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Operationalizing Psychic Distance

International Market Selection based on a knowledge
perspective: the case of Miitik, a Portuguese beachwear
company

Miguel de Albuquerque e Melo

Supervisor: Rute Xavier

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Abstract

Back in the days, Internationalization was a process exclusive to companies of great dimension. It requires a rather high amount of resources, reason why it was difficult and expensive for smaller companies to achieve. However, as the years went by, communication channels have improved and the world has become closer as information costs decreased. Given this, nowadays not only big multinationals but also Micro, Small and Medium Enterprises (SME's) have increased its operations abroad. If in the past internationalizing was considered an option, but some support that it has become a necessity given the high market concentration across many industries. Nevertheless, although it is advantageous to expand operations, it doesn't mean it has become an easy process. In fact, SME's still face several obstacles that must be considered and tackled.

As an example of the previous lines, I found Miitik. Miitik is a retailing beachwear start-up based in Portugal. The company started its operations 4 years ago and currently operates only in Portugal. Although it has sold some products abroad, it is not representative at all in the total sales. At the moment, the beachwear industry in Portugal is rather saturated both by big multinationals and also by other small actors, as Miitik. Due to this, Miitik has been struggling to achieve its financial goals. One of the options would be to internationalize, however the company is lacking resources and some insights about with countries to chase.

This thesis has the aim to support Miitik with its International Market Selection.

Resumo

No passado, Internacionalização era um processo adoptado essencialmente por grandes multinacionais. Tal acontecia, pois consiste num processo que envolve diversos recursos, o que tornava bastante difícil e dispendioso para pequenas empresas de obter. No entanto, com o decorrer dos anos, os canais de comunicação evoluíram bastante, o que levou a que a obtenção de informação se tenha tornado mais fácil e o mundo tenha ficado mais próximo. Posto isto, hoje em dia não apenas as grandes multinacionais, mas também as pequenas e médias empresas têm expandido as suas operações no estrangeiro. Se no passado internacionalização era considerado uma opção, hoje em dia é uma necessidade. Ainda que internacionalizar seja de facto vantajoso, não significa que seja um processo fácil, visto que continuam a existir diversas barreiras no processo.

Como exemplo do previamente exposto, temos a Miitik, uma start-up de comércio de fatos de banho sediada em Portugal. A empresa iniciou as suas operações há 4 anos e atua principalmente no mercado português. Apesar de ter efectuado algumas vendas no estrangeiro, estas não são representativas no total de vendas. Actualmente, a indústria de fatos de banho em Portugal, encontra-se especialmente saturada tanto por grandes multinacionais como por PME's. Por consequente, a empresa não tem conseguido alcançar os resultados desejados. Uma das soluções passaria por expandir as suas operações no estrangeiro, no entanto a empresa escasseia em recursos e tem pouco conhecimento acerca de mercados estrangeiros.

Esta tese tem o objectivo de ajudar a Miitik quanto à sua selecção de mercados.

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1. Introduction

1.2 The company - Miitik

This dissertation is based on an internationalization process oriented towards a real company, Miitik.

Miitik is a family business based in Portugal, precisely in Parede, district of Lisbon. It was founded in 2013. The company operates in the retail industry with a focus on textiles, precisely female beachwear. They offer three different lines of products - MIITIK swimwear, MIITIK kids and MIITIK sportswear. Nevertheless, it is noticeable that the former - MIITIK swimwear - is their core product, representing substantially 70% of its production volume.

Nowadays, the company uses 4 different sales channels:

- Street markets and fairs;
- Resellers;
- Showroom;
- Online (www.miiitik.com);

Miitik is responsible for all the activities across the products' value chain, from designing to marketing and sales, besides manufacturing which is outsourced. Despite that, the products are still entirely made in Portugal. They are slightly fancier and more adorned than common beachwear, reason why they can be considered a premium product in the industry.

Given the characteristics of the product, Miitik's target customers are mainly women from 25 to 40 years old, precisely young mothers. The beachwear is comfortable and allows women to hide some eventual pregnancy stretch marks, and at the same time keeps up with the latest fashion trends.

Miitik's competitive advantage comes from its high-quality products. This high quality is reflected on the products' prices, which can be considered slightly above the average price of beachwear, but still affordable to the majority of the population.

Concluding, it is worth to notice that Miitik is considered a micro-enterprise, according to the definition provided by the European Commission.

1.2 Problem Statement

Nowadays the firm is operating mainly locally, in the Portuguese market. The Portuguese swimsuit market can be considered rather saturated, since the competition is vast and strong. Several beachwear multinationals are present in the country and there is also a wide array of local and smaller retailers.

Thus far, having regard to international markets, Miitik has sold a few pieces abroad, in the United Kingdom and Luxembourg. However, it is still not representative on the total sales.

Given this, although the company has been growing its yearly revenues, it was not able to increase it to a desirable point.

To sum up, one of the solutions Miitik would like to explore in order to increase its revenue stream in the future, would be internationalization. The aim is to explore less saturated markets and compete with its premium products, and at the same time try to avoid the seasonality of the business.

1.3 Choice of Countries

The countries that will be analyzed in the study were not randomly chosen. This decision was made under the will and approval of the company.

Each one of the countries had to meet a certain criterion in order to be chosen. First of all, since Miitik products are primarily beachwear, it makes sense that the countries chosen are known for having a warm climate and are considered as good summer destinations. Ideally, we are speaking about countries with beaches and that are considered attractive touristic wise.

