control knowledge and technology, as an appropriate way to eliminate risks.

Too detailed a risk analysis was also questioned in case studies Alpha, Epsilon and Zeta. It was questioned if a too detailed information search would really reveal all problems with market-entry, while some might only be applicable at the moment of investigation. Reference values must also be questioned as, for example, other firms' experiences might not be fully transferable. A focus on possible risks can also hinder a company developing efficiently and possible positive sides of uncertainties cannot evolve. In case study Delta it was underlined that external risks did not prevent developing the venture in China, but the risk-preventing attitude of the company prevented the company from developing freely while internal problems were entirely neglected. The management came to the conclusion that certain risks must be accepted and uncertainties faced to develop alternative and creative ways of problem solving. Such companies should motivate themselves to find as many as possible acceptable facts, while accepting there are certain unknowns that will only surface during the actual entry process.

To consider risk management from a different angle the interviewees were asked if their market-entries also considered market exit strategies. It was considered that founding a WFOE is a strong commitment by the companies, owners and managers and an exit strategy could be understood as having less commitment and a weakness.

Individual investments were in each case on a scale that was substantial for each of the companies. Failure in China meant a loss of finance that could not be used elsewhere, or another investment opportunity that could not be taken. Still the smaller firms took a very pragmatic stance in claiming that not everything can be planned in advance in China and as such also not an exit. However the main concern amongst the smaller companies was the return of their investment in case of failure. But the larger firms also did not explicitly formulate exit strategies. The owners-managers accepted the risks of entering the Chinese market, which, in the worst case, could be a loss of investment. There are strong beliefs the companies studied are successful in their market-entry while individual investment strategies are low scale and in steps that could not result in a disaster if losses occur.

The interviewees in each case were convinced their companies would be successful in the future if control could be kept over activities. Only some unforeseen situations such as political instability, felt to be beyond a company's influence, could lead to closing down of activities.

5.6.1.2.3 Gaining Control

In all cases decision-makers drafted their decision to establish a WFOE at an early stage of the decision-making process. A JV solution was not developed in any of the companies to the extent that a company reached a point of deciding between a JV and a WFOE enterprise. Whereas patents offer some protection for technology a WFOE is seen as the only option to retain control of processes and finance.

A JV is believed to be to the advantage of the Chinese stakeholders and in the worst cases the Chinese JV partner would not treat the other JV partner well. Cultural differences could prevent harmony and, as a result, Swiss firms would be on the losing side. In all the cases analysed it was strongly underlined that only a WFOE can give control over activities in China. The interviewees claim that either they had heard of defaulting JVs or had experience in a previous and failed joint venture. JVs where the Swiss company would keep a maximum of shares are also not considered workable. Whereas control over activities was the most prominent statement in favour of a WFOE it was also agreed that a WFOE cannot guarantee ultimate control. It was said that in a WFOE a Swiss company also needs close associates and trusted people, to close the gap between the company and the Chinese side. Interfaces to the outside world of a WFOE must be managed with consideration of the Chinese way of doing business, which includes suppliers, administrations and local government. Although one has a 100 % WFOE ownership it cannot be assured that this guarantees control over activities. From the interviews it is clear that a WFOE only establishes the basis of control, but its concept and management will decide to what extent control can be practised.

5.6.1.2.4 Increased Flexibility in Decision-Making

Flexibility in decision-making differs greatly between the recognition-development and the selection-implementation phases. The analysed cases show that firms in an initial stage are very focused on their known company behaviour and processes and at first have in mind to transfer their business concepts to China. If a firm or its employees have international experience this experience is very valuable when a new market is entered. In the case of three firms with production plants in Eastern Europe, Companies Digamma, Gamma and Zeta, it is claimed that through this previous learning the companies are able to adjust quickly to the new decision environment in China. These companies are of the opinion that a new market place such as China has to be entered with a high degree of

management flexibility, and be aware that a business model must be greatly adjusted to the local circumstances. Inherent company and individual strength might not be sufficient for entering a market such as China. The faster a company can adjust its processes to the new environment the more efficient it will be. Insisting on previous behaviour can slow down the entry process. It was repeatedly claimed that a company must develop local flexibility for decision-making through its own experience, and support through its personnel.

The companies analysed had different requirements when they set off for the Chinese market and the type of flexibility was shown to vary amongst the cases. Those cases depending on technology and patents would never compromise on their core technology and would insist on adapting the business model needed to safeguard their know-how. But these firms also showed great willingness to adapt some of their processes to local circumstances. Such flexibility allows the companies to adjust their production technology to local circumstances and only do what is required. In Companies Delta, Gamma and Zeta this helped initiate local product development activities.

As the business application process in China was originally perceived by some of the companies as being complicated and bureaucratic it was in all cases viewed differently after operationalisation of the company took place. It was felt the application process must be accurate but that it does not develop with the same speed at all locations.

At present, in mid-2007, there does appear to be a certain bureaucracy in China that has to be accommodated to be operative in China. The faster a company learns to adapt to local circumstances the more flexible it will be in decision behaviour. This learning has helped the companies to be capable of deciding locally on issues that arise on an *ad hoc* basis. Such issues often need a less formal decision process although all information may not be available in a certain decision situation. As underlined in one of the cases '*…One must learn to delegate in China and accept the Chinese way of doing things – often done in an emotional way – as one cannot do everything on one's own. Contents and targets are important but the way to reach them should be variable*'.

Increased flexibility and accepting local conditions in China have shown in all of the analysed cases to be a learning process and acceptance is believed to help advance a company in China.

5.6.2 – Conclusion on Decision-Making Process

The different SMEs analysed show a different history of China engagement before the decision for a FDI took place. Consequently the individual experiences are rather different. The analysis shows China engagement is, or will develop into, a significant part

of a firm's activity and receive top management or owners' attention. The strategic importance of such China engagement at the moment of FDI commitment has grown into a situation where resources are, or will be, assigned and decisions will impact the whole organisation.

The premise on which a company launches its further China commitment greatly influences the approach to information gathering, decision-speed and how uncertainties and risks are approached. There is a certain tendency for smaller firms to act differently in their decision-making. Smaller firms or firms where owners are directly involved in the decision-making process are normally fast decision-makers, as are firms where *ad hoc* decisions can be made in a direct way. As shown in this study this can often be largely attributed to previous international experience of the decision-maker, and in some cases even to China experience.

Smaller firms indicate they carry out a less formal information gathering process that comes to a halt when decision-makers reach a saturation point and have answers to most of their questions. It is far less likely the process follows an optimisation strategy or alternative routes to search for every detail and eventuality. In contrast the larger firms look for multiple sources of information and analyse a market-entry as thoroughly as possible. The decision process in larger SMEs can pass several rounds of revision; often required by a non-executive board.

Regardless of the firm size the decision-making process faces uncertainties. Uncertainties which become most relevant when the firm enters the implementation phase of the entry process. The risks of entering China, and here it is underlined that Swiss SMEs mostly accept there are risks, are mostly business risks that all firms have to take to enter prospective markets. In particular risks of culture, language, HRM and technology transfer are understood to be of a level that can be managed by companies. Swiss firms thus approach the operationalisation phase accepting that only actual implementation will show if they are well prepared and can adjust their entry decisions.

