BEFORE YOU GO, YOU SHOULD KNOW: THE IMPACT OF WAR, ECONOMIC, CULTURAL AND RELIGIOUS ANIMOSITY ON ENTRY MODES

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One of the most important strategic decisions managers of multinational corporations have to make is the selection of entry mode into a foreign market. An extensive survey of the literature indicates that one of the main areas neglected in strategy research is the impact of animosity (war, economic, cultural and religious) on entry mode. The purpose of this study is to investigate the impact of animosity (war, economic, cultural and religious) of the host country on entry modes. A conceptual model is presented to provide a theoretical explanation for the impact of animosity on entry mode.

A man told his grandson: "*A terrible fight is going on inside me -- a fight between two wolves. One is evil, and represents hate, anger, arrogance, intolerance, and superiority. The other is good, and represents joy, peace, love, tolerance, understanding, humility, kindness, empathy, generosity, and compassion. This same fight is going on inside you, inside every other person too.*" The grandson then asked: "*Which wolf will win?*" The old man replied simply: "*The one you feed.*" Anon.

The fundamental source of conflict in this new world will not be primarily ideological or primarily economic. The great divisions among humankind and the dominating source of conflict will be cultural. Nation states will remain the most powerful actors in world affairs, but the principal conflicts of global politics will occur between nations and groups of different civilizations. The clash of civilizations will dominate global politics. The fault lines between civilizations will be the battle lines of the future. (Huntington 1993, p. 22)

The Marketing Management Journal
Volume 15, Issue 2, Pages 18 - 28

INTRODUCTION

One of the most important strategic decisions managers of multinational corporations have to make is the selection of entry mode into a foreign market. How firms enter foreign markets has been a topic of interest for many researchers in international business and marketing (Agarwal and Ramaswami 1992; Caves and Mehra 1986; Gatignon and Anderson 1988; Stopford and Wells 1972). The growing globalization of markets during the past two decades has become one of the most crucial issues in business today, representing numerous challenges and opportunities for domestic and international markets (Klein, Ettenson and Morris 1998; Darling and Arnold 1988). As national boundaries continue to disappear, more businesses seek opportunities abroad (Klein et al. 1998). Ettenson and Gaeth (1991) suggest that to compete successfully in this global market, managers need to have a thorough understanding of what consumers in different countries and cultures prefer. Although the knowledge of what consumers prefer in terms of foreign products and services is an important one, we argue that understanding the level of animosity (war, economic, cultural and religious) of the intended host country is as important and could lead to the success or failure of multinational corporations.

Entry Mode Selection

The firm's international experience and product diversification play an important role in entry mode selection (Stopford and Wells 1972). Woodcock, Beamish and Makino (1994) argue that cultural and other national differences between the host and home countries appear to influence entry mode selection. Caves and Mehra (1986) found entry mode selection to be influenced by several industry and firm-specific factors such firm size, advertising intensity, research intensity, industry growth and industry concentration. All types of entry modes are contingently influenced by locational, ownership and internationalization advantages (Kim and Hwang 1992; Agarwal and Ramaswami 1992).

Animosity and Entry Mode

An extensive survey of the literature indicates that one of the main areas neglected in strategy research is the impact of animosity (war, economic, cultural and religious) on entry modes. As the opening quote indicates, the clash of civilizations will only increase because differences among civilizations are not only real, they are basic. Huntington (1993) argues that differences in history, language, culture, tradition and, most importantly, religion will be the driving forces for conflict and history is full of examples of wars that have been fought based on religious and cultural differences. If religious and cultural differences can lead to armed conflict and atrocities, it is plausible that religious and/or cultural animosity toward a nation or culture might also affect how entry of foreign businesses is viewed and evaluated.

The purpose of this study is to investigate the impact of animosity (war, economic, cultural and religious) of the host country on entry modes. The following section discusses the impact of national culture on strategy, followed by a discussion of the four types of animosities and their proposed impact on entry modes. Finally, the advantages and disadvantages of different entry modes in the context of war, economic, cultural and religious animosity is presented and a theoretical model is proposed.

THE IMPACT OF NATIONAL CULTURE ON STRATEGY

Hofstede (1983) points out the role that cultural differences play by stating:

> The national and regional differences are not disappearing; they are here to stay. In fact, these differences may become one of the most crucial problems for management-in particular for the management of multinational, multi cultural organizations, whether public or private (p. 75).