Secondly, one of Miitik's goal would be to avoid the seasonality of the business. At the moment, Miitik is facing an huge volatility of sales in Portugal, due to the fact beachwear sales decrease abruptly during the winter. The idea is to maintain the production and sales levels stable during the whole year. The solution would be to start selling in countries where the summer occurs in a period of the year different that the one in Portugal. Since the summer months in Europe are mainly from June to September, it would be ideal to find countries where the summer occurs during the remaining months.

Thirdly, some countries were selected by being economically strong and also for having a good market size. By market size, I mean enough population situated in the target group chased by Miitik.

Lastly, the group of countries was selected in a way that it provides enough diversity, both in geographic, development and economic terms. This means that not all of them will meet all the criteria mentioned before, in fact each one of them is likely to meet only some of them.

Concluding, this is the list of 12 countries chosen:

- Spain
- France
- Italy
- Germany
- UK
- Greece
- Luxembourg
- Croatia
- Brasil
- Angola
- Mozambique
- Australia

1.4 Research Questions

R1: Which resource is paramount for Miitik's Internationalization process?

R2: Which indicators should be used to measure the Psychic Distance between 2 countries?

R3: Which countries are close to Portugal in terms of Psychic Distance?

1.5 Structure of this thesis

This thesis is divided in 3 sections. During the first I will go through the research of remarkable authors about internationalization, where some major insights and topics will be discussed and explained. Secondly, I will provide all the data collected and explain how the psychic distance index is elaborated. Thirdly, the results will be analyzed and debated, in order to draw some conclusions. This will be followed by stating some eventual limitations of the thesis, precisely of the psychic distance index.

2. Literature review

Along this chapter, several concepts created and studied extensively by wide array of authors, precisely by expert researchers on Internationalization, are going to be introduced and debated. These concepts aim to support the analysis that I will further conduct, on the internationalization of SME's, with a special focus on the Portuguese swimsuit industry.

2.1 What is internationalization?

During the past decades, we have seen huge advances and changes in the world, changes that impacted heavily the way how businesses run. Technological improvements have brought down communication, transportation, information and transaction costs, which among other factors culminated in an increasingly higher degree of globalization. The closer contact between people, institutions and corporations, has converged the tastes and consumer behaviors across borders. For this reason, companies faced the necessity to adapt quickly to changing environments in order to survive and thrive. Nowadays, competition comes rather from abroad than from domestic markets, and so staying domestic is no longer an option. Nonetheless, this must not be seen as a threat but as an opportunity instead (Korsakiené and Tvaronaviciené, 2012).

Given the aforementioned, Internationalization has become an *avant garde* topic of interest for several researchers and managers. Each of them can have a different theory and idea about the topic, more or less similar to other authors. Some strong attempts of defining Internationalization are given by Beamish (1990), who sees it as “*the process by which firms both increase their awareness of the direct and indirect influence of international transactions on their future, and establish and conduct transactions with other countries*”, or Welch and Luostarinen (1988), that mention it as a “*process of increasing involvement in international operations*”, or even Korsakienė and Tvaronavicienė (2012) define it as a process of expanding the firm’s operations abroad to foreign markets, while Buckley and Ghauri (1993) say that Internationalization is strictly related with firm growth, and lastly we have Calof and Beamish (1995) go even a bit further, defining it as “*the process of adapting firms’ operations (strategy, resources, structure, etc.) to international environments*”. The one thing we can clearly see that all the authors share, is their idea that internationalization has regard to international operations.

2.2 Different approaches to internationalization

The previously mentioned definitions and theories can accrue from the different approaches to internationalization, as examples we have stage, contingency and network approaches. The ones I will explore with more detail are the stage and network, since they seem to address and be more effective on companies that are on similar stages to Miitik. To introduce briefly, Stage approaches were developed since early and they defend that an enterprise should initiate its internationalization process through modes that require a low level of resources and commitment to the foreign market, as it is the example of exports. Only after acquiring some experience during its international activities the firm should increase its commitment overseas, if it finds it profitable to do so. This approach is supported by several researchers as Cavusgil (1980), Reid (1981) and Johansson and Wiedersheim-Paul (1975).

Regarding network approaches, authors state that a firm in order to thrive in an international environment should create relationships with partners operating in other countries, keep increasing its commitment to the network and integrate several networks in different countries if possible. The success of the firm in new markets depends on its *Insidership* within the network (Chetty and Blankenburg-Holm, 2000; Johanson and Vahlne, 1977).

2.3 Different entry modes on foreign markets

It is well known that when it comes to internationalize its operations, firms have several ways of doing it, in other words, they can opt for different entry modes on the target markets. This choice can be influenced by several factors. Among these, Pan and Tse (2000) identify as paramount, domestic country and host country characteristics, the relationship and interaction between both, and the industry to be considered. Pan and Tse (2000) and Kumar and Subramaniam (1997) defend that firms should approach this challenge through a hierarchical strategy in order to realize which entry mode is more suitable.

Pan and Tse (2000) designed a hierarchical model, where in the first level of the hierarchy they make the distinction between equity and non-equity entry modes. After having chosen whether one or another, managers should run a more detailed analysis in order to choose the specific mode within the equity and non-equity modes. In this second hierarchical level, the authors classify exports and contractual agreements as the two non-equity modes, and equity joint ventures and wholly owned subsidiaries as equity modes. All these 4 entry modes, presented in **Figure 1**, have an increasing level of inherent risk, resources commitment, control required and revenues stream, following the order in which I mentioned them. This increasing level of commitment on the foreign market will be further analyzed through the *uppsala model* designed by Johanson and Vahlne (1977).