Swiss SME owners-managers try to be analytical within their decision-making process and base their decisions on available information. Multiple sources are emphasised to help establish a base that allows comparison, as reference values might not be available at all or might be questioned. At the same time experience-based decision-making is observed especially when exercised by internationally experienced owners-managers.

Please refer to Exhibit 23 overleaf for the major findings on Decision-Making.

Case Study	Long term planning in China is difficult. Conditions and laws can change. Company plans long-term commitment in China. FDI is strategic	Operational aspects must be considered in early planning. Short-term planning is important	Non-executive board influential in decision-making	Owners-managers have the most influence in the decision-making process to materialize FDI	Decision to found WFOE followed by strong will of decision-maker to implement venture	Risk analysis is more detailed in China	A too detailed risk analysis does not reveal all circumstances met during market-entry. Uncertainties faced as they appear	Boards request detailed risk analysis for entry decision-making based on broad information base	Market-entry based on small steps over time to lower risks and not endanger the company. Companies have a strong feeling they are succeeding	High technology-based companies adjust production processes and technology to local circumstances. The decision is taken to use a 'Black Box Concept'	Only a WFOE gives a full base for control	The quicker a company adjusts and is flexible in decision-making, the quicker it advances	Overall entry costs and time exceeded plans	Time span from entry decision to implementation short	Actual market-entry confirms HRM is a challenging issue in implementing a China venture	Local management increasingly gains decision power	**Decision-Making**
Alpha	X	X		X	X	X	X		X		X	X		X	X		Allows decision flexibility. Rigid planning is not possible
Beta	X	X		X	X	X	X		X		X	X		X	X		An initial failed JV supported the decision for a WFOE. Decision for a JV with a Chinese company was later taken to strengthen position in China
Delta	X		X		X	X		X	X	X	X	X	X	X	X		Decisions are more and more delegated to local decision-makers. Concerns about uncertainties hindered company developing freely. The only company to evaluate the market-entry option of a JV
Digamma	X		X		X	X		X	X		X	X	X	X	X	X	Local management of opinion Chinese and Western aspects of decision-making have to be considered. Western managers must know when to compromise
Epsilon	X		X	X	X	X	X		X	X	X	X	X	X	X		Company started to question decision to found a WFOE. Results showed needed support was more than planned. Repeating and new issues continually need attention
Eta	X		X	X	X	X		X	X		X	X	X	X	X	X	Company heavily depended on knowledge of business partner for decisions on founding WFOE
Gamma	X	X		X	X	X			X	X	X	X		X	X		Three days visit to China gave information for final FDI decision
Zeta	X				X	X	X	X	X	X	X	X		X	X	X	Three months from decision for a WFOE until actual implementation

Exhibit 23: Major Findings on Decision-Making

Chapter Six ~ Synthesis of Research Results

6.0 Background

In this Chapter the key findings of the field study are discussed. The objective is to review the research propositions and address the research questions. Mintzberg's original conceptual decision-framework, see Exhibit 7, is revisited (Mintzberg *et al*. 1976) and its applicability, in terms of FDI market-entry of small and medium-sized enterprise [SMEs] into an emerging market, such as China, is discussed.

6.1 Decision-Making Patterns

This dissertation analyses the decision-making process for foreign direct investment [FDI] of Swiss small and medium enterprises [SMEs] into China. Within this research the opportunity is taken to draw on a sample of Swiss SMEs that have expanded to China and established a manufacturing platform. China has developed into an important and growing FDI destination for Swiss firms. The initial assumption was made that China fulfils the requirements of an emerging market. The field study and thoughts of interviewees have shown China is a dynamic environment with characteristics of an emerging market, offering an attractive business environment for Swiss SMEs, with more advantages than disadvantages for SMEs.

In developing a business in China there are considerable and relevant differences between bigger centres of importance and close neighbourhoods but there are even more drastic differences between the north and south of China. The development stage of industrial and related aspects in different geographical areas in China can greatly vary and is of concern to Swiss SMEs. Reflecting on the overall number of Swiss firms active in China reference values or indicators to market-entry are not readily available. Interviewees in this analysis experience market-entry to China as not greatly different from entering other new markets.

Reflecting on the eight SMEs in this research it is concluded certain limitations to generalisations are apparent. Two major reasons are deduced: First the overall constitution of the SME, mainly size and management, and secondly the individual development of the market-entry, shown in the early history of the individual firm, results in different entry process patterns. The limited number of cases and findings means general conclusions cannot easily be drawn. Nevertheless the market-entry process of Swiss SMEs to China does follow a certain decision pattern and indicates a certain tendency. This tendency shows SMEs can undertake a fast entry process once the foreign direct investment [FDI] decision is made and commitment to this decision is fostered.

Smaller and larger SMEs can behave differently in their decision-making process, largely explained here through the owner-manager's role in the firm. In considering these two major limitations, a chart is developed that pictures the FDI decision-making processes as found in this research project, as in Exhibit 24. The chart captures the current state of all the analysed cases – within their actual wholly foreign owned enterprises [WFOEs] – and includes those cases where previous joint ventures [JVs] had to be disbanded. A broad distinction between the decision phases of avowal, verifying and commitment, location and model, operational and reflection is extracted.

Regardless of the type and size of a SME, in each case the focus and resource commitment is found to be high. As such, the engagement in China is substantial, and is predicted to gain a major, or even the only share, of the firm's future activities. Common to all the case studies is the situation where a FDI market-entry to China is of a strategic nature. But *strategic planning* is handled individually, and different understandings of planning were found. This research project did not reveal any obvious and comparable link between the history of the firm and the drafting of an entry strategy.

The difference between the smaller and larger SMEs shows the preparation phase – until the trigger point for FDI is reached – does not influence strategic planning equally. Whereas smaller firms rather follow a route of evolving strategy, the larger SMEs have a more formal planning largely influenced, and enhanced, by a non-executive board. Whereas in some cases market-entry to China was planned in as detailed a manner as possible, in other cases details were basically omitted. Nevertheless in all cases the idea and execution of market-entry to China was shown complete commitment by owners-managers. This was mostly emphasised by exit planning not being of much interest to companies analysed. In most cases exit planning was considered a weakness as it would reflect a full, or partial, lack of commitment.

