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U.S. Business and Global Barriers to Entry

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U.S. Business and Global Barriers to Entry

Abstract

An exploratory view of barriers to entry in countries of significance to U.S. companies, this thesis provides a comprehensive overview of prevalent business strategies of U.S. trading partners as well as a forecast of their international business policies. Diverse macro-environmental variables, such as economy, culture, and regulations result in varying barriers to entry for U.S. based firms to conduct business in U.S trading partners' countries. This thesis will determine how these macro-environmental factors foster or stunt growth and strategies governments employ to attract businesses.

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U.S. Business and Global Barriers to Entry

Eastern Michigan University Honors College
Senior Thesis

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Introduction

An exploratory view of barriers to entry in countries of significance to U.S. companies, this thesis provides a comprehensive overview of prevalent business strategies of U.S. trading partners as well as a forecast of their international business policies. Diverse macro-environmental variables, such as economy, culture, and regulations result in varying barriers to entry for U.S. based firms to conduct business in U.S trading partners' countries. This thesis will determine how these macro-environmental factors foster or stunt growth and strategies governments employ to attract businesses.

An Overview of Barriers to Entry

As a business looking to invest in an international market, it is important to know where it wants to be and what will prevent it from being successful there. Throughout this thesis, general barriers to entry will be identified, three countries of interest to U.S. businesses will be looked at, and recommendations will be made as to the best strategies companies should employ to enter those markets.

First to define Barriers to entry: "Barriers are obstacles preventing entrant firms from being established in a particular market" (Pehrsson 64). Some common examples that can easily become barriers to entry are: tariffs, entry time, government policy, entry and exit costs, competition, infrastructure, etc... Depending on the targeted country, these factors become more or less relevant depending on the overall strategy of the firm.

Trade barriers will either be obvious or indirectly impactful based on some form of policy. For example, in an article from the *Economist Intelligence Unit*, it predicts that (due

to the current economic state) protectionism is on the rise and tariff increases seem to be the barrier of choice, but that there are several, “more subtle means of protection available”. Therefore, health and safety standards, licensing and certification requirements could be used to shield domestic industries as the global downturn continue. Furthermore, one national example of an indirect barrier is the government bailout of the Detroit automakers, which favors GM, Ford, and Chrysler over their competitors.

Exogenous or Endogenous Barriers

Barriers to Entry can then be classified in two ways: Exogenous or Endogenous. Exogenous barriers “are those that are embedded in underlying market conditions” that firms are not able to control (Pehrsson 66).

Examples of Exogenous barriers include: existing firms’ cost advantages, product differentiation, and brand image; entrant firms’ need for capital; customers’ switching costs; access to distribution channels; costs independent of economies of scale; government policy; number of competitors; seller concentration; and the need for research and development (including costs for adapting technology to the local market conditions and acquiring patents).

In contrast, Endogenous barriers “are created by the established firms through their market strategies and their competitive behavior and are thus based in incumbents’ reactions to new entrants’ efforts to become established (66).

Examples of Endogenous barriers include: Existing firms’ increased advertising or sales promotion, price competition, and their reactions in general to the entrant firms. For

example, an existing firm could deter new entry into its market by creating expectations of fear for its competitive reaction any entrant firms.

Therefore, companies looking to invest in a new market need to be aware of both internal and external barriers, and work to create an entry strategy that will result in success.

Entry Strategy

The timing of when a firm enters a market also affects the impact of barriers. There are usually early or late entrants in any given market. While late entry may result in less risk, early entry may result in a competitive advantage due to being the first company in a market to offer a certain product or service. The following research discusses the implications of being the early entrant in a market segment:

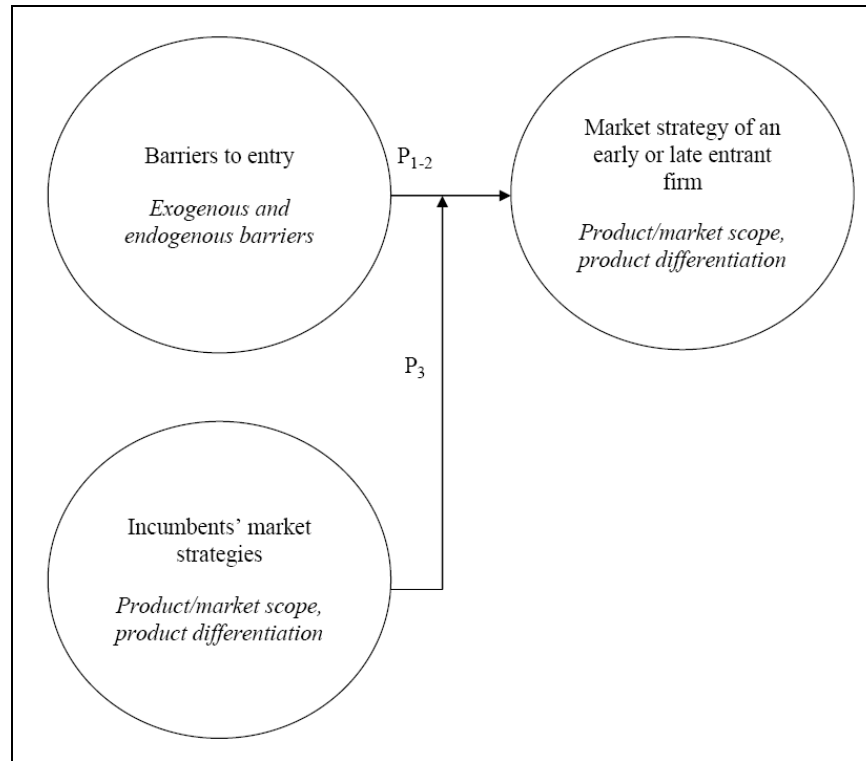
Entry timing advantages of first- and early-movers seem to be resistant to erosion by the entry of additional competitors in a market. Once a new competitor has entered the market, it is difficult to match the performance of the incumbents, due to extensive customer loyalties established previously. (Pehrsson 69)

For the late-entry firm, this results in a significant obstacle in terms of customer access. Once a firm has established a loyal customer base, it becomes increasingly difficult for a competitor to tap into that group of consumers. The author compiled a collection of research in order to demonstrate strategy for various entry barriers. The following table summarizes the findings:

| Studies | Barriers | Strategy component | Key findings |
|---|--|-------------------------|--|
| <i>Studies of entrant firms</i> | | | |
| Robinson and McDougall (2001) | Incumbents' cost advantages (scale effects), capital need, and product differentiation | Product/market scope | Larger negative performance effect when the scope of an entrant firm is narrow |
| Pehrsson (2001) | Government policy | Product/market scope | Deregulations cause adjustments in the product/market scope of an entrant firm |
| Han <i>et al.</i> (2001), Salavou <i>et al.</i> (2004) | Capital need | Product differentiation | Capital need stimulates innovativeness of an entrant firm |
| <i>Studies of incumbents</i> | | | |
| Pehrsson (2007) | Product differentiation, switching costs, and channel access | Product/market scope | Negative performance effects when the scope of an incumbent is narrow |
| Bonardi (1999), Delmas and Tokat (2005), Haveman (1993) | Government policy | Product/market scope | Deregulation causes adjustments in the product/market scope of an incumbent |
| Delmas <i>et al.</i> (2007), Russo (2001), Schlegelmilch and Ambos (2004) | Government policy | Product differentiation | Deregulation causes technology and other differentiations of an incumbent |

The table compares strategies to overcome barriers to entry with key findings from them. The strategy components are either the product or market scope, or product differentiation. The barriers evaluated are incumbents' cost advantages and capital need, government policy, product differentiation, switching costs, and channel access (Pehrsson 69). Some key findings were that there is a negative performance result from a firm employing a narrow product scope when faced with the barrier of incumbents' cost advantages, and deregulation causes incumbent firms in a market to adjust to increased competition (69).

