ISBN 978-1-84626-026-1
Proceedings of 2010 International Conference on Business, Economics and Tourism Management (CBETM 2010)
Singapore, *26-28 February*, *2010*

Internationalization of Malaysian Service Firms:

Business Strategy and Choice of Foreign Market Entry Mode

Mohammadreza Asgari [1] and Syed Zamberi Ahmad [2]

[1] Faculty of Business and Accountancy, University of Malaya, Kuala Lumpur

[2] College of Business Administration, Prince Sultan University (PSU), Riyadh, Kingdom of Saudi Arabia

Abstract. Despite the substantial amount of work undertaken on internationalization to-date, few have placed emphasis on the temporal processes and dynamisms of the international expansion of firms in the services sector. The numerous studies on internationalization from different theoretical and empirical approaches have their origin in manufacturing firms' perspectives. Recently, the rapid progress in the service sector has attracted many scholars to study the development, progress and behaviour of service firms. Therefore, this paper is a preliminarily investigation of the pattern of, and motives for, business strategy and choice of entry mode made by Malaysian service firms. Being among the fast growing economies in the Asia Pacific region, which mainly relies on the service sector for economic development, many nascent Malaysian service firms are now seeking to expand beyond their national territory. This research proposes to utilize a case study approach through in-depth interviews with key managers/executives in selected Malaysian service firms to explain the internationalization behaviour of these firms. Limitations of the current study and suggestions for future research are presented.

Keywords: internationalization, entry mode choice, Malaysian service firms.

1. Introduction

The rapid changes in the global business environment in recent decades had a strong effect on the internationalization processes of most companies around the world (Laanti *et al.,* 2007). The ending of the cold war between the superpowers caused changes in the political environment and governmental policies resulting in the removal of trade barriers and emerging new markets, and, thus, encouraged international business activities. In addition, the revolution in technology, particularly in communications, transportation and information processing made international business more feasible and more profitable, making the world a 'global village' (Griffin and Pustay, 2002; Hill, 2008). As Dicken (1992) pointed out, globalization is the result of the global behaviour and strategy of multinational corporations (MNCs). In order to have a confident future and find a sure marketplace, many MNCs have decided to cross their national borders and offer their products and services internationally. Among the main popular destinations of such multinational firms are the emerging Asian and Latin American markets as well as the large established markets in North America, Europe and Japan (Osland *et al.*, 2001).

The internationalization process requires firms to choose a suitable entry mode strategy and selection of a target foreign market (Kumar and Subramaniam, 1997). According to Ekeledo and Sivakumar (2004), a firm applies an entry mode strategy during the first three to five years of its foreign market operation. Adopting an appropriate entry mode may help a firm achieve better performance and better survival in a foreign market (Ekeledo and Sivakumar, 2004; Root, 1994). However, firms enter a specific target market through various entry strategies caused by the differential in their specific resources, capabilities and strategies. On the other hand, to enter different foreign markets, a specific firm does not apply a unique strategy because it faces dissimilar environments. Therefore, researchers have already recognized two types of factors that determine the choice of entry mode - internal and external factors (see Agarwal and Ramaswami, 1992; Anderson and Gatignon, 1986; Blomstermo *et al.*, 2006; Choo and Mazzarol, 2001; Dunning, 1977, 1980, 1988; Ekeledo and Sivakumar, 1998, 2004; Erramilli and Rao, 1993; Kwon and Konopa, 1993; Quer *et al.,* 2007; Root, 1994; Wernerfelt, 1984).

Another new phenomenon in current world business is the rapid growth of service firms. Hence, researchers have paid increasing attention to the internationalization process of service firms (Blomstermo *et al.*, 2006). Although most manufacturing firms focus on exporting as the easiest and fastest way to enter foreign markets, service firms have a tendency towards expanding internationally. For instance, in 2007, trade in services comprised 23% of total international trade ((UNCTAD, 2008), while 65% of total world outward foreign direct investment (FDI) was made by firms from the service sector. This amount accounts for more than 87% of outward foreign direct investment that was contributed by firms from developing countries (UNCTAD, 2009). Therefore, this study pays attention to the international expansion of service firms from developing countries, and, in particular, Malaysia.