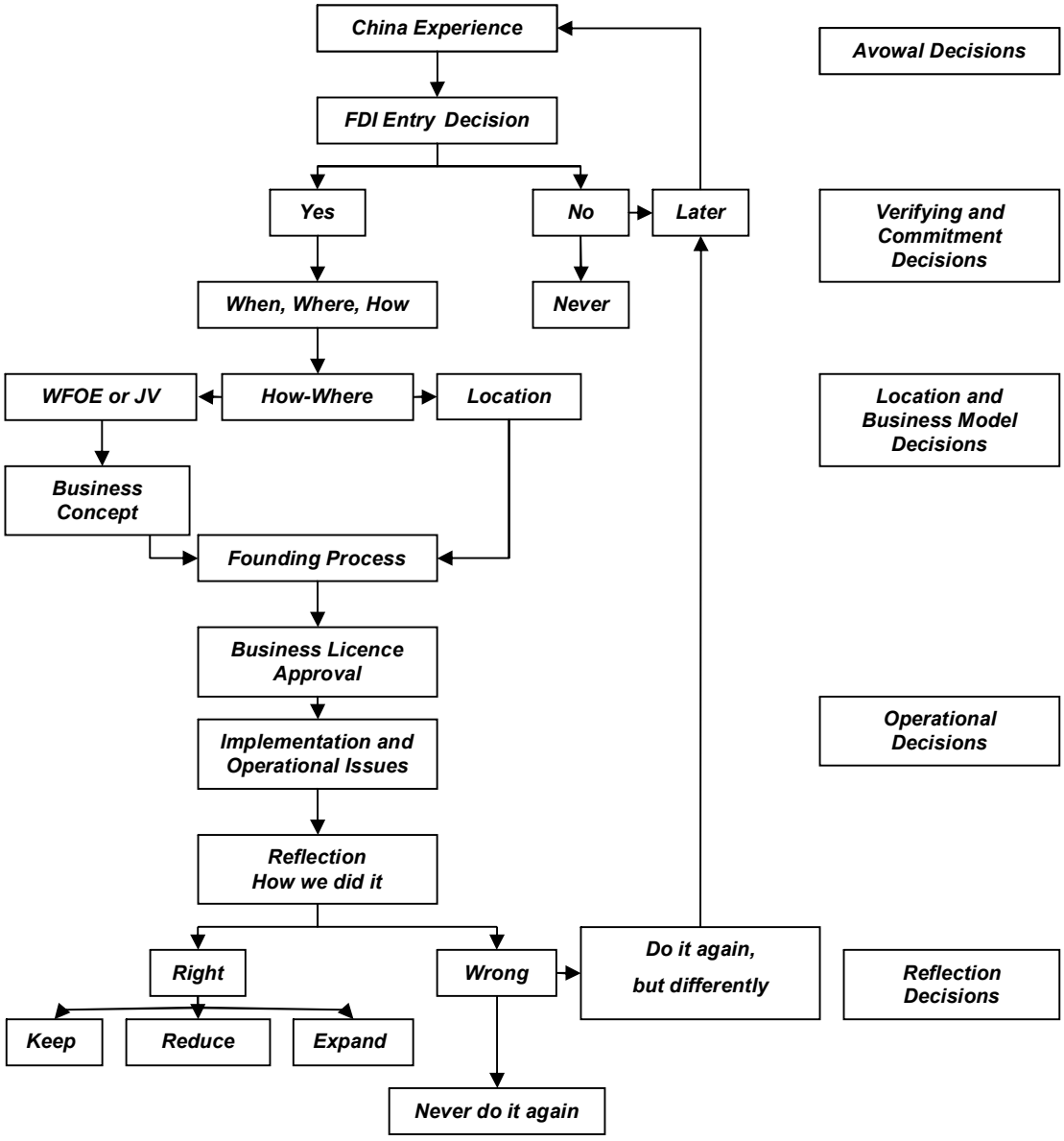

Exhibit 24: FDI Decision-Making Process

(Author, 2007)

6.2 The Decision-Making Process

In this section the research propositions are addressed. To allow for a theoretical contribution to the academic field the environment aspect of China is somewhat moderated. The following discussion thus basically refers to FDI decision-making within any dynamic environment. References to the specific case of China are introduced if required.

Three propositions are designed to address Research Question 1, which is:
What is the decision-making process for foreign direct investment by SMEs?

Research Proposition 1:

Small businesses undertake a series of well-defined decisions for FDI in sequential steps; accompanied by learning and feedback.

The theoretical decision framework shows clear phases of decisions and the actual case studies confirm there are indeed different stages within the decision process. A period of early market exposure however largely influences the timely development of market-entry and there is an actual trigger point within such an initial stage that determines if a firm explicitly formulates its entry plans. The initial market exposure period, even though an actual entry-decision is not being made here, results in a learning phase on doing business in a new environment, which largely influences the following decision stages.

It is confirmed that Swiss SMEs do not enter a specific decision stage requiring a decision between the different types of equity investment. Rather the decision-makers enter the decision-making process with an intended entry-type in mind. In the course of the further decision-making process confirmation of this mode of entry is sought. This is largely explained on the grounds that firms, or their decision-makers have extensive previous experience, even with failed JVs, or that information gathering in an earlier phase influenced a preference for a certain entry mode. A most obvious decision stage is shown to be the period when selecting and analysing a location for the new venture. A clear overall preference for a WFOE type of entry is confirmed; and firms make a location selection that results in the most benefits to their company. To the observer this stage in the decision process seems to be quite transparent. Owners-managers feel able to make the most attractive selection amongst different choices which enables them to justify the planned business model for optimising their investment. Decision-makers can accumulate a considerable database within this phase, which allows the optimisation of decision-making.

The theoretical research framework explicitly includes an implementation phase for entry decisions, and this was proven a significant stage in the decision-making process which should not be neglected in a decision process model. In practice not all small businesses undertake detailed entry planning, or consider every aspect of an entry decision, and, as a consequence, the volume of operational decisions varies which, in turn, determines the degree and type of management needed to operate the new venture.

The research project shows the proposed sequential development, as in the research framework, varies in the cases analysed. Sequences often cannot be clearly distinguished, can overlap and can even be entirely absent. This is explained where knowledge already exists in companies or is attributed to learning effects up to the point where the entry decision is made. Not only are sequences not always clearly distinguishable but they also differ from case to case, while sequences cannot be readily compared as time spans differ

greatly. Rather than classifying the decision development into sequential stages, it is more plausible to characterise the process into periods of experience-driven development. Five decision phases are identified:

1) Avowal Decision. 2) Verifying and Commitment Decision.
3) Location and Model Decision. 4) Operational and Adjustment Decision.
5) Reflection Decision: see Exhibit 24.

Research Proposition 2:

The decision-making process depends on diverse process factors: the ability to utilise internal and external networks, learning and building of organisational capabilities, ownership characteristics.

In this research proposition it is concluded that the case studies can be subdivided into two groups. Firstly, the group of companies operated and driven by owners, with the second group of companies having a well-defined non-executive board. The second group of companies – there were four firms in the first group and four firms in the second group identified in this research – can be characterised as medium to larger SME in terms of the number of employees. Most prominently it is concluded that owners that are directly involved in the decision-making process – as in the first group of firms – use their rights and their prerogative to make fast decisions. In contrast the operative managers of the larger firms have to consult the non-executive board for approval for entry-decisions. This is shown to impact on decisions; the decision speed is faster in small firms with adjustments to decisions taking place during the implementation phase of the process, whereas larger firms have a built-in control through their non-executive boards which can slow down decision speed.

Networks are important in all the cases studied, but do show a great variance amongst companies. For those firms with a long history of being active in China or which had started investment operations somewhere else in the world, considerable internal and informal networks were found. These firms' previous experience helped internalise decision capabilities for foreign market-entry and enabled them to draw on a considerable know-how. These firms claim that setting up operations in China is no more difficult than elsewhere. An external network is of equal importance, especially at the initial stage of the decision-making process where such firms tend to acquire external knowledge by using their existing networks, or establishing, or entering entirely new networks. External networks are mostly important at an early stage of entry decisions and during information gathering but do lose some significance in subsequent stages of the entry process. Networking activities are a means to an end and are taken up very purposively. There is a tendency for external networks, under certain circumstances, to be internalised where individual external people, or organisations, can take over key functions within a

company's operation during the market-entry process. Rather than using formal networks it is shown that social relationships are most important in culturally new market places, such as China, and these need to expand over time.