The impact of national culture of the host and the home country has been investigated by a number of researchers (Hennart and Larimo 1998; Erramilli 1996; Barkema and Bell 1996; Shane 1994; Kogut and Singh 1988). Hennart and Larimo (1998) stated that there are two ways through which culture can influence ownership policies: 1) the country's national cultural characteristics, such as its power distance and uncertainty avoidance can affect the preference of multinational corporation strategy or entry mode and 2) the cultural distance between the home base of the multinational and the target market can influence MNC's entry mode. Hennart and Larimo (1998) found that the lower the power distance and the uncertainty avoidance indices of the home base of the investing firm, the greater the likelihood that it will enter the United States with shared-equity ventures. They also found that the greater the cultural distance between the home base of the investors and the United States, the more likely that they will enter the United States through shared-equity ventures.

Erramilli's research (1996) revealed that the greater the power distance characterizing the firm's home country culture, the greater the likelihood that the firm will seek majority ownership in foreign subsidiaries and the greater the uncertainty avoidance characterizing the firm's home country culture, the greater the likelihood that the firm will seek majority ownership in foreign subsidiaries. Kogut and Singh (1988b) found greater cultural distance between the home country and the host country to increase the probability that greenfield joint ventures would be preferred to wholly owned greenfields and to controlling acquisitions. Additionally the greater the level of uncertainty avoidance in the home country of the investor, the greater the preference for partly or wholly owned greenfield investments over acquisitions (Kogut and Singh 1988b). The longevity of foreign ventures was found by Barkema, et al. (1996) to be negatively related to the cultural distance between the home and host country. More recent studies like Arora and Fosfuri (2000) found that cultural distance reduces the propensity of a firm to set up a wholly owned subsidiary rather than using licensing to exploit technological competencies in a foreign country.

Although these studies provided a wealth of information regarding certain elements of culture and its impact on foreign entry modes, none of them address the issue of cultural and religious differences that may lead to the civilization clash described by Huntington (1993). This paper attempts to fill this gap by providing a theoretical argument regarding the impact of war, economic, cultural and religious animosity on entry modes.

War, Economic, Cultural and Religious Animosity

Klein et al. (1998) conducted a study in China to investigate the impact of animosity on intention to purchase foreign goods. Klein's model, which developed scales to measure war and economic animosity (defined as remnants of antipathy related to previous or ongoing military, political or economic events), demonstrated the negative impact of these constructs on Chinese purchase intentions related to products from the source of this animosity, Japan. From that study Klein et al. proposed the construct of animosity between nations and concluded that consumers who harbor war or economic animosity toward a specific country are likely to choose not to purchase products manufactured in that hated country. They also found that consumers who are unwilling to buy products from the hated country may find it perfectly acceptable to buy products from friendly countries and showed how the animosity construct is different from the ethnocentrism construct. Kalliny and Hausman (2004) extended the Klein et al. animosity model by adding cultural and religious animosity constructs. Religious animosity is defined as one's intolerance of and antipathy toward another person, country or nation because of religious differences while cultural animosity is defined as one's intolerance of and antipathy toward another person, country or nation because of cultural differences. Kalliny and Hausman (2004) found that cultural and religious animosity impact consumers purchase decision in regard to foreign products. Those who harbor cultural or religious animosity toward a country are more likely not to purchase products from that hated country. Nijssen and Douglas (1999) tested the animosity model in The Netherlands and found support for the theory. They also found that those who are more willing to travel to foreign countries to have a more positive attitude toward foreign products. Shin (2001) tested the animosity model in Korea and found support for it as well.

Country Risk

Root (1987) identified four types of risks that play a significant role in MNC's entry decision. These risks include political risk (instability of political system as in some African countries), ownership/control risks (expropriation), operations risk (local content requirement), and transfer risk (remittance control). These risks usually play a significant role in determining the amount of resources that MNCs commit in a foreign market. For example, when these risks increase, MNCs may choose to commit the smallest amount of resources to increase their ability to exit quickly when needed. This argument may suggest that licensing or exporting may be the most desirable entry. Companies usually choose the entry mode based on risk/return or cost/control trade off effects (Goodnow 1985; Root 1987). The level of risk can be moderated by the type of control attained (Kwon and Konopa 1992) and although several authors suggested that these risks can be substantially reduced by limiting ownership in a foreign venture (Brandley 1977; Korbin 1983; Vernon 1983), the situation gets more complicated when we talk about war, economic, cultural and religious animosity. These animosities complicate the issue because if consumers who harbor any of these animosities are not willing to purchase products made in the hated country, then the multinational firm may be forced to consider other options to overcome the animosity problem. Kwon and Konopa (1992) provided the following comparison between exporting and foreign production in regard to risk:

1. Foreign production requires relatively more resource commitment (initial investment, operating costs) than exporting,
2. Foreign production entails relatively greater risk exposure than exporting,
3. Foreign production provides relatively greater control of market than exporting, and
4. Foreign production provides an expectation of a relatively higher rate of return than exporting.