As one of the successful Asian Newly Industrialized Countries (NICs) with a relatively high per capita income, Malaysia has improved its position in terms of FDI in the international business arena. Malaysia is chosen as a setting for this study as first, the service sector has played a pivotal role in its economic development, and second, its outward FDI flows have surpassed inward FDI flows since 2006, i.e. Malaysian firms are now major investors in foreign markets. In 2008, 45% of Malaysia's GDP was yielded by service industries and 51% of the labour force was involved in services (CIA, 2009). At the same time, outward FDI flows were more than US$14.06 billion while inward FDI flows accounted for US$8.05 billion, and in sum, outward FDI stocks were equivalent to 30% of the GDP of Malaysia (UNCTAD, 2009). Increasing understanding through the study of the entry mode strategies and motives for expansion of Malaysian service firms, the government and its related agencies can create policies to encourage firms to engage in international business.

As explained earlier, this research will conduct a preliminary investigation and explain the internationalisation process of some leading Malaysian service firms, through a historical approach. The aim of the study is to recognize the firms' behaviour during market selection and the strategic choice of entry into foreign markets, derived from their competitive advantages, motives for entry and business strategies while considering the effects of environmental forces.

2. Theoretical Views on the Choice of Entry Mode

Through the internationalisation process, firms gradually expand their business activities beyond their national authority and launch operations in other countries (Ahmad and Kitchen, 2008). To expand its activities to a foreign market, a firm must make three essential decisions, i.e. which markets to enter, when to enter the market, and on what scale and strategic commitments to enter those markets (Hill, 2008). The third decision requires the selection of an appropriate form of entry, which is an important strategic decision for a firm (Chung and Enderwick, 2001; Quer *et al.*, 2007), that determines the firm's performance and survival in foreign markets (Choo and Mazzarol, 2001; Chung and Enderwick, 2001; Ekeledo and Sivakumar, 2004; Root, 1994). As firms desire to minimize their risk, their favourite mode is the one that can decrease the risk and give them a higher return (Kwon and Konopa, 1993).

Generally, entry mode choices are divided into two categories: First, non-equity modes including market oriented modes (direct and indirect export) and contractual modes (turnkey projects, contract manufacturing, management contracts, strategic alliance, licensing and franchising), and second, equity or investment modes (FDI) including partly owned modes (Joint venture) and wholly owned modes or sole ownership (Kumar and Subramanian, 1997; Lotayif, 2003; Wild *et al.*, 2008). Applying an equity mode in turn requires a choice between setting up a business from scratch (Greenfield investment) or buying an existing firm (acquisition), or Brownfield, i.e. a combination of both strategies (Griffin and Pustay, 2002; Hill, 2008; Wild *et al.*, 2008).

Each form of entry has its own benefits and disadvantages. Firms may follow various criteria to choose a suitable mode at each stage. Gaining high return from foreign operations necessitates high resource commitment, which in turn, increases the risk of international investment. Therefore, firms have to exert higher control over their foreign operations and affiliates. For this reason, researchers have mostly focused on control as the main factor that indicates the type of entry a firm adopts (Blomstermo *et al.*, 2006; Ekeledo and Sivakumar, 2004). They divided entry modes to high control modes including wholly owned subsidiary, strategic alliance and direct export, and low control modes including indirect export, contractual modes and joint venture (Ekeledo and Sivakumar, 2004; Kumar and Subramanian, 1997; Lotayif, 2003).

As Table 1 indicates, researchers have offered different approaches to explain the choice of entry mode in foreign markets and the logic behind each decision. Since the 1980s, most studies in the field of internationalization and entry modes have utilized one of the three major theories, i.e. the eclectic theory (OLI), transaction cost theory (TC) or the resource-based view (RBV). Dunning (1977, 1980, 1988) in his eclectic model emphasized that the firms' choice of entry depends on their ownership advantages (firm resources), location advantages (host country factors) and internalization advantages (risk of contracts). According to Anderson and Gatignon (1986), when the transaction costs related to negotiating, monitoring and implementing a contract are high, firms will favour high control modes. On the other hand, the resource-based view (RBV) argues that firms with valuable resources and capabilities favour high control modes, especially when they follow a global strategy (Ekeledo and Sivakumar, 2004).

