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Cultural attractiveness:

A neglected variable in foreign direct investment

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CULTURAL ATTRACTIVENESS:

A NEGLECTED VARIABLE IN FOREIGN DIRECT INVESTMENT

ABSTRACT

Prior theory and research in international strategy focused on cultural differences and their impact on foreign direct investment (FDI), neglecting other potentially relevant variables attesting to the cultural interaction between a multinational enterprise (MNE) and its host environment/ partner. In this paper, we introduce the construct of cultural attractiveness, whereby members of a focal culture view another culture as desirable. The construct, which correlates with the overall perception and reputation of a given country, is used to extend theories such as cultural familiarity, internationalization, and transaction costs. Using FDI data for 23 nations between 1985 and 2008, we find that cultural attractiveness is a significant predictor of FDI inflows, whose explanatory power is superior to conventional cultural difference measures.

INTRODUCTION

National culture has been extensively studied in international management and strategy

(Leung *et al.*, 2005), and its impact on managerial and economic outcomes has been shown to

be profound (Franke, Hofstede, and Bond, 1991; Kirkman, Lowe, and Gibson, 2006). Of

particular interest have been situations in which different cultures come into contact with each

other. While a few studies show a positive impact generated from the meeting of cultures

(e.g., Chakrabarti, Gupta-Mukherjee, and Jayaraman, 2009; Morosini, Shane, and Singh,

1998; Shenkar and Zeira, 1992), the vast majority of the literature has focused on the

challenges, negativities, and difficulties that originate from such encounters (Vaara *et al.*,

2013).

The most widely used construct used to examine the differences between cultures is

that of cultural distance (Kogut and Singh, 1988), which measures how far apart two cultures

are on an aggregate of Hofstede's (1980) original four cultural dimensions. The main premise

behind this construct is that differences in cultures constitute hurdles, which hamper firms'

flow of information, knowledge, and competencies, increasing uncertainty and augmenting

the cost of doing business abroad (Barkema, Bell, and Pennings, 1996; Nachum, 2003). The

cultural distance formula has been applied to numerous international strategy phenomena

including foreign direct investment (FDI) (Lee, Shenkar, and Li, 2008), entry mode (Chang

and Rosenzweig, 2001), knowledge acquisition (Li, Poppo, and Zhou, 2010), and

multinational enterprise (MNE) and subsidiary performance (Barkema *et al.*, 1997), among

others. Similarly consistent with the hurdle logic are transaction cost economics (Hennart,

1982; Williamson, 1975) and internationalization theory, also known as the Uppsala Stage

model (Johanson and Vahlne, 1977).

While cultural distance helped generate some valuable findings (Kirkman *et al.*, 2006),

its key properties and resulting deficiencies have been criticized on both conceptual and

empirical grounds (Lee *et al.*, 2008; Tung and Verbeke, 2010; Zaheer, Schomaker, and Nachum, 2012), leading some to endorse a rejection of the construct and its underlying metaphor altogether (Shenkar, 2012; Shenkar, Luo, and Yeheskel, 2008). Indeed, subsequent empirical research has confirmed that many of the assumptions behind cultural distance were erroneous, including, for instance, symmetry (Lee *et al.*, 2008; Selmer, Chiu, and Shenkar, 2007). One illusion that has been criticized is the assumption of discordance (Tung and Verbeke, 2010), namely the belief that cultural difference invariably generates negative outcomes, neglecting evidence that differences can also be a source of benefits and synergies (e.g., Leung *et al.*, 1996; Morosini *et al.*, 1998; Vaara *et al.*, 2013). The concept of cultural attractiveness is introduced with the latter line of reasoning in mind and is consistent with calls for introducing novel cultural constructs and challenges to a simplistic distance metaphor (Lee *et al.*, 2008; Leung *et al.*, 2005).

In this paper, we define 'cultural attractiveness' as the desirability of a culture for a member of another culture. To examine the validity of the construct, we explore its relationship with the overall perception of a country in the form of that country's reputation. We test our propositions with country-pair FDI data for 23 nations during the 1985 to 2008 time period. The paper's contribution rests with providing a new lens with which to examine the cultural encounter, one that complements the limited and distorted perspective of 'distance.' This helps overcome problems endemic to the distance construct, e.g., erroneous assumptions of symmetry and discordance (Shenkar, 2001; Tung and Verbeke, 2010). The study challenges and extends cultural familiarity theory (Lee *et al.*, 2008), the Uppsala model (Johanson and Vahlne, 1977) and transaction cost economics (Chang and Rosenzweig, 2001; Hennart, 1982).

LITERATURE AND THEORY

National culture plays a prominent role in international business and economics (Franke *et al.*, 1991; Kirkman *et al.*, 2006). Defined as the "shared understandings made manifest in act and artifact" (Redfield, 1948: vii) cultures comprise the "values, beliefs, norms, and behavioral patterns of a national group" (Leung *et al.*, 2005: 357). Cultural values reflect "a broad tendency to prefer certain states of affairs over others" (Hofstede, 2001: 5), involving a form of judgment by a value-carrier whose enduring beliefs and attitudes are connected to whether a mode of conduct is deemed desirable or not (Rokeach, 1973). The value-based framework has been widely used in cross-cultural research and has proved its usefulness in deciphering culture (Javidan *et al.*, 2006; Schwartz, 1994; Trompenaars, 1993; see Kirkman *et al.* [2006] for a review). At the country level of analysis, most studies on culture in international management research have used the value-based framework to examine the effect of cultural distance, i.e. the extent of differences in cultural values, on organizational and country level outcomes (Kirkman *et al.*, 2006), centering on the comparison between what different cultures view as desirable or not.

Extant research has largely neglected to study the central idea of cultural values in determining what a cultural collective deems as positive/desirable or negative/undesirable, possibly owing to its heavy reliance on the cultural distance construct (Kirkman *et al.*, 2006; Zaheer *et al.*, 2012). This negligence is surprising, given the evidence on positive outcomes when individuals encounter practices, routines, and behaviors that they deem desirable and preferable. Empirical studies find that when individuals face practices and behaviors that reflect their desires, ideals, and values, they will feel more satisfied, comfortable, and committed (Newman and Nollen, 1996; Very *et al.*, 1997). Employees are not distracted because they do not have to grapple with behavioral patterns and rules that are incongruent with their deeply embedded values and expectations towards desirable conduct and outcomes (Sirmon and Jane, 2004). Prior work further documents that management practices that

enforce individuals' values and ideals are more likely to yield predictable behavior (Wright and Mischel, 1987), self-efficacy (Earley, 1994), and post-merger performance (Very *et al.*, 1997).