International Entry Modes and Propositions

Tse, Pan and Au (1997) argue that most past studies on foreign entry mode strategies of MNCs have adopted one of two theoretical approaches, the transaction cost approach or eclectic framework approach proposed by Dunning (1980, 1988). The transaction cost approach is based on the economic rationale that firms will minimize all costs associated with the entire value-added chain. This approach stresses the importance of firm-specific variables (Agarwal and Ramaswami 1992; Erramilli and Rao 1993; Gatignon and Anderson 1988; Kogut and Singh 1988). Dunning's (1980) eclectic framework integrates several strands of international business theories on cross-border business activities. Dunning (1980) argues that international business activities are influenced by three types of factors: host country-specific factors, ownership-specific factors, and internalization factors. The host country-specific factors deal with country risks and location familiarity (Hill, Hwang and Kim 1990), while ownership-specific and internalization factors focus on the industry-specific and firm-specific variables.

Of interest in this paper are the four primary international entry modes of joint venture, wholly owned subsidiaries, exporting and licensing. Researchers investigated the choice of entry modes of multinational corporations in regard to control and resource commitment. Several authors suggested that each of these entry modes is consistent with a different level of control (Calvet1984; Caves 1982; Davidson 1982; and Root 1987). Control is defined as the authority that the investing corporation has over operation and strategic decision making. Resource commitment is defined as dedicated assets that cannot be redeployed to alternative uses without loss of value. Hill, Hwang and Kim (1990) argue that while wholly owned subsidiaries can be characterized by a relatively high level of control and resource commitments, the opposite can be said of licensing agreements. With respect to joint ventures, the levels of control and resource commitments vary with the nature of the ownership split.

Alliances

For purposes of this paper, joint ventures and strategic alliances are treated equally. The formation of alliances is a crucial one because a firm can enter a foreign market by itself or by forming an alliance with another firm to reduce investment risks and enhance its competitive advantage. Kogut (1988, p. 319) defines joint venture as, "a joint venture occurs when two or more firms pool a portion of their resources within a common legal organization." Tse et al. (1997) argue that firms are motivated to form alliances with other firms to reduce investment risks, share technology, improve efficiency, enhance global mobility, and strengthen global competitiveness. According to Pan and Tse (1996) foreign firms form an alliance with another foreign firm for several reasons that include risk sharing, resource pooling, asset protecting, and the ability to react quickly to market changes. Investing firms can form alliances with firms from their own country or with foreign countries. Kwon and Konopa (1992) stated that foreign market involvement is inherently risky because of cultural differences, political instability and changes in the value of exchange rates. Moreover, they argued that firms are likely to enter foreign markets initially by a low resource commitment entry mode to minimize the risk of foreign market involvement. This paper focuses on the alliance formed between two firms from different countries. Auster (1987) argues that such international alliance is needed if the investing firm needs a partner with complementary expertise or resources.

Literature indicates that when country risk is high, MNCs would do well to limit exposure to such risk by restricting resource commitments in that particular national domain (Kobrin 1983; Bradley 1977). Here is where the concept of war, economic, religious and cultural animosity would play a role. Anecdotal evidence suggests that throughout history, economic, cultural and religious differences and animosities have played a critical role in many aspects of life including whether countries trade with each other or go to war. The impact of these animosities on consumers' purchasing intentions is well documented. It seems plausible to suspect that these animosities play a role in consumers' willingness to buy foreign products. As a result, we also suspect that foreign firms may take these animosities into consideration while devising their foreign entry. For example, a firm based in the United States may choose to form an alliance with another firm in the Middle East for two reasons: 1) to avoid the impact of animosities mentioned above by consumers toward products made in the United States by having the product made in the Middle East, or 2) to decrease the risk of loosing resources due to any military conflict that might start due to these animosities. This also has to do with resource commitments constituting an exit barrier and serve to limit the strategic flexibility of the firm (Harrigan 1981). When resource commitments are high, MNCs would not be able to exit from foreign markets without incurring substantial sunk costs. History is full of examples of businesses that lost investments in foreign countries due to conflicts. Take for example the current situation in Iraq which clearly indicates that foreign firms are being targeted due to war, cultural and religious animosities between the United States and the Muslim population of Iraq.