The various interfaces between a company and the external environment in China need a lot of management attention. Attention that will increase over time. Whereas in all cases networks are shown to be important they eventually change into more informal and social relationships, largely attributed to the experiences of a company during its entry process.

SMEs in this dissertation are mostly entities made up of specialised skills and capabilities – often for niche products – expressed in technology, service and management. Capabilities that cannot easily be separated from one another have resulted, over time, in inherent capabilities. The decision to set-up operations in China is shown to be the development of activities not previously undertaken by the company in this market. SMEs transfer their business concepts to China but accept the need for adjustment to local circumstances and the acquisition of certain local capabilities which they do not possess.

Differences between the larger and smaller SME groups must be considered, especially the degree to which 'gut feeling' and inherent capabilities influence the decision-making process for market-entry. It was well shown in this analysis that a more formal decision-making process and consultation with a non-executive board, as in larger firms, results in more explicit learning than in the smaller companies.

Organisational capabilities can be developed through externalisation and nurture of local networks when the business concept is adjusted to local circumstances. Development of local skills can allow learning opportunities to surface. The organisational capability effects can also help explain why SMEs choose WFOEs for their mode of market-entry. Ownership in a JV is felt to have the potential to erode the values of a firm's know-how and, as a result, a loss of control over activities. Collaboration is only preferred for non-critical areas and the business model is adapted accordingly. Adaptation helps build in certain safeguards, accepting thereby that worries on losing know-how in certain developments may be restricted. Here organisational capabilities must be separated into inherent and learned competencies and it must be accepted that organisational capabilities greatly influence the decision-making process of a SME.

Research Proposition 3:

The decision-making process shows some flexibility and considers operational aspects.

Those companies that have relevant market-entry experience do realise how important it is to adapt to a new environment and to its entry decision. The faster this takes place the

more efficient the market-entry. The smaller companies in this research possess greater agility that allows them to quickly adjust to a new market environment, whereas the larger firms are shown to need some adjusting time. This can mostly be attributed to the situation where operative owners can decide quickly and more flexibly without having to obtain approval from a board.

SMEs have proven they can adapt their business concepts on entering a new and dynamic market place, which emphasises the need for flexibility. But firms mostly do not compromise on the protection of technology or revealing too much production know-how. There are sacrifices when firms are going to localise, as local production needs certain production know-how or technology. But such sacrifices are believed to be well-balanced in exchange for receiving local knowledge. Certain key information is revealed, provided final products or key components are still protected.

Swiss SMEs appear to be purposely flexible after market-entry, so as to materialise the most beneficial way of establishing their venture in the new market. In all the case studies it was claimed that inflexible behaviour, such as insisting on established business procedures, or unwillingness to change will render the entry process less successful. Information gathering is reported to result in a sufficient, and rich, database, which leaves the impression that a firm can make further decisions without too much compromise. The initial decision model leaves the impression that decision-makers must be flexible throughout their entry decision-making, but in practice, flexibility is mostly needed in adjusting the business concept, and when activities are actually starting in the implementation phase of the venture. During this implementation phase the smaller SMEs appear to show greater flexibility as these firms are more likely to accept uncertainties during their market-entry and do not look for detailed information on every eventuality during the early information gathering stage. The smaller SMEs are fully aware that the operationalisation stage of the venture will need a high degree of flexibility. The external environment has its greatest impact on firms and owners-managers during operationalisation of the venture and less during the previous phases.

As the theoretical model proposes flexibility in decision-making this third proposition that '*The decision-making process shows some flexibility and considers operational aspects*', cannot be fully accepted. Flexibility in decision-making takes place but only at a later stage of the decision-making process when the venture reaches the operationalisation stage. In an early phase of decision-making the firms try to make their known decision-making models applicable to the new market environment.

The division between two groups of firms – the smaller and larger firms – is again confirmed, as the smaller firms show greater flexibility during the implementation stage.

Operational aspects and learning during implementation is reflected in the type of decision-making process later applied.

6.3 FDI Decision-Making Style ~ Owners-Managers

Three propositions were designed to address Research Question 2, which is:
How do owners-managers of SMEs make decisions on foreign direct investment?

Research Proposition 4:

The owner/manager of a SME has an influential decision-making role and available and accumulated knowledge at each step of decision-making builds competence.

Two groups of companies – a group of smaller and a group of larger SMEs – indicate that the decision-making process varies amongst different sizes of companies. Owners, who are at the same time managers, of smaller firms, in contrast to the larger firms where managers report to a board, can be fast decision-makers and can often decide *ad hoc* on a given situation. This situation is underlined where owners are also represented on non-executive boards and had to suppress their desire to make *ad hoc* decisions before the board was consulted.

In all the case studies the entrepreneurial character of the involved owners-managers was supported. Regardless of whether a person is an owner or manager, those persons shown to be motivators, carriers and implementers of the FDI idea are pioneers. These people took on a central role in distributing and promoting the idea of entering China and, if necessary, convincing non-executive boards. When owners are managing the entry-process they often take an 'interface' position. They are the direct link between home and foreign operations, as found in the smaller firms. In larger firms local activities are driven by managers who describe themselves as entrepreneurs, with a strong requirement for growing independence.

It is confirmed in this research project that previous international experience, either in the host country itself but also in other international markets, strongly supports market-entry. The openness of involved owners-managers to new markets, followed by relevant country experience, decides development of the market-entry. Openness for new markets is shown to stem from previous international experience and a positive attitude towards exploring new possibilities. In contrast a firm can have several years of experience in the host country before developing an equity market-entry in the form of a WFOE. Market-entry decisions are shown to be the result of inherent competencies and of learned competencies that, at a point, triggers a FDI entry-decision. In the more extreme cases this can be based

only on learned competencies, but, in all cases, has to do with the situation where an entrepreneur takes the initiative.

Research Proposition 5:

Small business owners-managers are well prepared for FDI decision-making and show a high commitment in launching a FDI process.

This proposition is fully supported. Swiss SMEs are well prepared when they launch their FDI process into China. Whilst there is a difference between the smaller and larger SMEs and their ability and willingness to collect market information SMEs are whole-heartedly developing their new ventures. If previous JV engagements can be considered, in retrospect, as a trial and error approach, Swiss SMEs are fully committed for subsequent WFOE entry and a long-term business engagement in the host country. The difference in the decision-making behaviour of smaller and larger SMEs is reflected in the larger firms having a more formal preparation phase in establishing a sufficient and rich database for further decisions.

The preparation phase for a market-entry in the form of a FDI – the early experience-making phase – is characterised as an experiential learning-commitment phase. The owners-managers involved get accustomed to their new business environment and, at the same time, learn and build their competencies. Moreover within this phase they generally convince themselves on their future market-entry. Within this early preparation phase the commitment to enter China is strongly fostered.

Either the owners or the top managers are normally involved in the development of the new venture, and the top priority of the project is thus underlined. Often owners-managers dedicate additional time outside of their daily business. A central role is to motivate their boards and, or, convince employees on the planned market-entry. It is shown throughout that a China venture can only be successful if the owners-managers are strong supporting pillars and personnel are behind the concept.