Building on the inherent idea of cultural values, we introduce a novel construct that measures whether another culture is perceived as desirable and positive (Hofstede, 1980, 2001; House et al., 2004). We coin this cultural construct 'cultural attractiveness'[1] with attractiveness being defined as the 'extent of positive perceptions towards' a given entity (Sarala, 2010: 44). Prior research finds that being attractive, i.e. inducing positive perceptions, can have important and beneficial effects, e.g., the attractiveness of an acquirer to a target may decrease post-acquisition conflict and help post-merger integration (Haunschild, Moreland, and Murrell, 1994; Sarala, 2010). We deem a culture as attractive if it evokes positive perceptions in an observer whose favorable judgment is based on the desirability of the culture's behavioral patterns, practices, and routines. Thus, if a culture/society values and desires high collectivism, it will perceive another culture with collectivistic behaviors and practices, e.g., strong integration of individuals into cohesive groups (Gelfand *et al.*, 2004), more positively than a culture with individualistic behaviors and practices, e.g., weak integration into cohesive groups. With the cultural attractiveness construct, we provide a new cultural approach consistent with calls for novel cultural constructs to help overcome some of cultural distance's inherent limitations (Leung *et al.*, 2005; Tung and Verbeke, 2010).

The concept of cultural attractiveness can help explain asymmetric cross-cultural impacts, overcoming cultural distance's unsupported assumption of symmetry (Shenkar, 2001; Tung and Verbeke, 2010). Whereas the cultural distance between two cultures is

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[1] While there are few studies that have mentioned the notion of cultural attractiveness (e.g., Shenkar, 2001; Shenkar *et al.*, 2008; Veiga *et al.*, 2000; Very *et al.*, 1997), we are, to our knowledge, the first to systematically develop the concept and measure for it.

inherently the same for both cultures, one culture may consider the other culture more/less attractive and desirable than the other way around. A cultural attractiveness lens also suggests that cultural differences do not always lead to negativities and difficulties, thereby helping to overcome the assumption of discordance embedded in the cultural distance construct (Lee *et al.*, 2008). While cultural distance typically attempts to relate positive and negative outcomes to the extent of cultural differences, the cultural attractiveness approach directly assesses the positive perceptions towards another culture independent of its cultural differences.

CULTURAL ATTRACTIVENESS AND COUNTRY REPUTATION

If a culture's attractiveness denotes the extent of positive perceptions towards that culture, then a nation's cultural attractiveness should positively relate to its overall perception. This is because culture constitutes a relevant and observable element of a nation that affects a wide variety of its facets and characteristics (House *et al.*, 2004). To assess this relationship, we employ the concept of reputation, which can be defined as the general standing of an entity and its "ranking on relevant criteria, which, as a whole, (beyond their aggregate sum) form the relative position of that [entity] in the eyes of given constituencies" (Shenkar and Yuchtman-Yaar, 1997: 1362). Prior research has studied the antecedents and consequences of firm (Phillipe and Durand, 2011; Roberts and Dowling, 2002) and individual reputation (Zajac and Westphal, 1996; Zhang and Wiersema, 2009). The reputation of countries has recently attracted renewed scholarly attention (Arikan and Shenkar, 2013; Berens *et al.*, 2011). As culture is a relevant and visible criterion of a country that likely contributes to its overall standing, we utilize the concept of country reputation and explore whether cultural attractiveness relates to it in a conceptually consistent way. In so doing, we are able to examine the validity of the cultural attractiveness construct.

CULTURAL ATTRACTIVENESS AND FDI

FDI is a momentous step of strategic importance and unusual uncertainty for MNEs resulting from the scale of capital committed to a less familiar foreign country (Hymer, 1976). Existing theories on FDI provide various motives for such investment decisions including market-seeking, efficiency-seeking, resource-seeking, and strategic-asset-seeking motives (Dunning, 1998; Nachum and Zaheer, 2005). Culture plays a pivotal role in FDI decisions because of the inherent involvement of different national cultures and the potential cultural friction that may arise from the interaction (Shenkar *et al.*, 2008). In order to capture culture's influence on FDI, a theory of familiarity has emerged. Cultural familiarity theory suggests that MNEs are less likely to invest and establish subsidiaries in culturally distant countries and will display poorer performance when they do (Lee *et al.*, 2008; Miller and Parkhe, 2002). Firms incur additional costs and face increased difficulties when operating in a cultural environment that is dissimilar to their own due to unfamiliarity with a host environment, specifically lack of knowledge on how to conduct business and operate in that environment (Hennart and Reddy, 1997; Zaheer and Mosakowski, 1997), which hampers the flow of information and knowledge (Luostarinen, 1980) and creates a liability of foreignness (Zaheer, 1995). Furthermore, the cost of unfamiliarity is not easily obviated since the knowledge needed to reduce it is itself costly to obtain (Bell, Filatotchev, and Rasheed, 2012).

We challenge and extend the cultural familiarity logic in predicting FDI and argue that familiarity only captures one aspect of culture's role in FDI whilst neglecting the important impact of a culture's attractiveness. We propose that, other things being equal, MNEs are likely to invest in countries that are culturally attractive because attractiveness decreases the costs and difficulties in operating in a country. MNEs that invest in an attractive host culture are also likely to perform better since they are more likely to accept practices and behavioral patterns consistent with their values and preferences. In so doing, MNEs incur lower

adaptation costs as domestic employees and other local stakeholders do not have to significantly alter the behaviors, practices, and routines they are used to (Fiol, 1991; Morosini *et al.*, 1998; Sirmon and Jane, 2004). Acceptance of host country practices and routines in a foreign subsidiary also enhances legitimacy and can help reduce opposition and hostile reactions from local constituencies who fear foreign dominance (Kostova and Zaheer, 1999).