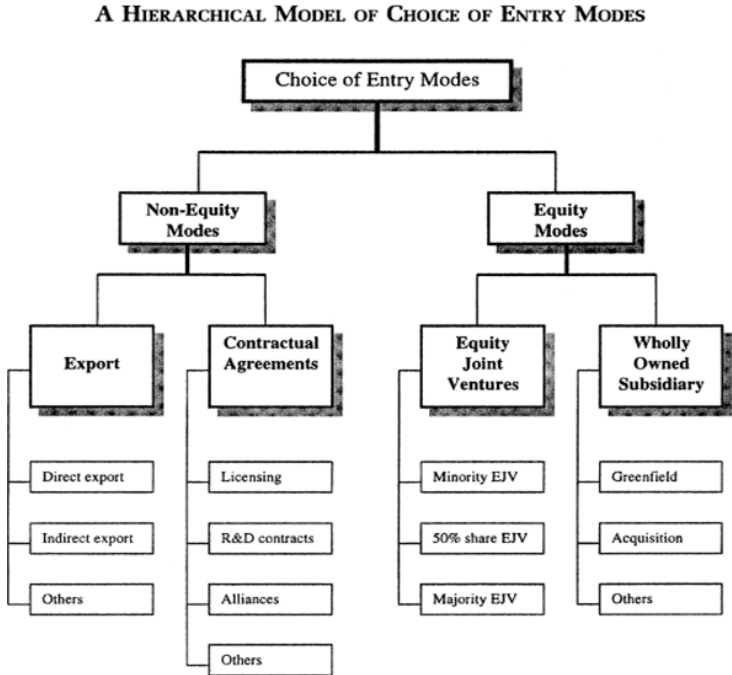


Figure 1 A hierarchical model of choice of entry modes

2.4 SME's and Micro Enterprise definition

The importance of Micro enterprises and SME's has increased significantly throughout the past decades (Reynolds, 1997). According to the European Commission, today it represents nearly 90% of all businesses in the European Union and are able to generate 2 out of every 3 jobs. These companies, sometimes forged by young individuals embedded with an entrepreneurial mindset, are driving disruptive innovations and changing business models in several industries (Kubíčková et al., 2014).

Following these trends, these enterprises have been a focus of study, as well as its definition. Once again, we can find distinct researchers with different perspectives and thus diverse definitions, that may vary across countries (Wignaraja, 2003) or industries ((Costică) Buculescu, 2013). Nonetheless, there is a particular one, "*companies whose characteristics respects certain criteria and do not exceed certain quantitative limits.*" ((Costică) Buculescu, 2013), that supports the one given by the European commission (2003b):

"The category of micro, small and medium-sized enterprises (SMEs) is made up of enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding 50 million euro, and/or an annual balance sheet total not exceeding 43 million euro."

The criteria used by the European Commission, is the number of employees and either the annual balance sheet or the annual turnover of the company.

Miitik is included in this category of enterprises, precisely it is considered a micro enterprise.

2.5 Business environment as a business network – The Uppsala Model

Nowadays managers have to keep in mind that companies cannot operate as an individual and independent business unit within its environment anymore. Markets have evolved along with information technologies, driving transaction costs way down, when compared with the past. Johanson and Vahlne (1977, 2009), designed the Uppsala model, in which they try to provide

fundamentals for an improved view of the markets as a *business network*. The authors support that an enterprise relies heavily on a varied network of stakeholders, from suppliers to customers, a phenomenon called *liability of outsidership*. In order to overcome this liability, the firm should establish and foster relationships to a certain extent and when it does so, it becomes an *insider*. *Insidership* within a relevant network can bring a wide array of benefits to the firm, as it will be discussed further.

Now, if we focus on the internationalization process of a firm, it is easy to realize that the *liability of outsidership* increases with the *liability of foreignness*. The fact that an enterprise is going to face an unknown market, it is going to be much more exposed to it and relying even more on the actors that already operate there. Given this, belonging to a *business network* is definitely a necessity when it comes to move beyond borders.

It is now important to understand what are the real advantages of the *business network* for the company. According to the authors, the relationships maintained with other stakeholders offer a lot of potential for trust and commitment among business units, which will allow them to acquire and create knowledge about the focal foreign market. The study conducted by Johanson and Vahlne (1977, 2009) showed that the knowledge creation has a positive impact on the performance of firms, not only because it allows firms to identify new market opportunities but also because by knowing each other, firms can align their operations in order to reach a better outcome. This might be more intuitive if we think about partners operating within the same value chain, that clearly have a benefit from understanding each other strategy and target groups, so that they can address properly the final costumers needs.

