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THE RELATIONSHIP BETWEEN INTERNATIONAL EXPANSION AND FIRM PERFORMANCE: AN INVESTIGATION OF U.S.-BASED RESTAURANTS FIRMS

By

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2003

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PART ONE

INTRODUCTION

Background of the Study

With the increasing trend of globalization, service industries are rapidly expanding into the international market. With no exception, many U.S.-based restaurants are expanding beyond the home country despite the risks. For example, Starbucks Coffee Company opened 1,672 net new stores in the international market in fiscal 2005 alone (Starbucks, 2005). Why is international expansion important? A company can grow by exploiting overseas market opportunities and imperfections through internationalization (Rugman, 1979, 1981) and growth has a positive impact on the firm performance. In short, international expansion can be profitable to companies. Moreover, why is the relationship between international expansion and firm performance important? Ultimately, a company's performance is the objective and outcome of the company. A company's value can be enhanced by increasing cash flow, decreasing risk, or both. International diversification is one of the ways to increase cash flow by increasing revenue. More specifically, the association between international diversification and firm performance is a significant subject not only for academics who have struggled with drawing a clear findings, but also for company managers who consider (1) expanding their stores into the international market (2) finding out the optimal point for mature multinationals. As a result, extensive research has been done on the effect of international diversification on firm performance (e.g., Buhner, 1987; Gomes &

Ramaswamy, 1999; Grant, 1987; Hitt, Hoskisson, & Kim, 1997; Kotabe *et al*., 2002; Tallman & Li, 1996).

Problem Statement

Despite the rapid growth and size of international expansion in service industries, academic research on examining the relationship between international expansion and firm performance in service firms is still in the initial stages (Kotabe *et al*., 1998; Murray & Kotabe, 1999). Early studies have focused on other aspects of the internationalization process of service firms such as foreign market entry mode (e.g., Erramilli & Rao, 1993), determinants of foreign direct investment (e.g., Li & Guisinger, 1992), and sourcing strategies of multinational enterprise (MNE) in service industries (e.g., Murray & Kotabe, 1999).

Meanwhile, the link between overseas investment and firm level financial performance has been an important topic for researchers in the manufacturing industries (e.g., Hitt *et al*., 1997; Gomes & Ramaswamy, 1999; Kotabe *et al*., 2002). Although previous studies have proposed a positive effect of multinationality on performance, empirical research has not been able to provide conclusive findings on the association between international diversification and corporate performance (cf. Geringer, Beamish, & daCosta, 1989; Rugman, 1979). Ramsawamy (1995) stated that "a clear understanding of the impact of international expansion on organizational performance still remains elusive". Prior studies have shown four conflicting findings: (1) a positive linear relationship, (2) a negative linear or no relationship, (3) a U-shaped relationship (which indicates that an initial stage of international expansion results in the negative effects on

performance, before the positive effects of international expansion are returned), and (4) an inverted U-shaped relationship (which indicates that international expansion increases company performance up to an optimal level, and again results in a negative slope on performance). Furthermore, early research has mostly examined the manufacturing industry (Habib & Victor, 1991). Due to the unique characteristics of service industry -- intangibility, inseparability, heterogeneity and perishability --, this study argues that the overall relationship between international diversification and firm performance in service industries possibly differs from the association in manufacturing industries.

Purpose of the Study

This study has three objectives. First, based on the above argument, this study aims to examine whether there is an association between international expansion and U.S.-based restaurants performance in terms of accounting-based measures. Second, this study intends to examine how the performance of service firms will indeed change within an observed time frame of international expansion. Finally, the research hopes to provide insights and assistance both to academics and to company strategists who are in charge of the international operations of service firms.

Organization of the Study

The paper is organized as follows. Part 1 provides the background of the study along with the significance and purpose of the study. Part 2 provides a theoretical background and extensive literature review of the international diversification-performance relationship and discusses the difference between manufacturing industry

and service industry. Finally, Part 3 describes the sample, data, variables, and research methods used in the empirical part of this study. In addition, Part 3 draws the main conclusions with a discussion of the managerial and theoretical implications, limitations of the study and suggestion for future research.

PART TWO

THORETICAL BACKGROUND

Introduction

This part will provide a theoretical background for the definition, purpose, and advantages of international expansion, and discuss how service industries differ from manufacturing industries and the implications of the differences. Moreover, this part will review previous studies that have thoroughly done but there has been a lack of conclusive results in terms of the association between international expansion and firm performance.