The following diagram demonstrates the correlation between entry timing and firm strategy relative to barriers (Pehrsson 70). Firms that enter a market late and face significant barriers should select a broader market or product scope than their existing competitors. These firms should also focus on differentiating their products more than the competition. These decisions will be indirectly impacted by existing firms' market strategies, which create barriers to entry.



Therefore, it is better for a company to be the early entrant in a market. However, when this is not possible, it is recommended for a company to invest in a wider product selection to minimize risk and create higher product differentiation in order to attract customers.

Mode of Entry

The mode of entry is an elemental decision a company makes when entering a new market. This decision effects marketing and production strategy, and may be made based on the existing barriers to entry. Johnson and Tellis identify five main ways to enter a market:

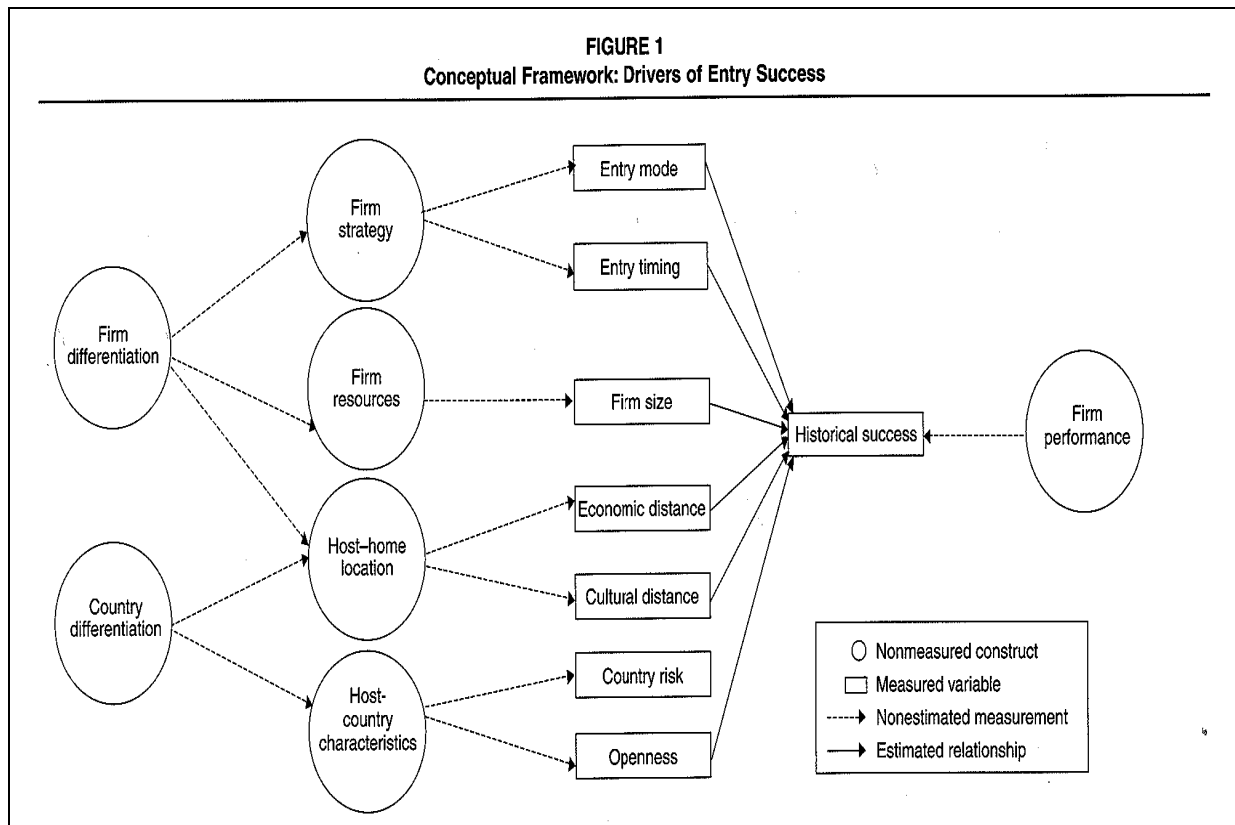
1. Export: a firm's sales of goods/services produced in the home market and sold in the host country through an entity in the host country.

2. Licensing and franchise: a formal permission or right offered to a firm or agent located in a host country to use a home firm's proprietary technology or other knowledge resources in return for payment.
3. Alliance: agreement and collaboration between a firm in the home market and a firm located in a host country to share activities in the host country.
4. Joint venture: shared ownership of an entity located in a host country by two partners, one located in the home country and the other located in the host country.
5. Wholly owned subsidiary: complete ownership of an entity located in a host country by a firm located in the home country to manufacture or perform value addition or sell goods/services in the host country. (2)

By evaluating several factors of countries attractive to U.S. business, recommendations can then be made, based on these modes of entry, as to which is the best mode for each economy.

Drivers of Entry Success

In addition to entry strategy and mode of entry, there are other measures that can be evaluated to determine the potential success of a business venture in another culture. The measures include: firm size, economic distance, cultural distance, country risk, and country openness. The following diagram from *Drivers of Success for Market Entry into China and India* summarizes the flow of variables (Johnson and Tellis 3).



Firm Size

Firm size simply evaluates the rate of success based on the size of the firm. Traditionally, "...larger U.S. firms have been more able to participate in global markets than smaller firms because of their financial and managerial resources" (Johnson and Tellis 4). However, large size is not a guarantee for success; one notable detriment to large firm size is a lack of flexibility due to bureaucracy, which impedes innovation (4).

Economic Distance

Economic distance is an important factor to consider, especially when dealing with developing or transition economies. The term is a measure of the differences between the

economies of two countries. The lower the economic distance between two trading partners, the more advantageous the business relationship will presumably be. Similar market segments typically sell like goods and services, as well as feature comparable infrastructure, which could result in lower operating costs. Firms also, “develop competencies or knowledge-based resources that are related to the markets they serve,” which means that these home skills can be best leveraged in a country with a similar economy (Madhok 48). Conversely, firm with a great economic disparity would have a lesser chance of success, due to the fact that they would need to adjust to new market conditions.

Cultural Distance

Cultural is commonly defined as shared values and meanings of the members of a society. Cultural distance, then, measures the “underlying cultural dimensions of a society affect its consumption pattern beyond what economic laws predict” and affects “not only the underlying behavior of customers in a market but also the execution and implementation of marketing and management strategies” (Johnson and Tellis 4). A practical example would be how easily partners in a joint venture or an alliance would be able to overcome their cultural differences. Firms that cannot adapt to each other will not succeed, regardless of the foreseen advantages to a partnership. A familiar example of failure based on cultural barriers is the dissolution of the much touted “merger of equals” between Daimler AG and Chrysler LLC.

Country Risk

Country risk is defined as uncertainty about the environment and is comprised of three factors: political, financial, and economic (Johnson and Tellis 5). Financial and

economic risks can cause a barrier through recessions or market downturns, currency fluctuation, and inflation (5). Political risk assessment is,

An attempt to forecast political instability to help management identify and evaluate political events and their potential influence on current and future international business decisions. Perhaps the greatest risk to international marketers is the threat of the government actually failing, causing chaos in the streets and markets...Risk assessment is used to determine the level of risk a company is assuming when making an investment and to help determine the amount of risk it is prepared to accept. (Cateora and Graham 174)

For example the political risk in the former Soviet Union or China might dissuade a company from investing there; however, firms with larger resources might choose to invest in order to reap long-term gains. Political, financial, and economic risk combined result in country risk, which can result in sudden losses for a company or slower investment, which can hinder or block success.