Obviously, both these processes, trust and knowledge creation, are very time consuming and thus they have to be done step by step. Some authors as Hood and Young (1979), defended in the past that firms should define their markets entries and entry form based just on cost and risk analysis and an overlook of its own resources. Despite the fact that the latter is indispensable when it comes to analyze a market entry, Johanson and Vahlne (1997) and Axelsson & Johanson (1992) contradict this approach, stating that the internationalization process has to be sequential and continuous, and labelled it as an *establishment chain*. Also, other authors as Carlson 1975; Forsgren and Kinch 1970; Hörnell, Vahlne & Wiedersheim-Paul, 1973; Nellbeck, 1967; Johanson, 1966; developed several studies about Swedish companies operating in international markets, that supports the following conclusions. According to it, the primordial steps taken by the firms are *ad hoc* export, which is several times based on agreements with intermediaries, as agents that represent the firm in the foreign market. Subsequently, with the increase of revenues, an own sales organization can be created and finally if the results are

favorable, foreign manufacturing could be considered in order to avoid any trade barriers that might exist. During this entire process, the company is supposed to develop its knowledge about the market which allows it to deepen its activities and operations, and have a better judgment about the decisions it has to take. At this point is worth to specify what kind of knowledge we are talking about. It can be divided in two sections: Institutional market knowledge and business market knowledge. The former has regard to the foreign language, foreign laws and country rules, whilst the latter focus on knowledge about requirements and infrastructures needed to develop its operations, about the target group needs and tastes, the firm capability to address the market needs, summed up, market-specific knowledge that gathered allow the firm to design its strategy, a market oriented strategy preferentially (Johanson and Vahlne, 1977; Barkema et al.1996; Erramilli, 1991).

2.6 Psychic Distance

During the study, Johanson and Vahlne (2009) identified another feature on the pattern of internationalization besides the *establishment chain*. The focal firms usually started their internationalization on countries that were close to the domestic market in terms of *psychic distance*, generally speaking the features that make it difficult for a firm to understand foreign markets. Again, we can say that this difficulty arises from the *liability of foreignness*. The concept was born in studies conducted in Uppsala university and it was defined as “the sum of factors preventing or disturbing the flows of information between firm and markets” (Johanson and Wiedersheim-Paul, 1975). It was extensively used, studied and expanded by several other authors (Brewer 2007; Andersen and Buvik 2002; Cicic et al., 1999). The concept states that *psychic distance* is measured through the perceived differences between the firm's home country and foreign markets. These differences constitute impediments for information and knowledge flows and thus they increase the *psychic distance*. Given the importance of knowledge on firm internationalization (Carlson 1974; Liesch and Knight 1999; Johanson & Vahlne 1977), it is easy to realize that the bigger the differences between countries, the bigger the distance and consequently the hardest to acquire and create market specific information. International Business Literature has considered *psychic distance* a strong indicator for International Market Selection (IMS). Basically, a firm is more likely to choose countries that they can get to know more easily and from which it can access more information. On the other

hand, a firm's manager will tend to avoid going into countries that he can hardly gather information about, since it will be much more difficult to succeed in these markets. It is important to mention that some authors (Cicic et al., 1999) argue that the *Psychic Distance* has different levels of impact depending on the type of firm we are facing. Precisely, it is much more relevant in enterprises on early stages of its international development and particularly on small and medium enterprises, the called SME's. Concluding, as a firm intensifies its activity and operations overseas, the importance of the distance on IMS decreases. (Benito and Gripsrud 1992). For this reason, since the company that is being subject of analysis, Miitik, is a micro-enterprise in its early stages of national and international development, this approach is very suitable for the analysis. As it will be discussed further, Miitik is likely to benefit from this sequential expansion, starting from countries that they might be more familiar with and with fewer environmental differences from its domestic market, Portugal.

In order to help managers on IMS, Brewer (2007), designed a tool that intends to measure the distances between each pair of countries. Basically, the objective is to provide the firm's managers a way to identify the countries that they are more likely to have attainable information, in a comprehensive way. Again, the author considers different types of knowledge, belonging to both the fields of institutional market knowledge and business market knowledge. Based on researches conducted by several other authors (Chetty and Campbell-Hunt, 2004; Child et al., 2002; Conway and Swift, 2000; Dow 2000; Dow and Karunaratna, 2006; Evans and Mavondo, 2002; Evans et al., 2000; Kim and Rhee, 2001; Stottinger and Schlegelmilch, 1998), he chooses a set of indicators that he perceives as impactful on the analysis of the distance. The indicators have regard to differences between the firm's home country and foreign country in terms of culture, language, political systems, education, religion, level of development, business practices and laws.

To operationalize the use of the psychic distance, Brewer (2007) opted to design an Index that aggregates the items considered directly responsible for driving the ease of information flows between the company and foreign countries, in other words, the indicators chosen. The Index purpose essentially is to measure the availability of information about the target market. It is important to bear in mind that although the choice of the Index components was based on research and data, they are also subject to a certain degree of subjectivity, descendant from debate and opinions of experts on the topic. In first instance, primary elements with strong influence were identified, which are composed and explained through secondary indicators that compound each one of the primary ones.

Commercial Ties - Intensified commercial exchanges between two countries are likely to provide companies a strong background about cross border characteristics, since it fosters the flow of information between countries (Johanson and Wiedersheim-Paul 1975; Wiedersheim-Paul 1972; Wiedersheim-Paul and Welch 1975).

Political Ties - Close political relationships have a strong impact on information flow as well. They can be reflected as trade agreements, defense treaties, level of diplomatic exchange and trade programs (Wiedersheim-Paul and Welch 1975).

Historical Ties - Close historic ties between two countries implies a closer relationship between organizations and individuals, which in turn foster the flows of information among them. These can be measured for example through previous colonial relationships or even alliances during certain wars (Ghemawat, 2001).

