

# Paths to foreign markets: Does distance to market affect firm internationalisation?

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## Abstract

An idea widely shared among international business scholars, economists and geographers is that geographic, cultural and psychic distance to market affects firm internationalisation in a number of ways. However, evidence for this broad proposition remains inconclusive. This study provides a comprehensive assessment of four separate hypotheses pertaining to the location of markets, the sequence of market entry, the rate of international expansion, and the relationship between sequentially-linked markets. In contrast with previous studies, the analysis is based on a large sample of non-repetitive foreign market entries ( $n = 1132$ ) made by diverse exporters in dissimilar locations within a single country (China). Market entry data thus exhibit substantial variation on the constructs of interest. The results reveal virtually no support for three traditional hypotheses linking distance to market with the sequence of markets entered and the rate of foreign expansion. This study challenges the long-held notion that there is a simple link between distance and market entry sequence. However, this study provides arguably the first demonstration of the “near-market effect” in the context of low-risk entry modes such as exporting. Specifically, the results show that consecutive export locations tend to be culturally related suggesting that exporters are able to transfer learning between similar markets.

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## 1. Introduction

Firm internationalisation is the result of managerial decisions pertaining to the location and control mechanisms of an organisation’s international production and marketing

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activities. This process has been scrutinised in research relating to the selection of foreign markets (Brewer, 2001; Davidson, 1983; Dow, 2000; Ellis & Pecotich, 2001), the modes of control used to enter those markets (Edwards & Buckley, 1998; Kogut & Singh, 1988), and the timing of market entry (Mittra & Golder, 2002). Much of this extant work is decision-oriented; which market? how? and when? Consequently little is known about whether the cumulative outcomes of these choices describe broader patterns of decision-making. In short, do firms' paths to foreign markets conform to predictable decision-making templates? One possible answer is that expansion patterns are constrained by the costs of overcoming distance to market, however defined (Benito & Gripsrud, 1992; Davidson, 1980; Ghemawat, 2001; Johanson & Wiedersheim-Paul, 1975; Linmão & Venables, 2001).

At first glance the friction of distance seems out of place in this age of global markets and cheap communications (Cairncross, 2001). But the evidence suggests otherwise. Based on his extensive analysis of freight expenditures, Hummels (1999) reported that while air transport prices have fallen dramatically in the post-war era, shipping costs have not declined. The link between distance, shipping costs and trade represents one of the more prominent questions being addressed by economists, geographers and international business researchers in recent years (Clark, Dollar, & Micco, 2004; Hummels, 1999; Linmão & Venables, 2001; Mellinger, Sachs, & Gallup, 2000). A typical conclusion from this body of work is the one returned by Linmão and Venables (2001). Drawing on their analysis of shipping costs from Baltimore, these authors calculated that a 10% increase in transport costs reduces trade volumes by 20%. A similar relationship is expressed in Frankel and Rose's (2002) statistic that bilateral trade declines about 1% for every percentage increase in the distance separating a pair of countries. Based on his own reading of Frankel and Rose's data, Ghemawat (2001, p. 138) concluded, "The amount of trade that takes place between countries 5000 miles apart is only 20% of the amount that would be predicted to take place if the countries were 1000 miles apart." These numbers support the idea that, "contrary to popular impression, the world is not getting dramatically smaller" (Leamer & Levinsohn, 1995, p. 1387), that "distance still matters" (Ghemawat, 2001), and that the much-publicised "death of distance" (Cairncross, 2001) has been greatly exaggerated.

If the internationalisation process of the firm reflects a pattern of increasing distance to market, empirical verification should be a relatively straightforward matter. Yet after some 50 years of research few conclusions can be drawn. Geographic distance effects which are often seen at the macro-level (e.g., Beckerman, 1956; Frankel & Rose, 2002; Leamer, 1974; Linmão & Venables, 2001), are rarely observed at the level of the firm (e.g., Czinkota & Ursic, 1987; Terpstra & Yu, 1988). Cultural and psychological distance effects measured in one country (e.g., Johanson & Wiedersheim-Paul, 1975), do not seem to operate in other countries (e.g., Ellis, 2000), or even in the same country with a different sample of firms (e.g., Engwall & Wallenstål, 1988). Some of these inconsistencies may be attributed to the mixing and matching of dissimilar entry modes. Effects observed in a sample of exporters (e.g., Dow, 2000) may not hold for higher risk expansion activities such as foreign direct investment where cost savings stemming from internalisation or location advantages come into play (e.g., Benito & Gripsrud, 1992). In ventures involving substantial commitments of company resources, the marginally increasing costs associated with overcoming distance to market may not be sufficient to tip the balance in favor of one investment location over another.

A bigger part of the problem may be empirical. In contrast with the well-documented gravity model which explains trade between nations, at the level of the firm the accumulated evidence relating to distance effects is highly fragmentary. Aside from a lack of consensus on matters of operationalisation (Combes & Lafourcade, 2005; Dow, 2000), empirical expansion patterns are often sought from samples containing very few firms or very few market entries. Even when large numbers are involved, firm-level expansion patterns may be insufficiently spread out to permit meaningful analysis. When two-thirds of a sample of investors fails to make a second foreign investment, as was the case with Benito and Gripsrud's (1992) study of Norwegian manufacturers, it is difficult to see how conclusions regarding dynamic patterns of expansion can be drawn.

The aim of this study is to redress some of these shortcomings by examining the effects of distance on the internationalisation patterns of three diverse groups of Chinese exporters. This study's contribution is primarily empirical as is warranted by the state of current research. To increase the chances of detecting distance effects, and to balance a research bias favouring relatively high-risk foreign investments, the scope of the study is limited to direct exporting, a low-risk entry mode involving production in the home market.

## 2. Distance to market as a barrier to trade

Firms export to foreign markets to exploit differences arising from geographically-bound comparative advantages (Heckscher, 1919/1949; Ricardo, 1817/1971), to pursue the gains of specialisation afforded by increasing the size of the market (Ethier, 1979; Young, 1928), and to better position themselves against foreign and domestic rivals. Alternative market choices are evaluated in terms of their comparative rates of return and this implies some consideration for the costs of expansion (Root, 1994). In the international trade literature, these costs have historically been framed in terms of the artificial barriers to trade created by government policy and the natural obstacles of overcoming distance to foreign markets (Hummels, 1999; Leamer, 1974). As such, the widespread reduction in tariff barriers from their protectionist highs of the mid-twentieth century has increased the relative importance of transport costs in determining the pattern of world trade (Linmão & Venables, 2001). Clark et al. (2004) find that for many Latin American countries, transport costs now constitute a greater barrier to US markets than import tariffs. One of the more significant factors affecting transport cost is the geographic distance separating exporters from importers (Leamer, 1974). For this reason distance-based proxies have been used in a number of studies measuring transport costs (Clark et al., 2004; Combes & Lafourcade, 2005).