Country Openness

Country openness is the “lack of regulatory and other obstacles to entry of foreign firms” and can either increase or decrease entry success (Johnson and Tellis 5). This is due to the fact that there are both advantages and disadvantages for a firm entering an open country. The following table compares the potential advantages and disadvantages to country openness (6).

| Advantages to Country Openness | Disadvantages to Country Openness |
|--|--|
| 1. Stimulates demand <ul style="list-style-type: none"> a. Increases variety of products in the marketplace | 1. Increases competition from other new foreign entrants <ul style="list-style-type: none"> a. Can lower prices significantly b. Keeps margins low, so only the most efficient survive |
| 2. Increases competition <ul style="list-style-type: none"> a. Improves the level of quality of the products being supplied | 2. Increases cost of purchases, the hiring of talent, and the marketing of products and services |
| 3. Competition increases efficiency and lowers prices <ul style="list-style-type: none"> a. Demand for products will increase | 3. Causes firms to lose leadership if they make strategic mistakes <ul style="list-style-type: none"> a. Target the wrong segment b. Price the product too high |

By evaluating the potential advantages and disadvantages of country openness, firms will be better prepared to develop an entry strategy that will result in success.

Hofstede Cultural Dimensions

In order to better understand the cultural differences between countries of interest to the U.S. and the U.S. country dimensions, it is important to understand the meaning of the Hofstede Cultural Dimensions. These measures can explain much about how people groups in a country will think and behave because they are directly related to culture. There are five factors measured in individual countries.

Power Distance Index (PDI) is defined as,

The extent to which the less powerful members of organizations and institutions (like the family) accept and expect that power is distributed unequally. This represents inequality (more versus less), but defined from below, not from above. It suggests that a society's level of inequality is endorsed by the followers as much as by the leaders. Power and inequality, of course, are extremely fundamental facts of any

society and anybody with some international experience will be aware that 'all societies are unequal, but some are more unequal than others'. (Hofstede)

Individualism (IDV) is rated versus collectivism, and is measured as,

The degree to which individuals are integrated into groups. On the individualist side we find societies in which the ties between individuals are loose: everyone is expected to look after him/herself and his/her immediate family. On the collectivist side, we find societies in which people from birth onwards are integrated into strong, cohesive in-groups, often extended families (with uncles, aunts and grandparents) which continue protecting them in exchange for unquestioning loyalty. The word 'collectivism' in this sense has no political meaning: it refers to the group, not to the state. Again, the issue addressed by this dimension is an extremely fundamental one, regarding all societies in the world. (Hofstede)

Masculinity (MAS) is measured versus femininity, and refers to,

The distribution of roles between the genders which is another fundamental issue for any society to which a range of solutions are found. The IBM studies revealed that (a) women's values differ less among societies than men's values; (b) men's values from one country to another contain a dimension from very assertive and competitive and maximally different from women's values on the one side, to modest and caring and similar to women's values on the other. The assertive pole has been called 'masculine' and the modest, caring pole 'feminine'. The women in feminine countries have the same modest, caring values as the men; in the masculine countries they are somewhat assertive and competitive, but not as much as the men, so that these countries show a gap between men's values and women's values. (Hofstede)

Uncertainty Avoidance Index (UAI) is how a country,

Deals with a society's tolerance for uncertainty and ambiguity; it ultimately refers to man's search for Truth. It indicates to what extent a culture programs its members to feel either uncomfortable or comfortable in unstructured situations. Unstructured situations are novel, unknown, surprising, different from usual. Uncertainty avoiding cultures try to minimize the possibility of such situations by strict laws and rules, safety and security measures, and on the philosophical and religious level by a belief in absolute Truth; 'there can only be one Truth and we have it'. People in uncertainty avoiding countries are also more emotional, and motivated by inner nervous energy. The opposite type, uncertainty accepting cultures, are more tolerant of opinions different from what they are used to; they try to have as few rules as possible, and on the philosophical and religious level they are relativist and allow many currents to flow side by side. People within these cultures are more phlegmatic and contemplative, and not expected by their environment to express emotions. (Hofstede)

Long-term Orientation (LTO) is rated versus short-term orientation, and is the newest Hofstede measure.

This fifth dimension was found in a study among students in 23 countries around the world, using a questionnaire designed by Chinese scholars. It can be said to deal with Virtue regardless of Truth. Values associated with Long Term Orientation are thrift and perseverance; values associated with Short Term Orientation are respect for tradition, fulfilling social obligations, and protecting one's 'face'. Both the positively and the negatively rated values of this dimension are found in the teachings of

Confucius, the most influential Chinese philosopher who lived around 500 B.C.; however, the dimension also applies to countries without a Confucian heritage. (Hofstede)

These measures will be referenced in the country profiles to draw comparisons between the United States and countries of interest to U.S. business. They will also highlight potential barriers to entry based on cultural differences.

Country Profiles

While U.S. businesses have ties all around the world, this thesis will evaluate three specific countries of interest to the United States. Those three countries are China, India, and Hungary. They were selected based on their attractiveness to U.S. business, whether it is through economic incentives or the forecasts of their future business attractiveness. The following section of the paper will include country profiles, barriers to entry, and a recommended strategy for entry into those countries.

China

Some forecasts predict that “by 2050 China will be the leading economy of the world, followed by the United States and India” (Johnson and Tellis 1). The country features a unique combination of a communist government with more market-oriented economy. This fact, coupled with the available resources makes China a desirable location for investment. In 2005, China attracted about \$1 billion per week in foreign direct investment (Johnson and Tellis 1).

Although the rate of growth in China has slowed due to the current economy, the overall investment outlook is still positive. However, U.S. firms need to proceed in a different manner than they would when investing in the United States. There are significant cultural barriers, political risk due to the type of government, and perhaps most importantly, companies cannot simply open a new business in China whenever they like.

Market Overview

Along with the rest of the markets in the world, China has not escaped the recent economic downturn. The country's economy is heavily dependent on exports to developed markets, and the sharp drop in global consumer demand has had a significant effect on China's economy. According to the U.S. Commercial Service,

In 2007 China's economy grew by 13 percent and had maintained double-digit growth for most of the past decade. In 2008 Gross Domestic Product (GDP) growth dropped to 9 percent, perilously close to the 8 percent growth that many economists believe to be required to feed China's economic engine. Preliminary Chinese economic figures for the last quarter (Q4) of 2008 indicate that this decline is continuing and accelerating. (Doing Business in China 2)

Although the country is experiencing an economic decline, overall economic growth is continuing, however and U.S. companies are benefiting. U.S. exports to China have continued to increase, and in 2008,

U.S. exports to China increased by 9.5 percent from the year prior, according to the U.S. Census Bureau, helping to make China one of the fastest growing foreign markets for U.S. goods. China-U.S. total trade grew to USD 409.2 billion, placing

China as our second largest trading partner behind Canada. Although U.S. imports of Chinese goods greatly exceed U.S. exports to China, China remains our third largest export market. U.S. exports of goods to China totaled USD 71.5 billion for the year in 2008. (Doing Business in China 2)

In addition to these numbers, China's middle class population is growing at a rapid rate, and the country is already the third largest market for luxury goods behind Japan and the United States. However, it continues to face the severe threat of environmental pollution, as well as some political and legal instability (3).

