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## Article

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## Foreign Direct Investment Determinants among Polish Companies: Greenfield Investments vs. Acquisitions

Małgorzata Jaworek, Włodzimierz Karaszewski, Małgorzata Szałucka

### Abstract

**Purpose of the article:** The purpose of this article is to identify FDI determinants that drive investment among Polish companies depending on their establishment mode choice (greenfield investment vs acquisition).

**Methodology/methods:** Article presents selected results of these authors' own research conducted as part of Research Project No. N N112 322338 entitled "Investment Activity of Polish Enterprises Abroad – Factors and Effects", financed by the Ministry of Science and Higher Education. 64 companies (out of 622), which implemented a total of 279 FDI, participated in this research. The majority of these investors (57%) decided to invest their capital abroad in the form of greenfield-investments, nearly 21% only made acquisitions, and 22% undertook both greenfield-investment and acquisitions.

**Scientific aim:** Increase in knowledge.

**Findings:** Market-seeking determinants were the most important factors in the Polish direct investors' decision making process on investing abroad, regardless of the establishment mode choice (greenfield investments vs. acquisitions). Within this group of determinants, Polish investors have most frequently indicated "new market" as the most important factor.

**Conclusions:** The study points to the fact that market-seeking factors explain most of the FDI undertaken by Polish firms. Resource seeking and efficiency seeking factors, falling in the category of economic factors, turned out to be of less importance for investors from Poland. Nevertheless, there were more significant differences in responses from the two groups of Polish investors among resource seeking factors.

**Keywords:** foreign direct investment, FDI determinants, FDI establishment modes, greenfield investments, acquisitions, Polish enterprises

**JEL Classification:** F21, F23

## Introduction

Entrepreneurship in Poland provides more and more examples which confirm that international success does not necessarily depend on decades of operating in the international environment. As a matter of fact, it was changes in the Polish economic system that have paved the way for Polish enterprises to investments, which in turn enabled them to conduct business operations abroad. In a relatively short period of just over 25 years, this group of FDI enterprises kept growing. With the increase in the number of completed foreign projects, in the form of both greenfield investments and acquisitions, the value of Polish foreign investments increased. The signals that suggested a good economic condition of many Polish enterprises who owned direct investment companies abroad will motivate them to intensify their internationalization processes and encourage direct investment abroad among those Polish companies that have so far only operated locally.

The benefits of foreign direct investment are one of the reasons researchers devote particular attention to the subject of FDI determinants (Sandhu, Gupta, 2016, p. 84).

The purpose of this article is to identify FDI determinants that drive investment among Polish companies depending on their establishment mode choice (greenfield investment vs acquisition).

The following research hypotheses guided the direction of this study.

H1: Regardless of the establishment mode choice, market seeking determinants were the most important for Polish investors.

H2: Resource seeking determinants were more important for those Polish investors who made foreign acquisitions than for investors who made greenfield investments abroad.

## 1. Conceptual framework

In the literature of the subject, there is generally no distinction between the motives

based on the FDI establishment mode choice. It seems, however, that some motives are particularly significant for acquisitions, and what is more – they can only be fulfilled via acquisitions (Jaworek, 2013, p. 52). International acquisitions are often dictated by the motivation to take over strategic assets or gain access to them (Blonigen, 1997, pp. 450–451; Kogut, Chang, 1991, p. 411).

The literature on the factors that influence foreign direct investment is so extensive that a full comprehensive review is simply not feasible (Blonigen, 2005, p. 1; Demirhan, Masca, 2008). Many studies also highlight the multidimensional nature of determinants underlying the decision to undertake foreign direct investment. It must be stressed at this point that the decision to make these investments is influenced by many factors (Athukorala, 2009, pp. 365–408; Mottaleb, Kalirajan, 2010, p. 2). Some studies on FDI determinants take a macroeconomic perspective, meaning that they focus on the relationship between the size of individual macroeconomic variables describing a given economy and the inflow of foreign direct investment (Schneider, Frey, 1985; Wheeler, Mody, 1992; Tsai, 1994; Loree, Guisinger, 1995; Wei, 2000; Hausmann, Fernandez-Arias, 2000; Asiedu, 2002; Demirhan, Masca, 2008; Kowalewski, Radło, 2014; Le Hoang Ba Huyen, 2015). Others, however, are based on surveys conducted among companies that had undertaken foreign direct investment (Wilson, 1990; Tatoglu, Glaisher, 1998; Bitzenis, 2007; Jaworek, 2013, pp. 59–63; Gorynia *et al.*, 2015).