The Definition of International Expansion

Hitt *et al*. (1997) defined international diversification as expansion across the boundaries of geographical regions and countries into different global locations, or market. Capar and Kotabe (2003) defined international expansion as a company's expansion beyond the boundaries of the company's home country across different nations and global regions. In other words, international expansion can be defined as a firm's growth practice beyond the physical borders of its home country across diverse countries and geographical areas. Terms such as international diversification, multinationality, and international diversity are often applied interchangeably in academic research (Capar & Kotabe, 2003).

Why Manufacturing Companies Expand Internationally

Manufacturing firms seek an international expansion strategy for the purpose of taking advantage of diverse benefits through international expansion. Essential advantages of international diversification are as follows:

1. Market opportunities for greater growth
2. Economies of scale, and geographic scope
3. Sharing core competencies
4. Global sourcing

First, Buhner (1987) argued that international expansion provides firms with potential market opportunities for growth. In particular, when the stage of the industry life-cycle is mature, and/or competitions is severe in a domestic market, MNE firms can gain market opportunities by exploiting market imperfections in less saturated and less competitive foreign markets. Less saturated foreign markets provide companies with ways to expand distribution and achieve market share (Dunning, 1993). In addition, enormous market opportunities for greater growth lie around the world. According to World Population to 2300 published by the United Nations (2004), 97 percent of the world's population and 75 percent of its purchasing power is outside of the U.S.

Second, MNE firms could gain from economies of scale and geographic scope (Barlett & Ghoshal, 1989; Grant 1987; Kim *et al*., 1989). By integrating a critical resource such as R&D across nation boundaries, MNE firms can have greater opportunities to achieve optimal economies of scale. Economies of scale and geographic

scope allow companies to have various cost differentiation advantages such as arbitrage potential (Contractor *et al*, 2003), bargaining power (Sundaram & Black, 1992), and better cross-subsidization (Contractor, 2002). Economies of scale also allow firms to increase their efficiency, learning and innovation (Kochhar & Hitt, 1995).

Third, a firm with strong core competencies at its domestic market can exploit and apply its core competencies among different business segments and geographic markets (Bartlett & Ghoshal, 1989). Porter (1990) suggested that the competitive advantages that generate profitability in home markets stimulate the company to apply the same competences in international markets to further enhance a firm's profitability. Furthermore, the resources applying among a firm's multiple international operations facilitate utilization of core competences to produce synergy (Grant, Jammine, & Thomas, 1988). Simply stated, the more a firm adopts international diversification, the higher the firm exploits its tangible and intangible resources, which is expected to lead to improved performance (Hymer, 1976).

Lastly, MNE firms have access to a variety of global sourcing such as cheaper labor, better qualified workforce, more advanced technology, country-specific resource (Jung, 1991), and greater know – how or international experience (Kobrin, 1991).

Why Service Companies Expand

Boddewyn et al. (1986) argued that theories developed for explaining the performance of MNE manufacturing firms could be applied to MNE service firms. In fact, service firms seek the international expansion strategy for the similar reasons as manufacturing firms: market access, resources, and labor cost, among others (Guile,

1988). Consequently, it can be argued that the fundamental theoretical rationale should be the same (Boddewyn *et al*., 1986; Dunning, 1989; Li & Guisinger, 1992). Dunning (1989) contended that geographic diversification in service markets provides benefits from economies of scale throughout the value chain process. Likewise, Campbell and Verbeke (1994) suggested that MNE service firms could take advantages of economies of scale in marketing activities. However, these discussions assume that just like manufacturing firms, service firms would incur certain fixed costs that have no relationship to a firm's outputs (Katrishen & Scordis, 1998).

Characteristics of Service firms vs. Manufacturing firms

Despite the similar motivations of service firms to expand internationally, there are also some differences between manufacturing and service firms (Capar & Kotabe, 2003). In the extensive literature on services, a lot of elements are used to define them: intangibility (a reservation by telephone call), perishability (a limousine ride), customization (a first class lounge for VIP customers), simultaneity of production and consumption (a check in /out at the hotel), consumer participation in production (food order processing), and use without a ownership (a car rental) (Boddewyn *et al*., 1986). Because of these characteristics of service, service firms have more intangible assets or sales which are probably hard to measure precisely compared to tangible assets or sales. Consequently, it can be argued that the relationship between international diversification and performance in service firms is somewhat different than that in manufacturing firms.