Market Barriers

Entering the Chinese market can be complicated due to a lack of set regulations, the government's mercantilist policies, and the fact that there are still many aspects of the marketplace that are stunted in bureaucracy due to central planning. Also, an additional barrier to consider is the lax enforcement of intellectual property laws.

In terms of predictability, the Chinese government lacks a transparent set of laws, which would spell out regulations and policies for investors. As it is, "China's current legal and regulatory system can be...arbitrary. Implementation of the law is inconsistent. Lack of effective Chinese government protection of intellectual property rights is a particularly damaging issue for many American companies" (Doing Business in China 3). Relative to intellectual property rights, both those firms operating and not operating in China have had their property stolen by Chinese firms.

Furthermore, the government continues to protect local, notably nationalized firms, from imports through bureaucracy. It also implements a planned economy, with a five year

map for economic goals. This involvement from the State and Communist Party prevents a free market economy from fully being realized in all aspects of the marketplace. Another example is that the State and Communist Party run the only legal labor union in China, thus, permeating the arena of employee rights (3).

The lack of transparent laws impacts the area of intellectual property rights, as the Chinese government has thus far failed to introduce a successful system for protecting intellectual property. This problem is impactful because it doesn't merely hurt firms entering the Chinese market, but firms outside the market as well. Research from the International Intellectual Property Alliance estimated that

85% to 95% of copyrighted "hard goods," such as publications, compact discs (CDs), and digital video discs (DVDs), were pirated, with records and music at an 85% piracy rate, and business software at 82%. Many consumer-goods companies report that, on average, 20% of their products in the Chinese market are counterfeit...Compounding these problems are widespread squatting of others' trademarks, company names, domain names, and design patents, employee theft of trade secrets, and smuggled exports of infringing products. Chinese-origin infringing goods can be found throughout the world. (Doing Business in China 19-20)

Companies looking to enter the Chinese market must take all precautions to protect their intellectual property and be aware of the real threat of thievery and trademark squatting.

In order to overcome these problems, U.S. businesses must utilize thorough research, as well as take into consideration standards of quality and of potential business partners. The biggest pitfall for U.S. businesses is when they do not take precautions in entering China. Whether it is through ignoring regulations, failing to adequately research a prospective

business venture, ensure intellectual property rights, or create a satisfactory contract, these oversights can cost a company dearly, and result in an ultimate failure in the Chinese marketplace.

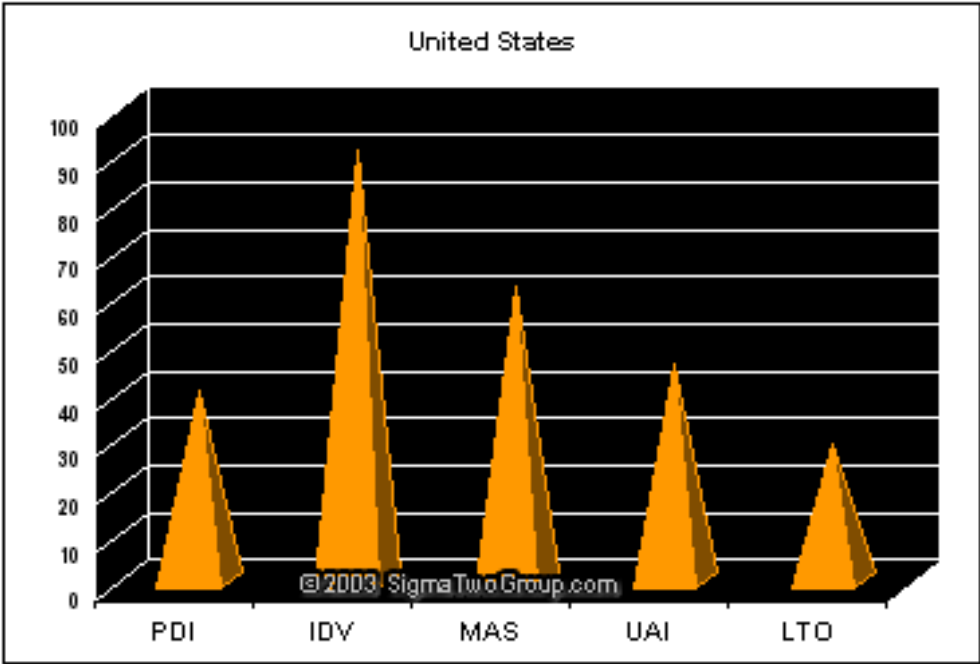
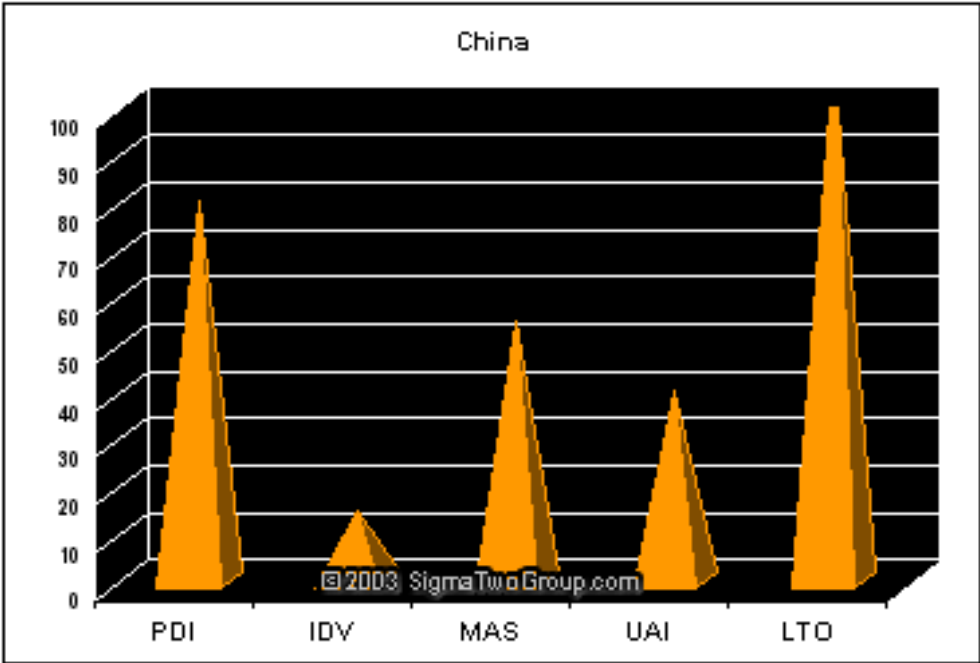
Cultural Barriers

Culture is, “The human-made part of human environment—the sum total of knowledge, beliefs, arts, morals, laws, customs, and any other capabilities and habits acquired by humans as members of society” (Cateora and Graham 676). When two differing culture sets interact with each other, it is imperative to have an understanding of the differences in order to better formulate a relationship strategy. If there is a lack of cultural sensitivity, businesses can fail to create the partnerships necessary to do business in any given country. To demonstrate how cultural factors play into barriers to entry in China, Hofstede’s cultural dimensions show that,

The Chinese rank lower than any other Asian country in the Individualism (IDV) ranking, at 20 compared to an average of 24. This may be attributed, in part, to the high level of emphasis on a Collectivist society by the Communist rule, as compared to one of Individualism. The low Individualism ranking is manifest in a close and committed member 'group', be that a family, extended family, or extended relationships. Loyalty in a collectivist culture is paramount. The society fosters strong relationships where everyone takes responsibility for fellow members of their group.