The commitment to founding a WFOE – a commitment shown to be made at an early stage of developing the concept of an FDI entry – shows firms already dedicate themselves at a very early decision stage. As a WFOE is also related to a financial commitment, such an engagement can tie down scarce resources which cannot be easily recovered. It is well reflected in the opinion of owners-managers that only a long-term commitment in China will materialise successful business results.

The preparation time for developing the decision to start a WFOE is of differing length for each firm until the trigger point of accepting a WFOE is reached. But SMEs then

quickly develop and materialise their WFOEs. Once SMEs take a decision to found a WFOE, no time is lost in founding and implementing the new direction. This is probably due to the circumstance where SMEs are no longer only going through a 'convincing' phase for FDI market-entry but, by and large, are already making preliminary analyses and planning location and organisational issues.

Research Proposition 6:

The decision-making process is characterised by numerous external uncertainties and owners-managers apply a mix of rational and intuitive approaches to decision-making.

In all the case studies the decision environment in China is perceived as not being as transparent as in Switzerland. The different phases of the decision-making process are also exposed to different environment impacts. SMEs understand that the long distance to China and the unfamiliar business environment need special consideration. In this research project two different views are found.

1. China is completely different and an effort has to be made to analyse the different market-entry risks, which easily results in a more stringent analysis than would be carried out when entering another market in a familiar context, or
2. China is completely different and it is impossible to analyse all risks, and there are many uncertainties that will only surface during the actual market-entry.

An early exposure to the new environment should be approached with a quite open mind. Reports and experiences of others must be carefully viewed. Information received may not fit the context of one's own case and relevant key information might not be released. It was found that even third source information can draw an incorrect picture of the business environment in China.

In Swiss SMEs owners-managers normally enter the decision-making phase rather well prepared. It is accepted the general environment in China offers uncertainties that are sometimes beyond the control of a SME; mainly political and social unrest. However these uncertainties appear to be bearable as each foreign company is exposed to the same conditions. The general environment uncertainty appears to be of major concern during a very early phase of market-entry, which was also underlined in the initial talks with experts. In the process of market-entry it loses significance and concern can largely be attributed to the familiarisation circumstances in the new environment. Of great concern is the immediate environment of a firm; the industrial setting. SMEs understand that technological level, copying, production know-how, competitors' impact and other aspects can produce uncertainties to be dealt with. HRM in China gives rise to the biggest

uncertainty. It is realised a company has to undergo their own HRM experience which cannot just be acquired through case studies and other third-hand sources of information. Swiss SMEs look for relevant information deemed necessary for their individual case. Information, and especially hard facts, on China are readily available if one is persistent and can acquire information from different sources. There is general acceptance that not everything can be analysed in detail, and it is acknowledged that certain pieces of information may be missed and only surface during implementation. It is largely accepted that China is in a process of continuous development and, for this reason, environment changes are frequent.

Overall it is accepted that the implementation phase needs certain adjustments. This does not mean there need be a resignation or that market-entry is a gamble. Swiss SMEs accept certain uncertainties and follow a route of risk control. Such risk control normally takes place when the FDI is being materialised in the form of a WFOE. Only a WFOE appears to give a sound base for control and adjusting one's business concept to the new market environment.

The decision-making process is characterised by establishing a broad information base, and learning and building on inherent knowledge. Swiss SMEs often do this in a mostly formal way. In the circumstance of an emerging market there can be a lack of reference values and some values may only be compared to each other. As a distinction is made between hard and soft factors in China it is shown that Swiss SMEs follow a route of making decisions based on available information. Such decision-making is based on bounded rationality, based on relevant facts or hard factors, and also on experiential learning and intuition in the case of soft factors. This is a far cry from being wild guesses. Market-entry is driven by the spirit of owners-managers, and decision-making for soft factors is based on well-grounded experience.

This last proposition: *The decision-making process is characterised by numerous external uncertainties and owners-managers apply a mix of rational and intuitive approaches to decision-making*, cannot thus be fully accepted. Swiss SMEs follow a route of risk management by founding a WFOE thus establishing the base for control.

Following an entry strategy that allows for guidelines provides room for adjustment. Learning during the decision-making process allows grounded decisions based mostly on facts, whereas accepting uncertainties needs decisions based on experience.

In conclusion, it is more appropriate to describe the decision-making process as bounded rational instead of pure rational, and experience-based rather than intuitive.

6.4 Revisiting the Decision-Making Framework

Mintzberg's conceptual decision-framework was supportive in conducting the field study. After analysing eight case studies the initial assumption of including the early phase of the decision process as well the implementation phase was a correct one. The actual pre-entry situations of the firms do not lead to the same decision problems and learning within the process does influence decision-making differently.

In congruence with Mintzberg's proposal of having defined decision phases it is confirmed in this research that the decision process is divided into phases but that these can largely overlap, a relevant amendment to Mintzberg's model.

Further it is shown from the findings of this research that SMEs, regardless of size, often enter the decision-making process with a preconceived concept for the intended type of FDI. Planning a venture, and exerting as much control as possible, demands a WFOE type entry. This is emphasised to the degree that an entry through a JV was barely an option.

The differing periods SMEs have in a dynamic business environment before a trigger point for FDI is reached, can more easily be explained in terms of a phase rather than a stage. The FDI trigger point is central to the process and whether this point is reached through an emergent process or through planning is not relevant. The trigger point is often either through personal motivation of owners-managers, the needs for external markets or from demands from clients, and most likely are less formally reached. At one point these forces become so strong the FDI decision is made. In contrast to Mintzberg's core development and selection phases the actual process is shown to be much condensed and SMEs look for confirmation of their preconceived idea rather than enter a selection phase with different options. Within this identified and actual core phase SMEs mainly carry out the decision for a final WFOE location.

The implementation phase shows SMEs adjust and reflect on their former decisions; the most prominent learning period of the process. From the results of this study it is deduced that the implementation phase must not be excluded from the decision process since some SMEs, on purpose, do not undertake an in-depth analysis during the early decision-making process but rather accept that adjustment of processes is needed during operationalisation.

Swiss SMEs do not completely ignore the option of entering JVs with Chinese partners. The case studies show that some companies had bad previous experiences that led to subsequent WFOE decisions. SMEs that have reached the operationalisation phase indicate that JVs can be a further means of expanding after their own WFOE experience

in the new market place. This firmly indicates a WFOE can be the first FDI learning step, thereby setting the control base before entering a next FDI phase.

Considering the research findings the initial decision model is adapted as in Exhibit 25.