Under cultural attractiveness, home country personnel will encounter a culture that is consistent with their desired behaviors (House *et al.*, 2004; Sirmon and Jane, 2004) and will likely be more committed and satisfied, thus perform more efficiently on a consistent basis (Earley, 1994; Newman and Nollen, 1996; Wright and Mischel, 1987). The positive perceptions towards a culture resulting from desirable routines and practices further yield more predictable behavior and higher self-efficacy (Earley, 1994; Wright and Mischel, 1987) thereby facilitating better individual performances of home country personnel and superior overall subsidiary outcomes. As a result, firm-specific advantages will more easily transfer and overall subsidiary performance will likely be superior compared to subsidiaries in locations where the host country culture is not attractive.

To illustrate our argument, consider an MNE from a home country that values and desires high individualism and the MNE's foreign investment in the form of an R&D subsidiary. The MNE's managers will prefer to manage or deal with R&D operations in a host country that displays high individualism practices and routines, e.g. in the form of rewards and freedom for individual innovators to be creative (Gelfand *et al.*, 2004; Shane, 1992, 1993). If the host country already practices high individualism, it will not be necessary to greatly modify these practices and behaviors or even introduce entirely new practices to match the manager's preferences. Host country employees can continue to perform tasks the way they are used to and the subsidiary does not have to go through the costly and time-consuming process of adopting new practices, routines, and rules. At the same time, the home

country managers are likely to display higher commitment and more efforts in managing the subsidiary located in the attractive and desirable culture, which will likely lead to superior subsidiary performance (Newman and Nollen, 1996; Very *et al.*, 1997). If, however, the host culture displays low individualism practices and routines, the managers may either have to reluctantly operate in an undesirable culture that is incongruent with their values and ideals or 'forcefully' introduce new practices and routines that differ from the way host country employees have been operating. While the former alternative can lead to inferior subsidiary and manager performance, the latter can be costly and difficult to implement (Morosini *et al.*, 1998; Sirmon and Jane, 2004). Thus, we use the cultural attractiveness concept to challenge and extend the basic cultural familiarity framework by arguing that MNEs are more likely to invest and operate in countries that are culturally attractive in addition to the countries' cultural familiarity. As a result of our discussion, we hypothesize

> Hypothesis 1: Other things being equal, a host country's cultural attractiveness relates
> positively to FDI flows it receives from a home country.

With hypothesis 1, we extend the cultural familiarity framework, which centers on the difficulties, complexities, and negativities when investing in a different culture (Lee *et al.*, 2008). While prior research based on this conventional notion is certainly valuable, focusing primarily on negative outcomes and difficulties has hindered our understanding of the processes and conditions that create benefits when operating in a different culture (Shenkar, 2012). With the cultural attractiveness approach, we introduce a novel perspective that concentrates on the positive aspects and benefits of a culture whereby challenging and complementing the notion that cultural differences are always liabilities (Chakrabarti *et al.*, 2009; Tung and Verbeke, 2010). The development of a second cultural approach gives rise to the question how the new cultural attractiveness approach fares against the traditional cultural

distance construct. In order to explore the significance of the cultural attractiveness approach vis-à-vis the cultural distance logic, we compare these two competing frameworks in explaining FDI by proposing two competing hypotheses

> Hypothesis 2a: The impact of a host country's cultural attractiveness on the FDI flows it receives from a home country is greater than the impact of cultural distance.

> Hypothesis 2b: The impact of cultural distance on the FDI flows a host country receives from a home country is greater than the impact of the host country's cultural attractiveness.

METHODS

Data

To test the hypotheses, we collected data for the dependent variable from the OECD Statistical Compendium database on bilateral FDI over the 1985–2008 period. The OECD Statistical Compendium includes bidirectional FDI flows reported by its member nations. We included the 23 OECD members for which we can construct the cultural attractiveness measure. We excluded non-OECD members in order to capture the perception of another culture resulting from the congruency between cultural values and practices rather than the perception resulting from economic status differences. Data for the main independent variable, cultural attractiveness, are based on the cultural dimension scores of the GLOBE research project. We compiled data for the control variables from a number of sources that include the CIA's *World Factbook*, GLOBE project (House *et al.*, 2004), Henisz's (2000) veto point index, Hines and Rice's (1994) list of tax havens, Hofstede (2001), La Porta *et al.* (1999), Ronen and Shenkar (1985, 2013), and the World Bank's *World Development Indicators* (WDI). Table 1 provides a full list of variable definitions and data sources used.

*** Insert Table 1 here ***

Measures

Dependent variable

We use annual bilateral FDI flows for the dependent variable to study the scope of MNE investments from the home into the host countries (Li and Vashchilko, 2010; Siegel, Licht, and Schwartz, 2013). Because the data are sharply skewed, we employ the natural logarithm of (FDI flows + 1).

Independent variable

To measure cultural attractiveness, we use cultural dimensions from the GLOBE project. Several reasons support this decision. First, the GLOBE project is the only large scale study that explicitly measures cultural values and cultural practices of societies (House *et al.*, 2004) and thus allows us to examine the desirability of a culture's behavioral patterns, practices, and routines. Second, GLOBE is theory driven, having specified the nature of the constructs before developing items and scales (Javidan *et al.*, 2006). Third, GLOBE is suitable for our study as its items were sent to 17,300 managers of 951 firms across three industries. The respondents represent a sample of individuals that most likely resembles the individuals that are involved in the foreign investment decisions of MNEs. Finally, GLOBE represents, to our knowledge, the most recent attempt to conceptualize and measure culture involving over 160 researchers across the globe.