In the literature of the subject, there are various proposals for the division of the determinants that impact a company's business activity abroad. One of them is the division of the motives into five groups: market seeking, raw material seeking, productivity seeking, knowledge seeking and political security seeking motives (Hogue, 1967, pp. 1, 2; Nehrt, Hogue, 1968, pp. 43, 48). A similar division was applied by H. Baumann, who

divided all FDI motives into four groups: market and sales motives, cost or revenue motives, procurement motives and political motives (Baumann, 1977, pp. 5–9). The internationalization motives can also be assigned to four groups of factors: market, cost, competition and government motives (Yip, Hult, 2012).

An interesting division was made by Albaum *et al.* (2002, p. 40), who attributed the motives to four groups: reactive external, reactive internal, proactive external, proactive internal. The last group includes motives related to management ambitions. While the motives that belong to the first three groups impact shareholders' wealth growth in the short and long term, managerial motives are sometimes in conflict with this core business objective. These motives have been reflected in a behavioral theory that explains why enterprises undertake FDI. This behavioral approach raises the question of a utopian assumption of full rationality, among other things, and points to the usefulness of the studies on limited rationality (Cyert, March, 1963). Providing a behavioral explanation of FDI decisions was undertaken by Aharoni (1966, p. 45–46). Given the fact that the decision on FDI is most often taken by the management, he pointed out that the motives for these decisions should be sought in the management's attitudes and experience, especially in the pursuit of their own particular goals. This idea was further developed by other authors (Jansen, Meckling, 1976, pp. 305–360; Buckley, 2002, p. 16; Eun, Resnick, 2012, p. 422), who also pointed out that the explanation of FDI motives should be sought in the attitude of the management. It must be stressed, however, that the role of behavioral approach described in the literature of the subject is not confirmed by empirical study results in this case as the conclusions are often based on respondents' declarative answers.

Another frequently quoted classification of FDI determinants groups them into three

sets: institutional and legal factors, economic determinants, factors that are the responsibility of countries and regions (Dunning, 2006, p. 206; UNCTAD, 1998, p. 109; Dunning, Lundan, 2008, pp. 99–100). The first set includes tax and trade policies, rules governing the structure and functioning of the market as well as economic, political and social stability. Economic determinants divide FDI into resource seeking, market seeking, efficiency seeking and strategic asset seeking investments. Business facilitation factors that depend on host countries and regions can be divided into investment promotion, investment incentives and social facilities. This classification was adopted in the study, the results of which are presented in this paper. It also took into account the establishment mode choices.

The identification of determinants that influenced the choice between the two alternative establishment mode choices in the form of FDI (greenfield investment vs. acquisition) was also presented in the literature of the subject (Hennart, Park, 1993; Brouthers, Brouthers, 2000; Datta *et al.*, 2002; Werner, 2002; Larimo, 2003; Shimizu *et al.*, 2004; Brouthers, Hennart, 2007; Gorynia, 2007; Slangen, Hennart, 2007; Slangen, Hennart, 2008; Demirbag *et al.*, 2008; Demirbag *et al.*, 2009; Arslan, Larimo, 2011; Slangen, 2011; Kowalewski, Radło, 2014; Gorynia *et al.*, 2015). It is worth noting that the results of the research presented in these articles generally refer to corporations from highly developed countries. The originality of this paper is in the presentation of results of the authors' own empirical research, which identifies in detail FDI determinants among Polish companies while taking into account the establishment mode choice.

## 2. Data collection, method and sample

The results presented in this paper come from a study conducted between 2012 and 2015. It

covered 622 enterprises based in the Republic of Poland, which engaged their capital abroad through direct investment. All of them, regardless of their ownership of capital, had the status of Polish companies according to the current laws. The bulk of these companies held only Polish capital (61.7%). The remaining 38.3% were companies with foreign capital, with only 26.3% of them having solely foreign capital (26.3% with majority ownership and 42.1% with minority ownership). The number of enterprises in each group classified according to their type of business activity was different. Almost 40% of them conducted exclusively commercial operations. Enterprises that operated exclusively in the service sector accounted for 30% and those exclusively in production – only 5% of the total number of companies. The share of enterprises operating in all three: production, trade and services, was 19%.