This is crucial given that several authors found that U.S. multinational firms have a predominant preference for wholly owned subsidiaries (Erramilli 1996; Stopford and Wells 1972). Bradley (1977) found that joint ventures with local partners experienced a relatively low rate of expropriation when compared to wholly owned subsidiaries. Our argument is based on two rationales: 1) if consumers realize that the product is made in their own country, they may be less likely to associate that product with the hated country and 2) if a political unrest or a conflict between the host country and the home country take place, the local partners in the joint venture may be able to save the business. Thus we propose:

> *Proposition 1:* Other things being equal, in countries where war, economic, religious and cultural animosity is high, country risk will be high and foreign companies will prefer to commit the least amount of resources and therefore exporting or joint venture would be the preferred mode of entry.

Subsidiary

There is no doubt that globalization has increased competition and moved it from the domestic level to the global level. Due to this new level of competition, MNCs have found it necessary to look for the least expensive resources of production to stay competitive. This has forced some MNCs to look for cheaper resources outside the home country. To take full advantage of cheap labor and raw materials, MNCs may choose to set a subsidiary in a desired host country. Birkinshaw (1997) defines subsidiary as any operational unit controlled by the MNC and situated outside the home country. The subsidiary ownership decision could be a very complex function of several factors including country characteristics, industry characteristics, product characteristics and firm characteristics (Erramilli 1996). The initiative for setting up a subsidiary lies in the identification of an opportunity to use or expand the MNC's resources (Birkinshaw 1997). The theory of internationalization argues that firms expand globally to realize the value of intangible assets (Buckley and Casson 1976). Subsidiaries often have unique capabilities and critical links with local customers and suppliers and in such situations the ability of the subsidiary to pursue local opportunities and subsequently to exploit them on a global scale is an important capability (Bartlett and Ghoshal 1986; Harrigan 1983; Hedlund 1986).

On the other hand, problems encountered by the new subsidiary can affect the entire corporation (Newbould, Buckley and Thurwell 1978). U.S. multinationals were found to have a predominant preference for wholly owned subsidiaries (Stopford and Wells 1972). Weinstein (1974) found that 62 percent of the subsidiaries were either fully- or majority-owned. Gatignon and Anderson (1988) observed that American multinationals had an intrinsic tendency to prefer wholly owned subsidiaries. Although American companies prefer subsidiaries, setting up a subsidiary is more risky than other forms of entry (Yip 1982). For example, when setting up a subsidiary, the entire cost is absorbed by the MNC. In addition, the subsidiary may lack information necessary for success in a particular environment or culture. History is full of examples where companies lost their business to expropriation, confiscation or destruction especially during time of conflict. Consider what happened to the Jews' businesses in Egypt when the national government was established in 1952. Many American companies lost their investment when communist regimes were established in countries like Cuba and others. We argue that during times of conflict, the hated country will be more likely to be targeted by citizens and governments.

Wild, Wild and Han (2003) argued that the events of September 11, 2001 have literally changed the world. They base their argument on a study that was conducted in the United States and nine Muslim countries where it was found that the majority of U.S. citizens feel that the Muslim world does not respect the American culture and vice versa. There is a sense of animosity and we think that this sense of animosity will play a role in the foreign entry mode selection. It is plausible to think that companies will take into consideration the level of animosity in the host country and devise their entry strategy accordingly. Based on this argument we propose:

> *Proposition 2:* Other things being equal, in countries where war, economic, religious and cultural animosity is low, country risk will be low and multinational companies will be more likely to prefer committing a high amount of resources and therefore a subsidiary mode of entry would be preferred.

Exporting

Exporting is the marketing and direct sale of domestically produced goods in another country. There are several reasons as to why companies may choose to export. For example, exporting does not require that goods be produced in the target country so no investment in foreign production facilities is required. Exporting allows companies to increase their samples by targeting and selling in foreign markets. Moreover, exporting helps companies diversify their markets, reduce their vulnerability to lags in domestic demand, extending product life cycles, using idle capacity, and reducing unit costs through economies of scale. Exports also help sharpen competitiveness, broaden contacts, and enhance understanding of global markets and cultures. In addition, the nation benefits from exporting because increased exports create jobs, spur economic growth, bring in tax revenues, and improve the balance of payments (Food Export USA).