We defined cultural attractiveness as the desirability of a culture, i.e. the degree of congruence between the practices and routines of a culture and the desires, preferences, and values of the observer. Given two cultures A and B, each culture has their own cultural values V and practices P for the cultural dimension d. The observer is from culture A and possesses certain values $V_{A,d}$ for dimension d. Culture B is assessed by the observer on its attractiveness

based on the cultural practices $P_{B,d}$ for dimension d. We use the Euclidean distance to measure the *cultural attractiveness* of the culture B across all nine GLOBE dimensions for observer A:

$$\text{Cultural attractiveness}_{(A,B)} = \sqrt{\sum_{d=1}^{9}[6 - |P_{B,d} - V_{A,d}|]^2} \quad (1)$$

We use the value six in equation (1) because it is the largest possible score between practices and values of any dimension based on the scale of the GLOBE items (GLOBE items' scale is 1–7). Thus, cultural attractiveness for each dimension d is six when the congruence between host country practices and home country values is largest. Cultural attractiveness for each dimension d is zero when the congruence between host nation practices and home nation values is smallest. We employ all nine GLOBE dimensions: assertiveness, future orientation, gender egalitarianism, humane orientation, in-group collectivism, institutional collectivism, performance orientation, power distance, and uncertainty avoidance. We use all GLOBE dimensions to calculate cultural attractiveness because we expect a multitude of a nation's cultural facets and traits, as captured by all nine cultural dimensions identified in the GLOBE project, to influence the overall reputation and perception of a country and the total amount of bilateral FDI flows. This assumption may not be valid when examining other topics of international management and strategy for which specific dimensions are considered much more important than others (Shenkar and Zeira, 1992). Table 2 provides the cultural attractiveness scores for the 10 OECD member countries that became members before the year 1985 with the largest total GDP over the sample period 1985–2010.[2] The scores suggest that cultural attractiveness is asymmetric between two countries in contrast to cultural distance measures. For example, Spain has a cultural attractiveness score of 14.13 for the observing country Canada while the reverse attractiveness

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[2] A full list of cultural attractiveness scores for all countries covered by GLOBE is available from the authors upon request.

score, i.e. the cultural attractiveness of Canada for the observing country Spain, is 14.83 (1.3 standard deviations higher).

*** Insert Table 2 here ***

Control variables

We control for several factors that drive FDI. Cultural familiarity theory suggests that MNEs are less likely to invest in culturally distant countries (Lee *et al.*, 2008). Prior research provides evidence that cultural distance negatively influences FDI (Sethi *et al.*, 2003), although mixed empirical findings exist. As we aim to demonstrate the explanatory power of cultural attractiveness on top of the conventional cultural distance construct, we control for the cultural distance between host and home country using the *Kogut and Singh (1988) index*. We further employ *Ronen and Shenkar's (1985, 2013) clusters* classification. This cluster approach overcomes the additive assumption of the conventional cultural distance measure (Zeng *et al.*, 2013).

In addition, we control for the size of the home and host country economy through the logged product of GDP of the home and host country (*log product home-host GDP*) (Siegel *et al.*, 2013). We also include the growth rate of the host country's GDP per capita (*GDP per capita growth*) as a proxy for its market potential (Slangen and Beugelsdijk, 2010). We enter the *logged* great-circle *geographic distance* between home and host nation, which influences transportation costs between MNE headquarters and foreign affiliates and the cost of managing the affiliates (Holburn and Zelner, 2010). Prior research finds that a low tax rate attracts inward FDI (Loree and Guisinger, 1995). Thus, we use a dummy variable to control for the *tax haven status* of the host country. We also include a control for political risk through Henisz's (2000) *political constraint* index (Siegel *et al.*, 2013). We further include a set of dummy variables indicating whether host and home countries share a *common language*, common *colonial ties*, and common *legal origins* (Siegel *et al.*, 2013).

All variables are lagged by one year to avoid potential reverse causality and because country reputation and FDI decisions are likely based on previous year's data (Sethi *et al.*, 2003). Time dummies are included to account for overall effects in the individual years.

Empirical model

We employ a gravity equation model to test our hypothesis. Originally rooted in the international trade literature, the gravity equation model has now been regularly applied to and verified in the field of FDI (e.g., Siegel *et al.*, 2013; Zwinkels and Beugelsdijk, 2010). As we have cross-sectional time-series data, we are able to employ econometric panel techniques for our models. Modified Wald chi-squared test for heteroskedasticity and Wooldridge's (2002) test for autocorrelation indicated that the data contain heteroskedasticity and autocorrelation. We therefore employ Prais-Winsten feasible generalized least squares (FGLS) estimation, which corrects the standard errors of the regression coefficients for panel-specific autocorrelation and heteroskedastic disturbances (Wooldridge, 2003).

Cultural attractiveness and country reputation

To explore the relation between cultural attractiveness and country reputation, we use country reputation data consisting of 153,547 reputations ratings made by individual respondents for 34 countries between 2009 and 2013. We aggregate the data to create country-dyadic reputation scores (see Appendix). We calculate cultural attractiveness with the same measure described in the Measures section above. We further include a broad set of competing accounts, including the effects of conventional cultural distance measures and various features of the economic, legal, and political environment. Panel A of Table 3 provides a full list of variable definitions and data sources used. To account for heteroskedasticity and autocorrelation in the data, we use feasible generalized least squares regression. We find that

cultural attractiveness has a significant and positive effect on country reputation (see Panel B of Table 3). The results are robust to different competing accounts. The findings support the intuition that cultural attractiveness contributes to the extent of positive perceptions towards the entire country in a conceptually compatible way and provides validity for the new cultural attractiveness construct.

*** Insert Table 3 here ***

RESULTS

Table 4 presents the summary statistics and the correlation matrix. VIFs are less than 2.0 for all variables. The correlation matrix and the VIFs indicate that multicollinearity levels are low.

*** Insert Table 4 here ***

Table 5 presents the results of the FGLS estimations. Model 1 includes only the control variables without cultural distance measures. We propose that the cultural attractiveness of a host country has a positive influence on the amount of FDI flows in that country. For Model 2 we enter the cultural attractiveness measure in addition to the controls. Models 3 and 4 include the two different measures of cultural differences based on Kogut and Singh (1988) and Ronen and Shenkar (1985, 2013). We find that cultural attractiveness has a positive and significant influence on the level of FDI abroad at the 0.001 p-level in all Models 2–4. Thus, hypothesis 1 receives strong statistical support. The results indicate that cultural attractiveness has significant explanatory power beyond the conventional Kogut and Singh (1988) cultural distance approach based on Hofstede's (1980) cultural dimensions and Ronen and Shenkar's (1985, 2013) cultural clusters measure.

Cultural attractiveness also has an economically meaningful impact on FDI flows. While controlling for a broad set of economic, cultural, and institutional variables, we find

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that a one standard deviation increase in cultural attractiveness is associated with a +4.8

percent change in mean log FDI flows when converted to US dollars. At the level of (mean

dependent variable + one standard deviation in dependent variable), this equates to an

increase of $74 million in bilateral FDI flows from $1.54 billion to $1.61 billion.