Table 1: Theories of Entry Mode Strategy for Internationalization

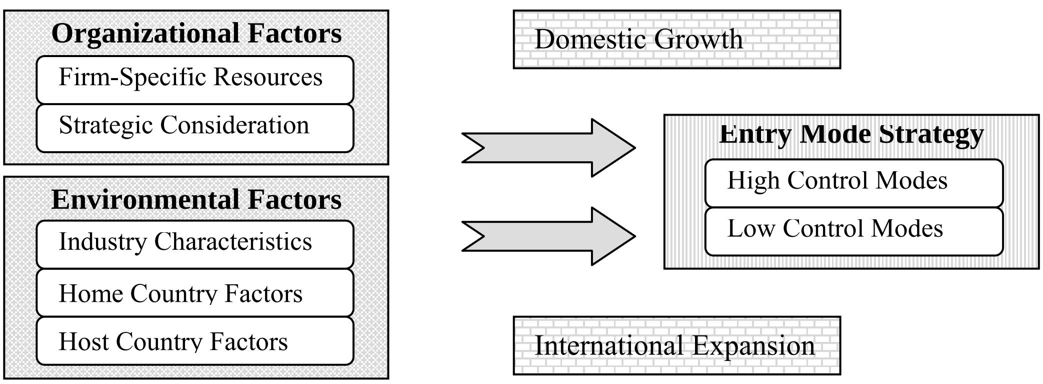
Theory	Explanation of the internationalization and entry strategy	Outstanding studies
Monopolistic Advantage Theory	High market imperfection and monopoly helps MNCs for FDI while in the markets with low imperfection, licensing is preferred.	Hymer (1960)
International Product Life Cycle Theory (IPLC)	When product is in early product life cycles (PLC) stage, firms prefer exporting but in the later PLC stage, FDI occurs.	Vernon (1966)
Internationalization Theory	Choice of entry is sequential from exporting to full ownership.	Johanson and Vahlne (1977)
Networks Theory	High competitive advantages and networking facilitate FDI.	Håkansson (1987)
Internalization Theory	High market failure results in FDI; otherwise, licensing preferred.	Buckley and Casson (1976)
Eclectic Theory	Location advantage favours home market: Exporting Location advantage favours host market: when internalization advantage is low, licensing; and when it is high, FDI is preferred.	Dunning (1977, 1980, 1988), Agarwal and Ramaswami (1992)
Transaction Cost Theory	High transaction cost forces firm to choose high control modes.	Anderson and Gatignon (1986)
Resource-Based View	Firms with valuable resources select high control modes.	Wernerfelt (1984)
Contingency Theory	Firms in separable industries prefer JV or licensing while firms in inseparable industries use franchising or full ownership.	Kumar and Subramaniam (1997), Ekeledo and Sivakumar (1998)

Adapted from: Cumberland (2006), Sharma and Erramilli (2004).

2.1 Factors Influence the Choice of Entry Mode

The choice of entry mode is affected by two types of factor including internal (organizational) factors and external (environmental) factors. Internal factors can be controlled by firms but external factors are usually beyond the firms' control (Ekeledo and Sivakumar, 1998, 2004). While most previous research and FDI studies have focused on only one aspect or factor, this study considers both internal and external factors affecting the international expansion of Malaysian service firms. The proposed model is shown in Figure 1.

Figure 1: Factors Influencing the Choice of Entry Mode of Service Firms



3. Methodology

The present study utilizes two types of data, including secondary and primary data, to analyze and evaluate the historical trend and the determinants of the choice of entry mode strategy among Malaysian service firms. Secondary data is extracted from various sources such as the companies' annual reports, and the statistics of government organizations and international organizations. By analyzing secondary data, an insight about the trends of foreign investment made by Malaysian service firms is obtained.