In addition to the costs of transporting goods to market, exporters must also deal with the costs of uncertainty. These costs tend to be greater for international neophytes (Ellis & Pecotich, 2001), in volatile markets (Wong & Ellis, 2002), and in settings where the transfer of organisational routines involves tacit, non-codifiable knowledge (Kogut & Zander, 1993; Scott & Storper, 2003). In the international business literature much of the uncertainty of foreign expansion has been described in terms of the learning costs associated with entering culturally unfamiliar markets (Barkema, Bell, & Pennings, 1996; Benito & Gripsrud, 1992). The costs of dealing with differences in language and business practices create an economic incentive for firms to initially export to culturally similar markets (Davidson, 1983; Johanson & Vahlne, 1990). Hence, distance is defined here in

cultural, or psychic, terms (Benito & Gripsrud, 1992; Dow, 2000; Edwards & Buckley, 1998; Johanson & Wiedersheim-Paul, 1975; Mitra & Golder, 2002).

The costs of overcoming distance are the costs of moving goods to foreign markets plus the costs of learning about those markets. The manner in which these costs shape trade patterns has been the subject of two separate streams of research considered here under the labels of “geographic” and “cultural/psychic distance.”

### *2.1. Geographic distance*

Geography affects trade via the imposition of transport costs incurred in delivering goods to distant markets and via the depreciation costs of goods in transit (Clark et al., 2004; Leamer, 1974; Linmão & Venables, 2001). These costs have been quantified by Hummels (2001) who estimates that every additional day of ocean transit reduces the probability of trade between two countries by 1.5% for manufactured goods. The negative correlation between trade volumes and the distance separating trading partners can be traced back to Beckerman's (1956) study of intra-European trade. Since then several studies have affirmed the hypothesis that geography is a barrier to trade between nations (e.g., Frankel & Rose, 2002; Hummels, 2001; Leamer, 1974; Linmão & Venables, 2001; Linnemann, 1966). But at the level of the individual firm the effects of geography are less clear. Terpstra and Yu (1988) found no evidence that geography affected the expansion activities of US advertising agencies. Neither were Czinkota and Ursic (1987) able to establish a link between the expansion activities of small and medium-sized US manufacturers and the physical distance separating them from their foreign markets. However, Davidson (1980) observed a tendency of US multinationals to enter markets that were both geographically proximate and culturally similar. In a more recent study, Dow (2000) reported that geographic distance was negatively correlated with the early market selections of a sample of Australian exporters.

### *2.2. Cultural/psychic distance*

In contrast with their economist-counterparts, business scholars have generally measured distance in terms of culture rather than kilometers (Barkema et al., 1996; Benito & Gripsrud, 1992; Dow, 2000; Mitra & Golder, 2002). Work in this tradition can be traced back to early studies done in Scandinavia investigating the trade-constraining aspects of psychic or cultural distance (Engwall & Wallenstål, 1988; Johanson & Vahlne, 1977; Johanson & Wiedersheim-Paul, 1975). Psychic distance is created by “factors preventing or disturbing flows of information between firm and market” (Johanson & Wiedersheim-Paul, 1975, p. 308). (Psychic distance results from factors affecting the flow of information to the individual whereas cultural distance results from factors affecting the flow of information to the group or country (Sousa & Bradley, 2006). For the sake of expository convenience, the two terms will be used interchangeably here.)

The greater the psychic distance to a market, the greater the uncertainty and learning costs associated with entering that market. Psychic distance-based moves accounted for about 50% of the agency and subsidiary establishments of four Swedish multinationals recorded by Johanson and Wiedersheim-Paul (1975). In the case of these firms early expansion activities were largely confined to neighbouring Scandinavian markets of

Denmark, Norway and Finland. Only later did these firms move into Western European markets and beyond.

Johanson and Wiedersheim-Paul's (1975) intuitive conclusion—that firm internationalisation conforms to a pattern of increasing psychic distance to market—provided the stimulus for a number of follow-up studies many of which have failed to support the original hypothesis. No evidence was found linking cultural distance with the expansion activities of three Swedish banks (Engwall and Wallenstål (1988), 93 Norwegian companies (Benito & Gripsrud, 1992), nor 19 consumer products firms (Mitra & Golder, 2002). However, in their study of 225 investments made by 13 Dutch firms, Barkema et al. (1996) found that the number of foreign expansions made by a firm was positively correlated with cultural distance, suggesting that market entries are initially made closer to home.

In most of the studies just mentioned cultural distance was operationalised using data taken from Hofstede's (1980) values survey of IBM employees (Barkema et al., 1996; Benito & Gripsrud, 1992; Mitra & Golder, 2002). This suggests that the results obtained pertaining to expansion patterns may be undermined by the shortcomings inherent in Hofstede's original conceptualisation and measurement of cultural distance. These limitations include the assumptions that cultural distance is stable over time, uniform within countries, and symmetrical between countries (Shenkar, 2001). Comparative country rankings, such as those performed by Nordström and Vahlne (1994), suggest that assessments of cultural and psychic distance are measuring different things. Based on subjective ratings provided by 118 Swedish managers, these authors showed that countries judged as being culturally close using Hofstede's metric, were relatively distant when rated in psychic terms (e.g., the Netherlands dropped from third to eighth place) and vice versa (e.g., Germany rose from twelfth to fifth spot). This observation prompted Nordström and Vahlne (1994) to redefine psychic distance as the difference between distance-creating factors (such as culture and language) and distance-bridging factors (such as international travel).

Taking his cue from Nordström (1991), Dow (2000) measured psychic distance by asking a panel of Australian trade commissioners to provide distance estimates for a list of 25 export markets. The combined ratings of eight judges were then used in a regression model explaining the frequency with which a given country was among the first five markets entered by a sample of 315 Australian exporters. This model showed that psychic distance is significantly and negatively correlated with the early market choices. In contrast, a cultural distance measure based on Hofstede (1980) was found to be a comparatively poor predictor of foreign expansion.

### *2.3. Distance to market and foreign expansion*

In summary, a core proposition underlying much of the research investigating firm internationalisation is that entry into new markets will describe a pattern of successively broader steps (Benito & Gripsrud, 1992; Dow, 2000; Engwall & Wallenstål, 1988; Johanson & Wiedersheim-Paul, 1975; Terpstra & Yu, 1988). Initial moves made during the early and most uncertain stages of internationalisation will tend to be cautious and proximate. As the firm acquires experience more ambitious entries, further afield, will be undertaken. Distance to market has been defined in both spatial and cultural/psychic terms. Yet, and despite decades of work, definitive conclusions on all points are lacking. For every study that finds a result another fails to. Several reasons have been advanced to

explain this state of affairs. Some scholars point to the inconsistent measurement and testing of distance measures (Dow, 2000). Others attribute the mixed results to unmeasured effects of external initiators and the implicit assumption that gaps between buyers and sellers are equidistant (Ellis, 2000, 2006). Still others argue that psychic distance research has benefited from the repeated use of Scandinavian companies with the implication that conditions in this part of the world are idiosyncratic and not generalisable (Sullivan & Bauerschmidt, 1990).<sup>1</sup> These concerns define the criteria for which future work on this topic must be judged.