The research sample was selected in a non-random way (target selection)<sup>1</sup>. The study used a direct interview method and was conducted by interviewers from a market research company using a standardized questionnaire developed by the research team. The part of the direct interview questionnaire which related to the research area described in this study contained only closed multiple choice questions but allowed the respondents to add their own options. 64 questionnaires were filled out correctly, which meant a return rate of 10.3%.

<sup>1</sup> Polish data protection laws prevent researchers from accessing the database of Polish companies that are foreign direct investors (such databases are owned by the Central Statistical Office and the National Bank of Poland). The method of selecting companies for a research sample and the lack of accurate identification of the structure of the examined population calls for caution when generalizing the above conclusions. There is no scientific basis for the generalization of conclusions based on the results obtained in the course of the study.

The companies that participated in the study had completed a total of 278 FDI projects. Out of these, 144 projects had been undertaken as acquisitions (51.8%) and 134 as greenfield investments (48.2%). The bulk of investors who chose acquisitions decided to buy part of the foreign company shares (96 projects), whereas 48 investors acquired all the shares in foreign companies.

Most investors participating in the survey decided to engage their capital in host country markets solely by investing from the ground up (37 out of 64 respondents indicated this establishment mode choice). 13 respondents indicated that they entered the market solely by purchasing part or all of the foreign company shares. The remaining 14 enterprises completed greenfield investment projects as well as made acquisitions of foreign companies. Research results presented later in this paper refer to two out of three groups considered in this survey: enterprises that have chosen only greenfield investments and those that entered foreign markets only via acquisitions. Excluding from the analysis those enterprises that made both foreign acquisitions and greenfield investments is dictated by the fact that it cannot be definitely said to what extent each of the establishment mode choices influenced their FDI determinants.

While analyzing the results of the study, a validity index was used, which had the following formula (Karaszewski, Sudol, 1997, pp. 17–18):

$$W = \frac{\sum_{i=1}^k n_i \cdot w_i}{k \cdot N}, \quad (1)$$

where:

$W$       importance indicator,  
 $i$         evaluation index,  
 $n_i$       the number of indications for a  
             given factor at the  $i$ -th position,  
 $k$         maximum rating on a scale of 1 to  
              $k$  (the order of the factors meant

assigning them ratings in reverse order),  
 $N$  the number of respondents who answered the question,  
 $w_i$  a rating corresponding to the location of the  $i$  factor.

Statistical calculations were performed using the IBM SPSS Statistics software version 21.0.0.1.

### 3. Results

Enterprises that participated in the study, regardless of their establishment mode choice, identified market seeking factors (belonging to a group of economic determinants) as the most important determinants of foreign direct investment. Only some minor differences were found in the position of some of the determinants of this group.

Table 1. FDI determinants among Polish enterprises.

FDI location determinants		Greenfield		Acquisition		
		Indicator	Position	Indicator	Position	
I. An institutional and legal framework		the tax system in the host country	0.67	10	0.62	10
		legal regulations governing business operations in the host country	0.68	9	0.64	8
		positive attitude to entrepreneurship	0.73	6	0.68	6
		regulatory stability	0.70	8	0.55	12
II. Economic determinants:	Market seeking	new markets	0.89	1	0.80	1
		proximity of existing markets	0.80	2	0.80	1
		low competitiveness among companies in the host country	0.71	7	0.69	5
		finding a niche market	0.76	4	0.64	8
		avoiding trade barriers	0.65	12	0.66	7
		pursuing clients	0.70	8	0.73	4
		favorable prospects of economic growth	0.80	2	0.74	3
	Resource seeking	availability of natural resources	0.43	19	0.53	14
		availability of workforce	0.65	12	0.64	8
		availability of materials, half-finished products (auxiliary services)	0.62	13	0.56	11
		access to new technology	0.55	16	0.53	14
	Efficiency seeking	the cost of natural resources	0.54	17	0.55	12
		the cost of labor	0.66	11	0.62	10
		the cost of materials, half-finished products (auxiliary services)	0.61	14	0.54	13
		property prices	0.58	15	0.62	10
		better use of own resources	0.77	3	0.75	2
		reducing operational risk	0.74	5	0.63	9
		benefits of replacing exports with production in the host country	0.53	18	0.51	15
	III. Business facilitation		positive attitude to entrepreneurship	0.73	6	0.68

Source: own study on the basis of survey results.