To collect comprehensive and holistic primary data from Malaysian service firms that have ventured abroad, a qualitative method in the form of a case study is used (Ahmad, 2008; Yin, 2009). The reason for selecting a case study is that first, due to the lack of helpful and comprehensive statistics for Malaysian service firms, applying a case study helps researchers collect data from various sources (Ahmad, 2008); second, as the target population of the study refers to Malaysian service firms that have ventured abroad and the number of such firms is limited, the sample of research is too small to run a quantitative study; and third, conducting a case study research results in more exact and useful findings and deep knowledge regarding the entry strategies of firms. The primary data is provided through in-depth interviews with key managers of the selected sample from different industries within the service sector. The interviewees are questioned by semi-structured open-ended questionnaires to explain their opinions, experiences and arguments.

4. Challenges and Future Research Directions

As Ahmad (2008) stated, the use of case study on a small and limited sample, makes generalizing the results to all service firms inconclusive and rather impossible. However, comparing the research findings with the findings of previous studies may lead to some understanding of the general rules of entry strategies. The study of the internationalization of firms from developing countries is an attractive area of research. However, further studies in the subjects such as the effect of government support on the internationalization of service firms, the impact of decision makers on the choice of entry mode, and the entry mode strategies of SMEs from developing countries are proposed to be undertaken.

5. Conclusion

The rapid growth of the Malaysian economy and the speed of development in this developing country have facilitated the expansion of Malaysian firms internationally, especially in the service sector. As the study describes, various factors affect the choice of entry strategies of Malaysian service firms including organizational and environmental factors. Using the case study method, the research will provide helpful information about the motives of these firms to enter foreign markets, their competitive advantages and the environmental threats that limit their investment decision. Finally, the limitations and challenges of the study are recognized to help future research.

6. References

[1] S. Agarwal and S.N. Ramaswami. Choice of Foreign Market Entry Mode: Impact of Ownership, Location and Internalization Factors. *Journal of International Business Studies*. 1992, **23** (1): 1-27.

[2] S. Z. Ahmad. The Internationalization Process of Third World Multinational Firms: A Study of Malaysia's Government-linked Corporations. *International Journal of Business Research*. 2008, **8** (5): 35-47.

[3] S. Z. Ahmad, and P. J. Kitchen. Transnational corporations from Asian developing countries: The internationalisation characteristics and business strategies of Sime Darby Berhad. *International Journal of Business Science and Applied Management*. 2008, **3** (2): 21-36.

[4] E. Anderson, and H. Gatignon. Modes of Entry: A Transaction Cost Analysis and Propositions. *Journal of International Business Studies*. 1986, **17** (3): 1-26.

[5] A. Blomstermo, D. D. Sharma, and J. Sallis. Choice of Foreign Market Entry Mode in Service Firms. *International Marketing Review*. 2006, **23** (2): 211-29.

[6] P. J. Buckley, and M. C. Casson. *The Future of Multinational Enterprise*. New York: Holmer and Meier Publishers, 1976.

[7] S. Choo, and T. Mazzarol. An Impact on Performance of Foreign Market Entry Choice by Small and Medium-Sized Enterprises. *Journal of Enterprising Culture*. 2001, **9** (3): 291-312.