The Service Sector

Before beginning the study, the fact that substantial differences exist even in the service sector in terms of capital intensity and knowledge intensity should be acknowledged. Contractor *et al*. (2003) categorized the services into the two sectors: the capital-intensive service sector and the knowledge-based service sector. While the capital-intensive service sector employs a "seek-the-market" strategy, the knowledge-based service sector employs a "follow-the-client" strategy which implies it has clients already established (Contractor *et al*., 2003). Furthermore, Boddewyn *et al*. (1986) classified service sector into three bounds: the foreign-tradeable service, a location-bound service, and combination services. The foreign-tradeable service, which is similar to the knowledge-based service, creates a product that is separable throughout the whole process from production to consumption as well as transportable across different countries- for instance, financial loans. On the other hand, a location-bound service, which is similar to the capital-intensive service, is stuck to the production place since its time and space are shared by producer as well as consumer- for instance, hotel accommodations. Lastly, combination services are literally a combination of the foreign-tradeable service and a location-bound service.

In essence, knowledge-based service sectors (accounting, legal services, advertising, and market research) are more affected by intangible assets, have a much lower fixed capital cost, and have a lower cost per entry based upon a global standardization. By contrast, for capital-intensive service sectors (air transport, hotels/casinos, and restaurants/fast food chains), the fixed capital investment cost is much higher and a larger size is required before the net benefits of expansion are generated

(Contractor *et al*., 2003). Contractor *et al*. (2003) argued that knowledge-based services enable the positive benefits of foreign expansion to be reaped faster than capital-intensive sectors. As seen below, Table 1 presents a comparison between knowledge-based and capital-intensive service sector in sum.

Although these classifications are not ideal practices, this exercise has significant research implications. Since capital-intensive services probably require foreign direct investment or alternative non-equity forms of international product from the very beginning and the process of the production-delivery-use chain must be performed abroad, a comparison of knowledge-based services vs. capital-intensive services is not suitable (Boddewyn *et al*., 1986). As this study will empirically investigate the sample of restaurants and fast food chains which are capital-intensive, the result of this study will possibly be different from a study in another service sector in terms of the relationship between performance and expansion.

Table 1 *Comparison of Service Sectors*

	Knowledge-based Service Sector	*Capital-based Service Sector*
Classification	Foreign tradeable service	Location bound service
Strategy	Follow the client	Market seeking
Characteristics	Lower fixed capital cost burden More driven by intangible assets	Higher fixed capital investment cost A larger global scale is required
Examples	Accounting, Legal service, Advertising	Hotels/casinos, **Restaurants/Fast food chains**

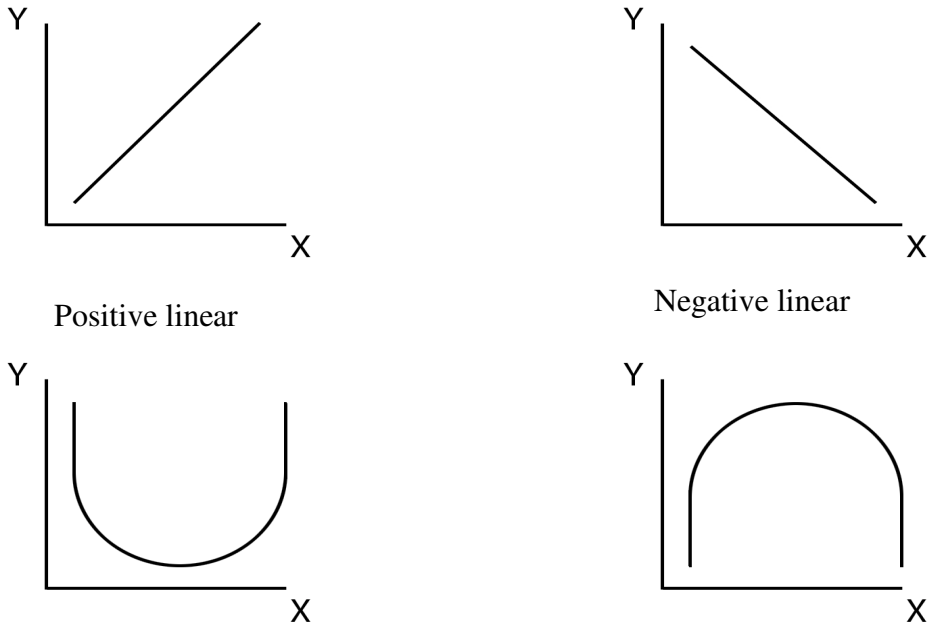
Previous Studies that link International Expansion and Firm Performance