Among both groups of companies, market factors related to access to new markets were considered to be the most important factors (Table 1). In addition to this, investors who made only foreign acquisitions also ranked another market determinant first – “the proximity of existing markets”. It was also an important factor for investors who entered foreign markets in the form of greenfield investment and who ranked it second. It should be noted that the main direction of foreign expansion among the studied companies was Europe, where 97% of direct investment companies were established. Investors in both groups also evaluated similarly the importance of the factor associated with the economic growth prospects of the host country. This factor was ranked second among the companies that made greenfield investment and third among those who acquired foreign entities.

Investors who entered foreign markets exclusively via foreign acquisitions regarded pursuing clients as an important determinant of their investment decision (4<sup>th</sup> position). The situation was different among investors who entered foreign markets via greenfield investments – the factor was ranked 8<sup>th</sup>. It seems that this can be explained by a better understanding of clients’ first links with local companies. The evaluation of the factor connected with finding a niche market was the exact opposite. The companies that made a greenfield investment ranked this factor fourth whereas the companies that entered the host country markets via acquisitions ranked it eighth. This may mean that companies which undertook greenfield investments entered the foreign markets with products that were new to local markets.

The biggest difference in the market seeking determinants can be seen in the evaluation of the ability to avoid trade barriers. This factor was considered more important among the companies that made acquisitions (7<sup>th</sup> position vs. 12<sup>th</sup> position for greenfield investments). Higher ratings in the group of companies that made acquisitions may be

explained by the fact that in mature markets with significant entry barriers, the only possibility to enter the market and avoid the barriers is the acquisition of a foreign company. It must be stressed that all the market factors were ranked in the top 10 most important determinants of FDI regardless of the establishment mode choice. There was only one exception and only in the group of greenfield investors – namely avoiding trade barriers (12<sup>th</sup> position).

The above results may be considered to be indications that, regardless of the establishment mode choice, market seeking determinants, which belong to the group of economic determinants, were the most important factors for Polish investors.

When analyzing the responses connected to resource seeking determinants, it should be emphasized that they were considered more important by investors who had made foreign acquisitions. All four factors in this group were ranked higher by these investors. What is surprising, however, is that these factors were generally ranked lower in the hierarchy of importance among these FDI determinants. This is particularly surprising for companies that only made foreign acquisitions. This applies, among other things, to the factor connected with an access to new technologies – this determinant ranked 14<sup>th</sup>. Similar results were observed in the group of companies that had made only greenfield investments (16<sup>th</sup> position).

The literature indicates that acquisitions are often motivated by the prospect of acquiring resources, including modern technology and the know-how, of the acquired company. On the other hand, workforce turned out to be important for these foreign acquisitions and was ranked eighth compared to the 12<sup>th</sup> position for greenfield investments. This may suggest that acquiring workers with specific sets of skills was an important motive for foreign acquisitions. One of the difficulties for greenfield investments is to acquire qualified workforce in the local labor market. In

this case, the solution may be to take over a foreign company that provides almost immediate operational readiness without the need to recruit and train new employees.

The above results may indicate that resource seeking determinants were more important for those Polish investors who made foreign acquisitions than for investors who made greenfield investments abroad.

Among the efficiency seeking economic factors, the possibility to make a better use of own resources was ranked highest by Polish investors. Investors who made only foreign acquisitions ranked this factor second, while investors who had made exclusively greenfield investments ranked it third. This high evaluation of the above factor among the investors who invested from the ground up may be explained by their will to adjust the scale and the structure of the newly created company via FDI to the real needs of the investor. An optimal design of the technical and economic requirements enables a more efficient transfer of the investor's company ownership advantage and their subsequent use. On the other hand, one of the advantages of foreign acquisitions is the ability to make use of synergy effects, which leads to a better use of resources that are at an investor's disposal.

There were significant differences in the evaluation of the determinant related to reducing operational risk. Investors who made only greenfield investments ranked this factor fifth, while investors who only made acquisitions ranked it ninth. A lower ranking of this factor among the investors who acquired foreign companies may result from the fact that, on top of the risks that affect any form of FDI, investors making foreign acquisitions are also exposed to the risk of operational integration associated with the incorporation of an acquired company into its organizational structure. The acquiring company bets blindly on a product which includes the skills and resources of the acquired entity "packaged" in a specific organizational form.