### 3. Foreign expansion hypotheses

The proposition that international expansion of the firm will be influenced by the costs associated with overcoming distance to market leads to four testable predictions pertaining to (i) the location of early markets, (ii) the sequence of the firm's entry into subsequent markets, (iii) the rate of international expansion and (iv) the gaps between sequential pairs of market entries. These predictions, which are not mutually exclusive but capture the main conceptual approaches undertaken by past work, are presented in hypothesis form in Table 1.

Much of the existing work investigating international expansion patterns is encapsulated in the first two hypotheses listed in Table 1. Each has been tested using a mix of geographic and cultural/psychic distance data (Benito & Gripsrud, 1992; Czinkota & Ursic, 1987; Dow, 2000; Engwall & Wallenstål, 1988; Johanson & Wiedersheim-Paul, 1975; Terpstra & Yu, 1988). The mixed results returned by these studies justify the inclusion and retesting of H1 and H2 here. In contrast with the export-heavy emphasis in the international trade literature, most of these firm-level studies have examined patterns of foreign direct investment. This hints at an opportunity to see whether distance effects observed at the macro-level are evident in the trading decisions made by individual managers.

The third and fourth hypotheses have received comparatively little attention in the literature and require some elaboration. In the Scandinavian view of firm internationalisation, foreign market entry (FME) decisions are shaped by managers' experiential knowledge, hence the tendency to enter neighbouring countries before expanding outwards (Johanson & Vahlne, 1977, 1990). One testable implication arising from this view is that tentative steps will be followed by more aggressive moves as managers gain experience operating in diverse markets, as predicted in H3. A contrary prediction was made by Benito and Gripsrud (1992) who speculated that the expansion rate, or cultural distance to new investment locations, would diminish with experience. But these authors did not provide any rationale for why this should happen and their own results were inconclusive on this point.

However, Benito and Gripsrud (1992) did find that the distance between two consecutive investment locations was highly correlated. This observation supported their conjecture that the experience gleaned in one market reduces the uncertainty attached to entering

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<sup>1</sup>Psychic distance effects might be more readily observed in the expansion patterns of Scandinavian firms given that successive cultural boundaries (Sweden, Scandinavia, Western Europe) coincidentally describe a pattern of increasing geographic distance. The implicit question is whether Johanson and Wiedersheim-Paul (1975) would have reached the same conclusions if their four case studies had involved Mexican or Singaporean firms, rather than Swedish firms.

Table 1  
Internationalisation hypotheses and past findings

	Hypothesis	Relevant studies and distance measure (with findings)	Mode of entry
1.	Early FMEs will be closer to home than later FMEs.	Benito and Gripsrud (1992)—CD (NS) Child, Ng and Wong (2002)—CD & PD (MS) Czinkota and Ursic (1987)—GD & CD (NS) Dow (2000)—GD & PD (Supported); CD (NS) Ellis (2000)—PD (NS)	FDI FDI Exports Exports Exports
2.	The FME sequence will be positively correlated with the distance to market.	Benito and Gripsrud (1992)—CD (NS) Engwall and Wallenstål (1988)—CD (NS) Johanson and Wiedersheim-Paul (1975)—PD (Supported) Mitra and Golder (2002)—CD (NS)	FDI FDI FDI/exports FDI
3.	The rate of international expansion increases with experience.	Benito and Gripsrud (1992)—CD (NS)	FDI FDI
4.	The distance to country $n$ will be correlated with the distance to country $n-1$	Benito and Gripsrud (1992)—CD (Supported) Barkema, Bell, and Pennings (1996)—CD (Supported) Mitra and Golder (2002)—CD (Supported)	FDI FDI FDI

Notes: FME = foreign market entry, G/C/PD = geographic/cultural/psychic distance, FDI = foreign direct investment (including equity joint ventures), NS = not supported, MS = mixed support.

other, similar markets, even if those markets are far from home. This “near-market” effect was subsequently verified by Barkema et al. (1996) and Mitra and Golder (2002). Barkema et al. (1996) investigated the pattern of new foreign ventures made within and between cultural blocks of similar countries and found that firms benefit more from previous expansions made in other countries within the same block than expansions made across cultural blocks. The rationale offered to explain this behaviour was that “learning effects are stronger if the cultural context of the new venture resembles more closely the culture where the firm expanded previously” (Barkema et al., 1996, p. 155). Mitra and Golder (2002) also found that near-market knowledge was a stronger factor influencing the probability of a new market entry than cultural distance from the home market. Mitra and Golder defined near-market knowledge as “a firm’s understanding of the culture of potential new markets based on knowledge generated from operating in similar markets” (p. 354).

To summarise, the near-market effect has been demonstrated in three studies investigating the selection of investment locations by Dutch, Norwegian and other multinational firms (Barkema et al., 1996; Benito & Gripsrud, 1992; Mitra & Golder, 2002). These studies highlight the cost-minimising role of knowledge gleaned by a multinational’s subsidiaries in foreign markets on the firm’s subsequent entry into other, culturally similar markets (Mitra & Golder, 2002). However, all three of these studies focused on foreign direct investment and measured distance solely in terms of culture.

No study has yet examined whether the near-market effect can be captured with other distance measures and whether it applies to lower-risk entry modes such as exporting.

#### 4. Recording internationalisation patterns: methodology and data

The internationalisation process of the firm has been extensively researched in mature Western economies such as Scandinavia (Benito & Gripsrud, 1992; Engwall & Wallenstål, 1988; Johanson & Wiedersheim-Paul, 1975), Western Europe (Barkema et al., 1996; Sullivan & Bauerschmidt, 1990), North America (Czinkota & Ursic, 1987; O'Grady & Lane, 1996; Terpstra & Yu, 1988) and Australia (Dow, 2000; Ellis & Pecotich, 2001). This has resulted in a body of work that under-represents those fast-emerging nations which are leading the world in developing international trade. China is the most notable example of this group with export growth rates averaging above 25% annually from 2000–2005. Over the same period exports as a proportion of national GDP grew from 23% to 34% while China's share of world trade increased from 3.9% to 7.3% (China Statistical Yearbook, 2006; World Trade Organization, 2006). In the league of exporting nations China ranked third in 2005, behind Germany and the United States and ahead of Japan and France. Much of China's trade exited the country via Hong Kong on the south coast of Guangdong Province. Although Hong Kong enjoys a high level of political and economy autonomy, its trading position is inextricably entwined with its Chinese hinterland. Consequently, we define the boundaries of the study as mainland China plus Hong Kong.