(Hofstede)

The following graph compares the Hofstede dimensions between China and the United States (Hofstede).



As the graphs demonstrate, there are significant differences between the United States and China, most significantly in terms of Long-Term Orientation, Individualism, and Power Distance Index. The following table compares the numbers of the Hofstede Dimensions to further demonstrate the disparity between the United States and China:

| Cultural Dimension | China | United States |
|-----------------------------|--------------|----------------------|
| Power Distance Index | 80 | 40 |
| Individualism | 20 | 91 |
| Masculinity | 60 | 62 |
| Uncertainty Avoidance Index | 35 | 46 |
| Long-Term Orientation | 118 | 29 |

The significance of the differences has to do with communication and perseverance. The United States is a highly individualistic culture that pays less heed to any social hierarchy, which could be problematic for relating to Chinese firms. There can be a lack of respect and structure, as well as miscommunication from attempting to force Americanized ideals on a Chinese firm. This is especially true when considering the long-standing business partnerships between Chinese firms and how they interact with each other.

Many business partnerships in China have been in existence for centuries and are built on interpersonal relationships lasting for generations.

“It is important to note that in China..., not only are domestic firms eager players of the networking game, but foreign entrants have also enthusiastically cultivated their web of interorganized networks and relationships as, as evidenced by the numerous international strategic alliances with local firms (Peng, Wang, and Jiang 928).

Based in this knowledge, companies looking to invest in China must cultivate the necessary connections to be successful players in the marketplace. If unsuccessful, this can be a barrier to entry.

Recommendation for Investment in China

While this information points to joint ventures as the obvious answer, data shows that wholly owned subsidiaries routinely outweigh joint-ventures. For example, in 2001, 60 percent of new foreign direct investment in China was from wholly owned subsidiaries and

only 34 percent was from joint-ventures. Moreover, in 2005, 74 percent were wholly owned subsidiaries, while 24 percent came from joint-ventures (Peng, Wang, and Jiang 928).

For firms with the cultural know-how and resources, wholly owned subsidiaries would be the recommended route to take, but for smaller firms, joint-ventures would still be able to provide an attractive avenue into China due to the host firm's resources and existing relationships with the government, businesses, and customers.

Whatever mode of entry a business employs to enter China, once the decision to go forward has been made, companies should first consider partnering with the U.S. Embassy and U.S. Department of Commerce in order to obtain up-to-date country information. Companies should also invest the time to visit China to better understand the culture, as well as setting up face-to-face meetings with potential partners, which conveys interest in commitment and a long-term business relationship. Developing a network of contacts is also beneficial, as is employing an agent with local knowledge and expertise to aid in the entry process (Doing Business in China 4).

India

With a GDP growth rate of 7.3 percent in 2008 and a government that has become more open toward foreign direct investment through deregulation and liberalization of the marketplace, India is a targeted emerging economy for U.S. business (CIA Factbook). The Indian economy is being advanced due, in large part, to the entrepreneurial and quickly globalizing private sector. These are the firms that are investing in,

Infrastructure projects, growing their advanced manufacturing capabilities, and inventing in new volume-based business models that tap into rising incomes and

consumption in towns and rural economies across the country. Whether it is consumer goods and services, high technology and industrial goods, healthcare, or infrastructure development, Indian firms are bullish about their economy and are eager for U.S. commercial and joint venture partnerships, technologies, brands, services, and know-how. (India Country Commercial Guide 2)

Market Overview

With the rate of trade between the United States and India continuing to grow, the country could become a top-ten for U.S. goods and services in the near future. Moreover, U.S. exports to India rose 75 percent to \$17.6 billion in 2007, while expanding only 12 percent worldwide. “Advanced technologies, including aerospace, specialized materials, information and communications technologies, electronics and flexible manufacturing systems underpinned this growth” (India Country Commercial Guide 2).

Forecasts estimate that in the next 15 to 20 years, 40 percent of the Indian population, or 400 million people, will rise to middle class status. Adding to this purchasing power is the fact that 71 percent of the population is under the age of 35, and the median age is 25 (2). The young population will ensure that India has a competitive advantage in production and knowledge-based skill sets for many years. Other reports forecast that India will, “have and sustain the fastest growth rate in the world by 2011” and, “will become the 3rd largest economy in the world in 2032” (2).

Market Barriers

However, there are still many barriers to entry that should be considered, such as the economic disparity between the U.S. and India. Although there is a growing middle class, the majority of the population lives in poverty and would not be able to afford many U.S. products as they are manufactured for sale here. The idea that U.S. products would not be compatible with an Indian lifestyle without alteration may mean additional costs. This could prove any type of entry to be ultimately unprofitable.

Another significant barrier is a lack of sufficient infrastructure, which can create bottlenecks, inefficiencies, and waste. “For example, more than 20 percent of the food items in India are wasted because of lack of proper storage, transport, and processing facilities” (Manian 287). Furthermore, the U.S. Commercial Service highlights the critical role infrastructure plays when entering into India,

Problems with the country's roads, railroads, ports, airports, education, power grid, and telecommunications may be the toughest obstacles for India's economy to grow to its full potential. Nonetheless, a process of liberalization in these areas has been underway, led by a more liberal environment in the information technology, airline, and telecom sectors, with increasing roles for the private sector in ports, roads and other key sectors. However, the absence of a clear policy framework has hindered critical private investment in infrastructure overall. (India Country Commercial Guide 3)

Perhaps one issue with the development of India's infrastructure is the methodology the country employs when building it versus that of other countries. To contrast India and China's approaches to infrastructure,

When China wants to attract investment in a particular region, they build infrastructure: roads, railways, airports...Then they woo investors. In India, things work the other way. The investors bring the funds, and the infrastructure grows as a result. (Manian 207)

The following media is an image of a proposed economic city in China, with the infrastructure pre-designed to draw business, rather than the other way around.



This method of creating infrastructure to preempt business investment ensures fewer barriers in terms of transportation and storage. The current method of building infrastructure in India as business comes is haphazard and can become tedious and expensive.

Another barrier to entry is the slow reform process instigated by the Indian government. Although the government has deregulated the market significantly,

Higher limits on foreign direct investment [are] permitted in a few key sectors, such as telecommunications...tariff spikes in sensitive categories, including agriculture, and incremental progress on economic reforms still hinder foreign access to India's

vast and growing market. Privatization of government-owned industries remains stalled and continues to generate political debate. (CIA Factbook)

While there has been some progress by various political parties since the nineties, tariff and non-tariff barriers are still relatively high compared to other countries. In addition, the counties codes and regulations remain complex and full of loopholes for investors.

