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Decision-Making Process in Foreign Investment Choices

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Abstract

This exploratory investigation aims to develop a managerial decision model that assist international firms and investors in selecting the right valuable foreign country for their international operations. Two comparative and rich-information case studies were purposefully selected from among Arabian large firms. Additionally, six international investment decisions were investigated within these two cases and data were collected by in-depth interviews, follow-up interviews and questionnaire instrument. Within and cross-case analyses were undertaken in the current investigation. The findings demonstrated that a methodical and international experience-based strategic decision-making process was adopted to attain a profitable foreign country choice. The decision process comprised five critical managerial phases; that is, (1) analysis of internationalization drivers, (2) searching and development of location determinants and country alternatives, (3) obtaining adequate and related-information about potential countries, and, ultimately, assessment for these alternatives, (4) selection of a final beneficial foreign country choice, and, finally, (5) effective implementation of the selected country choice. The research findings provide theoretical and practical implications to the internationalization of firms as well as international investment. Further, it provides significant methodological contributions to international business research in relation to an effective multiple case study approach to capture elements of the international market selection process.

Keywords: Decision model, foreign investments, Arabian international firms

Introduction

The internationalization activity of firms and foreign market entry and selection have received increasing research attention among scholars during the last decade due to the significant contribution of this movement to the economic and social development in both home and host countries (Akbar and McBride 2004; Jansen and Stockman

2004). According to the "eclectic paradigm of international production" proposed by Dunning (1980, 1988), firms which decide to internationalize their business activities face a very vital, complicated, and strategic decision concerning the selection of a foreign country for their international operations. Consequently, during the phase of the foreign country selection, firms have to choose the most appropriate entry strategy for that foreign market such as exporting, franchising, licensing, joint venture, and foreign direct investments (FDI) (Buckley and Casson 1998). The internationalization activity of Arabian firms is a relatively recent phenomenon and has attracted extremely little attention from scholars. Therefore, as an attempt to fill this evident shortcoming and gap in FDI literature, two comparative in-depth, and information-rich case studies of the Arabian premium manufacturing and service firms were undertaken to explore and analyse the foreign direct investment decision-making process. More specifically, this paper underlines the important managerial decision-making aspects that should be considered by international firms to arrive at a beneficial foreign country for their outward FDI.

Literature Review

The Internationalization Process of Firms

Internationalization refers to the process through which a firm shifts its business operations from the local market to foreign markets (Buckley and Casson 1998). The literature on the internationalization process of firm can generally be categorized under two main approaches: the economic approach and the behavioural approach (Andersson 2000). The economic approach has its roots in economics, and it primarily assumes that firms are likely rational in their choice of foreign investments and that the decision-maker has access to perfect and complete information (Andersson 2000; Buckley et al. 2007a). According to this school of thought, the choice of country for foreign investment is a premeditated decision and motivated, led by the principal goal of profitability. Thus, firms select the most profitable locations (Buckley et al. 2007a). The behavioural approach focuses on the influence of international experience of the firm on the speed and direction of succeeding internationalization.

An important aspect in this school is the important role of organizational knowledge in the internationalization process (Clercq et al. 2005). The approach considers individual learning and top managers as important aspects in understanding international behaviour of firms (Andersson 2000). Eclectic theory proposed by Dunning (1980, 1988) underlines the importance of firm and location-specific factors to explain international operations. Dunning (1988) states that specific organizational skills or technologies allow a firm competitive advantage in the marketplace. He also indicates that country-specific factors are also essential to successful international operations. He argues that the characteristics of the selected foreign country influence significantly the firm's international efforts. Vernon's

International Product Life Cycle Model (Vernon 1966) considers the internationalization process to be a systematic, incremental, and predictable chain where the type of entry into foreign markets depends on the life stage of the products passing through the phase of introduction, growth, and maturity. The roots of the transaction cost approach go back to Ronald Coase (1937) who argued that due to the transaction costs of foreign market activities, it is more efficient for a firm to engage in a local market rather than enter foreign ones.