Although exporting has many advantages and may seem very appealing to companies especially those that are faced with a saturated home market, exporting has several disadvantages. One of the main issues exporting companies face is the decision of adaptation versus standardization. When companies are faced with a situation that calls for adaptation, this may increase the cost of the product. Exporting companies may have to develop new promotional materials which may add to the cost of the product and companies that are engaged in exporting may incur added administrative costs. Moreover companies may have to wait longer for payments and finally, exporting companies may have to obtain special export licenses (Food Export USA 2004).

As can be seen from the above points, exporting can be a complicated process and may not be easy. The situation gets even more complicated when cultural and religious animosities are added to the equation. As discussed above these animosities do impact consumer preference and purchasing intentions. Kwon and Konopa (1992) argue that the foreign entry mode choice depends not only on the characteristics of the firm but also on the characteristics of the foreign market. Goodnow (1985) and Root (1987) viewed the characteristics of the firm and the product as internal factors and the characteristics of the foreign market as external factors. We argue that the level of cultural and religious animosities would fall under the external factors because they are part of the foreign market characteristics. Moreover, we argue that these animosities will play a role in the decision of the exporting country as to where to export and what to export to which country. For example, Saudi Arabia and Kuwait banned Barbie toys from their markets calling them a threat to morality and complaining that the revealing clothes of the "Jewish" toy are offensive to Islam (CBS News 2003; Gulf Marketing Review 1996). The banning of the Barbie toy reveals the cultural and religious animosity between the West and the Arab countries and shows their impact on purchasing intentions. Our rationale is based on the reasoning that companies engaged in producing products that may be viewed negatively by the foreign consumer should find a local element to help in decreasing the negative aspects that is caused by animosity. Thus we propose:

Proposition 3: Other things being equal, the level of cultural and religious animosity will play a role in determining how the foreign product is perceived by foreign customers.

Proposition 4: Other things being equal, in countries where war, economic, religious and cultural animosities are high, exporting will not be the preferred entry mode.

Licensing

Licensing is the process by which the right to use intangible intellectual property is granted by one party (licensor) to another (the licensee). Licensing permits a company in the target country to use the property of the licensor and such property usually is intangible (e.g., copyrights, patents, trademarks, and so forth). The licensee pays a fee in exchange for the rights to use the intangible property and possibly for technical assistance needed. There are a number of advantages for using licensing for the licensor and the licensee. Licensing allows many businesses to enter international markets through creative use of intellectual property rights in partnership with other companies. The low level of risk taken by the licensor for licensing requires little investment on the part of the licensor. Licensing allows companies to maximize income by expanding market opportunities without large capital expenses. A benefit to the licensee may include rapid entry into a market using technology developed and tested by others (Food Export USA 2004).

Although licensing may have a number of advantages, it also poses certain risks to the licensor. When an MNC grants a license to a foreign enterprise to use firm specific know-how to manufacture a product or market a product, it runs the risk of that licensee disseminating that know-how, or using it for purposes other than those originally intended (Hill and Kim 1988). Although the risk of dissemination of know-how is not limited to licensing, the risk is significantly higher in licensing. The licensor's profit opportunity may be limited by the license fee and royalty structure, and revenue from the licensing arrangement will be dependent on the licensee's performance. Additionally, the licensor may face excessive costs in providing support to the licensee, including cost of training, technical assistance and supervision depending on the license agreement. Finally, inadequate product quality and legal protection may expose the licensor to product liability risks.