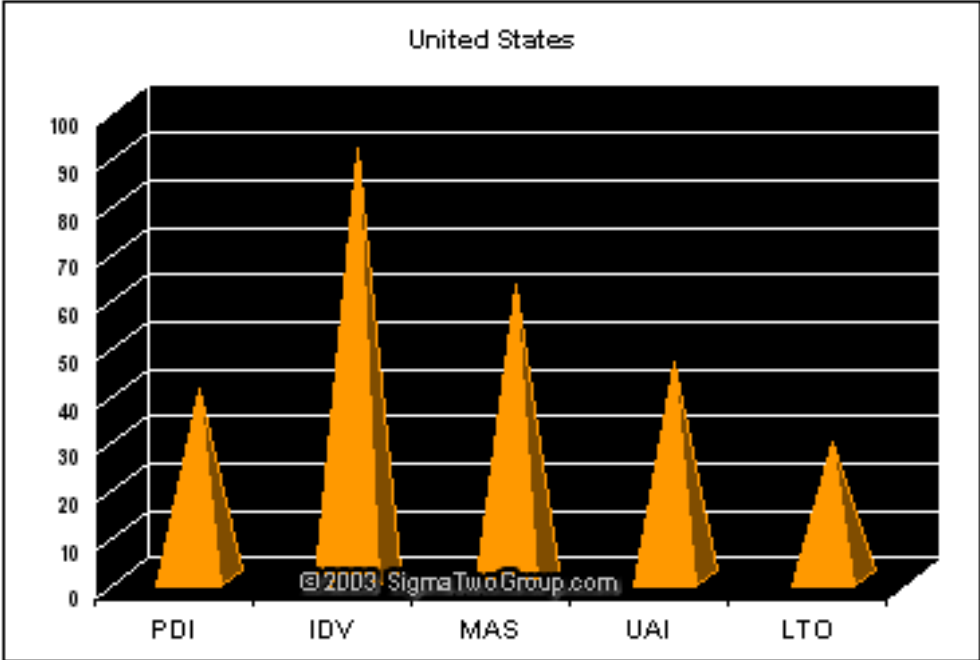
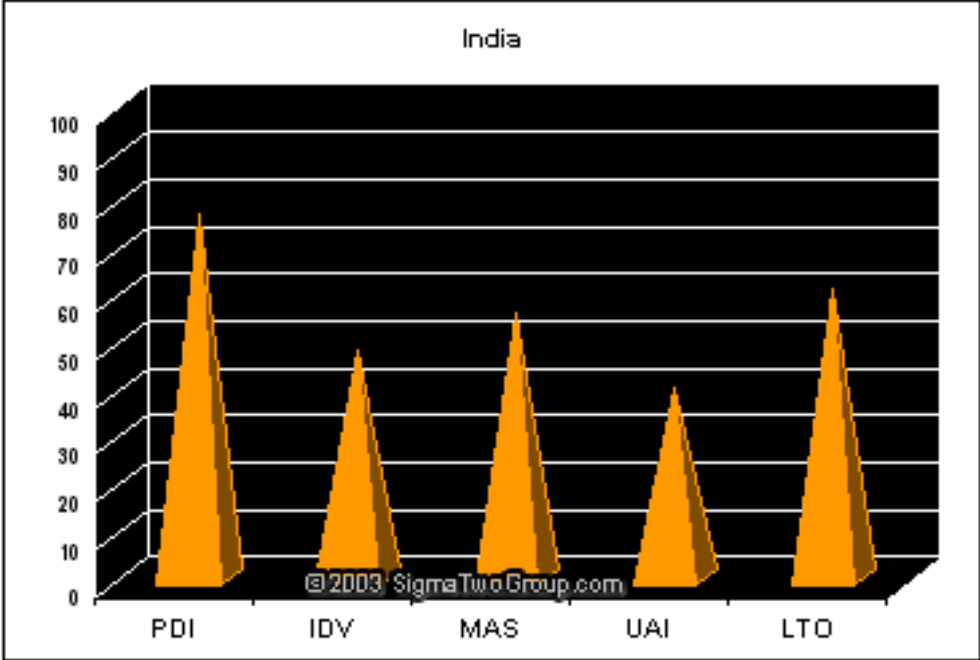
Cultural Barriers

To evaluate the cultural differences between India and the United States, it will again be advantageous to reference the Hofstede Cultural Dimensions. The measures between India and the United States are much more similar than those between the United States and China. The following table compares the numbers:

| Cultural Dimension | India | United States |
|-----------------------------|--------------|----------------------|
| Power Distance Index | 77 | 40 |
| Individualism | 50 | 91 |
| Masculinity | 56 | 62 |
| Uncertainty Avoidance Index | 40 | 46 |
| Long-Term Orientation | 61 | 29 |

Although the differences between India and the United States are not as large, the differences in cultural dimensions do need to be considered. India has a higher Power Distance Index than the United States, meaning a larger gap between levels of authority. This can be seen through the continued existence of the caste system in India. Also, Individualism is lower than in the United States, while Long-Term Orientation is higher. The positive factors are that both cultures are defined as Masculine and have similar Uncertainty Avoidance Index numbers. These comparable factors may aid in the communication and relationship-building process. However, companies must take care to respect the levels of authority and cultural

community, lest they offend potential business partners with a seemingly brash and offensive manner. The graphs for each country are featured below to visually compare the differences (Hofstede).



Recommendations for Investment in India

Although barriers to entry in India come in a cultural context, through corruption issues, political instability, labor strikes, infrastructure, and terrorism, the country remains an attractive location for doing business. There are several options for entry into the Indian market, including: a liaison/representative office; a branch office; a project office (for specific projects only); utilizing business process outsourcing; entering into a joint venture; and opening a wholly owned subsidiary (Manian 78-83). The “office” approach may prove to be restrictive in terms of the scope of what a business can actually accomplish in India. While opening a wholly owned subsidiary would give a company control over its operations, it may not be the best method in light of the different cultural, political, and economic scopes of India and the United States.

Therefore, in order for a firm to successfully mediate the nuances of the Indian market, it can be advantageous to enter into a joint venture with an Indian firm “because it uses a powerful synergy...Joint ventures have many benefits, which include warehousing, transportation, and built-in distribution” (Manian 81). Moreover, the U.S. Commercial Service recommends that U.S. business do their research by hiring agents or representatives before committing to any business venture,

New business must address issues of sales channels, distribution and marketing practices, pricing and labeling, and protection of intellectual property. Relationships and personal meetings with potential agents are extremely important. Due diligence is strongly recommended to ensure that partners are credible and reliable. (India Country Commercial Guide 3)

Furthermore, it would be strategically advantageous for U.S. firms to develop a regional impact by, "...focusing on multiple locations and markets within India and finding the appropriate partners and agents within each region" (India Country Commercial Guide 3); this is due to the many various culture sets within India. Obtaining localized information is the key to establishing reliable partnerships with native businesses.

Hungary

Hungary is a transition economy, an Eastern European market that has promise due to the country's recent democratization. A transition economy,

Consists of a number of major issues such as democratization, restructuring of the industry (away from heavy industries to industries producing consumer goods), privatization and the reorientation of trade flows...to more demanding (Western European) markets. The integration of these economies in transition into the world economy is largely a function of expansion in foreign trade as well as of changes in their communication and transport infrastructure and technology. (Hibbert 70)

In order to understand how far Hungary has come in terms of stability and growth, it is necessary to look at a synopsis of its history,

Hungary became a Christian kingdom in A.D. 1000 and for many centuries served as a bulwark against Ottoman Turkish expansion in Europe. The kingdom eventually became part of the polyglot Austro-Hungarian Empire, which collapsed during World War I. The country fell under Communist rule following World War II. In 1956, a revolt and an announced withdrawal from the Warsaw Pact were met with a massive military intervention by Moscow. Under the leadership of Janos KADAR in 1968,

Hungary began liberalizing its economy, introducing so-called "Goulash Communism." Hungary held its first multiparty elections in 1990 and initiated a free market economy. It joined NATO in 1999 and the EU in 2004. (CIA Factbook)

Currently the country is in a financial recession similar to that of the United States, having received a \$25.1 billion loan from the International Monetary Fund and other institutions to service its short-term debts (The Associated Press). However, there is still motivation to invest through such factors as, "...the domestic market and the potential for exports to third countries," moreover, foreign officials regard Hungary as, "...a 'regional center' of foreign investment, with many advantages compared with other possible locations" (Szanyi 3).