A high extent of transaction cost gives rise to a preference for internalizing the transaction (Johanson and Mattsson 1987). Firms therefore prefer to produce offshore if they recognize that the decrease in transaction costs will be greater than the cost of organizing such activities internally. Otherwise, foreign markets will be supplied by exports, licensed sales, or some other type of foreign market entry. The Uppsala model is perhaps the most cited model of internationalization process. Johanson and Wiedersheim-Paul (1975) found that firms who decided to internationalize their business activities go through distinct steps, starting from no exports to exports, to independent representatives (agents), to the establishment of sales subsidiaries, and, finally, to the establishment of owned or joint production facilities. In their view, the flow of information between the firm and the market is critical in the internationalization process, and they significantly underlined the concept of "psychic distance" which determines the location choice of international manufacturing firms.

Psychic distance was defined as the costs of obtaining significant information about business conditions in other countries, the perception of risk and uncertainty involved in international operations, and the resources required to access foreign networks. The model asserts that the costs expended in overcoming "psychic distance" decrease over time due to the experience achieved by the firm. Therefore, firms often first enter adjacent markets because of their historical familiarity and then expand to other foreign markets. Afterward, models of innovation-related internationalization were developed on the basis of the Uppsala model. Among the best-known models are from Cavusgil (1980) and Reid (1981). These models focus on the learning chain in relation to adopting an innovation, and thus, the internationalization decision is considered an innovation for the firm. They state that the decision-maker's attitude, experience, motivation, and expectations are main determinants in firms engaging in foreign market entry (Reid 1981) and, therefore, the entry into exporting is considered to be traced to an innovator inside the firm.

Foreign Direct Investment Decision-Making Process

Foreign direct investment (FDI) was defined as "a category of cross-border investment made by a resident in one economy (the direct investor) with the objective of establishing a lasting interest in an enterprise (the direct investment enterprise) that is resident in an economy other than that of the direct investor"

(OECD 2008, p. 10). Empirical research in the area of foreign direct investment decision-making process is relatively little. For instance, Aharoni's behavioural decision-making model (Aharoni 1966) described the foreign investment decision as a multifaceted social process that is influenced by social relations within and outside the firm. Generally, in the first international operation decision, the firm often has had export experience but has no experience in the field of foreign investment. It has no clear standard decision procedures to deal with that decision. As a result, the firm will gain from its experience when foreign investment decision processes needed to be carried out. He concluded that the FDI decision-making process involves three main phases: initial idea generation, investigation and development, and finally presentation and decision. Likewise, Wei and Christodoulou (1997) examined the decision-making process undertaken by international firms to select a foreign country for their FDI. He observed that the foreign country selection process incorporates three key stages: initiation and preliminary thinking, investigation, and evaluation and final decision-making. Wahab (1978) attempted to make some developments in Aharoni's decision-making model. He found that the profit was an imperative consideration in FDI decisions that is why firms invest in countries with high profit potential. He also concluded that firms were not only receivers of information in various forms, as stated by Aharoni, but also, they were information seeker and were continuously searching for opportunities and take advantage of them where they exist.

Research Design and Methodology

The international investment decision is a very strategic one which is carried out by senior managers of the firm; therefore, the phenomenology paradigm was adopted in the current exploratory research to enable the researcher to "get inside" the decision-makers' minds and seeing the foreign country selection process from their point of view (Hassard 1993) and experiences (Smith and Heshusius 1986; Yeung 1995). The case study method was employed in our study due to the close connection of this strategy with philosophical assumptions and foundations of the selected paradigm and because it represents one of the primary research methods for studies adopting the phenomenology paradigm (Perry 1994). Moreover, the exploratory nature of this research required the use of the case study method as it offers an opportunity for in-depth exploration and results in rich understanding about the research issue (Rowley 2002). A multiple case (embedded) design was chosen because two information-rich Arabian firms, which carried out various international investments' decisions, were investigated. The selected two comparative companies were information-rich, accessible, proximal, large, leading, and well-established Arabian international manufacturing and service firms which established various foreign investments worldwide.

Data Collection Method

Case Descriptions

Company A is one of the largest and most profitable petrochemical manufacturers in the Middle East and the world. It involves in industrial marketing as it produces chemicals, fertilizers, plastics, and metals to be used by other companies. The company's remarkable accomplishment is the outcome of focusing on three important issues: investment in local partnerships, research and technology (R&T) programs, and an ambitious global growth strategy. In order to achieve its global vision, the company invested heavily in R&T, as it has R&T facilities worldwide. Recently, the company launched a new company, and it is a leading global supplier of engineering thermoplastics. Finally, the company has a global presence as it has manufacturing facilities in the Middle East and Africa, Asia, the Americas, and Europe.