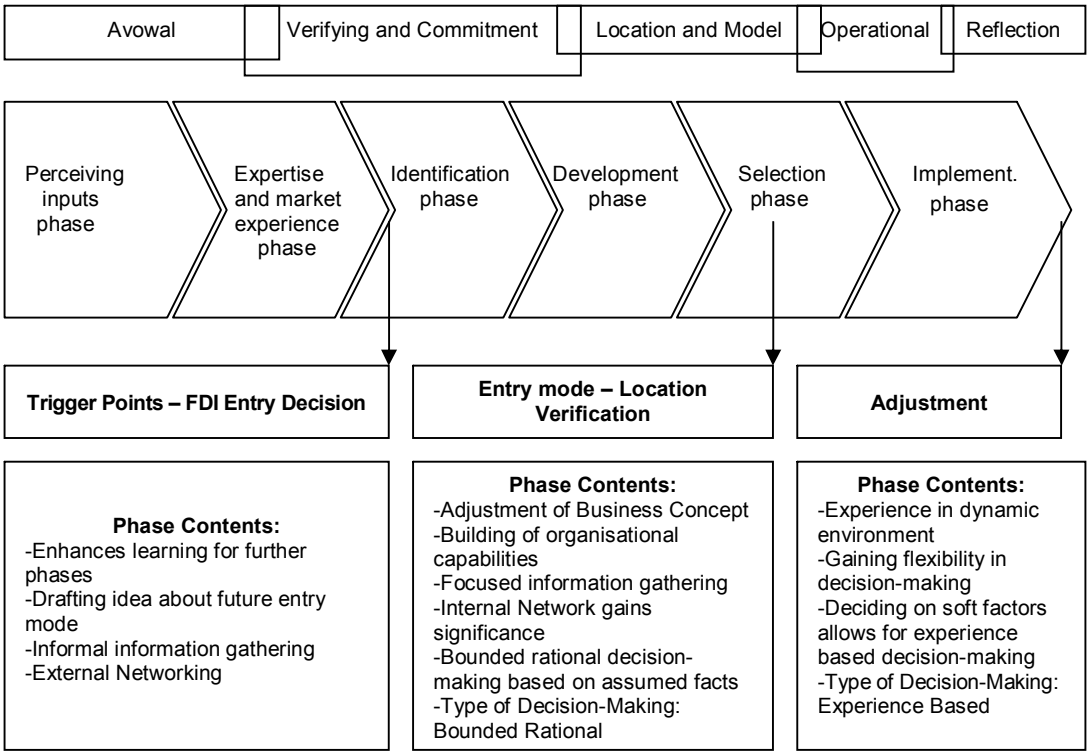

Exhibit 25: Adjusted Decision-Making Model

(Author, 2007)

6.5 Conclusion

This Chapter synthesises the empirical results of the field study. The first three propositions are used to analyse the decision-making process. It is considered the original decision-making framework is not exactly applicable for Swiss SMEs, although it helps visualise an overall decision process direction. The proposed decision stages are not exactly present as outlined in the model. The findings show the decision process rather takes place in subsequent and overlapping phases. These process phases are accompanied by learning. Subsequent phases are in nexus with preceding phases. Inherent and accumulated knowledge decide how fast the decision-making process takes place; shown to greatly differ between the cases analysed.

Influencing networks must be divided into external and internal networks, which within the different decision-making phases are either more or less relevant. As a tendency, in an initial phase of market-entry external networks are more important than in the following phases. As SMEs look for control over their activities in new market environments, external networks are very purposively used; mostly for information gathering and support. No proof was found that external networks propelled the firms into market-entry

or opened up new opportunities. Rather the opposite is observed; firms are trying to internalise and safeguard know-how in an overall attempt to remain in control of their activities. Outsourcing into new and attractive markets can well result in internalising certain activities to apply control mechanisms.

The analysis confirms decision flexibility is needed but mostly when FDI is being implemented and when operational aspects have a considerable impact. These cannot be detached from the previous decision phases as shown by SMEs that can follow a decision strategy of least detail in the initial decision phases but with more focus during implementation. The initial decision-making framework is revisited to compare with the findings of this research. These findings are applied in a conceptual way and the framework accordingly adjusted, to reflect the FDI decision-making process of Swiss SMEs. From Exhibits 24 and 25 it can be deduced that the timing of development of market-entry can vary greatly.

The remaining three propositions help analyse the FDI decision-making style. Here a tendency for different decision-making processes became obvious. It is shown that owners-managers have a central role in the decision-making process, while smaller and larger SMEs have a different decision process development. Faster *ad hoc* decision-making takes place where SME owners are directly involved in the decision process. More formal decision-making takes place in larger SMEs where the role of a non-executive board is important. Contrary to the stated propositions decision-makers are not facing uncertainties throughout decision-making; Swiss SMEs enter the decision-making process well prepared and exercise risk management. This largely contributes to a key finding of this research that although China, as an example, is a distant market, it is a business environment that is manageable for SMEs. The decision to only enter such a market environment in the form of a wholly foreign owned enterprise reflects profound risk management. In their decision-making style decision-makers try to be as analytical as possible. Appropriate previous experience and learned competencies allow for experienced-based decision-making, mainly in the implementation phase.

Chapter Seven ~ Conclusion

7.0 Background

This Chapter presents, in a reflective way, the conclusion to this dissertation. The contributions to academic literature and the practical impacts are considered. A critical reflection underlines the limitations of this study and areas for further research are discussed.

7.1 Summary of Results

The environment in which the research took place offers a scene to allow new insights into the decision-making processes of SMEs in a dynamic environment. This study is motivated on the grounds that there is no similar research on market-entry decisions for Swiss SMEs, which underlines its academic contribution and value for practitioners. Two main areas are investigated: the process and type of decision for FDI, which are found to be strongly related. The type of decision-making process – by owners-managers – largely determines the decision process and the empirical findings helped uncover a series of determinants that propel SMEs into market-entry. These determinants reveal appreciable variations between the motivation for setting up an FDI, in the form of a wholly foreign owned enterprise [WFOE], and the time span to reach a final decision for FDI, which cannot readily be compared between companies.

The case studies reveal the importance of the role of SME owners-managers, mostly highly committed individuals, who have reached a point where entering an emerging market in the form of a FDI is a real option; a point of no return. The initial phases of business involvement or market exposure, are informal but important; learning phases that clearly shape the concept of the entry mode to be pursued. This phase helps foster capabilities that speed up decision-making in subsequent phases. Overall Swiss owners-managers follow a route of risk-management, with the objective of keeping control over their activities; materialised in undertaking a FDI by founding a WFOE.

The findings of the field research show there are two groups of SMEs. The first group consists of smaller SMEs where the owners are directly involved in managing the business and are shown to mostly be quick decision-makers without the need for further approval of decisions. The second group includes larger SMEs where managers have to consult a non-executive board for decision approval. The research results show that in the first group decisions, as a tendency, are faster with the added observation that information gathering is less formal, whereas in the second group a more formal information gathering and decision-making style takes place. This largely explains why smaller SMEs

set themselves broader guidelines for the implementation phase of the venture, thus giving room for reacting and adjusting during implementation.

In Chapter 2 it was deduced that different components of uncertainties shape the market-entry decisions of firms. The environment and context setting of China motivates the assumption that such an environment is loaded with various uncertainties Swiss SMEs will have to face, which influences the type of decision-making. The empirical observations show that owners-managers in practice are trying to make analytical decisions that are well grounded. Despite the initial assumption owners-managers do not feel there are many uncertainties that will threaten their investments. The attitude of least risk is reflected in the way owners-managers make their investments; not at a maximum business risk which may endanger the whole company if the FDI fails.

Expert views on market-entry to China are considered at the outset of this research project. Reflecting now on these views there is a gap between *the planned* and *the actual* market-entry. The empirical findings mark considerable differences on how planned and actual market-entry is perceived and materialised. Firms and individuals planning their market-entry to China approach this task quite carefully. The overall learning effects are shown after the actual decision process takes place and the type of decision-making develops from an analytical approach into an experienced-based approach.