##### 4.1. Sampling and data collection

The sampling aim of this study was to identify a diverse group of exporters evidencing high variation on a number of dimensions including trading experience, the number and variety of foreign markets entered and languages spoken. An additional aim was to rule out in advance extraneous sources of influence relating to specific research settings. These aims were met by collecting internationalisation data from firms in three Chinese cities; Hong Kong, Shanghai and Xi'an. Economically these cities have little in common. Hong Kong prospered under Britain's former colonial administration and has been labelled the world's freest economy (Heritage Foundation, 2006). With a nominal GDP per capita of US\$25,622 in 2005, equivalent to US\$36,800 in purchasing power terms, Hong Kong is Asia's wealthiest society after differences in the cost of living have been taken into account (China Statistical Yearbook, 2006; NationMaster.com, 2006). Situated in the rapidly industrialising Yangtze Delta region, Shanghai's economic ascendancy has seen the city cement its reputation as the pro-business capital of China's eastern seaboard. Shanghai's nominal GDP per capita of RMB51,474 (equivalent to US\$6283<sup>2</sup>) makes it one of the most prosperous cities in China (China Statistical Yearbook, 2006). In contrast, the city of Xi'an, which is located in central Shaanxi Province, ranks among the second tier of China's industrial cities with a per capita GDP of only RMB17,141 (or US\$2092) (China Statistical Yearbook, 2005). Lacking easy access to a river- or sea-port Xi'an's exporters face significant impediments to trade. In contrast with Shanghai and Hong Kong where exports

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<sup>2</sup>Currency conversions were based on the official exchange rates for 2005 listed in the China Statistical Yearbook (2006, p. 734): USD1 = RMB8.19.

per person were worth US\$6670 and US\$41,592 respectively in 2005, the comparable figure for Shaanxi Province was just US\$827 (*China Statistical Yearbook*, 2006).

At all three locations—Hong Kong, Shanghai, and Xi'an—data were collected via personal interviews with top managers of indigenous manufacturer-exporters. During the interviews managers were asked to list all their foreign markets and then provide detailed information about their firm's entry into each market (dates of entry, control modes used, key initiators, share of income from each market, etc.). A standard questionnaire was used at each location. Traditional Chinese and simplified Chinese versions of the questionnaire were back-translated and then pre-tested on three to five managers at each city. Owing to the descriptive emphasis on the collection of non-sensitive historical data, the only changes required after pre-testing were cosmetic.

In Hong Kong, interviews were conducted in Cantonese with the managers of 42 manufacturers randomly selected from the *Directory of Hong Kong Industries* and a *Hong Kong Toy and Games Fair Catalogue*. These firms employed on average 39 staff in Hong Kong and an additional 1327 workers in factories across the border in neighbouring Guangdong Province. In Shanghai and Xi'an, interviews were conducted in Mandarin with 215 and 101 manufacturers (in various light industries) respectively. The mainland firms employed on average 1215 workers, had been in business for an average of 14.4 years, and exported around a third of their total output. In contrast, their Hong Kong counterparts were older (25.0 years on average) and much more internationalised earning 98% of their income from exports.

In the two mainland Chinese cities data collection was conducted by local interviewers operating out of the Shanghai University of Finance and Economics and Xi'an Jiatong University. In both cities the interviewers were personally trained by the author and then supervised by local colleagues at each university. Incoming questionnaires were reviewed by the field supervisors and then mailed to the author every two weeks. The questionnaires were then checked again by two independent Chinese research assistants unaffiliated with either of the interviewing teams in China. These Mandarin-speaking assistants also made random phone-calls to more than 70% of the interviewees to verify the collection of data. This follow-up procedure revealed one instance of interviewer-opportunism in Shanghai and all questionnaires completed by this person were discarded.

For the purposes of analysing expansion patterns across markets, FMEs were counted as discrete events. Where firms had made multiple entries into the same foreign market, only the first entry was counted. Subsequent entries into existing markets will be made with less uncertainty than initial entries into new markets. Distance effects, which include the costs of overcoming uncertainty, will therefore be stronger for initial entries. The decision to restrict the sample to non-repetitive FMEs represents a significant departure from the past practice of treating new and repeated market entries indiscriminately (Barkema et al., 1996; Child et al., 2002; Engwall & Wallenstål, 1988).

At the close of data collection, full descriptive details had been recorded for 313, 828 and 333 FMEs made by exporters in Hong Kong, Shanghai and Xi'an respectively. However, 293 of the observed FMEs involved indirect exporting which describes the outsourcing of foreign marketing activities to a domestic trade intermediary. As few international business scholars consider indirect exporting to be anything more than "exporting by proxy", little different from other domestic sales, these FMEs were excluded from the final database. In addition, a small number of FMEs were based on entry modes other than exporting. As the aim of the study was to investigate low-risk entry modes involving production

within the home market, these were also removed from the database. A total of 1132 FMEs involving direct exports to around 70 markets were retained for analysis.

#### 4.2. Measurement

Distance to market was operationalised in geographic, cultural and psychic terms. Geographic distance was defined as the shipping distance in nautical miles between Shanghai and Hong Kong and the closest port in each foreign market. (Exporters from Xi'an were presumed to ship via Shanghai.) Previous studies measuring geographic distance have relied on great circle measurements (Terpstra & Yu, 1988). However, as shipping routes seldom follow the shortest line between two ports, actual shipping distance is a more accurate reflection of the costs of trade (Combes & Lafourcade, 2005). Distance data came from shipping tables maintained by [Maritimechain.com](http://Maritimechain.com) (2005).

Following conventional practice, cultural distance was calculated using Kogut and Singh's (1988) index with data drawn from Hofstede (2001). Specifically, distance scores for each foreign market were calculated by combining the deviation between the foreign and home markets over each of four cultural dimensions after factoring in the variance observed on each dimension. Although Hofstede's work is not without its critics (Drogendijk & Slangen, 2006; Shenkar, 2001), few other cultural theories have been subjected to similarly widespread levels of testing (Nakata & Sivakumar, 2001). The number of replication studies based on Hofstede's original work is sufficiently great that an Appendix A for the second edition of his book contains entries for 66 different nations.

Psychic distance was measured following Dow's (2000) method with informants in Hong Kong ( $n = 54$ ) and mainland China ( $n = 14$ ) being asked to rate the psychic distance to 42 and 55 foreign markets respectively. Following the approach originally devised by Nordström (1991), managers at both locations were asked to rate a list of foreign markets on a scale from one to 100 with their home market anchored on one. Prior to making these ratings informants were given two Chinese-language definitions of psychic distance taken from Johanson and Wiedersheim-Paul (1975) and O'Grady and Lane (1996). Individual country ratings were then aggregated and checked for consistency. In the mainland dataset, four data points (out of 770) were subsequently identified as being outliers (defined here as being more than 2.5 standard deviations from the mean score for each country) and these were dropped from the analysis. Three outliers were removed from the Hong Kong sample for similar reasons. Cultural and psychic distance scores for selected countries are presented for both Hong Kong and China in the Appendix A.<sup>3</sup>

The dependent variable, entry sequence, was operationalised on the basis of entry dates (year of entry) provided by informants. One shortcoming of this approach became apparent only during the analysis stage when it was realised that multiple entries within a single year can make it difficult to untangle the sequence of entry-events. To remedy this situation, entries reported as occurring within the same year were separated on the basis of the proportion of sales going to each market. Markets generating more sales for the firm

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<sup>3</sup>I am indebted to my graduate student Wong Hui Kan who collected the Hong Kong psychic distance data. Not surprisingly, cultural distance was significantly correlated with psychic distance for both the Hong Kong ( $r = .31, p < .05$ ) and mainland China ( $r = .45, p < .01$ ) samples. Yet as can be seen from the Appendix, there are several examples of countries being ranked relatively high on one index but low on the other (e.g., USA, Pakistan, New Zealand). Distance scores were also comparable across the two groups of respondents with strong correlations observed for both cultural ( $r = .86, p < .01$ ) and psychic distance ( $r = .97, p < .01$ ).

were deemed to have been entered earlier.<sup>4</sup> However, no discrimination was applied to same-year FMEs resulting from attendance at trade fairs. Given that a firm might generate multiple leads at a single trade fair, it was assumed that FMEs arising immediately after a trade fair could legitimately be considered simultaneous entries. After making these adjustments, the mean (and maximum) number of entries for exporters from each study location are as follows: Xi'an, 2.95 entries (8); Shanghai, 3.15 entries (9); and Hong Kong, 4.10 entries (8).