The *Kogut and Singh* (1988) *cultural distance* between two cultures has a negative and

significant effect on FDI flows. *Ronen and Shenkar (1985) clusters* is positive and significant.

The *cultural distance* and *clusters* results suggest that cultural familiarity has a positive

influence on FDI flows. The *logged product* of *home* and *host* country's *GDP* has a positive

and significant influence on FDI flows, while *logged geographic distance* has a negative and

significant effect, consistent with the gravity equation model. The *GDP per capita growth*

variable is positive and significant. The *tax haven status* of the host country and the *common

language* and *colonial ties* between the host and home country are positive and significant.

Political constraint of the host nation and a common *legal origin* between host and home

country do not yield consistent statistical results.

*** Insert Table 5 here ***

Comparison between cultural attractiveness and cultural distance

We hypothesized that cultural attractiveness has a positive influence on FDI flows and find

support for the hypothesis, even when accounting for conventional cultural distance measures.

At the same time, we also find support for the cultural familiarity framework as the cultural

difference measures relate negatively to FDI flows. Thus, while the results suggest that

cultural attractiveness has been a neglected variable with significant explanatory power for

FDI, both cultural approaches receive support in explaining FDI flows.

The empirical support for both cultural approaches gives rise to the question, which

construct has a stronger effect on FDI. In order to find out which construct has a greater

impact on FDI, we proposed two competing hypotheses 2a and 2b. Hypothesis 2a suggests that cultural attractiveness has a stronger impact on FDI flows than cultural distance while hypothesis 2b suggests that cultural distance has a greater influence on FDI flows than cultural attractiveness. To test the hypotheses, we assess the size differences between the standardized coefficients of cultural attractiveness and cultural distance. The standardized coefficients for cultural attractiveness (CA) are $\beta_{CA} = 0.845$ and $\beta_{CA} = 0.789$ (Models 3 and 4) respectively. For the cultural distance measures, the standardized betas are $\beta_{Kogut/Singh} = -0.249$ and $\beta_{Ronen/Shenkar} = 0.380$. The betas suggest that cultural attractiveness has a larger coefficient than the absolute values of the cultural distance coefficients. A Wald test confirms that the differences between the absolute values of the betas are significant at the 0.001 p-level for both cultural distance measures (Table 6). Therefore, a comparison between the two cultural approaches shows that the novel cultural attractiveness concept has a significantly stronger influence on FDI flows than the conventional cultural distance approach, offering support for hypothesis 2a while rejecting hypothesis 2b.

<center>*** Insert Table 6 here ***</center>

Sensitivity analyses

We performed several additional tests to assess the robustness of our results for both datasets. First, we ran our regressions using Heckman's (1979) two-stage procedure to correct for potential sample-selection bias. This can be useful as the sample has missing values that may be systematically omitted. We ran a binary cross-sectional time-series probit regression of the determinants of whether a particular country-dyad/year observation was included in the sample. A binary correction term for sample selection is generated that takes the value 1 if a country-pair/year observation is included in our sample and 0 if it is not included. In a second

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step, we added this correction term to the regression models. The results of Heckman's two-stage procedure are highly similar to our previous results.

Second, we replace the one-year lagged control variables with controls that have longer time lags to capture long-term influences that may potentially affect country reputation and FDI decisions. We employ two-year and three-year lagged variables to create new sets of control variables by calculating the average value of a control variable over the past two and three years respectively. The results are, again, highly similar to the original results provided in Table 5.

Third, we divided the 24-year period covered by our FDI sample into smaller segments to account for potential changes in culture over time. While it is often argued that culture remains relatively stable over long periods of time (Brodbeck *et al.*, 2007; Hofstede, 2001), changes can still be observed (Leung *et al.*, 2005). To mitigate the effects of potential variations in cultural values and practices during our sample period, we divided the sample into five-year segments and 10-year segments respectively and ran our analyses separately for each segment. The results of the analyses remain very robust. The additional sensitivity tests suggest that our results are robust to potential sample selection biases, alternative long-term influences on FDI, and changes of culture over time.

DISCUSSION AND CONCLUSION

Grounded on the desirability of a culture, we have developed the novel concept 'cultural attractiveness.' To demonstrate its value, we show that cultural attractiveness overcomes some of the limitations endemic to the cultural distance construct and employ the concept to challenge and extend cultural familiarity theory. We assess the effect of cultural attractiveness on FDI flows based on FDI data across 23 nations for the 1985–2008 period. The results show

that cultural attractiveness is a fundamental factor in determining FDI flows and further reveal that it has a stronger influence on FDI than the conventional cultural distance construct.

Implications for research

Our study helps to advance the field of international strategy in three major ways. First, it provides a new approach to assess the relationship between cultures that overcomes some of the incorrect assumptions of the often-used cultural distance construct. The cultural distance logic examines the relation between two cultures through their differences, often relying on the premise that differences are liabilities (Shenkar, 2001). In contrast, the cultural attractiveness approach centers on the positive perception towards a culture in the form of the desirability of its cultural practices and behaviors. By focusing on the desirability of a culture's practices and routines, cultural attractiveness helps to overcome some of the limitations persistent in international management research due to its constant reliance on the cultural distance approach (Leung *et al.*, 2005; Kirkman *et al.*, 2006). Specifically, cultural attractiveness is detached from cultural distance's erroneous assumptions of discordance and symmetry. As cultural attractiveness is not based on the premise that differences equal liabilities, it may be used to explain conflicting findings on the relationship between cultural differences and internationalization performance that have not been fully resolved with existing cultural frameworks (Tung and Verbeke, 2010). Cultural attractiveness can also be useful in examining and explaining asymmetric cultural phenomena (Lee *et al.*, 2008). For example, Selmer *et al.* (2007) find that German expatriates are better adjusted in the USA than American expatriates are adjusted in Germany. While cultural distance cannot explain this finding because of its symmetric nature, cultural attractiveness can help to shed light on this issue. In fact, the cultural attractiveness scores show that the US culture is more attractive

to Germans (14.43) than the other way around (13.69, i.e. 1.4 standard deviations less; see Table 2), making it easier for Germans to adjust to the foreign culture.