Geographical Ties - As the name implies, these ties are strictly related with the geographic distance between two countries. This relation can be explained through transportation costs, which decrease with the distance between countries, thus favouring the commercial exchange (Beckerman, 1956; Ghemawat, 2001).

Social Ties - The existent community differences or similarities also have influence on the flow of information between countries (Davidson 1983). These differences can be analyzed through the sporting interaction, language similarities and even some distance indexes as it the case of Fletcher and Bohn's one (Eichengreen and Irwin, 1998; Wiedersheim-Paul and Welch, 1975).

Information Availability - This component has regard to the information available regarding the different countries. It can vary due to the size and importance of each country or even due to exchange of people temporarily or permanently between countries (Wiedersheim-Paul and Welch, 1975).

Level of Development - The higher the level of development of any country, the higher the likelihood of existent available information regarding the markets. These countries are usually more open to foreign markets and tend to produce comprehensive and more reliable information. Finally, it is also less likely to find hidden costs, such as corruption, in developed

countries (Ghemawat, 2001). This parameter can be accessed through Human development and Transparency Indexes.

These 7 primary indicators were the ones that Brewer (2007), through extensive research, debate and also based on the work of previous authors on the matter, found more suitable to build *Psychic Distance* index. In appendix 1, you can see a more detailed table with each indicator depicted.

3. Methodology

Following the aforementioned, the study further conducted has the aim to support Miitik with its International Market Selection, by other words, to help Miitik identifying the markets where it easier to gather information and knowledge, and consequently reach its goals. As it was referred, acquiring knowledge is paramount, given the fact that the company is in its early stages of national and international development (Cicic et al., 1999).

In order to address the problem, I am going to use the Psychic Distance approach, introduced in the 70's by Johanson and Wiedersheim-Paul (1975) and depicted in the Literature Review chapter. The approach is especially useful in this context, given the classification of Miitik as micro-enterprise and its nearly inexistent international development. Currently, Miitik has a lack of information on international markets, a gap that needs to be filled before starting any operation abroad. Only after having understood the basics of a specific market, both in terms of institutional and business market knowledge, the company can effectively operate abroad and thrive. (Cicic et al., 1999; Brewer 2007).

Brewer (2007), based on the work of previous authors and on his findings, designed an index with the aim of operationalizing the concept of psychic distance, the *Psychic Distance Index*. The index allowed him to compare a batch of 25 countries with regard to their psychic distance from Australia. The index incorporates a wide array of indicators that, all combined provide a value that the represents the psychic distance between home and away country. In turn, each of the indicators influence the exchange of information between the 2 countries. So, in short, he was inferring about the extent of information available in Australia about each away country.

The home country in our study is Portugal, and the goal of the study is to identify how far are several countries in terms of psychic distance. This way, it is intended to identify the countries that may be more likely for Miitik to succeed. To run this analysis, Brewer's (2007) index was used, however, to turn it more useful for a Portuguese corporation it has been submitted to some changes that express better the company and the country reality.

One of the reasons this approach can be so useful, it that even though the index was slightly adjusted to the reality Miitik facing, it can be used by any company, operating in any industry, in any country. Nevertheless, according to the reality faced it might have to suffer again some changes.

4. Choice of Countries

The pre-selected countries that will be analyzed in the study were not randomly chosen. This decision was made under the will and approval of the company.

Each one of the countries had to meet certain criteria in order to be chosen. First of all, since Miitik products are primarily beachwear, it had to be countries known for having a warm climate and are considered good summer destinations. Ideally, we are speaking about countries with beaches and that are considered attractive touristic wise.

Secondly, one of Miitik's goal would be to avoid the seasonality of the business. At the moment, Miitik is facing a huge volatility of sales in Portugal, due to the fact beachwear sales decrease abruptly during the winter. The idea is to maintain the production and sales levels stable during the whole year. The solution would be to start selling in countries where the summer occurs in a period of the year different that the one in Portugal. Since the summer months in Europe are mainly from June to September, it would be ideal to find countries where the summer occurs during the remaining months.

Thirdly, some countries were selected by being economically strong and also for having a good market size. By market size, it means enough population situated in the target group chased by Miitik.

Lastly, the group of countries was selected in a way that it provides enough diversity, both in geographic, development and economic terms. This means that not all of them will meet all the criteria mentioned before, in fact each one of them is likely to meet only some of them.

Concluding, the list of 12 countries chosen is:

- Spain
- France
- Italy
- Germany
- UK
- Greece
- Luxembourg
- Croatia
- Brasil
- Angola
- Mozambique
- Australia

5. Psychic Distance Index

As it was mentioned before, the index incorporates diversified indicators, precisely 7 primary indicators:

- Commercial Ties;
- Political Ties;
- Historic Ties;
- Geographic Ties;
- Social Ties;
- Information Ties;
- Development Ties;

Each of them represents the ties that Portugal has with each country, with regard to that specific matter. Each primary indicator is then broken down into secondary indicators, as it will be specified after.

Each of the analyzed countries will be classified according to his score in each indicator, however it is important to bear in mind that only the final value, of all the indicators together,

is relevant. This is especially important because every component of the index has the same weight on the final value, since there is no evidence of the opposite.

5.1 Commercial Ties

Since early, Vahlne and Wiedersheim-Paul (1975) conducted studies which showed that Swedish companies tended to increase the level of exports especially to countries with higher economic development. They realized that one of the reasons for this was the information available with respect to the importing country, and furthermore, that this information was correlated not only with economic development of the importing country but also with the existing commercial ties with Swedish companies. Carlson (1974), also states that firms establish subsidiaries with the objective of acquiring information about a specific market, once it is easier to transfer information within an organization than between an organization.