Company B is a large, leading, and well-established Arabian international professional service firm that engaged in providing world-class engineering and construction services to the Saudi and the Middle East market. The company is a key member of a large group of companies which established diverse business activities in Saudi Arabia and the Middle East. The group commenced operations in Saudi Arabia 60 years ago in the business and transport sectors with a large transportation fleet that covered a wide network in the region. The group established new companies in the fields of construction, operations, maintenance, health care, medical equipment, hospital supplies, and commerce.

The current annual turnover of the group is in excess of US$377 million, and it has over 7,000 employees worldwide. The Engineering and Constructions Company is a dynamic and expanding construction organization which was established in 1975. The company is classified among the top three construction companies in Saudi Arabia and one of the largest and most reputable in the Middle East. It has over 3,500 employees, significant construction plant and equipment resources, strong financial capabilities, and three decades of sustained successful construction track record. In its 28-year history of considerable progress, the Engineering and Constructions Company has made significant achievements in the construction industry. Finally, the company has expanded its services internationally as it established service operations and working relationships for construction business in Qatar, UAE, Bahrain, and Lebanon.

The data was mainly collected via in-depth personal interviews, follow-up telephone interviews, a questionnaire instrument, documents review when available and field notes. Initial telephone calls were made with the selected companies, which agreed to participate in the study, to explain to the company's executive the purpose of study and the issues that will be covered during the interview sessions. The accessible most knowledgeable senior executives, involved in international investment decisions, were in-depth interviewed. Multiple interviews were carried out and each interview

lasted 1 hour. All the interviews were recorded during the interview sessions using high-quality recording devices. The interview questions were open-ended and designed to explore the drivers of FDI decisions and elements of the decision-making process relating to the international investments and selection of foreign country. The questionnaire instrument was designed to obtain information about the company background and to confirm the interview responses.

Data Analysis

For the purpose of the data analysis, the researcher listened carefully to the tape interviews more than once in order to capture the key ideas and themes linked to the main research questions. The field notes which taken during the site visits to the participating firm were very valuable and necessary in assisting the researcher in preliminary identification for the anticipated main themes about the international investment decision process story. Within and cross-case analyses were utilized in the current research (Creswell 1998; Eisenhardt 1989; Yin 2003). Accordingly, we developed a detailed description or report for the selected single case study. The developed case study report described and organized all information and details relevant to the case company.

Seeing that an assurance as to the confidentiality of the interviewees' responses and identities during the data collection and analysis processes was given to the informant by the researcher, all the names indicated to individuals or organizations were removed from the report. In cross-case analysis, categorizing the case studies based on the size and type of industry such as large firms vs. small firms, manufacturing firms vs. service firms and followed by search for similarities and differences among these categories was adopted as an analytic strategy for cross-case pattern (Eisenhardt 1989). The data analysis method employed in analysing the interview data was based on the descriptions written by Miles and Huberman (1984, 1994) which imply data reduction, data display, and conclusion drawing and verification.

Findings and Discussions

The research findings revealed that Arabian international firms undertook a thorough and comprehensive decision process in order to successfully arrive at a beneficial foreign country for their outward FDI. In general, the decision process encompassed five imperative managerial stages; that is, (1) analysis of internationalization drivers, (2) searching and development of location determinants and country alternatives, (3) obtaining adequate and related-information about potential countries, and, ultimately, assessment for these alternatives, (4) selection of a final beneficial foreign country choice, and, finally, (5) effective implementation of the selected country choice. More details about the managerial procedures of the earlier managerial stages are provided below:

Selecting an experienced team consisting of a team leader who is internationally experienced in addition to other senior managers with different international experiences, and then the selected team should identify carefully the drivers of international investment, the organization's overall strategy and financial and human resources capabilities, and the financial and human resources commitments toward the international investment. If the prospective entry mode to the foreign country is by a greenfield operation, it is better to select and identify a trustworthy and internationally experienced expatriate manager for the international investment at this stage who will become another important part in the FDI team. In the case of an internationalizing firm which does not have sufficient international experience, it is recommended to recruit an external internationally experienced team leader, seek advice from professional consulting firms, and develop international experience prior to pursuing the international investment process, especially, if the FDI involves massive financial and human resources commitments.