## 5. Results

FMEs occur as a result of deliberate actions undertaken by exporters, importers, and mutually-related third parties (e.g., brokers, traders, commission agents, etc.). FMEs may also arise serendipitously and as a consequence of chance meetings between potential exchange partners, such as may happen at an international trade fair (Ellis, 2000; Meyer & Skak, 2002). During the interviews managers were asked to identify the initiation scenario underlying each FME with five response options offering: (1) we approached them (exporter-initiated), (2) they contacted us (outsider-initiated), (3) we were introduced by a mutual associate/acquaintance (outsider-initiated), (4) we met at a trade fair/exhibition (trade fair-initiated) and (5) don't remember. In Xi'an and Shanghai, trade-fair initiated FMEs dominated the entry choices accounting for 45% and 39% of each sample respectively. In Hong Kong, FMEs were more likely to arise as a result of approaches made by outside parties (60%). Consistent with previous research (Brewer, 2001; Ellis, 2000), exporter initiations were found to play a relatively minor role in explaining the expansion patterns of firms from Xi'an (19% of FMEs), Shanghai (19%), and Hong Kong (10%). Given that our hypotheses are predicated on assumptions pertaining to exporters' experience, and that no predictions are made regarding the experience of outsiders (e.g., buyers and third parties), the following hypothesis tests were done twice; once for the entire database of FMEs at each location, and then again for those FMEs arising solely from the exporters' own initiative.

Prior to testing the hypotheses, the mean distance scores for different FMEs were examined for each sample. Table 2 reveals two instances where the dispersion of FMEs conforms to the predicted pattern of increasing distance. (In the Table, the fourth and subsequent FMEs have been collapsed into a single category.) In Xi'an, successive entries returned higher psychic distance means; in Shanghai the same pattern was evident for geographic distance. In the majority of cases the distance means for later FMEs are further than those for first entries hinting at a possible relationship between distance and expansion sequence.

Across the combined database there were 504 instances of a first (or equal-first) FME and 628 instances of subsequent entries. To test the hypothesis that early markets tend to be closer to home, the mean distance scores for the first markets entered were compared with the scores for all subsequent FMEs using one-tailed *t*-tests. The results, shown in Table 3, reveal statistically significant differences in the hypothesised direction were observed for geographic distance in the Shanghai sample only. Shanghainese exporters

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<sup>4</sup>An examination of the uncorrected sequence data revealed that earlier FMEs account for a greater share of a firm's income (35 percent) compared to later FMEs (18 percent;  $t = 12.762$ ,  $p < .000$ ). That is, entry sequence and export proportion are correlated ( $r = -.344$ ,  $p < .001$ ) indicating that the longer a firm is in a market, the more time it has to develop sales. The raw (uncorrected) and corrected entry sequences were highly correlated ( $r = .83$ ).

Table 2  
Foreign market entries by entry sequence (all FMEs)

Entry	Xi'an				Shanghai				Hong Kong			
	N	GD	CD	PD	N	GD	CD	PD	N	GD	CD	PD
1	117	4.66	2.25	32.87	281	4.60	2.38	33.57	106	6.48	2.04	30.19
2	77	4.57	2.06	33.22	144	4.85	2.18	32.12	19	7.24	2.23	35.59
3	66	4.28	1.93	34.35	99	4.94	2.13	32.65	13	5.17	2.33	32.84
>3	38	5.32	2.33	37.53	154	5.69	2.25	34.60	18	7.29	2.19	34.48
<i>F</i>		.68	1.72	2.91		3.00	1.71	2.20		1.49	1.09	1.51
<i>p</i>		.56	.16	.03		.03	.16	.09		.22	.36	.21

Notes: GD = geographic distance ('000NM), CD = cultural distance, PD = psychic distance.

Table 3  
Comparing early and subsequent foreign market entries

	Xi'an			Shanghai			Hong Kong		
	First entries	Later entries	<i>t</i>	First entries	Later entries	<i>t</i>	First entries	Later entries	<i>t</i>
<i>N</i> <sup>a</sup>	117/21	181/35		281/45	397/87		106/11	50/5	
Geographic distance									
All FMEs	4.66	4.62	.08	4.60	5.20	-2.10 <sup>b</sup>	6.48	6.72	-.44
Exporter-initiated FMEs only	3.37	4.34	-1.03	3.92	4.99	-1.54	7.30	6.22	.98
Cultural distance									
All FMEs	2.25	2.07	1.41	2.38	2.19	2.11 <sup>b</sup>	2.04	2.24	-1.73
Exporter-initiated FMEs only	1.84	2.19	-1.09	2.76	2.30	2.24 <sup>b</sup>	2.24	2.00	.83
Psychic distance									
All FMEs	32.87	34.57	-1.64	33.57	33.20	.53	30.18	34.48	-1.92
Exporter-initiated FMEs only	29.89	32.29	-.93	31.63	32.22	-.34	29.12	31.95	-.40

<sup>a</sup>All FMEs/Exporter-initiated FMEs only.

<sup>b</sup>*p* < .05.

typically began their foreign expansion in geographically proximate markets. However, contrary to expectations, Shanghaiese exporters were found to begin with a culturally-distant market before entering markets more similar to home. No statistically significant distance differences were observed between early and subsequent market entries in Xi'an or Hong Kong. To assess the practical significance of the statistically significant results, *t* statistics along with their relevant degrees of freedom were used to calculate effect sizes following Cohen's (1988) conventions.<sup>5</sup> Neither of the two statistically significant results

<sup>5</sup>Effect sizes for the *t* tests were calculated using the following equation:  $d = 2t/\sqrt{(df)}$ . Effect size cut-offs for Cohen's *d* are: .20 (small), .50 (medium) and .80 (large). Cut-offs for the product moment correlation *r* (relevant to the interpretation of H2–H4) are: .10 (small), .30 (medium) and .50 (large) (Cohen 1988, pp. 25–26, 82).