Second, our study uses the cultural attractiveness concept to challenge and extend cultural familiarity theory and further has implications for related theoretical frameworks (Lee *et al*., 2008). We argue that the cultural familiarity framework only captures the hurdle logic of culture based on the notion that differences between cultures lead to negativities and difficulties whilst neglecting the aspect of attractiveness. We extend the theoretical framework using the cultural attractiveness concept and provide arguments for its ability to help both, lower the costs and difficulties to operate and invest abroad and increase foreign subsidiary performance. The findings not only confirm cultural attractiveness' significant and economically meaningful impact on FDI flows, but also reveal that cultural attractiveness has a stronger effect than cultural familiarity in explaining FDI. Thus, we show that cultural attractiveness is an important and neglected factor that needs to be accounted for when studying the impact of culture on the very decision to launch foreign investments even more so than the culture's familiarity.

Beyond its implications for cultural familiarity theory, the cultural attractiveness approach also has ramifications for the broader management literature that builds on theories consistent with cultural distance's hurdle logic. A prominent theory used to explain the sequence and gradual commitment of FDI is the Uppsala Stage model of internationalization (Barkema *et al.*, 1996; Johanson and Vahlne, 1977). The Uppsala model relies on the premise that firms progressively expand from their home country into other countries with greater "psychic distance" in order to gradually gain knowledge of the more "distant" countries before increasingly committing larger stakes (Johanson and Vahlne, 1977; Luostarinen, 1980). However, support for the proposed foreign entry sequences has been limited (Shenkar, 2001). The cultural attractiveness logic may help to refine the theory and explain some of the

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unexpected expansion patterns through a complementary approach. Taking cultural attractiveness into account, an MNE will likely continue its expansion into countries that have similar cultures to a culturally attractive country it has previously entered, whereas it will redirect its expansion course upon encountering a culturally unattractive location and avoid locations that are similar in culture. At the same time, MNEs will likely increase their commitment in countries that are culturally attractive as opposed to countries that are unattractive. Therefore, cultural attractiveness can help to refine the Uppsala stage model by predicting a more selective foreign entry pattern.

Cultural attractiveness also has implications for transaction cost theory, which has become the main theoretical pillar in explaining the relationship between culture and foreign entry mode (Chang and Rosenzweig, 2001; Hennart, 1982). Transaction cost theorists associate larger cultural distance with higher costs of transaction resulting from greater information and enforcement costs (Tihanyi, Griffith, and Russell, 2005). These costs are accounted for by MNEs through greater control over their foreign operations (Buckley and Casson, 1976). However, cultural distance also increases the costs of direct control due to higher administrative/management costs, which can then be lowered through less control (Brouthers and Brouthers, 2001; Hennart and Reddy, 1997). Thus, employing cultural distance leads to two conflicting predictions for FDI mode. Prior research finds support for both claims, further necessitating a different approach to account for culture's role in FDI mode (Shenkar, 2001). Cultural attractiveness may provide a novel approach that helps to clarify the nature of culture's impact on transaction costs and FDI mode. In contrast to cultural differences, cultural attractiveness does not influence costs of transaction. Cultural attractiveness does have an impact on costs of direct control, however, as it is easier for MNEs to manage foreign subsidiaries in culturally attractive countries with practices consistent with the MNEs' home country values. Thus, cultural attractiveness provides an

unambiguous account on culture's role in foreign entry mode: MNEs will increase their control in culturally attractive countries, as the costs of direct control are smaller in those countries than the costs of transaction.

Third, we present evidence on the consistent relation between cultural attractiveness and a country's overall reputation and perception. As culture is an important and observable element of a country, its attractiveness should intuitively relate to the country's overall positive perception and reputation. This finding further helps demonstrate the methodological validity of the cultural attractiveness operationalization. Although we measure cultural attractiveness through the actual desirability of cultural practices, routines, and behaviors consistent with our definition of cultural attractiveness, we cannot assure that the observer also perceives the actual desirability the same way. In fact, prior research in cross-cultural psychology suggests that the perceptions of a national culture in the form of lay stereotypes may differ from the empirically-derived findings of the actual characteristics of that culture (Peabody, 1985; Smith, Bond, and Kagitcibasi, 2006). By confirming the positive relation between the cultural attractiveness measure and a country's reputation, we provide evidence for the validity of the cultural attractiveness measure. The confidence in the cultural attractiveness measure allows scholars to employ the measure to study a wide range of international strategy phenomena in the future.

Managerial implications

This research also has implications for managers. Our findings show that a culture can be attractive to an observer irrespective of its differences. In other words, being culturally different is not necessarily negative. This insight can be useful in evaluating the fit between firms involved in cross-border mergers and acquisitions (M&As) or joint ventures (JVs). Whereas the traditional notion recommends caution and hesitation when cultural differences

are large, our concept suggests a complementary approach. Carefully examining the cultural attractiveness of the cultures involved can be just as critical as, if not more so than, considering the cultural differences when determining the success of the international business undertakings.

Limitations

This study has limitations. Similar to the cultural distance construct, the cultural attractiveness operationalization suffers from the assumption of spatial homogeneity (Tung and Verbeke, 2010), i.e. it does not account for differences between regional cultures within a country. While prior research suggests that national cultures are relatively homogeneous due to strong forces that maintain a shared culture even across different industries (Brodbeck *et al.*, 2004; Rokeach, 1973), within-country variations in culture can still be observed (Tung and Verbeke, 2010). As we use GLOBE scores to calculate cultural attractiveness, we are not able to incorporate regional differences.

Further, the use of aggregate FDI data prevents us from considering firm-level influences on MNE investments. Using national FDI patterns of MNE populations in line with prior research (e.g., Nachum and Zaheer, 2005; Siegel *et al.*, 2013) appears to be appropriate for our analysis as our research centers on country-level culture. However, doing so prevents us from considering firm-level effects such as firms' prior internationalization experience (Berry, 2006; Shaver, Mitchell, and Yeung, 1997) or firm-specific advantages (Makino, Isobe, and Chan, 2004; Rangan and Drummond, 2004).

