THE IMPACT OF DISTANCE IN RELIGION BETWEEN COUNTRIES ON FOREIGN DIRECT INVESTMENT FLOWS FROM THE EUROPEAN UNION (EU) DIRECTED TO TURKEY AND POLAND

T. Mesut Eren
Istanbul Kultur University
Assist. Prof. Dr.
m.eren@iku.edu.tr

Abstract

This paper examines a controversial issue: whether the psychic distance stimulus in religion is a possible reason of differently inflowing FDI from EU-Countries directed to Poland and Turkey. The examination highlights that after the application of a regression model between the psychic distance measures and FDI stocks, we are not in the position of claiming this. The difference between the FDI stocks of Poland and Turkey should not be necessarily a result of the differences in religion. Other dimensions should be included to the investigation.

Key Words: Foreign direct investments, religion, psychic distance, Turkey, Poland

JEL Classification: F21, F23

1. INTRODUCTION

The purpose of this paper is to analyze the influence of religion dimension as a cultural distance on foreign direct investment (FDI) incoming from the European Union (EU) directed to Turkey and Poland until the end of 2011.

2. LITERATURE REVIEW

Psychic Distance was initially used by Beckermann in 1956 in his expedition of the importance of distance in determining the structure of Western European Trade. Johanson and Vahlne (1977) described Psychic distance by quoting the Uppsala School, as the sum of factors preventing the flow of information from and to the market. Examples are differences in language, education, business practices, culture, and industrial development.

Hofstede (1980) described distances between countries according to the specific differences in national cultures. Kogut and Singh (1988) developed an index for examining the similarities of cultural distance with psychic distance used by Uppsala school.

O'Grady and Lane (1996) proposed modifications to concept and measurement of psychic distance stimuli. They used the experiences of Canadian retailers entering United States as a close country to examine psychic distance concept in greater detail. The greater the cultural distance between the home and the foreign market, the greater is the psychic distance, thus the cultural distance is one of the most important determinant of psychic distance. Sousa and Bradley (2006) Dow and Karunaratna (2006) advanced new instrument in measuring psychic distance stimuli like levels of education, democracy and religion instead of Hofstede's composite scale of cultural dimension.

Håkanson and Ambos (2010) demonstrated by means of a survey that perceived psychic distance is influenced by a complex array of factors and cannot reliably be approximated by cultural distance alone.

Magnusson and Boyle (2009) tried to prove that significant psychic distance will be detrimental to the relationship in its early stages, where it may serve as an asset in later stages of the relationship.

Dow and Ferencikova (2010) extend the generalizability of the Dow and Karunaratna (2006) scales and support it as a significant predictor of FDI market selection and performance.

Tung and Verbeke (2010) claimed that some cultural distance dimensions and related scores for distance measures actually are affected by intra-national location elements. They also claim that cultural dimensions and measures do not fully capture psychic distance, which is really the key parameter affecting many managerial choices in an IB context.

Several other authors claim that cultural psychic distance is a more broader concept than cultural distance and that additional factors must be included in the analysis such as education Doytch and Eren (2012), industrial development and political systems, in order to be able to correctly understand it (Shenkar, 2001; Evans and Mavondo, 2002).

Finally, differences in religion may also be a source of uncertainty and transaction costs, since religion not only has an impact on economic growth (Barro and McCleary 2003) but can also be considered one of the principal sources of conflict (Triandis 2000). Religion also plays an undeniable critical role in the way in which a society communicates and interacts and even what kinds of behavior is desirable or tolerable (Shenkar 2001; Dow and Karunaratna 2006), thereby affecting firm's investment decisions (Martin et al. 2013). Therefore, I propose the following hypotheses:

H1: "The greater the psychic distance in religion between investor countries and Turkey, the lower the FDI flows".

H2: "The lower the psychic distance in religion between investor countries and Poland, the higher the FDI flows

3. DATA AND THE MODEL

In this section, I sketch a simple regression model to examine the effect of home-country religion on incoming FDI. Dependent variable is bilateral foreign direct investment stocks by the end of 2011, from 25 countries of EU (Except Malta and Cyprus) to Poland on one dataset and to Turkey on the other dataset. The religion dimension is calculated through 5 point scales developed by Dow, focused on differences between the dominant religion of any two countries, and the bilateral influence of each country's dominant religion on the other one. (See Dow 2011) Given limitations of space, the model makes a number of simplifying assumptions that produce a world where Poland and Turkey differ merely in their religion compared to the investing countries from the EU.

4. ANALYSIS

Building on the provided description of cultural distance, most studies have traditionally claimed that risk and transaction costs are increased by difficulties in learning about the host market and the higher possibility of erroneously understanding its specific idiosyncrasies and environment. A foreign investor should be familiar to some extent, with the pattern of beliefs and perceptions, attitudes, self-definitions, country specific ethic norms, values, horizontal and vertical relations in the society, and finally business habits that comprise cultural characteristics of a country. Otherwise, it is likely that greater cultural distance between investing countries and host countries will reduce the intensity of investment between them.

Since the dissimilarities between host countries and investing countries influence the location decisions of foreign investors; we can postulate that cultural similarities encourage FDI. Investments in countries with similar cultural identities will be preferred over those in other countries with dissimilar cultures. The effects of home country characteristics on location decisions of foreign investors can be inspected through the examination of FDI in target countries.