[8] H. F. L. Chung, and P. Enderwick. An Investigation of Market Entry Strategy Selection: Exporting vs. Foreign Direct Investment Modes. *Asia Pacific Journal of Management*. 2001, **18** (4): 443-460.
[9] CIA. The World Fact Book 2009. Washington DC: Central Intelligence Agency. 2009.
[10] F. Cumberland. Theory Development within International Market Entry Mode - An Assessment. *The Marketing Review*. 2006, **4**: 349-373.
[11] P. Dicken. Global Shift: The Internationalization of Economic Activity. London: Paul Chapman Publishing. 1992.
[12] J. H. Dunning. Trade, Location of Economic Activity and the MNE: A Search for an Eclectic Approach. In B. Ohlin, et al (eds.). *The International Allocation of Economic Activity*. London: Macmillan, 1977.
[13] J. H. Dunning. Toward an Eclectic Theory of International Production: Some Empirical Tests. *Journal of International Business Studies*. 1980, **11** (1): 9-31.
[14] J. H. Dunning. The Eclectic Paradigm of International Production: A Restatement and Some Possible Extensions. *Journal of International Business Studies*. 1988, **19** (1): 1-31.
[15] I. Ekeledo, and K. Sivakumar. Foreign Market Entry Mode Choice of Service Firms: A Contingency Perspective. *Journal of Academy of Marketing Science*. 1998, **26** (4): 274- 292.
[16] I. Ekeledo, and K. Sivakumar. International Market Entry Mode Strategies of Manufacturing Firms and Service Firms: A Resource-Based Perspective. *International Marketing Review*. 2004, **21** (1): 68-101.
[17] M. K. Erramilli, and C. P. Rao. Service Firms' International Entry-Mode Choice: A Modified Transaction Cost Analysis Approach. *Journal of Marketing*. 1993, **47**: 19-38.
[18] R. W. Griffin, and M. W. Pustay. International Business: A Managerial Perspective. Third Edition. New Jersey: Pearson Education Inc, 2002.
[19] H. Håkansson. Industrial Technological Development: A Network Approach. London: Croom Helm, 1987.
[20] C. W. L. Hill. Global Business Today. Fifth Edition. New York: McGraw-Hill/Irwin, 2008.
[21] S. H. Hymer. The International Operations of National Firms: A Study of Direct Foreign Investment. PhD Dissertation. US: Massachusetts Institute of Technology, 1960.
[22] J. Johanson, and J. E. Vahlne. The Internationalization Process of the Firm - A Model of Knowledge Development and Increasing Foreign Market Commitments. *Journal of International Business Studies*. 1977, **8** (1): 23-32.
[23] V. Kumar, and V. Subramaniam. A Contingency Framework for the Mode of Entry Decision. *Journal of World Business*. 1997, **32** (1): 53-72.
[24] Y. C. Kwon, and L. J. Konopa. Impact of Host Country Market Characteristics on the Choice of Foreign Market Entry Mode. *International Marketing Review*. 1993, **10** (2): 60-76.
[25] R. Laanti, M. Gabrielsson, P. Gabrielsson. The Globalization Strategies of Business-to-Business Born Global Firms in the Wireless Technology Industry. *Industrial Marketing Management*. 2007, **36**: 1104-1117.
[26] M. Lotayif. A Theoretical Model for Matching Entry Modes with Defensive Marketing Strategies. *Journal of American Academy of Business*. 2003, **2** (2): 460-466.
[27] G. E. Osland, C. R. Taylor, S. Zou. Selecting International Modes of Entry and Expansion. *Marketing Intelligence & Planning*. 2001, **19** (3): 153-161.
[28] D. Quer, E. Claver, and R. Andreu. Foreign Market Entry Mode in the Hotel Industry: The Impact of Country- and Firm-Specific Factors. *International Business Review*. 2007, **16**: 362- 376.
[29] F. R. Root. Entry Strategies for International Markets. Lexington: D. C. Heath, 1994.
[30] V. M. Sharma, and M. K. Erramilli. Resource-based Explanation of Entry Mode Choice. *Journal of Marketing Theory and Practice*. 2004, **4**: 1-18.
[31] UNCTAD. Handbook of Statistics 2008. New York: United Nations Conference on Trade and Development, 2008.
[32] UNCTAD. World Investment Report 2009: Transnational Corporations, Agricultural Production and Development. New York: United Nations Conference on Trade and Development, 2009.
[33] R. Vernon. International Investment and International Trade in the Product Cycle. *Quarterly Journal of Economics*. 1966, **2**: 190-207.
[34] B. Wernerfelt. A Resource-Based View of the Firm. *Strategic Management Journal*. 1984, **5** (2): 171-180.
[35] J. J. Wild, K. L. Wild, and J. C. Y. Han. International Business: the Challenges of Globalization. Fourth Edition. New Jersey: Prentice hall, Pearson Education Inc, 2008.
[36] R. K. Yin. Case Study Research- Design and Method. Fourth Edition. California: Sage, Thousand Oaks, 2009.