Future research directions

The findings and main ideas of our study pose a number of interesting directions for future research. Different measures and concepts can be developed to improve and extend the

cultural attractiveness construct. We used the GLOBE study's cultural scores to calculate cultural attractiveness. While this measure immediately gives scholars the opportunity to study cultural attractiveness across 62 societies, other measures may be constructed to refine the operationalization. One possibility is to collect data using surveys and interviews to examine the perceived cultural attractiveness of a culture. Surveys can also help to uncover within-country differences in cultural attractiveness, whereby overcoming the assumption of spatial homogeneity. Besides exploring alternative ways to measure cultural attractiveness, there may yet be other perspectives and constructs beyond cultural attractiveness and cultural distance that have been neglected altogether. Identifying and developing these novel perspectives can be a promising way to extend existing cultural frameworks and help advance the field of international strategy (Lee *et al.*, 2008; Leung *et al.*, 2005).

The cultural attractiveness concept can be used to challenge and refine management theories that are based on the hurdle premise of culture, such as transaction cost economics (Hennart, 1982; Hennart and Reddy, 1997) and the Uppsala process model of internationalization (Barkema *et al.*, 1996; Johanson and Vahlne, 1977) as discussed above. Cultural attractiveness may further be helpful to examine a large variety of international management and strategy phenomena in which different cultures come into contact. Cultural attractiveness can be applied to study a variety of international strategy topics including cross-border M&As, international JVs, foreign entry mode choice, cross-cultural knowledge transfer, and international human resource management. It can be used as both, an alternative or a complement, to the existing cultural distance construct. While some issues are best addressed with the help of the cultural distance construct, other questions may be best attended to with the cultural attractiveness construct. For even other issues cultural attractiveness and cultural distance can be used as complementary sources of explanations.

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TABLES

Table 1

Variable definitions and sources.

Variable	Definition	Data source
Log (FDI flows + 1)	Log of FDI flows in host country + 1 (in US dollars)	OECD Statistical Compendium
Cultural attractiveness	Cultural attractiveness of host country	GLOBE project
Kogut/Singh index	Cultural distance between home and host nation cultural values (higher value indicates larger distance)	Kogut and Singh (1988); Hofstede (1980)
Ronen/Shenkar cluster	Membership of the home and host country in the same cultural cluster (0/1 dummy)	Ronen and Shenkar (1985, 2013)
Log product of home-host GDP	Log product of home country GDP and home country GDP (in US dollars)	World Bank's WDI
Log geographic distance	Log of great circle geographical distance between home and host county (in km)	www.cepii.fr
GDP per capita growth	GDP per capita growth rate of host country (in %)	World Bank's WDI
Tax haven status	Tax haven status of host country (0/1 dummy)	Hines and Rice (1994)
Political constraint	Political constraints index of host country based on veto points (higher value indicates tighter control and constraint over decisions)	Henisz (2000); www.management.wharton.upenn.edu/henisz/
Common language	Common language spoken in home and host nation (0/1 dummy)	CIA's World Factbook
Colonial ties	Common colonial historical link between home and host nation (0/1 dummy)	CIA's World Factbook
Legal origin	Common legal origin of home and host nation (0/1 dummy)	La Porta *et al.* (1999)

Table 2

Cultural attractiveness between 10 OECD member countries based on GLOBE scores.

Observing country		Cultural attractiveness of									
		AUS	CAN	FRA	DEU	ITA	JPN	NLD	ESP	GBR	USA
Australia	(AUS)	.	15.14	14.13	13.51	14.05	14.75	14.78	14.27	14.47	14.72
Canada	(CAN)	14.53	.	13.99	13.37	14.01	14.16	14.46	14.13	14.27	14.55
France	(FRA)	14.95	15.33	.	13.72	14.02	15.28	15.00	14.23	14.66	14.83
Germany	(DEU)	14.47	14.86	13.83	.	13.93	14.88	14.52	13.81	14.17	14.43
Italy	(ITA)	14.30	14.73	13.75	13.09	.	14.58	14.37	13.52	14.06	14.06
Japan	(JPN)	15.20	15.36	14.71	14.42	14.28	.	15.13	14.61	14.82	15.27
Netherlands	(NLD)	14.56	14.95	13.90	13.34	13.96	14.80	.	13.84	14.25	14.52
Spain	(ESP)	14.30	14.83	13.76	13.35	13.32	14.50	14.57	.	14.23	14.07
United Kingdom	(GBR)	14.91	15.23	14.27	13.65	14.09	14.89	14.84	14.32	.	14.87
United States	(USA)	14.83	14.95	14.18	13.69	14.04	14.37	14.79	14.44	14.45	.

Cultural attractiveness: mean = 14.34; standard deviation = 0.54.

Table 3

Cultural attractiveness and country reputation.

Panel A: Variable definitions and sources		
Variable	Definition	Data source
Reputation	Country reputation (0–100) (higher value indicates better reputation)	Reputation Institute
Cultural attractiveness	Cultural attractiveness of rated country	GLOBE project
Kogut/Singh index	Cultural distance between rated and rater nation (higher value indicates larger distance)	Kogut and Singh (1988); Hofstede (1980)
Ronen/Shenkar cluster	Membership of the rated and rater country in the same cultural cluster (0/1 dummy)	Ronen and Shenkar (1985, 2013)
Common language	Common language spoken in rated and rater nation (0/1 dummy)	CIA's World Factbook
Colonial ties	Common colonial historical link between rated and rater nation (0/1 dummy)	CIA's World Factbook
Legal origin	Common legal origin of rated and rater nation (0/1 dummy)	La Porta *et al.* (1999)
GDP growth	GDP growth of rated country (in %)	World Bank's WDI
GDP per capita	GDP per capita of rated country (in US dollars)	World Bank's WDI
Geographic distance	Great circle geographical distance between rated and rating county (in km)	www.cepii.fr
Population	Total population of rated country	World Bank's WDI
Political constraint	Political constraints index of rated country based on veto points (higher value indicates tighter control and constraint over decisions)	Henisz (2000); www.management.wharton.upenn.edu/henisz/
Crime rate	Homicide rate in rated nation (per 100,000 population)	United Nations Office on Drugs and Crime
Military spending	Military expenditure of rated country (% of GDP)	World Bank's WDI

Panel B: FGLS estimation results, 2009–2013			
	Model 1	Model 2	Model 3
Cultural attractiveness	2.203***	2.196***	2.157***
	(0.222)	(0.222)	(0.221)
Kogut/Singh index		-0.431†	
		(0.252)	
Ronen/Shenkar cluster			1.691***
			(0.412)
Controlling for common language, colonial ties, legal origin, GDP growth, GDP per capita, geographic distance, population, political constraint, crime rate, military spending, time dummies			
Observations	1,085	1,085	1,085
Country-dyads	247	247	247
Wald (chi2)	2,560.10***	2,569.92***	2,616.83***

Standard errors are in parentheses. †$p < 0.1$; *$p<0.05$; **$p<0.01$; ***$p<0.001$.