Many prior studies have extensively examined the association between international expansion and firm performance. However, empirical studies have produced inconclusive results. Research has shown the relationship between international expansion and firm performance to four different shapes. There include:

1. Positive linear
2. Negative linear
3. U-shaped non-linear
4. Inverted-U-shaped non-linear

These four relationships are described in diagrams in Figure 1.

Figure 1 *Diagrams of Various Relationships from Previous Studies*



X: Expansion, Y: Performance

First, a positive linear relationship agrees with a growth theory of international business studies. The more a firm expands internationally, the better a firm's performance is (e.g., Daniels & Brackers, 1989; Jung, 1991; Grant, 1987; Haar, 1989). Second, a negative linear relationship implies that as a company expands abroad, it produces a negative effect on firm performance (e.g., Kumar, 1984; Siddharthan & Lall, 1982).

Third, a U-shaped non-linear relationship indicates that due to the barriers and costs to early international expansion, after the initial stage of international diversification there are negative effects on performance, and then positive effects of international expansion are returned later (e.g., Capar & Kotabe, 2003). It is suggested that initial

international diversification require firm to invest in learning about foreign markets. After that, the fixed costs and R&D investment can be spread over nations (Porter, 1985). The incremental benefits of more international diversification are now greater than the incremental costs of more diversification.

Lastly, an inverted U-shaped non-linear relationship indicates that international expansion strengthens company performance up to an optimal level resulting from the benefits of internationalization, and again results in a negative slope on performance caused by the operation costs and complication in managing widely scattered properties (e.g., Gomes & Ramaswany, 1999; Hitt *et al*., 1997; Kotabe *et al*., 2002; Tallman & Li, 1996). That is to say, even though the initial overseas growth generates moderately high levels of performance benefits due to the company's core competencies, the increasing complexities and costs associated with higher degree of multinationality eventually decrease the levels of performance. The following hypothesis summarizes these arguments:

> **Hypothesis:** The relationship between international expansion and performance in service firms will be inverted U-shaped nonlinear, with performance increasing up to an optimal level, beyond which higher levels of international expansion will lead to performance decline.

Table 2 indicates explanation of each relationship in short and Table 3 summarizes previous literature on the relationship between international expansion and firm performance.

Table 2 *Brief Explanation of Various Relationships*

Relationship	*Explanation*
Positive Linear	International Expansion ↑ → Performance ↑
Negative Linear	International Expansion ↑ → Performance ↓
U-shaped Non-linear	Due to the costs and barriers to initial I.E., negative up to a certain point And positive beyond the point resulting from benefits of internationalization
Inverted U-shaped Non-linear	Resulting from benefits of internalization, positive up to a certain point And negative beyond the point due to the incremental cost and complexity

Table 3 *Summary of Previous Literature that link Performance and Degree of Multinationality*

Relationship	*Author(s) and Year*	*Samples*	*Performance indicators*
Positive Linear	Errunza and Senbet (1981)	U.S. Multinationals	Excess return
	Grant (1987)	British Manufacturing	ROA, ROE, ROS
	Grant et al. (1988)	British Manufacturing	ROA, ROE, ROS
	Jung (1991)	U.S. Multinationals	(After-tax net income)/ (Total assets)
	Kim and Lyn(1987)	U.S. Manufacturing	Excess market value; Tobin's Q
	Vermon (1971)	U.S. Manufacturing	ROI, ROS
Negative Linear	Brewer (1981)	U.S. MNE, NATL	Stock return
	Collins (1990)	U.S. Firm	Total risk, Debt to equity ratio, Beta
	Michel and Shaked (1986)	U.S. Multinationals	Risk-adjusted return
	Siddharthan and Lall (1982)	U.S. Manufacturing	Sales growth
U-shaped Non-linear	Capar and Kotabe (2003)	German Service	ROS
	Qian (1997)	U.S. Firm	ROE
	Ruigrok and Wagner (2003)	German Manufacturing	ROA
Inverted U-shaped Non-linear	Daniels and Bracker (1989)	U.S. Firm	ROA, ROS
	Gomes and Ramaswany (1999)	Manufacturing	ROA, Operating cost/total sales
	Hitt, Hoskisson and Kim (1997)	Manufacturing	ROA