Based on these studies, we can assume that existing commercial ties can foster the information flows between countries, even more, they are intensified with the purpose of acquiring information about firms operating in a specific market, as well as other market conditions.

According to the authors, it is clear that the commercial ties between each pair of countries have a strong impact on the creation and acquisition of information between them and this it is worthful to analyze the relationship that Portugal has with each of the countries in study. These commercial ties are going to be accessed on the levels of international trade between home and away country, and also on the level of Foreign Direct Investment exchanged between them.

5.1.1 International Trade between Portugal and each away country

When we speak about the commercial ties between 2 countries, it is intuitive that one major component must be the international trade between them. The international trade can be depicted in inflows and outflows, in this case from Portugal. These two-sided flows have respect to goods and services. Eurostat provides a clearer and more extent definition:

“In national accounts exports consist of transactions in goods and services (sales, barter, gifts or grants) from residents to non-residents:

An export of a good occurs when there is a change of ownership from a resident to a non-resident. Also smuggled goods must be included in exports.

Change of ownership does not necessarily imply that the good in question physically crosses the frontier. If goods cross the border due to financial leasing, as deliveries between affiliates of the same enterprise or for significant processing to order or repair national accounts impute a change of ownership even though in legal terms no change of ownership takes place.

Export of services consist of all services rendered by residents to non-residents. In national accounts, any direct purchases by non-residents in the economic territory of a country are recorded as exports of services; therefore all expenditure by foreign tourists in the economic territory of a country is considered as part of the exports of services of that country. Also international flows of illegal services must be included.”

Analogously, the national accounts’ transactions in goods and services from non-residents are called imports.

Having now defined all the concepts, we have the respective values for each country provided in the tables bellow. In **Table 1**, it is presented the value of imports from each away country to Portugal in 2014 and 2015, both in absolute and relative terms. Through the percentage of each country on total imports, we can infer about the weight that each of the countries represents on Portuguese total imports, in both periods.

In **Table 2**, the methodology used is the same, but the values have respect to Portuguese exports to each of the away countries, in 2014 and 2015.

Concluding, there is a positive correlation between the weight that each country represents on Portuguese international trade levels and the information available about the respective country. On other words, the more intensified are the international trade levels between home and away country, the closer they are in terms of psychic distance.

	2014	2014 (%)	2015	2015 (%)
Spain	21062,1	26,92%	21950,1	32,89%
France	4991,9	6,38%	4927,6	7,38%
Italy	3976,8	5,08%	3596,9	5,39%
Germany	8604,1	11,00%	8588,4	12,87%
UK	2292,9	2,93%	2062,1	3,09%
Greece	150,6	0,19%	139,7	0,21%
Luxembourg	71,8	0,09%	130,9	0,20%
Croatia	53,9	0,07%	54	0,08%
Brazil	1236,6	1,58%	954,1	1,43%
Angola	1920	2,45%	1260	1,89%
Mozambique	52	0,07%	44,7	0,07%
Australia	33	0,04%	40,2	0,06%

Table 1 Imports from each away country to Portugal, 2014 and 2015 (million USD).
Source OECD 2016, OECD Quarterly International Trade Statistics 2016, Issue 3.

	2014	2014 (%)	2015	2015 (%)
Spain	15001,7	23,50%	13833,4	25,01%
France	7508,7	11,76%	6706,1	12,13%
Italy	2044,2	3,20%	1765	3,19%
Germany	7476,4	11,71%	6536,4	11,82%
UK	3898,7	6,11%	3714,5	6,72%
Greece	227,8	0,36%	141,1	0,26%
Luxembourg	95,8	0,15%	96,9	0,18%
Croatia	24,2	0,04%	19,8	0,04%
Brazil	844,3	1,32%	633	1,14%
Angola	4220	6,61%	2300	4,16%
Mozambique	461	0,72%	448	0,81%
Australia	123,7	0,19%	119,8	0,22%

Table 2 Portuguese exports to each away country, 2014 and 2015 (million USD).
Source OECD 2016, OECD Quarterly International Trade Statistics 2016, Issue 3.

5.1.2 FDI inward and outward positions of Portugal related to the other countries

Besides the levels of international trade, the second indicator used to measure the commercial ties of Portugal with each away country is FDI stocks at home and abroad. However, to understand what FDI stocks represent, we must have a clear notion of what is Foreign Direct Investment. Below we have the definition provided by Eurostat (2007):

“Foreign direct investment is the category of international investment in which an enterprise resident in one country (the direct investor) acquires an interest of at least 10 % in an enterprise resident in another country (the direct investment enterprise). Subsequent transactions between affiliated enterprises are also direct investment transactions. As it gives the investor an effective voice in the management of the enterprise and a substantial interest in its business, FDI implies a long-term relationship between the direct investor and the direct investment enterprise. Investment may take place through the establishment of an entirely new firm, so-called ‘greenfield’ investment, or through the complete or partial purchase of an existing firm via a merger or an acquisition. “

To sum it up, it is an investment made by a home enterprise in an international country, to a certain extent that the company has some power and rights over the investment it has done. The investment can take the form of a merger, acquisition or even the creation of a new enterprise.