The remaining efficiency seeking economic determinants, regardless of the establishment mode choice, were ranked much lower – 10<sup>th</sup> position and further down the list. These included: cost of natural resources (12<sup>th</sup> position for acquisitions vs. 17<sup>th</sup> position for greenfield investments), the cost of labor (10<sup>th</sup> position for acquisitions vs. 11<sup>th</sup> position for greenfield investments), the cost of materials and semi-finished products (13<sup>th</sup> position for acquisitions vs. 14<sup>th</sup> position for greenfield investments). It should be noted that within this group of determinants, the largest differences in indications were related to real estate prices (10<sup>th</sup> position for acquisitions vs. 15<sup>th</sup> position for greenfield investments). Investors who had taken over foreign companies ranked this factor significantly higher in the hierarchy of importance. This may be due to the fact that the property value constituted a small fraction of the total price paid for the company and thus the buyer did not feel the burden of its purchase unlike the investors who made greenfield investments. Investors from Poland also considered the benefits of replacing exports with production in the host country to be an important determinant.

In principle, there was no difference between the responses of the two studied groups of investors in relation to the FDI determinants from the "institutional and legal framework" group. Both groups of investors ranked "friendly attitude towards entrepreneurship" sixth – the highest position in this group of determinants. Legal regulations governing business operations in the host country turned out to be slightly less important for investors. Investors who had made only foreign acquisitions ranked this factor eighth, while investors who had undertaken only greenfield investments ranked it ninth. The tax system in the host country was evaluated equally by both groups of companies. This proves that the advantages associated with the ability to optimize the tax structure can be used to the same extent regardless of



the establishment mode choice. In this group of determinants, the only significant difference was in the evaluation of regulatory stability. Investors who had made greenfield investments attributed more weight to this factor and ranked it 8<sup>th</sup> compared to the 12<sup>th</sup> position attributed by foreign acquisitions.

On the other hand, a determinant from the “business facilitation” group was evaluated equally by the two groups of respondents (6<sup>th</sup> position). According to the investors, it is a factor that significantly influences the decision to invest in a particular country.

#### 4. Conclusion

Foreign direct investment is motivated by a number of factors, both internal and external, including an investor’s home country factors in the form of various FDI support programs as well as the host country location factors associated with business facilitation for foreign investors. However, as shown by the results of studies conducted worldwide (Wilson, 1990, p. 29; Demirbag *et al.*, 1995, pp. 35–51; Tatoglu, Glaisher, 1998, p. 214; Karaszewski, 2001, pp. 274, 280; Bitzenis, 2007, pp. 83–111; Jaworek, 2013, pp. 59–63; Gorynia *et al.*, 2015, p. 94; Shukurov, 2016, p. 87), confirmed by the study, the results of which are presented in this paper, it is market factors that play the most important role among all the determinants of foreign direct investment. This is regardless of the establishment mode choice (greenfield investment vs. acquisition). Resource seeking and efficiency seeking factors, falling in the category of economic factors, turned out to be of less importance for investors from Poland. Nevertheless, there were more significant differences in responses from the two groups of Polish investors among resource seeking factors.

When analyzing the differences between the determinants that accompany foreign acquisitions and greenfield investments, one

should not forget that some determinants are only observed in foreign investment in the form of acquisitions or gain greater importance. This is true with resource determinants. At times, accessing a foreign market in the form of FDI can only be possible in the form of acquisition. This is the case when entry barriers are very significant.

The interpretation of this study’s findings needs to be done in consideration of several limitations. Data protection laws in Poland prevent researchers from accessing the database of Polish companies which are foreign direct investors (such databases are owned by the Central Statistical Office and the National Bank of Poland). This has influenced the way companies were selected for the research sample and the structure of the investor groups studied. The study was also limited by the size of the study sample, which prevented the use of tests planned for this research procedure and resulted in the researchers being unable to generalize the results for the whole group of Polish foreign direct investors. The experience of the researchers, whose work is presented in this paper, is identical in this regard to the experience of other research teams. For many years, almost all scientific research centers in the world have found it difficult to encourage companies to participate in research and development projects (Wilson, 1990, p. 28). It seems that the problem is getting more and more widespread. Future studies on FDI determinants among Polish enterprises will strive to make use of statistics tools. In addition to this, future research may broaden the scope of factors to be evaluated as well as complete an analysis from a time perspective, including discussing the sectors in which investors operate.

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