Conclusion

The literature discussing international expansion indicated that international diversification possesses both positive and negative effects on company performance. The point depends on when and how a company employs the international expansion strategy. This part provided a literature review for the definition, purposes, and merits of international expansion, discussed the differences between manufacturing and service industries in terms of international diversification. In addition, this section discussed inconclusive results which are four different relationships that link between international expansion and firm performance based upon previous studies.

Further understanding into the effect of international expansion on firm value can be gained through the quantitative review of MNE secondary data. The next part will describe the sample, data collection, and a variety of variables which will be used in the research.

PART THREE

METHODOLOGY

Introduction

For the purpose of empirically testing the curvilinearity hypothesis, this study will employ the sample of U.S.-based restaurants and fast food chains. Multiple regression analysis will be used in order to explore the association between multinationality and firm performance. The sample, data collection, explanations of each variable and the method respectively, will be presented in this chapter.

The Sample

A sample of U.S.-based service firms will be drawn from the Fortune 500 U.S. Service Firms list. To be included in the sample, a firm should (1) be a restaurant and/or a fast food chain among the service industry, (2) have at least 10 percent of its sales overseas, and (3) be either single or non-diversified business.

Restaurants and fast food chains will be chosen as the firms of interest. Gomes and Ramaswamy (1999) implied that this industry seems ideal since a large proportion of U.S.-based restaurants and fast food companies are currently operating as major players in the international hospitality industry. Among those U.S.-based restaurants and fast food chains, firms generating at least 10 percent of their sales overseas will be selected similar to many previous studies (Daniels *et al*., 1984; Geringer *et al*., 1989; Gomes & Ramaswamy, 1999; Habib & Victor, 1991; Stopford & Wells, 1972; Siddharthan & Lall, 1982). Finally, single and dominant non-diversified businesses will be chosen for the

purpose of preventing the potential effects that the type of diversification might have on performance results (Capar & Kotabe, 2003; Gomes & Ramaswamy, 1999; Hitt *et al*., 1997). As seen below, Table 4 presents the sample of U.S.-based restaurants and fast food chains.

Table 4

The Sample of U.S.-based Restaurants and Fast food chains

Rank by sales	*Companies*
1	McDonald's
2	KFC
3	Burger King
4	Pizza Hut
5	Subway
6	Wendy's
7	Starbucks
8	Taco Bell
9	Domino's Pizza
10	Applebee's Neighborhood Grill & Bar
11	Dunkin' Donuts
12	Tim Hortons
13	Chili's Grill & Bar
14	Sonic Drive-In
15	Outback Steakhouse
16	Arby's
17	T.G.I. Friday's
18	Jack in the Box
19	Dairy Queen
20	7-Eleven
21	Red Lobster
22	Olive Garden
23	Denny's
24	IHOP
25	Chick-fil-A
26	Papa John's
27	Hardde's
28	Cracker Barrel Old Country Store
29	Popeyes Chicken & Biscuits
30	Panera Bread
31	Ruby Tuesday

32	Quiznos Sub
33	Golden Corral Buffet & Grill
34	Carl's Jr.
35	Baskin-Robbins
36	The Cheesecake Factory
37	Bob Evans
38	Church's Chicken
39	HomeTown Buffet/Old Country Buffet
40	Little Caesars
41	Krispy Kreme Doughnuts
42	Whataburger
43	Hooters
44	Red Robin Gourmet Burgers
45	Ryan's Grill, Buffet & Bakery
46	Perkins Restaurant & Bakery
47	Long Jonn Silver's
48	Texas Roadhouse
49	Romano's Macaroni Grill
50	Waffle House
51	Panda Express
52	Boston Market
53	Bennigan's Grill & Tavern
54	P.F.Chang's China Bistro
55	Steak 'n Shake
56	LongHorn Steakhouse
57	Friendly's
58	Buffalo Wild Wings Grill & Bar
59	Chipotle
60	Checkers Drive-In/Rally's Hamburgers
61	Sbarro
62	O'Charley's
63	Carrabba's Italian Grill
64	California Pizza Kitchen
65	White Castle
66	Del Taco
67	Captain D's Seafood
68	Chuck E. Cheese's Pizza
69	CiCi's Pizza
70	Culver's Frozen Custar
71	El Pollo Loco
72	Lone Star Steakhouse & Saloon
73	Uno Chicago Grill
74	Bojangles' Famous Chicken 'n Biscuits
75	Shoney's
76	Logan's Roadhouse
77	Joe's Crab Shack