This article analyses one issue: the role of psychic distance in religion, one of the main components of host country characteristics as determinants of foreign direct investments that has so far not received much attention in literature. The impact of religion on foreign direct investments originating from EU-countries directed to Poland, as well as to Turkey. Contrary to Turkey, Poland belongs to the

mainstream religion, same religion family with all other EU-Countries. Theoretically an investor from an EU-Country would face acquainted environment in Poland. For that investor, doing business in Poland should be easier than doing business in Turkey. We can pick that from the following figures, since as of 2011, the accumulated amount of inward FDI of Turkey was 139 billion USD, during Poland's FDI stock was 198 billion USD at the same time.

5. RESULTS AND CONCLUSION

Although the coefficients of the psychic distance dimensions in religion is negative and not significant, it is not easy to predict whether the psychic distance in religion between investing countries and host countries plays a relevant role in incoming FDI, so we cannot validate or reject Hypothesis 1, and Hypotheses 2 due to the low R^2 values. So to conclude we can claim that after testing the hypotheses we can claim that the differences in the level of incoming FDI to Poland and Turkey from the EU-Countries, it does not necessarily stem from the psychic distance in religion. There must be other factors that influence the volume of incoming FDI from country to country differently.

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Annex: Model and Data

x denotes the value religion_f, y denotes FDI.

$$y=\beta_0+\beta_1 x$$

Dependent Variable: Y_POL
Method: Least Squares
Date: 04/14/13 Time: 15:05
Sample: 1 25
Included observations: 25

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	1796.312	2658.499	0.675686	0.5060
X_POL	-4025.434	2758.536	-1.459265	0.1580

R-squared	0.084739	Mean dependent var	5100.000
Adjusted R-squared	0.044945	S.D. dependent var	7130.205
S.E. of regression	6968.128	Akaike info criterion	20.61270
Sum squared resid	1.12E+09	Schwarz criterion	20.71021
Log likelihood	-255.6587	F-statistic	2.129454
Durbin-Watson stat	1.438616	Prob(F-statistic)	0.158016

Dependent Variable: Y_TUR
Method: Least Squares
Date: 04/14/13 Time: 15:18
Sample: 1 25
Included observations: 25

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	15580.93	6656.606	2.340672	0.0283
X_TUR	-10253.53	5468.845	-1.874899	0.0736

R-squared	0.132574	Mean dependent var	3237.040
Adjusted R-squared	0.094860	S.D. dependent var	5161.188
S.E. of regression	4910.294	Akaike info criterion	19.91267
Sum squared resid	5.55E+08	Schwarz criterion	20.01018
Log likelihood	-246.9084	F-statistic	3.515245
Durbin-Watson stat	1.928902	Prob(F-statistic)	0.073561

Country_i	Country_j	Relig_f	Country j's FDI in Country i (mill. Euro, Stocks)
Poland	Austria	-1,29153	4702
Poland	Belgium	-1,03204	4206
Poland	Bulgaria	-0,53052	44
Poland	Czech Republic	-0,77256	270
Poland	Denmark	-0,79	3059
Poland	Estonia	-0,27103	80
Poland	Finland	-0,79	1356
Poland	France	-1,03204	19051
Poland	Germany	-1,03204	20558
Poland	Greece	-0,79	723
Poland	Hungary	-1,03204	622
Poland	Ireland	-1,29153	898
Poland	Italy	-1,03204	8106
Poland	Latvia	-0,77256	25

Poland	Lithuania	-1,03204	-25
Poland	Luxembourg	-1,29153	15737
Poland	Netherlands	-1,03204	22956
Poland	Portugal	-1,03204	1238
Poland	Romania	-0,53052	19
Poland	Slovakia	-1,03204	244
Poland	Slovenia	-1,03204	80
Poland	Spain	-1,29153	8593
Poland	Sweden	-0,53052	9078
Poland	Turkey	1,277159	62
Poland	United Kingdom	-0,53052	5818
Country_i	**Country_j**	**Relig_f**	**Country j's FDI in Country I (mill.Euro, stock**
Turkey	Belgium	1,017674	4918
Turkey	Bulgaria	0,758188	2
Turkey	Czech Republic	1,277159	182
Turkey	Denmark	1,277159	248
Turkey	Estonia	1,277159	0
Turkey	Finland	1,277159	3418
Turkey	France	1,017674	5514
Turkey	Germany	1,017674	10284
Turkey	Greece	1,017674	3413
Turkey	Hungary	1,277159	14
Turkey	Ireland	1,277159	1200
Turkey	Italy	1,277159	2304

Turkey	Latvia	1,277159	0
Turkey	Lithuania	1,277159	0
Turkey	Luxembourg	1,277159	4905
Turkey	Netherlands	1,017674	23138
Turkey	Poland	1,277159	12
Turkey	Portugal	1,277159	190
Turkey	Romania	1,017674	6
Turkey	Slovakia	1,277159	0
Turkey	Slovenia	1,017674	0
Turkey	Spain	1,277159	5185
Turkey	Sweden	1,277159	253
Turkey	United Kingdom	1,017674	7391