Table 4  
Distance and market entry sequence correlations

	H2 Correlations					H3 Correlations			
	1	2	3	4		1	2	3	4
Xi'an ( $N = 298/56$ )									
1. Entry #		.005	.112	-.102	Entry #		-.139	.030	-.222
2. GD	.005		.419 <sup>b</sup>	.525 <sup>c</sup>	GD gap	-.054		.317 <sup>a</sup>	.534 <sup>b</sup>
3. CD	-.034	.364 <sup>c</sup>		.491 <sup>c</sup>	CD gap	.093	.250 <sup>b</sup>		.478 <sup>b</sup>
4. PD	.104	.474 <sup>c</sup>	.305 <sup>c</sup>		PD gap	.029	.462 <sup>c</sup>	.355 <sup>b</sup>	
Shanghai ( $N = 678/132$ )									
1. Entry #		.091	-.176 <sup>a</sup>	.116	Entry #		-.099	.003	.018
2. GD	.116 <sup>b</sup>		.537 <sup>c</sup>	.480 <sup>c</sup>	GD gap	-.010		.357 <sup>b</sup>	.409 <sup>c</sup>
3. CD	-.056	.407 <sup>c</sup>		.545 <sup>c</sup>	CD gap	.100	.282 <sup>c</sup>		.626 <sup>c</sup>
4. PD	.055	.422 <sup>c</sup>	.252 <sup>c</sup>		PD gap	-.004	.391 <sup>c</sup>	.321 <sup>c</sup>	
Hong Kong ( $N = 156/56$ )									
1. Entry #		-.078	-.021	-.226	Entry #		-.218	.274	-.696
2. GD	.070		.103	-.081	GD gap	.147		-.619	.540
3. CD	.124	.129		-.529 <sup>a</sup>	CD gap	.153	-.211		-.866
4. PD	.139	.417 <sup>c</sup>	-.305 <sup>c</sup>		PD gap	-.142	.445 <sup>b</sup>	-.211	

Notes: Correlations below the diagonal are for all FMEs; exporter-initiated FME correlations are above the diagonal. G/C/PD = geographic/cultural/psychic distance. "Gap" refers to the distance separating  $FME_n$  and  $FME_{n-1}$ .

<sup>a</sup> $p < .05$ .

<sup>b</sup> $p < .01$ .

<sup>c</sup> $p < .001$  (2-tailed tests).

for the "all FMEs" group, was big enough to register even as a small effect. However, two results that were just outside of the bounds of statistical significance (cultural and psychic distance in the full Hong Kong sample) did meet the cut-off point for a small effect. Thus, the possibility that a true effect exists in this group but was undetected due to the small size of the Hong Kong sample cannot be ruled out. However, in terms of testing the prediction that exporters make early FMEs closer to home, the restricted sample of exporter-initiated FMEs provides a firmer basis for drawing conclusions about exporter behaviour. Removed from the analysis is the confounding influence of outsiders with experience levels that differ from exporters. An examination of the results obtained for the exporter-initiated FMEs revealed that none conformed to the predicted pattern of expansion. Collectively these results constitute weak to no support for H1.

Hypotheses 2 and 3 relate to overall expansion patterns. To test the link between distance to market and entry sequence, correlations were calculated for each group of exporters. The results are shown in Table 4. On the left side of the table are correlations pertaining to H2. Only one of these conforms to the predicted pattern of expansion: geographic distance is correlated with entry sequence in the full Shanghai sample. In practical terms this result constitutes a small effect according to Cohen's (1988) criteria for gauging effect size. However, none of the results obtained for the restricted exporter-initiated sample of FMEs matched the prediction of increasing distance to market. (The statistically significant result for cultural distance in Shanghai was in the wrong direction.) On the right side of the table are correlations pertaining to H3. These correlations measure

the strength of association between entry sequence and the distance separating consecutive market entries. None of the correlations relevant to this hypothesis are statistically significant.

The correlational, ANOVA and between-group tests conducted so far are useful for examining the location of all FMEs taking place at particular points in the sequence of international expansion. A better test of H2 and H3 is one that examines the location of FME  $n$  in relationship to the location of FME  $n-1$  for each company. If international expansion patterns are characterised by increasing distance from the home market, the distance to FME  $n$  should exceed the distance to FME  $n-1$  for individual companies. A test designed specifically for this purpose was devised by Benito and Gripsrud (1992) in their search for patterns underlying foreign direct investment decisions of Norwegian manufacturers. Their regression model is adapted here:

$$Dist_{.n} - Dist_{.n-1} = a + b FME_n,$$

where  $Dist_{.n}$  is the distance to the location of FME number  $n$  for a given company;  $Dist_{.n-1}$  the distance to the location of FME number  $n-1$  for a given company;  $FME_n$  is the FME number  $n$  for a given company; and  $a, b$  are the intercept and slope.

Following this procedure a total of 18 regression equations were estimated for all the FMEs preceded by another FME (three exporter groups  $\times$  three distance measures  $\times$  two initiation scenarios). Support for the underlying predictions was ascertained by examining the coefficients of each model. A positive and statistically significant constant ( $a$ ) in a model would constitute support for H2 whereas a positive slope ( $b$ ) would support H3. In 12 out of 18 equations, the sign of the intercept was positive, as predicted, but none of these cases was statistically significant. These results provide no support for either H2 or H3.

Finally, Benito and Gripsrud (1992) proposed that even in the absence of sequential expansion patterns based on increasing distance to market, FME choices may be made in the neighbourhood of past choices allowing managers to transfer experience from one decision to another. That is, managers may be inclined to enter new markets that are culturally or psychically similar to existing markets, as predicted in H4. If so, then the distance to a new foreign market will be correlated with the distance to the market previously entered by the same company. This was found to be the case for ten (out of 18) combinations of distance, sample and initiation type. These correlational results prompted a more rigorous regression-based analysis using the following equation adapted from Benito and Gripsrud (1992):

$$Dist_{.n} = a + b Dist_{.n-1}$$

The intercepts ( $a$ ), regression slopes ( $b$ ), and  $F$  statistics are listed in Table 5. (Coefficients of multiple determination ( $R^2$ ) and inflection points are provided for the ten statistically significant regression equations.) These results show that the distance to new markets is related to the distance to markets already entered. Specifically, the results show that when firms begin by exporting to proximate markets, subsequent market entries will be further away and vice versa. The inflection point for each sample is listed in the table. To take the first example listed, if the geographic distance to a market exceeds 4610 nautical miles, the regression predicts that the next market entered by exporters from Xi'an will be geographically closer. Below this threshold point and subsequent entries will take