78	Wawa
79	On the Border Mexican Grill & Cantina
80	Krystal
81	Papa Murphy's Take 'N' Bake Pizza
82	Cold Stone Cremery
83	Circle K
84	Hard Rock Café
85	Ponderosa/Bonanza
86	Tony Roma's
87	Chster's
88	Johnny Carino's Italian
89	Ruth's Chris Steak House
90	In-N-Out Burger
91	Fazoli's
92	Sizzler
93	Round Table Pizza
94	Einstein Bros. Bagels
95	Village Inn
96	Jamba Juice
97	Baja Fresh Mexican Grill
98	Fuddruckers
99	Jason's Deli
100	Blimpie

Source: Restaurants & Institutions'2006 ranking of the Top 400 chains

The Data

The data used in the empirical analysis will be primarily gathered from various public information sources including Form 10-k, annual reports and directories. In addition to financial resources, the data will also use other information such as company demographics, company structure, and market size. These data will be collected and averaged for a five-year period between 2002 and 2006 in order to reduce random variation (Capar & Kotabe, 2003; Hitt *et al*., 1997).

Dependent Variable (Performance)

Three accounting-based profitability measures were initially taken into consideration as dependent variables: ROE (Return on equity), ROA (Return on assets) and ROS (Return on sales). Since ROE is more sensitive to capital structure differences, it will not be used in this study (Hitt *et al*., 1997). In addition, although many of the prior studies have used ROA to measure firm performance, ROA will not be employed in this study for the following reasons. Both ROA and ROS are highly correlated and thus, tend to produce similar findings (Contractor *et al*., 2003; Hitt *et al.,* 1997). In addition, Capar and Kotabe (2003) implied that service companies incline to hold larger portions of intangible assets than manufacturing companies, and the degree of intangible assets is likely to vary significantly across different service sectors (for example, knowledge-based firms vs. capital-based firms). Therefore, assets-based performance measures are less likely to consider this difference. Consequently, among these variables, ROS will be used as a dependent variable to examine the association between degree of international diversification and firm performance. ROS has been widely used in many previous studies (e.g., Capar & Kotabe, 2003; Grant, 1987; Haar, 1989). Moreover, ROS prevents the potential impacts of diverse asset valuations caused by depreciation (Contractor *et al*., 2003; Geringer *et al*., 1989).

Independent Variable (International diversification)

Multidimensional measures will be employed to measure the degree of international diversification. Sullivan (1994) argued that international diversification includes various factors and multinational companies are comprised of a

multidimensional construct. Ramaswamy *et al*. (1996) argued for the use of a single-item measure based upon problems that it might have with content validity, criterion validity, and reliability. Therefore, previous studies have applied composite methods to measure the degree of international expansion. The most generally used measures are the ratio of foreign sales to total sales (Contractor *et al*., 2003; Geringer *et al*., 1989; Grant, 1987; Tallman & Li, 1996), the ratio of foreign assets to total assets (Daniels & Bracker, 1989; Gomes & Ramaswamy, 1999; Ramaswamy *et al*., 1996), and the number of foreign countries in which a firm has subsidiaries (Tallman & Li, 1996). Each of these methods has its own advantages and tends to measure the depth of international diversification (Contractor *et al*, 2003). Consistent with previous studies, this study will measure a multiple index including all three dimensions which are foreign sales, foreign assets, and nations of operation. In addition, all three measures will be loaded on one single component and treated as weights to derive the combined multinationality index (Contractor *et al*., 2003; Gomes & Ramaswamy, 1999). Since the component variables (percentage of foreign sales, percentage of foreign assets, and number of countries) involve different scales, the multinationality index will be standardized. This process will ensure that a result of index represents greater fidelity, and is especially appropriate in nonlinear modeling (Cohen & Cohen, 2003).