Market Overview

After the fall of communism in 1989, the government moved from a centrally planned economy to a market economy. With a population of 10 million people, "the country Per capita income is nearly two-thirds that of the EU-25 average and total GDP is US\$182 billion. The private sector accounts for more than 80 percent of GDP" (Doing Business in Hungary 2). The location of Hungary is advantageous to businesses and has resulted in foreign ownership of and investment in Hungarian firms, "with cumulative foreign direct investment totaling more than \$60 billion since 1989" (CIA Factbook).

The country location is, therefore, significant, because Hungary is viewed as a launching pad for international companies to other countries in Europe. To support the positioning benefit of Hungary, the U.S. Commercial Service has reported that,

Hungary's strategic location in Europe, access to EU markets, highly skilled and educated work-force, sound infrastructure and other advantages have led companies

such as GE, Alcoa, Morgan Stanley, IBM and many others to locate facilities here, both in manufacturing and services. Hungary's geographic position in Central Europe offers a strategic logistical hub within the region. Road, rail, aviation, and waterway networks fan out and offer access to the east and south – Russia and the newly emerging Balkans. (Doing Business in Hungary 2)

By investing in the Hungarian market, U.S. businesses could be opening the door to broader possibilities due to increased access within Central Europe.

Aside from the strategic location, there are other market factors that make Hungary attractive for U.S. investment, such as the quality of labor. In a research study entitled *Experiences with foreign direct investment in Hungary*, the authors found that aside from the cultural and behavioral factors in the region,

Hungarian labor was generally declared by the respondents to be talented and valuable, relatively appropriately skilled, disciplined, and creative and intelligent. U.S. respondents even declared the average educational level among workers to be higher than in the United States. This is another clear advantage of Hungary over competitor states. There was a consensus among the respondents that skills that were lacking could be taught to Hungarians quite easily... (Szanyi 4)

Not only is the location attractive, but the workforce is capable as well. Although training and employing Hungarians would be more expensive than in emerging economies such as India or China, in some instances, the knowledge-base of the worker is worth the investment.

The researchers also compared what makes Hungary more attractive to investors than developing countries, especially in terms of cost disadvantages.

As regards production inputs, the comparative advantages of CEE countries, especially Hungary, lie far more in qualitative factors (skill and education of labor, technological and infrastructural background, small cultural distances, a Westernized way of life, etc.) than quantitative ones (raw materials, masses of cheap labor, etc.). Thus not even in the field of production inputs (not in any case a first priority in FDI decisions) do CEE countries compete with low-cost locations. But the differences of markets and production possibilities, geographical location, and so forth give plenty of reasons why FDI in the CEE region is developing much more rapidly than in the overwhelming majority of less-developed countries of the Third World, precisely because these have been unable to provide what multinationals have been looking for. (Szanyi 11)

Because of Hungary's advancement, then, it is able to offer more attractive gains than cheap labor in some developing countries. This is important for U.S. businesses to note; while developing countries may offer lower costs, Hungary provides quality labor, a strategic hub in Central Europe, and other advantages.

Market Barriers

Due to the current economic downturn, investors might view Hungary as both a political and financial risk. The Hungarian Prime Minister, Ferenc Gyurcsany announced his resignation in the wake of the country's economic crisis (The Associated Press). Aside from the unsure political future of the country, there is also the matter of the USD 25.1 billion loan taken out from the International Monetary Fund, European Union, and World Bank. The package was designed to help improve the government's fiscal stability, bail out the banking

systems, and foster confidence to obtain external financing (Doing Business in Hungary 3). With the state of the economy as it is, the IMF estimates that growth in Hungary won't reach its projected potential of three percent until 2011 (3). These factors could prove to be a barrier for investors based on the forecast that firms risk stunted growth until 2011. With an economic outlook that is hazy, firms are not likely to invest.

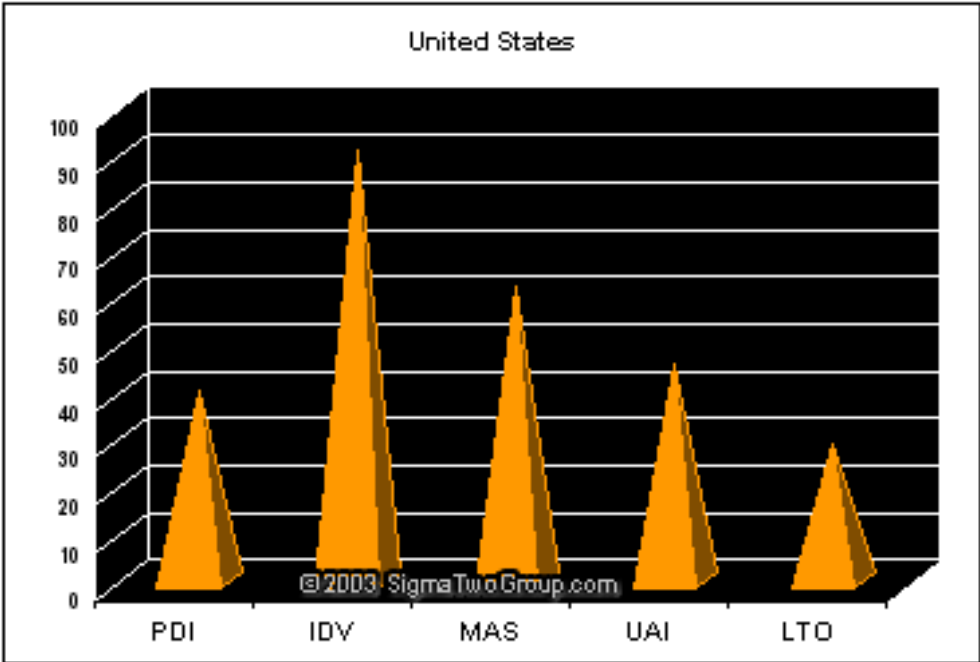
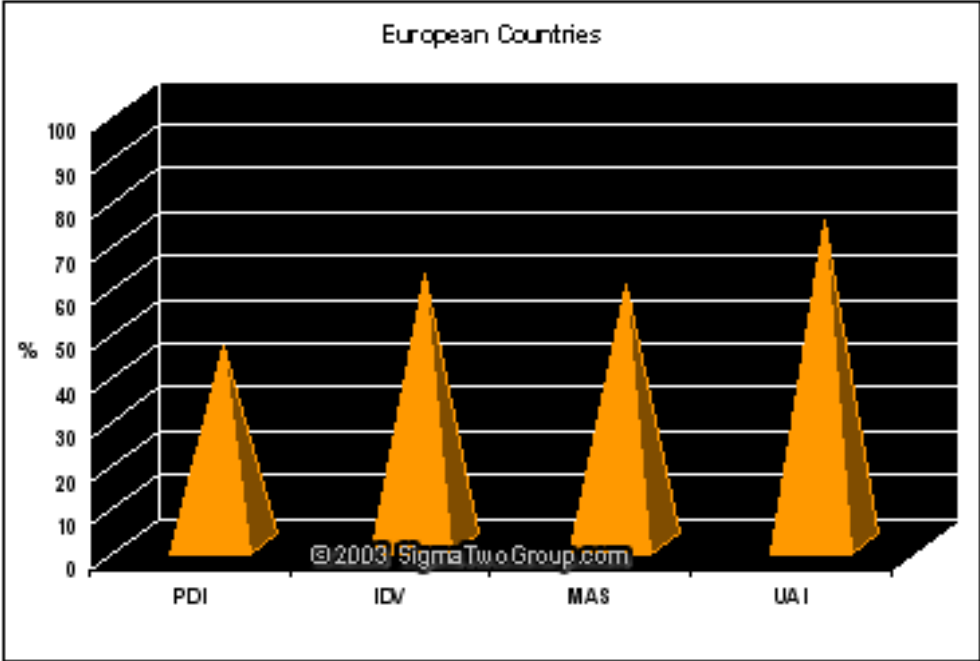
Cultural Barriers