The selected FDI team develops a list of primary and secondary foreign country factors taking into consideration the drivers of the internationalization decision, the organization overall strategy. For manufacturing firms entering the foreign country through international joint venture (IJV), developing local partner factors or criteria is important; trust a high level of local knowledge is very important.

Searching and determining potential foreign country options relying on a set of established country factors, international experience, and the country knowledge of the FDI team and external consultations with international business experts. In addition, for IJV, searching for a local partner should be carried out together with the search for a country. The proposed country options should be developed within the scope of the country knowledge and international experiences of the team.

Collecting satisfactory information relevant to the developed foreign country factors from appropriate governmental trade departments of both home and host countries and through external consultations with business experts from the home country and the potential countries.

Assessing the gathered information by comparing it with the developed country factors. In addition, rely on the international experience and country knowledge of the FDI team as well as the external consultations with business experts from the home country and the potential countries; assess the opportunities and threats, the financial and nonfinancial costs and benefits, and the global risk factors of each country option. As a result, eliminate the less feasible foreign country options.

Maximizing the knowledge of the most feasible foreign country options through exploratory field visits to these countries. Consequently, selecting the most beneficial foreign country choice relying on the international experience and country knowledge of FDI team as well as the external consultations with business experts from the home country as well as from the potential countries. For IJV, select the local

partner based on the identified criteria simultaneously with the foreign country choice.

Reviewing the decision consultatively with FDI team members and not to hurry in performing the decision and once the decision has been agreed, obtaining official authorization if required for pursuing the remaining parts of FDI process.

Finally, consulting international business experts and consulting firms about how to implement the international investment decision and conduct field visits to the selected foreign country and negotiate with its foreign investment officials about their incentives and regulation.

The results relating to drivers of international investments decisions were in line with the past internationalization theories addressed by (Al Qur'an, 2011; Clercq et al. 2005; Andersson 2000; Johanson and Mattsson 1987; Dunning 1980,1988, etc.). Furthermore, the FDI decision-making process adopted by Arabian international firms confirmed the behavioural and bounded rational model disused earlier in the literature review (Wei and Christodoulou 1997; Aharoni, 1966, etc.). Nonetheless, the findings of the current investigation revealed that selecting the foreign country of the international investment relied heavily on the international experience and country knowledge of the management team along with the external consultations with business experts from the home country and the prospective countries. This result was not indeed addressed in the previous body of knowledge and, thus, providing new insights into importance of international consultation in international investments decisions.

Conclusion and Implications:

The intention of this study was to develop a managerial decision model that assist international firms in selecting the right profitable foreign country for their international operations.

In general, the current research findings provide benefits to foreign investment policy-makers and local development administrators in the Arab countries by assisting them to increase their outward FDI and, accordingly, enhance the economic development movement in their countries. The research provides insight into how Arabian investors select the country for their foreign investments in relation to how they develop prospective beneficial countries, what type of characteristics they require in a foreign country, what type of location factors they produce, what type of information they gather and how they assess country options, and finally how they implement the country decision. Understanding these issues would assist considerably the Arabian firms and their local government trade departments concerned with increasing their business involvements with foreign countries to improve the foreign investment decision-making process. Minimizing the risk associated with foreign investment decisions will bring economic benefits to the

national economy through assisting firms to attain successful international growth. In addition, they could establish a governmental consulting body and recruit internationally experienced directors and academic experts in the area of international investments to assist substantially the Arabian international firms willing to undertake foreign investments, but which lack of adequate international experience, to arrive at successful international investments. Furthermore, the international trade policy-makers could increase the international participations of Arabian firms by reaching positive trade agreements with foreign countries to provide attractive foreign investment incentives to the investors and facilitate the implementation process in relation to international investments, legal requirements, and registration procedures.

In conclusion, the beforehand discussed recommendations and implications of the current research findings within the Arabian context could be applied to any foreign country to assist in the economic and social development in that country.

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