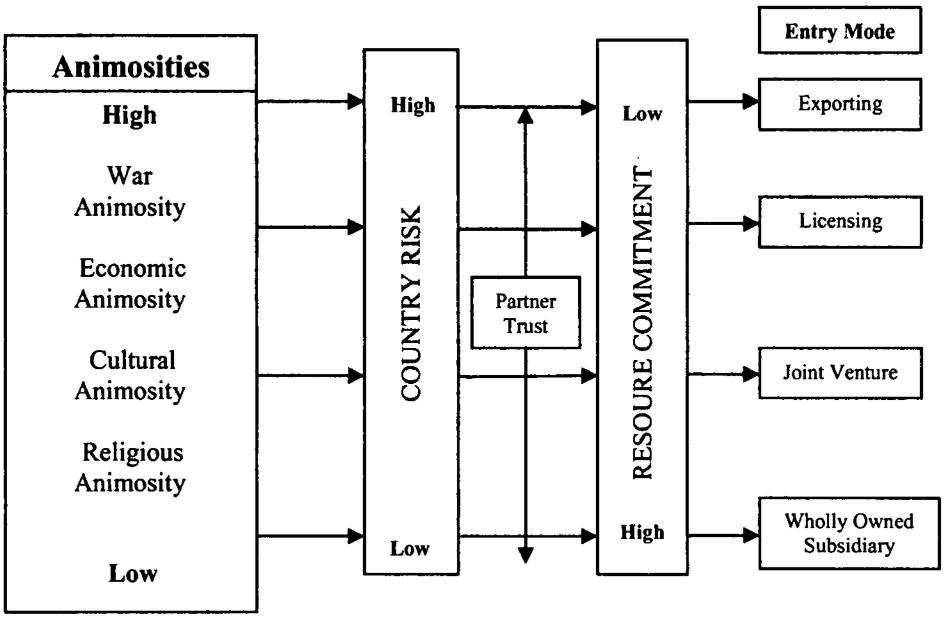
We believe the animosities discussed above will play a role in determining whether MNCs choose to grant licenses and to which countries licenses will be granted. We also argue that this relationship will be moderated by the level of trust between the licensor and the licensee. For example, if the level of animosity is high between two countries, a licensor may be less willing to grant a license to companies in that particular country for fear of loss of control. If, however, the level of trust between the licensor and the licensee is strong, the licensor may still grant a license. Trust and commitment of the business partners are two vital elements needed for the cohesiveness and stability of any business (Park and Hwang 2002). Thus we propose:

> *Proposition 5:* Other things being equal, licensing may be a preferred entry mode in countries that war, economic, cultural and religious animosities are high provided that the level of trust between the licensor and the licensee is high.

> *Proposition 6:* Other things being equal, the impact of war, economic, cultural and religious animosities' impact on licensing and joint venture choice is moderated by partner trust.

The following model represents the proposed relationships based on the preceding arguments:

FIGURE 1
Relationships of Animosities to Market Emmy Mode



In the model we propose that the animosities represented by war, economic, cultural and religious will determine the level of country risk. We also propose that the country risk level will determine the amount of resources that the firm will be willing to commit. Moreover, we propose that the amount of resource commitment that the firm chooses will play a role in determining the entry mode preference. For example, if war, economic, cultural or religious animosity is high, but the firm does not perceive the country risk to be high, the firm's entry mode choice may not be impacted by these animosities. It is expected that the relationship between animosities and licensing and joint venture will be moderated by the level of trust between the investing firm and the joint venture partner or licensee. For example, the level of animosity could be high between two countries, but the level of trust between two firms could be so high that the investing firm may still be able to go into that hostile country with a partner from that hostile country. Finally, we propose that the impact of the moderator, country risk, will also be moderated by the level of trust. For example, if the level of animosity is high and the level of trust is also high, the investing firm may perceive the country risk to be low due to the level of trust that is or could be established with partners or licensees. The level of war, economic, cultural and religious animosities will play a role in the level of resource commitment. For example, if the firm perceives the level of animosity to be high, the firm may be reluctant to commit as many resources to a particular location and that will play a role in determining the entry mode choice because entry mode choice is linked to resource commitment.

CONCLUSION

This paper presents a model of war, economic, cultural and religious animosities and their impact on foreign entry modes. The literature reveals that the relationship between war, economic, cultural and religious animosities and foreign entry modes has not received adequate attention in the business literature. Because these animosities were found to have an effect on purchasing intentions (Klein et al. 1998; Kalliny and Hausman 2003), it is expected that these animosities will also have an impact on entry mode choice. The purpose of this paper has been to provide a theoretical model that would fill this gap in the literature. The model includes proposed relationships between war, economic, cultural and religious animosities and entry modes. The discussion was focused on joint venture, wholly owned subsidiary, exporting and licensing, the primary modes of entry into foreign countries. The arguments are based on the level of risk and the trust and resource commitment MNCs are willing to take when considering entry to foreign markets.

The importance of this study lies in the fact that cultural and religious animosities are increasing as hypothesized by Huntington 1993. For example, Wild, Wild and Han's (2003) report of a survey following the terrorists attacks of September 11, 2001 found that most U.S. citizens believed Muslims did not respect Western values, while Muslims felt the same way about Americans. This indicates that the American consumers are likely to harbor both cultural and religious animosity toward the Arabs and Muslims. Based on our model, international firms interested in entering foreign markets should take into consideration the level of animosities between their home country and the country of interest. These animosities should play a critical role in assessing the country risk based on which level of resource commitment should be determined. International firms should also assess the level of trust between them and their foreign partners because that could play a critical role in the level of country risk.

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