The cultural barriers between the United States and Hungary go farther than a language barrier, and can be examined utilizing the Hofstede Cultural Dimensions. Although there is not a graph for Hungary specifically, U.S. business can compare the European averages to the U.S. cultural dimensions. Furthermore, the numbers for the Hungarian dimensions are given and can be seen in the table below (Hofstede):

| Cultural Dimension | Hungary | United States |
|-----------------------------|----------------|----------------------|
| Power Distance Index | 46 | 40 |
| Individualism | 80 | 91 |
| Masculinity | 88 | 62 |
| Uncertainty Avoidance Index | 82 | 46 |

While Power Distance Index and Individualism are somewhat similar between Hungary and the United States, there is a larger gap between Masculinity rankings. However, the most significant gap occurs between the countries regarding the Uncertainty Avoidance Index. This could prove problematic, since U.S. businesses don't trend toward long-term planning or developing extensive options or in-case-of-failure scenarios. Hungarian firms may lose confidence in a U.S. firm, seeing it as unprepared or unorganized.

Below are the graphs of the Hofstede Cultural Dimensions for European countries and the United States (Hofstede).



It can be shown that the European dimensions are very similar to those of Hungary, although Hungary typically ranks higher in all of the measures than the average.

Other cultural barriers include language and communication style. Hungarians tend to be more open than Americans in business conversations and may go to a personal level. One

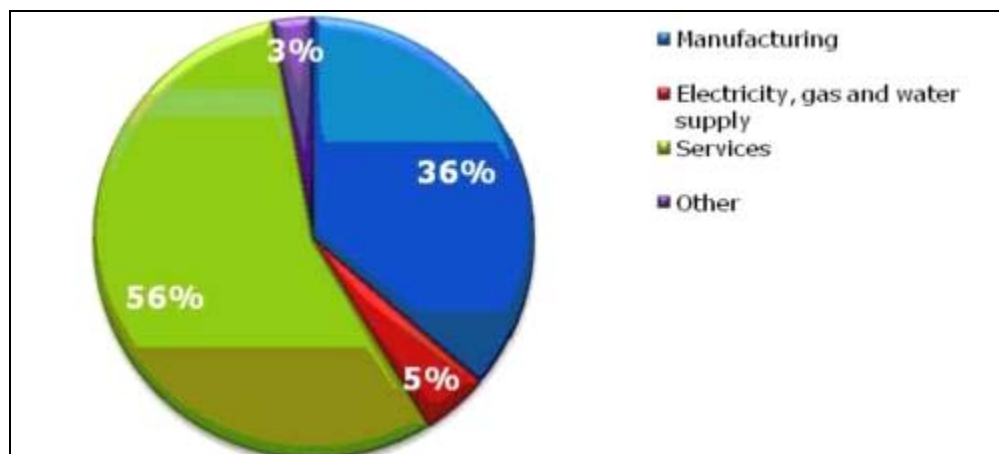
advantage, however, is that Hungarians do not require long-standing relationships in order to engage in a business association (Hungary Business Etiquette). This ensures that entering the Hungarian market from a relational aspect will be easier than in China or India, especially in terms of forming a business partnership.

Recommendations for Investment in Hungary

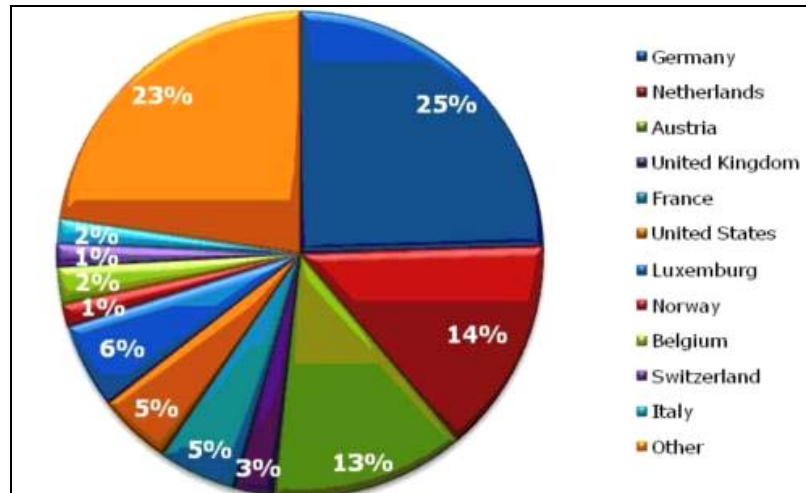
The United States has had a successful business history with Hungary, with American companies investing

...more than \$9 billion in Hungary since 1989, making the U.S. the 4th-largest foreign investor behind Germany, Austria and the Netherlands. Meanwhile, U.S. exports to Hungary have topped US\$1 billion dollars in each of the last five years, led by IT equipment, automotive components, industrial engines and other manufacturing supplies. (Doing Business in Hungary 4)

The fiscal gains from entering the Hungarian market are evident. Moreover, the government of Hungary provides a breakdown of the most successful areas of foreign direct investment (Foreign Direct Investment):



With this knowledge, businesses can evaluate the untapped areas of FDI, as well as determine the areas in which there is already experience in the country. The government also provides a chart recording the largest sources for FDI (Foreign Direct Investment):



The United States is second after Germany for FDI, which demonstrates a solid precedent for entering the marketplace.

As in any country, research is necessary, as well as formulating a strategic business plan. However, due to the overall security of doing business in Hungary, any given U.S. firms should feel the freedom to choose the entry mode that best suits its business. Whether that is through the implementation of a wholly owned subsidiary, joint venture, or some other mode of entry, the outlook for success is raised due to the similarities between the markets in Hungary and the United States.

Conclusion

Based on the information discussed in this thesis, there are several general recommendations U.S. businesses can keep in mind when looking to engage in foreign direct investment that will aid in dealing with barriers to entry.

1. Have a comprehensive understanding of the culture in which the firm wished to invest in, including traditions, expectations, government policy, stability, openness, economy, and infrastructure.
2. Actively pursue relationships with potential business partners and take opportunities to network.
3. Create a comprehensive business plan and entry strategy in order to gain governmental support, as well as anticipate the competition and barriers.
4. Develop and implement policies for dealing with barriers, especially in the area of ethics.

This being said, every country will have differing barriers, which require their own strategies. Due to the nature of Indian business, forming a joint venture is recommended; however, in China opening a wholly owned subsidiary is the most feasible mode of entry. To contrast both of those, there isn't one clear mode of entry to choose for Hungary. Three different countries and three varying recommendations demonstrate the larger global picture of firms deciding where to invest all around the world. Only through careful research and strategic planning can firms develop individual business plans that fit both the firm and the host country it wishes to enter.

Of all the nuances in deciding what mode of entry to take to avoid barriers to entry, one key factor in overcoming those barriers continues to be the quality of business connections made with host firms and the host government. Through cooperation and developing a strategic network, U.S. companies will be better equipped to survive long-term in the global arena and foster growth within the host country.

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