In Chapter 3 Mintzberg *et al.'s* (1976) decision framework is extended to suit the field research of this dissertation. This theoretical model helps capture the actual decision process of the eight SMEs analysed. Reflecting the research findings on the presumed research framework it is shown that Mintzberg's model helps explain the decision process and its direction in SMEs. At the same time it explains that, in practice, the different decision phases greatly overlap and decision-makers enter the decision-making process with a clear idea of how to set-up a new business in a new market environment; in this study the case for China. Decision-makers enter the process with a preconceived entry mode in mind and look for justification of their intentions. As such Mintzberg's *et al.* (1976) framework is highly appreciated but it is recommended that it be adjusted to consider the circumstances of SMEs and make it more applicable for smaller firms.

The rationale, developed in Chapter 4, was that the case study method is the most suitable research method for this dissertation. During the progress of the investigation it became obvious that the chosen method is indeed a most suitable approach; a method that is especially appropriate for novel and contemporary topics as dealt with in this research. An important aspect of the research findings is that the eight cases do not allow for broad generalisation, albeit they allowed the development of the understanding that there are certain tendencies in how a SME's FDI decision-making process takes place in practice.

Only the research method applied allowed the author to revisit each single case in an orderly manner, reflect on the findings, build and rebuild clusters of information and produce links between research findings in a cognitive way. This was only possible as each in-depth interview was transcribed and stored for replication, thanks to the use of the MAXQDA software.

The actual field study in Chapter 5 has conceptually and empirically examined the FDI decision-making process of SMEs. Despite the field research being based on a given decision-making framework it allowed for broad guidelines during the interview process. The case study findings were consistently used to improve the interview technique for subsequent interviews. The early field findings on why an individual company materialises a venture into China reveals the rationale for the FDI of Swiss SMEs differs greatly between the cases and, as a result, the individual development of the decision processes.

7.2 Contributions

The dissertation contributes to decision-making and SME research, and has both a theoretical and practical value.

7.2.1 – Contribution to Academic Literature

The present study, to the best knowledge of the author, is the first research to analyse the FDI decision-making process for Swiss SMEs. The integrative approach taken, in assuming the dynamic market environment of China where the FDI decision-making process takes place, contributes to decision-making theory. The unique position of Switzerland, with a small economy in the middle of Europe, is utilised to show expansion into a culturally-unrelated country. The findings contribute as follows:

- Firstly, the recent advance in decision-making theory and the growing interest in research on intuitive decision-making (Sinclair and Ashkanasy, 2005) is of relevance within this research. Acknowledging that intuitive events originate beyond consciousness, information is processed holistically and intuitive perceptions are frequently accompanied by emotion, underscoring the role of an individual decision-maker and their personality in the firm. This dissertation shows owners in SMEs can follow the route of less analytical decision-making in the form of experienced-based or even intuitive decision-making.
- Secondly, new insights into internationalisation theory are given. Currently there is an ongoing debate among researchers on different internationalisation paradigms and their validity. This dissertation appreciates the phase model of internationalisation by Johanson and Vahlne (1977), which contributes in a constructive manner. As this research considers the time aspect in the decision-

making process it visualises that different phases are of different lengths, are overlapping and, in the more extreme cases, some do not even occur. These findings strongly contribute to the newer research streams of *fast internationalisation* where the time aspect is most relevant.

- Thirdly, this dissertation underlines the notion of uncertainty and the belief that uncertainty should earn a more positive role with inherent opportunities for market development. Uncertainty and its components must not only be seen as a threat (Miller, 1992). The positive side of uncertainties must be considered (Thurner, 2005). Unmistakably decision-makers in SMEs are not halted by various uncertainties. Moreover decision-makers face such uncertainties during their decision processes. This dissertation shows the acknowledgement of uncertainties can advance market-entry and future research and literature should consider this aspect.
- Fourthly, planning of market-entry strategy is shown to be more or less formal. Strategy literature may take up this finding. This dissertation indicates that strategy can indeed evolve in iterative steps, similar to the proposals of Mintzberg (1987) whereas owners-managers can set least-boundary conditions but rather acknowledge the operational side of business development.

7.2.2 – Practical Implementation by Management

This dissertation provides relevant practical results for practitioners. Small firms, even micro firms, can be rather successful with their market-entry into an emerging market such as China. There are many characteristics other than *size* which are important. Ability of staff and company know-how provide a momentum that can help firms make good decisions and this should motivate smaller firms. From this viewpoint a large firm size may even be a disadvantage that can appreciably slow down decision-making.

An open atmosphere and company climate with information transparency is shown to be important for successful market-entry and its underlying decision-making processes. Staff involvement in decision-making is important and the management of SMEs should foster such a culture. Building and maintaining this characteristic will eliminate fears of foreign market-entry and strengthen staff support.

HRM in China causes continuous difficulties from the planning phase until the implementation phase of the venture. Indeed HRM issues are only directly experienced when activities are taken up in the host country. There can be additional costs involved when HRM solutions have to be implemented which have not been considered. Whereas it is beyond the capacity of the author in this dissertation to make concrete recommendations on how to tackle HRM issues in China in an effective way SMEs must prepare well to plan for, and address, this aspect.

Decision-making may be perceived differently in China. Owners-managers should accept that there is not always a ready answer or solution for all issues raised. Fact-based decisions and ready-made solutions are often absent in China. Decision-making style should acknowledge this circumstance and companies must be able to accept local circumstances and opinions.

7.3 Limitations and Areas for Future Research

7.3.1 – Limitations

This dissertation has purposely focused on Swiss SMEs that have set up manufacturing in China. Although similar theoretical conditions have been assumed this categorisation is rather broad in that generalisation of the results is limited for several reasons:

- The number of sample firms is somewhat limited. It only allows literal replication. The evidence from the two groups of smaller and larger SMEs found can at this stage only be called a tendency. Although the research approach helps to compare different cases and finds two different groups of SMEs, intra-group generalisation is less feasible. The two groups have been broadly described as groups of smaller or larger SMEs. These groups could also be described in different terms, for example, are owners operationally active in contrast to a group of firms that have a steering board. Overall future research may well be conducted amongst groups of SMEs, with the aim of contrasting different theoretical boundary conditions, as in the above example with a group that has owners or managers as decision-makers or a group that has an influential steering board, which should improve generalisation.
- Regardless of a SME's size the resourcefulness of a SME has not been considered in this dissertation. Whereas the owner-manager role and its international experience have been underlined in this research, financial resources have not been explicitly addressed. Financial constraints are assumed to be a serious threat against international expansion and how market-entry proceeds.
- China, as the chosen environment for this study, is a large country and is in a continuous state of transition. Geographical differences, and, as a result, the regulatory and institutional framework for FDI, can vary greatly between different places in the country. Although the overall assumption was made that China is an overall emerging market its geographical heterogeneity and possible boundary conditions must be considered.
- In most cases analysed some time had passed since the original idea of market-entry and the current stage. Recalling the decision process from the interviewee's memory brings challenges. Although every effort was made to apply a multiple level approach within one case, and the interviewing technique requested at least two decision-makers from each company, this circumstance must be kept in mind. It

must be accepted that certain details on the decision-making process may not be fully memorised. To overcome this weakness a longitudinal research method might be applied, with the researcher occupying an observer position and closely following a real time decision-making process.