Table 4

Correlation matrix.

		Mean	Std. dev.	1	2	3	4	5	6	7	8	9	10	11
1	Log (FDI flows + 1)	17.57	5.44	1										
2	Cultural attractiveness	14.36	0.54	0.035	1									
3	Kogut/Singh index	7.74	6.01	-0.174	0.097	1								
4	Ronen/Shenkar cluster	0.18	0.39	0.183	-0.013	-0.458	1							
5	Log product of home-host GDP	53.88	1.92	0.489	-0.015	-0.123	-0.035	1						
6	Log geographic distance	7.95	1.16	-0.277	0.318	0.051	-0.167	0.133	1					
7	GDP per capita growth	2.23	2.13	0.034	0.108	0.012	0.016	-0.076	-0.029	1				
8	Tax haven status	0.10	0.30	0.013	0.169	-0.090	-0.002	-0.203	-0.137	0.123	1			
9	Political constraint	0.47	0.09	-0.007	0.152	0.051	-0.035	-0.013	-0.048	-0.082	0.218	1		
10	Common language	0.12	0.32	0.179	0.126	-0.388	0.640	0.056	-0.008	-0.005	0.131	-0.068	1	
11	Colonial ties	0.06	0.24	0.141	0.077	-0.211	0.338	0.134	0.073	0.033	-0.034	-0.138	0.462	1
12	Legal origin	0.26	0.44	0.130	-0.154	-0.426	0.693	0.003	-0.147	-0.009	-0.030	-0.046	0.498	0.251

Notes: 5,617 observations. Correlations ≥ 0.021 or ≤ -0.021 are significant at the 0.05 level.

Table 5

Effect of cultural attractiveness on FDI flows, 1985–2008, FGLS estimation results.

	Model 1	Model 2	Model 3	Model 4
Cultural attractiveness		0.819***	0.845***	0.789***
		(0.064)	(0.064)	(0.064)
Kogut/Singh index			-0.249***	
			(0.063)	
Ronen/Shenkar cluster				0.380***
				(0.057)
Log product home-host GDP	3.861***	3.864***	3.818***	3.911***
	(0.078)	(0.077)	(0.077)	(0.077)
Log geographic distance	-1.602***	-1.824***	-1.830***	-1.766***
	(0.051)	(0.053)	(0.053)	(0.053)
GDP per capita growth	0.537***	0.285†	0.291*	0.259†
	(0.147)	(0.147)	(0.147)	(0.146)
Tax haven status	0.319***	0.227***	0.196***	0.273***
	(0.058)	(0.058)	(0.058)	(0.058)
Political constraint	-0.037	-0.378**	-0.361*	-0.418**
	(0.141)	(0.142)	(0.141)	(0.141)
Common language	0.529***	0.376***	0.329***	0.173*
	(0.064)	(0.065)	(0.066)	(0.071)
Colonial ties	0.125**	0.108*	0.103*	0.085†
	(0.048)	(0.048)	(0.048)	(0.048)
Legal origin	0.100	0.273***	0.193**	-0.017
	(0.068)	(0.069)	(0.071)	(0.081)
Observations	5,617	5,617	5,617	5,617
Dyads	362	362	362	362
Wald (chi2)	3,740.20***	4,012.12***	4,039.21***	4,087.66***

Estimation with time dummies.

Standard errors are in parentheses.

†p <0.1; *p<0.05; **p<0.01; ***p<0.001.

Table 6

Comparing the effects of cultural attractiveness and cultural distance on FDI flows.

	Coefficient	Chi-square (1)
Cultural attractiveness (Model 3)	0.845	
Kogut/Singh (1988) index	-0.249	
|Cultural attractiveness| > |Kogut/Singh index|		49.41***
Cultural attractiveness (Model 4)	0.789	
Ronen/Shenkar (1985, 2013) index	0.380	
|Cultural attractiveness| > |Ronen/Shenkar index|		21.33***

*p<0.05; **p<0.01; ***p<0.001

APPENDIX: METHODOLOGY EMPLOYED TO COLLECT COUNTRY REPUTATION
DATA

The Reputation Institute conducted surveys in the Group of Eight (G8) countries consisting of the world's largest eight economies with high and very high Human Development Index (HDI), i.e. Canada, France, Germany, Italy, Japan, Russia, the United Kingdom and the United States of America (Berens *et al.*, 2011). Samples were obtained from online consumer panels in each G8 country. Consumers in the G8 countries were asked to rate the reputation of up to two countries that they are familiar with. A 4-item measure is used to assess the bilateral reputation and perception of countries. The items were measured on a 7-point scale and were then converted to a 0–100 scale. The items used are:

We would now like you to give us your impressions of [COUNTRY]. Below, we provide you with a variety of descriptions. Please tell us how well you believe they describe [COUNTRY]. Share your impressions of [COUNTRY] based on both your personal experience and anything you have read, seen, or heard. Please enter a number from "1" to "7" where "1" means "I strongly disagree" and "7" means "I strongly agree".

Item 1:	[COUNTRY] has a good reputation
Item 2:	I have a good feeling about [COUNTRY]
Item 3:	I admire and respect [COUNTRY]
Item 4:	I trust [COUNTRY]

We calculated the average reputation scores for each country-dyad. We included the 34 rated countries with high or very high HDI, for which we were able to calculate cultural attractiveness scores. We included those countries with higher HDI to mirror the economic development of the G8 member countries (United Nations, 2014), as the positive/negative perception towards another culture may result from differences in economic status between

the rated and rater country (Brannen, 2004) rather than congruencies between cultural values and practices. 153,547 respondents from the G8 countries rated the 34 countries on their reputation between 2009 and 2013. Total number of respondents ranged between 52 and 1,857 for the country-dyads examined. To establish measurement equivalence across nations, we calculated the reliability of the reputation measure for each country-dyad. The reputation measure has reliabilities of 0.82 and higher for all dyads we included, which are above the recommended reliability criterion of 0.60 and higher (Cohen *et al.*, 2003).