The FDI originary from a country to another can be measured on a specific period of time, usually a year, and is called FDI flow. However, I am interested in a more representative measure, the FDI stock. Nevertheless, I provide again both definition according to Eurostat (2007):

“FDI flows and positions: through direct investment flows, an investor builds up a FDI position that has an impact on an economy's international investment position. This FDI position (or FDI stock) differs from the accumulated flows because of revaluation (changes in prices or exchange rates), and other adjustments like rescheduling or cancellation of loans or debt-equity swaps. “

In a simple way, the FDI stock is the accumulated FDI flows over the years, however the accumulated flows suffer some adjustments based on price and exchange rates variations.

Given the definitions, we can now infer about the FDI stocks. Below we have two tables, **Table 3** represents the FDI stocks hosted in Portugal, by country of origin. **Table 4**, represents the Portuguese FDI stocks abroad, by country of destiny. Both the tables have the FDI inward and outward position during 2 years, 2011 and 2012, in absolute and relative terms.

	2011	2011 (%)	2012	2012 (%)
Spain	22425,1	20,03%	26928,6	22,48%
France	6966,1	6,22%	7356,1	6,14%
Italy	5551,2	4,96%	4630,8	3,87%
Germany	3820,1	3,41%	4510,8	3,77%
UK	8319,6	7,43%	8460,6	7,06%
Greece	1,5	0,00%	1,5	0,00%
Luxembourg	12646,6	11,30%	15126,3	12,63%
Croatia	0	0,00%	0	0,00%
Brazil	2594,5	2,32%	1968,1	1,64%
Angola	533	0,48%	1361	1,14%
Mozambique	0	0,00%	0	0,00%
Australia	28,5	0,03%	32,2	0,03%

Table 3 FDI stocks hosted in Portugal, per each away country (million USD).

Sources OECD 2014, OECD International Direct Investment Statistics 2014, OECD Publishing; United Nations Conference on Trade and Development 2014, Bilateral FDI statistics 2014, The Division on Investment and Enterprise.

	2011	2011 (%)	2012	2012 (%)
Spain	8181,3	11,31%	9637,7	12,674%
France	573,6	0,79%	879,4	1,156%
Italy	1443,5	2,00%	1519	1,998%
Germany	2445,4	3,38%	2820,9	3,710%
UK	1502,2	2,08%	1405,8	1,849%
Greece	4,1	0,01%	2,7	0,004%
Luxemb.	3835,5	5,30%	2259,9	2,972%
Croatia	2	0,00%	2	0,003%
Brazil	5632	7,79%	4909,6	6,457%
Angola	4285	5,93%	5220	6,865%
Mozambique	776	1,07%	875	1,151%
Australia	36,6	0,05%	44,7	0,059%

Table 4 Portuguese FDI stocks abroad, per country of destiny (million USD).

Source OECD 2014, OECD International Direct Investment Statistics 2014, OECD Publishing; United Nations Conference on Trade and Development 2014, Bilateral FDI statistics 2014, The Division on Investment and Enterprise.

5.2 Social Ties

Davidson (1983) proved that the similarity or divergence between countries, more precisely between business communities, has some impact on the extent of knowledge exchange and business interaction between them and thus on its psychic distance. The researcher conducted a study on 954 products, which suggest that firms have a strong preference for markets similar to the home market. This effect decays over the amount of knowledge a firm and its manager have, however it is significantly strong on firms in its early stages of expansion. The latter is explained by the fact that very different markets are correlated with increased uncertainty and thus a higher liability of foreignness (Johanson and Vahlne, 1977).

The aforementioned leads us to believe that social differences should be taken into consideration when it comes to measure the psychic distance. In order to do so, I will use Hofstede's approach, a tool that measures several characteristics of a population and thus can be useful when comparing 2 different countries (Hofstede, 2001). However, other authors

defended that there are other characteristics that might have an impact, as it is the case of sporting and language preferences (Eichengreen and Irwin 1998; Pressey and Selassie 2002; Wiedersheim-Paul and Welch 1975). To measure these preferences, 2 others indicators will be used. The first has regard to the number of matches between home and away national teams, with respect to the 2 preferred sports at home, Portugal. The second one focus on the language similarities between Portugal and each of the other countries.

5.2.1 Cultural Similarities

Cultural similarities or differences between two pairs of countries are inevitable and they can be measured with respect to different dimensions. Geert Hofstede, a Dutch researcher, dedicated a good part of his life analyzing cultural characteristics of different populations and trying to come up with behavioral patterns within a country. It is worth to mention that every individual that belongs to a specific country doesn't necessarily behaves in the same way or has the same beliefs than all the other countryman, however, according to the law of the big numbers it is possible to identify what are the major characteristics of a country population. Along with other researchers, he developed a tool - The 6D model of national culture. The model uses 6 indexes that characterize each country according to 6 cultural dimensions, from a scale from 0 to 100.

The dimensions are:

- **Power Distance:** This index expresses the extent to which people in a society accept and expect that the power is distributed unequally. A higher score represents societies where accept a perfectly structured hierarchical order, whilst a low score represents a society do not comply with inequalities about power distribution.
- **Individualism versus Collectivism:** Regarding this index, lower values express individualism. On individualist societies, individuals have a preference for social frameworks in which they only have to take care of themselves and close relatives. The opposite, collectivism, represents societies where individuals have a preference for social frameworks more protective, by other words, they expect society to take care of them in case of need.
- **Masculinity versus Femininity:** The Masculinity side of this dimension, expressed by higher scores of the index, has regard to societies where individuals tend to prefer

achievement and rewards for their success. On the other extreme we have Feminist societies, expressed by lower scores, represent societies that care more about solidarity, cooperation and caring for the weak.