Table 5  
Near-market effects observed at each location

Distance Measure	Sample	Intercept ( <i>t</i> stat)	<i>B</i> ( <i>t</i> stat)	<i>F</i>	<i>R</i> <sup>2</sup>	Inflection point	Effect	
							<i>r</i>	Size
<i>(a) All FMEs</i>								
Geographic	Xi'an	3.66 (9.03) <sup>c</sup>	.21 (2.99) <sup>b</sup>	8.92 <sup>b</sup>	.04	4.61	.207 <sup>b</sup>	Small
	Shanghai	4.00 (13.86) <sup>c</sup>	.24 (5.19) <sup>c</sup>	26.93 <sup>c</sup>	.06	5.26	.235 <sup>c</sup>	Small
	Hong Kong	6.26 (9.09) <sup>c</sup>	.01 (.11)	.01	–	–	.010	
Cultural	Xi'an	1.68 (9.44) <sup>c</sup>	.21 (2.92) <sup>b</sup>	8.55 <sup>b</sup>	.04	2.13	.217 <sup>b</sup>	Small
	Shanghai	1.51 (12.34) <sup>c</sup>	.31 (6.42) <sup>c</sup>	41.24 <sup>c</sup>	.09	2.18	.302 <sup>c</sup>	Medium
	Hong Kong	1.60 (8.49) <sup>c</sup>	.22 (2.55) <sup>a</sup>	6.52 <sup>a</sup>	.06	2.05	.234 <sup>b</sup>	Small
Psychic	Xi'an	30.23 (12.00) <sup>c</sup>	.11 (1.54)	2.37	–	–	.111	Small
	Shanghai	28.89 (16.10) <sup>c</sup>	.14 (2.66)	7.05 <sup>b</sup>	.02	33.47	.129 <sup>b</sup>	Small
	Hong Kong	35.61 (10.28) <sup>c</sup>	–.09 (–.93)	.86	–	–	–.087	
<i>(b) Exporter-initiated FMEs</i>								
Geographic	Xi'an	2.65 (3.42) <sup>b</sup>	.44 (3.01) <sup>b</sup>	9.08 <sup>b</sup>	.18	4.70	.426 <sup>b</sup>	Medium
	Shanghai	3.21 (4.96) <sup>c</sup>	.36 (3.43) <sup>b</sup>	11.80 <sup>b</sup>	.12	5.01	.351 <sup>c</sup>	Medium
	Hong Kong	2.17 (.60)	.47 (.32)	1.02	–	–	.319	Medium
Cultural	Xi'an	1.81 (5.20) <sup>c</sup>	.06 (.42)	.18	–	–	.067	
	Shanghai	1.64 (5.03) <sup>c</sup>	.29 (2.53) <sup>a</sup>	6.38 <sup>a</sup>	.08	2.31	.277 <sup>b</sup>	Small
	Hong Kong	2.26 (2.25)	.04 (.08)	.01	–	–	.028	
Psychic	Xi'an	28.31 (5.40) <sup>c</sup>	.12 (.77)	.59	–	–	.119	Small
	Shanghai	23.85 (6.37) <sup>c</sup>	.22 (2.00) <sup>a</sup>	4.02 <sup>a</sup>	.05	30.53	.220 <sup>a</sup>	Small
	Hong Kong	21.50 (2.00)	.15 (.49)	.24	–	–	.160	Small

Note: *R*<sup>2</sup> values and inflection points are only provided for statistically significant equations.

<sup>a</sup>*p* < .05.

<sup>b</sup>*p* < .01.

<sup>c</sup>*p* < .001.

place in more distant markets. For Shanghaiese exporters, the inflection point is higher (5260 NM).

To facilitate the interpretation of the statistically significant results, the correlations (effect sizes) are also provided in Table 5. Ten small- and four medium-sized effects were observed (although four of these were not statistically significant). Cohen (1988, p. 25) argues that effect sizes are likely to be small in new areas of research when phenomena are not under good experimental or measurement control. Research into the near-market effect, particularly as it applies to low-risk control modes, falls into this category. Thus, the presence of the near-market effect at all three study locations and for both initiation groups can be taken as reasonable support for H4.

## 6. The effects of distance on foreign expansion via direct exporting

In contrast with previous work, this study has examined four predictions relating to the effects of distance on foreign expansion patterns using multiple distance measures, three diverse samples and a large database of low-risk, non-repetitive FMEs. Collectively the results returned from the three samples may be summarised as follows: the link between

distance and expansion patterns received very weak to no support (H1 and H2)<sup>6</sup>; the hypothesis linking the rate of international expansion with experience received no support (H3); but the near-market effect was evident in one form or another at all three study locations (H4). These three broad conclusions are discussed in turn.

In Johanson and Wiedersheim-Paul's original study (1975), the correlation between psychic distance to markets and FME via independent agents was statistically significant in only two of the four cases studied. At first glance, it appears that this mixed-result is repeated in the current study at least in the context of geographic distance. For the Shanghainese sample, geography was weakly correlated with entry sequence, although no such relationship was observed in Xi'an or Hong Kong. One explanation is that distance effects are context-dependent with some locations being more susceptible than others. This is an argument others have made to explain why psychic distance effects tend to show up in studies involving Scandinavian companies (Sullivan & Bauerschmidt, 1990). But a safer conclusion is that distance does not affect firm internationalisation in the simple ways predicted by H1 and H2. The best test of whether firm expansion describes a pattern of increasing distance to market is company-specific and here the results are unequivocal. Equations regressing the distance separating consecutive FMEs as a function of the number of entries previously made by individual firms returned non-significant results for all of the distance/sample combinations examined. Whatever their reasons were for selecting new foreign markets to enter, the Chinese exporters in this study were not significantly impelled by cost considerations arising from minimising the geographic or cultural/psychic distance from home.

Additionally, across the three samples there was no support for the conjecture that the rate of outward expansion is affected by experience (H3). These findings refute Benito and Gripsrud's (1992) hypothesis that the rate of international expansion is affected by experience.

To summarise the story so far, the evidence from the three study locations challenges the proposition that internationalisation patterns conform to a monotonic pattern of increasing distance to markets. On what basis then, do exporters make FME decisions? Some answers can be found by looking at the modal choices made by managers at each location. Shanghainese exporters exhibited a strong predilection for two neighbouring markets; Japan and Korea. In addition to their geographical proximity both countries share a common Confucian heritage with China and neither was rated as being particularly distant in psychic terms. (Although with a psychic distance score of 32.5 Japan was just over the inflection point of 30.5 returned for Shanghainese exporters suggesting that subsequent export markets would be psychically closer to home. Korea's psychic distance score for this group was 28.1.) Both Japan and Korea happen to be substantial consumers of Chinese exports. In short, economic factors, rather than geography or culture, may have been more significant in influencing early export decisions. Post-hoc correlational analysis bares this out. Market size, measured in terms of the purchasing power-equivalent of GDP, is more strongly correlated with entry sequence than any of the three distance variables. Large economies also dominated the top three market choices of exporters from Xi'an (USA, Japan and Germany) and Hong Kong (USA, UK and Germany). As none of

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<sup>6</sup>Out of 27 results for the "All FME" group obtained for H1 and H2 using three analytical tests (*t*-test (H1), correlational and regression analyses (H2)), only two were statistically significant. Of these, only one was "large" enough to register as a small effect. Of the 27 results obtained for the "exporter-initiated FMEs", none was statistically significant.

these markets is particularly close to Xi'an or Hong Kong in geographic, cultural or psychic terms, a reasonable conclusion seems to be that entry decisions were driven more by market opportunities than by minimising the costs of overcoming distance (Ellis, 2006). In Hong Kong's case historical ties to the UK also appear to have played a role in shaping FME patterns, a finding consistent with Ghemawat's (2001) claim that colonial links between countries boosts trade by 900%. These ties are reflected in a relatively low psychic distance score of 21.6. Still, the UK was often entered ahead of other psychically and geographically closer countries, such as Taiwan (13.3), Singapore (18.9), and Thailand (20.9). This pattern of behaviour adds weight to the idea that market size is a more important factor explaining the FME sequence of Hong Kong exporters, a conclusion consistent with the results of other, firm-level investigations of internationalisation patterns (Davidson, 1980; Mitra & Golder, 2002; Terpstra & Yu, 1988).