Dummy Variable

The home country of multinational companies will be selected as a dummy variable. Hitt *et al*. (1994) insisted that the home of the multinational firm can describe differences in performance and this hypothesis proved the positive indication for the U.S.

dummy. Since the service industry has grown earlier and comprehensively in the U.S. relative to other countries, U.S. - based companies are more likely to have a performance advantage (Contractor *et al*., 2003).

Control Variable

Control variables in this study are hypothesized to affect firm performance. Consistent with previous studies (e.g., Buckley, Dunning, & Pearce, 1977; 1984; Capar & Kotabe, 2003; Contractor *et al*., 2003; Gomes & Ramaswamy, 1999; Haar, 1989; Hitt *et al*., 1997; Kumar, 1984), firm size will be utilized as control variables to further investigate the association between expansion and performance. According to Jung (1991), firm size, relative to the market, could affect rates of return. Large companies are more likely to be able to borrow in the capital market at lower cost and to operate at lower cost because they can spread their risk. They can obtain economies of scale in managerial sectors such as R&D, marketing, and finance as well. Firm size will be measured by the natural logarithm of total sales. While early studies exercised the industry effect as a control variable, the industry effect will not be included in this study in that this research mainly focuses on restaurant industry, and thus, the sample of this study is comprised of restaurants firms. The industry effect does not need to be utilized in this situation.

The Method

This study will develop and test two models in order to analyze the association between international expansion and firm performance. The two models regress firm

performance (PERF) for various combinations of main and control variables. Accordingly:

$$PERF = \alpha 0 + \alpha 1 DOI\% + \alpha 2 SIZE + \alpha 3 C + \acute{\imath} \quad (1)$$

$$PERF = \beta 0 + \beta 1 DOI\% + \beta 2 DOI\%^2 + \beta 3 SIZE + \beta 4 C + \acute{\imath} \quad (2)$$

Where,

PERF = firm performance estimated by ROS

DOI% = degree of internationalization estimated by the sum of FSTS (Foreign sales/total sales), FATA (Foreign assets/total assets), and FCTC (Number of operations in foreign countries/total number of operations)

$DOI\%^2$ = quadratic terms

FIRM SIZE = market capitalization estimated by natural logarithm of total sales

C = home country effect to control for U.S.-based vs. non U.S.-based home nation

1= U.S.-based, 2= Non-U.S.based

$\acute{\imath}$ = error term

Model 1 is to examine the impact of general internationalization on firm performance by using DOI% as a main variable and controlling for firm size. Furthermore, Model 2 includes $DOI\%^2$ to investigate a quadratic relationship between international expansion and firm performance.

CONCLUSIONS

Summary of the Study

A significant number of U.S.-based restaurants and fast food chains have expanded their properties into overseas. International expansions provide companies with the benefits as a way to gain competitive advantage. However, in spite of these benefits, a point in question is whether international expansion actually has a positive impact on firm performance. Although extensive research has been done on this subject, they failed to reach consistent results. This study suggests an inverted U-shaped non linear relationship which is positive up to an optimal level resulting from the advantages of internationalization and negative beyond that level caused by the complication between international expansion and firm performance.

Implications for Management

Expansion overseas possesses a variety of potential benefits. However, due to the complexity of international diversification, the ability to implement and manage expansion effectively is critical and necessary in order to achieve those advantages. Based upon the result of the study, this research hopes to offer better understanding and guidance to both academics who have struggled with inconsistent results and to especially company strategists operating the international service firms. With better knowledge, managers are able to decide when and how to implement such expansion and ultimately achieve the optimal level. For instance, if managers are more clearly concerned about the negative aspects of initial international expansion, they can be better prepared to lower the costs of early internationalization.

Limitations and Suggestions for future study

This study does not examine the possibly confusing issue of causation. In other words, since companies continue to expand their properties during a period of this study, continuing international expansion may affect future output. Moreover, this study remains the unaddressed possibility of whether the relationship is stable over time. Given a longer period of time, and detailed assumptions, one may be able to examine a link between international expansion and firm performance more precisely and explicitly. Finally, the differences existing between knowledge-based service sector and capital-based service sector might generate different results in terms of the relationship between expansion and performance in that capital-based service sector requires more extensive initial capital investment than knowledge-based service sector. One might examine empirically testing the differences between these two sectors.

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