These limitations can well be the basis for improved research on this specific research topic.

7.3.2 – Further Research

In this research project the owners and managers were mainly Swiss nationals. On reflection it would be of value to understand how a decision-making process is influenced if these positions are occupied by other nationalities. From this viewpoint it would be most interesting to know how company values, presumably Swiss values, are conveyed and how they influence the decision-making processes. At the same time a comparison between Swiss and other nationality SME decision-making processes would be a valuable contribution to current SME and decision-making literature.

The eight cases analysed had all entered a WFOE at the time of research. Further insights into the FDI decision-making choice are expected if similar research amongst Swiss SMEs that have entered JVs is undertaken. In contrast to this dissertation where each SME entered the decision-making process with a strong intention of establishing a WFOE in China it must be clarified if a JV selection has followed a similar path; with a strong intent on the part of decision-makers to found a JV. It should also be analysed if such research results could be replicated in another market environment; that of a different emergent or dynamic market.

The problem of analysing SMEs with different sizes was underlined on several occasions and it is concluded that this is a major limitation to this research. The role of the non-executive board was noted and accepted but not analysed in any detail. This limitation might well be taken as an opportunity for further research: Firstly, on an analysis of the influence of a non-executive board on a decision-making process and secondly, the task of comparing the decision-making process of large Swiss firms, presumably MNEs, with SMEs.

The initial expert opinions and the empirical findings indicate a possible difference between the *planned* and the *actual* decision-making process. Further research may prove, if there is indeed a gap, how the decision-making process is perceived, in addition to identifying if there are clear links between the idea, or need, to enter a market place like China and a firm's strategy formulation.

Appendix A ~ List of Experts

Swiss Managers and Managers of Swiss Firms

Name	Position/Title	Company
Aepli, F.	CEO	Geberit International, China
Eicher, B.	CEO	Fatzer AG
Fokas, D.	CEO	Polyverix-Meister AG
Frutiger, U.	CEO	Frutiger AG
Fuchs, Ch.	Managing Director	Inducs AG
Ghidini, A.	Director of Sales	Trasfor SA
Huang, J.	Key Account Manager	PRECI-DIP DURTAL SA
Michel, D.	Sales Director China	Premech AG
Müller, P. G.	Sales Director China	Straub Werke AG
Schmocker, A.	Sales Director China	Orion-Alko AG
Schuerch, H.R.	Former China Delegate	Bühler AG
Wilhelm, M.	Head of Purchasing	Thomson Broadcast and Multimedia AG
Zwygart, B.	CEO	Lemantec SA

Consultants/Advisors and Scholars

Name	Position/Title	Organisation
Bürgi, B.	Managing Director	Swiss Business Hub Beijing, Embassy
Cui, D.	Expert, China	Swiss Organisation for Facilitating Investment-SOFI, Zurich
Fernandez, J.	Prof. Dr.	Chinese European Business School-CEIBS, Shanghai
Grimm, K.	Former Managing Director	Auslandshandelskammer- AHK, Shanghai
Morneweg, H.	Managing Director	Auslandshandelskammer- AHK, Shanghai
Jenster, P.V.	Prof. Dr.	Chinese European Business School-CEIBS, Shanghai
Küng, D.	CEO	Business Network Switzerland-Osec, Zurich
Lüthi, E.	Managing Director	Former Managing Director of Swiss Business Hub Beijing, Embassy
Lüthi, R.	CEO	School for International Business-SIB, Zurich
Noll, R.	Senior Consultant	Business Network Switzerland-Osec, Zurich
Rechsteiner, A.	Senior Consultant	Business Network Switzerland-Osec, Zurich
Zwahlen, P.	Managing Director	Selective International Management-SIM, Shanghai

Appendix B ~ Swiss SMEs and Interview Partners for Cases

Company Name	Interviewee and Position	Data (as valid in spring 2007)
Asico AG	Von Niderhäusern, F. *CEO* Qian Zhong Rong, *General Manager*	1) 1998 2) Nanhui 3) 70 4) 3
Frutiger AG	Frutiger, U., *CEO* Lamparter, E., *Sales Director*	1) 2007 2) Changsha 3) 3 4) 21
Metar SA	Herren, E., *Chairman of Board* Souyris, F., *General Manager*	1) 2006 2) Shanghai 3) 9 4) 25
Plaston AG	Bitterlin, R., *General Manager* Dobry, J., *CEO*	1) 1996/2004 2) Jiaxing 3) 130 4) 130
Proftech International GmbH	Lu, L., *Business Development* Rath, P., *General Manager*	1) 2006 2) Nanhui 3) 5 4) 3
SSM – Schaerer Schweiter Mettler AG Textile Division	Nadalin, W., *CEO Itema Weaving, Sultex, Former Schweiter Technologies* Trittibach, S., *General Manager* Zinetti, C., *Chief Purchasing Officer*	1) 2003 2) Zhongshan 3) 50 4) 220
Stopinc AG	Schär, W., *CEO* Niggli, I., *Chief Financial Officer*	1) 2005 2) Shanghai 3) 7 4) 60
Wolfensberger AG	Schild, F., *Technical Director* Schmidhauser, M., *CEO* Staab, J., *Vice President Operation*	1) 2006 2) Foshan 3) 23 4) 250

(1) Established in China, (2) Location in CN, (3) Staff in China, (4) Staff in Switzerland

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Curriculum Vitae

Christian-Otto Schmidli
Born: 25th June 1963
St. Gallen, Switzerland
cschmidli@proftech.org

Education

April 2003 – February 2008	**Doctoral Candidate** Asia Research Centre	University of St. Gallen, Switzerland
September 2000 – October 2002	**Master of Business Administration**	University of Strathclyde UK and JiaoTong University, China
November 1991 – November 1994	**Bachelor Degree** Mechanical Engineering	University of Applied Science Brugg-Windisch, Switzerland
November 1986 – November 1990	**Marine Chief Engineer Licence** Merchant Navy	Maritime College of Southampton Warsash, United Kingdom
April 1979 – April 1983	**Apprenticeship** Car Mechanics	Technical Vocational College St. Gallen, Switzerland

Professional Experience

February 2001 –	**Establish and operate Proftech International GmbH** St. Gallen CH, Shanghai PRC, and Hanoi VN **www.proftech.org**	**Managing Director** Active in industrial consultancy, production, engineering, ship-building and offshore gas-oil industry. Supports firms in emerging markets such as China and Vietnam
November 1996 – January 2001	**Assignments on various shipbuilding projects** China	**Project Manager** Shipbuilding for various clients
February 1996 – October 1996	**Acomarit/Massoel** Geneva CH and Shanghai PRC	**Marine Superintendent and Chief Engineer** Ship building and operations
April 1995 – October 1995	**American Bureau of Shipping** New York, Norfolk, Newport News/USA	**Ship Classification Surveyor** Ships' conversion and survey at Norfolk US Navy shipyard
May 1983 – October 1991	**Suisse Atlantique** Lausanne CH	**Senior Marine Engineer** World-wide sailing and shipbuilding activities