While distance effects were not found to influence the pattern and pace of outward expansion in a direct or monotonic fashion, the results nevertheless show that consecutive FME locations are related and that the direction and extent of movement between two subsequent market entries can be explained as a function of the location of the earlier FME. Specifically, closer FMEs tend to be followed by more distant FMEs and, once a certain point is reached, vice versa. These results closely match those reported by Benito and Gripsrud (1992) in their analysis of foreign investment patterns. In that study the near-market effect was limited to cultural distance and the inflection point (the value at which subsequent investments are made closer to home than a previous investment) was 2.13, well within the range of results returned for cultural distance in this study (2.05–2.31).<sup>7</sup> For the Hong Kong exporters, this means that if the cultural distance of the previous FME exceeds 2.05 (El Salvador is closest to this score), the next FME is likely to be culturally closer to home, and vice versa. For the mainland Chinese exporters, the analogous figure (or market) lies in the 2.13–2.18 range (say, Argentina).

The near-market effect suggests that experience gained in one market reduces the uncertainty associated with entering other, culturally similar markets (Barkema et al., 1996). This is the best explanation of why subsequent FMEs are correlated even when there is no link between distance and overall expansion patterns. The implication is that cultural knowledge generated in similar markets is a better predictor of foreign expansion than cultural knowledge acquired at home (Mitra & Golder, 2002). Interestingly, the near-market effect supports the Scandinavian idea that experiential learning shapes firm internationalisation, but not in the manner originally conceived. Relevant experience is not gained at home, but from operating in foreign markets that are similar to the new market being entered. This transference between culturally similar markets is logical if new markets have more in common with recent markets than the exporter's country of origin (Mitra & Golder, 2002).

This study extends previous work on the near-market effect in two ways. First, by observing the near-market effect in the context of low-risk entry modes, the study shows

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<sup>7</sup>Can the results of cultural distance studies done in separate countries be compared? Undoubtedly specific country-pairings will be incomparable. (The distance separating Norway from the US will not be the same as the distance from China from the US.) But if cultural distance studies contain a mix of both near and far markets, then individual differences may balance out, or at least they may be too small to undermine predictions about the relationship between near and far markets. Interestingly, the means and standard deviations for cultural distance in this study (2.20/1.08) and the studies by Benito and Gripsrud (1992, 1.95/1.44) and Barkema et al. (1996, 2.64/1.14) are very similar. No study reported a mean that was more than one standard deviation away from the mean of either of the other two studies.

that exporters are able to transfer their experience from one market to another in much the same way that multinationals transfer learning between subsidiaries. Second, the study further reveals that the near-market effect can be detected when distance is operationalised in psychic terms. This makes intuitive sense. Managers should be able to leverage their experiences between markets which are psychically similar.<sup>8</sup>

The central question asked in this study is whether distance to market affects firm internationalisation. The results show that distance does indeed affect internationalisation, but does so in ways which are not yet well-understood. Near-market knowledge, whether measured in cultural or psychic distance terms, was found to be a better predictor of FME than distance from the home market. This result is consistent with recent research investigating the timing of FDI decisions (Mitra & Golder, 2002).

In summary, two important contributions can be identified. First, by drawing on a large database of non-repetitive FMEs drawn from diverse exporters in dissimilar locations, the study provides a substantial evidentiary basis for testing four distance-related hypotheses. This represents a significant departure from the past practice of drawing distance-related conclusions from data-sets evidencing limited variation on the constructs of interest and which fail to discriminate between entries into new and existing markets. Second, the study has provided arguably the first demonstration of the near-market effect in the context of low-risk entry modes. Non-zero benchmarks have also been provided against which future effect sizes may be compared. For scholars working in the field, the challenge is now to expand upon this idea that culture-specific learning is an asset that can be transferred between markets. The actual means by which this transfer process serves to reduce the uncertainty of exporting to new markets, remains to be explained.

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## **Appendix A. Cultural and psychic distance scores—selected countries**

See Table A1.

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<sup>8</sup>Somewhat unexpectedly, the near-market effect was also evident when distance was measured geographically. However, the geographic results may be spurious as there is no reason to expect that managers can transfer learning between proximate markets, except when those markets happen to be culturally or psychically similar. An examination of the link between geographic and cultural distance bares this out. For mainland Chinese firms, neighbouring markets such as Hong Kong (.14), India (.45), Vietnam (.51), and the Philippines (.25) generally had much lower cultural distance scores than distant markets such as the US (3.09), the UK (3.08), the Netherlands (4.49) and Denmark (4.93). Hong Kong is the exception which proves the point. For exporters in this city there is a non-significant correlation between the cultural and geographic distance to foreign markets. Consequently a near-market effect observed when distance was measured in cultural terms failed to materialise when distance was measured geographically.

Table A1

Cultural distance from...				Psychic distance from...			
... Hong Kong	Score	... China	Score	... Hong Kong	Score	... China	Score
Hong Kong	.00	China	.00	Hong Kong	1.00	China	1.00
China	.14	Hong Kong	.14	China	12.81	Hong Kong	8.31
Vietnam	.21	Philippines	.25	Taiwan	13.29	Malaysia	21.15
Singapore	.27	Singapore	.44	Singapore	18.90	Singapore	21.36
India	.32	India	.45	USA	19.61	Thailand	22.85
Philippines	.50	Malaysia	.50	Japan	20.61	Taiwan	23.21
Malaysia	.72	Vietnam	.51	Thailand	20.88	United Kingdom	26.79
Taiwan	.86	Pakistan	1.20	United Kingdom	21.65	Korea	28.14
Pakistan	.89	Taiwan	1.21	Korea	22.04	Russia	31.00
Thailand	.90	Thailand	1.32	Vietnam	23.00	Japan	32.50
Korea	1.62	Korea	2.00	Malaysia	24.21	Germany	33.14
Germany	1.93	Germany	2.51	New Zealand	37.64	USA	33.43
Italy	2.30	Russia	2.66	France	38.13	India	35.79
United Kingdom	2.37	Italy	2.68	Germany	39.17	Australia	36.43
United States	2.40	Japan	2.86	Italy	40.79	France	36.43
France	2.43	France	2.89	Netherlands	43.51	Vietnam	38.43
New Zealand	2.51	United Kingdom	3.08	India	44.31	Netherlands	41.07
Australia	2.54	United States	3.09	Australia	44.82	Denmark	45.36
Russia	2.58	Australia	3.29	Denmark	46.45	Argentina	48.00
Japan	2.97	New Zealand	3.42	Israel	54.00	Pakistan	48.36
Netherlands	3.24	Netherlands	4.49	Pakistan	55.96	Israel	51.64
Denmark	3.46	Denmark	4.93	Argentina	58.00	Kenya	62.50

Note: Low scores reflect low distance.

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