- **Uncertainty Avoidance Index:** As the name implies, the index represents to which extent a society is willingness to take risks or not, especially about the future. The tendency is that societies with low willingness for risk have more strict rules and rigid code of behaviors, whilst the opposite ones have a looser code of conduct. Low scores represent uncertainty tolerant countries. High scores represent uncertainty avoidance countries.
- **Long Term Orientation versus Short Term Orientation:** There are societies that are very attached to old traditions and beliefs and thus are suspicious about social exchange. The latter are represented by low scores on the index. The opposite, high index scores, represent countries that are more future oriented and are not afraid of change in order to face future challenges.
- **Indulgence vs Restraint:** Indulgent societies tend to be more easy going and relaxed, by not having very strict rules. Enjoyment is a life goal. On the other hand, societies that are more restrained tend to have a strict code of conduct and certain types of hobbies don't sit well within the society. High scoring societies are characterized as indulgent, while low scoring ones as restrained.

The scores of each country are only meaningful when compared to other countries. For this reason, in **Table 5** it is provided the Portuguese scores in each of the 6 indexes so that they can be compared with each of the other 12 countries.

	Power distance	Individualism	Masculinity	Uncertainty Avoidance	Long Term Orientation	Indulgence
Portugal	63	27	31	99	28	33
Spain	57	51	42	86	48	44
France	68	71	43	86	63	48
Italy	50	76	70	75	61	30
Germany	35	67	66	65	83	40
UK	35	89	66	35	51	69
Greece	60	35	57	100	45	50
Luxemb.	40	60	50	70	54	56
Croatia	73	33	40	80	58	33
Brasil	69	38	49	76	44	59
Angola	83	18	20	60	15	83
Mozambiq.	85	15	38	44	11	80
Australia	36	90	61	51	21	71

Table 5 Country scores according to “The 6D model of national culture”, by Geert Hofstede. **Source** The Hofstede Center 2012, Itim International, viewed 16 July 2017, < <https://geert-hofstede.com/>>.

5.2.2 Sport preferences

In Portugal, following the European trend, football is the most famous sport, followed by indoor football. It may be observed that Portugal national teams in both sports perform pretty well in the international scene.

As it was mentioned before, sporting has actually an impact of information exchange between 2 countries, reason why I decided to analyze the frequency that Portugal plays each of the away countries in these 2 specific sports.

In the **Tables 6 and 7** it is represented the number of matches that Portugal played against each of the away countries in football and indoor football, respectively. The more matches have been played, the closer the countries are in terms of psychic distance.

	Nº of matches against each national team
Spain	36
France	25
Italy	25
Germany	18
UK	23
Greece	14
Luxembourg	15
Croatia	4
Brasil	19
Angola	3
Mozambique	2
Australia	0

Table 6 Matches between the Portuguese national team of football and each away national team.

Source Zerozero 2003, ZOS lda, viewed 23 June 2017, < <https://www.zerozero.pt/>>

	Nº of matches against each national team
Spain	15
France	1
Italy	12
Germany	0
UK	0
Greece	1
Luxembourg	0
Croatia	3
Brasil	6
Angola	0
Mozambiq.	1
Australia	0

Table 7 Matches between the Portuguese national team of indoor football and each away national team.

Source Zerozero 2003, ZOS lda, viewed 23 June 2017, < <https://www.zerozero.pt/>>

5.2.3 Language Similarities

Classification by distance:

- 0: Portuguese is the native language;
- 0,25: English is spoken by more than 60% of the population;
- 0,5: Other languages that use the roman alphabet and where English is not spoken by more than 60% of the population fluently;
- 1: Languages that use different alphabets and where English is not spoken by more than 60% of the population fluently;

The levels previously mentioned are very similar with the ones defined by Brewer (2007). Nevertheless, there is a slight difference when it comes to the analysis of English as a second language. Instead of defining countries that widely use English in business, I opted to define that level of proximity to Portugal, as countries in which more than 60% of the population speaks English fluently as a second language, by other words, high proficiency English speaking countries according to the EF English Proficiency Index (2015).

	Language proximity
Spain	0,5
France	0,5
Italy	0,5
Germany	0,25
UK	0,25
Greece	1
Luxembourg	0,25
Croatia	0,5
Brasil	0
Angola	0
Mozambiq.	0
Australia	0,25

Table 8 Language proximity to Portugal, based on the English Proficiency Index.

Source Education First 2015, EF English Proficiency Index 2015, 5th edition.

5.3 Historical Ties (Colonial Relationship; World War I)

The historical ties of a country can be of major importance when it comes to its interaction with other countries. Intuitively, the closer the historic ties, the closer it is the psychic distance between both. The latter is especially important for countries that were born very early in history, which is the case of Portugal.

A long-lasting relationship between 2 countries doesn't only fosters the interaction among governments, but also among citizens and organizations, which can also lead to increasing levels of trust, knowledge about each other and consequently higher levels of trading and investment (Ghemawat 2001).

Close historic ties can arise from previous colonial relationships and also from shared wars in which 2 countries might have participated, either in the quality of enemies or allies. Nowadays, we still have examples of economic and trade benefits between some countries and its old colonies, as it is the case of Portugal and France and their respective empires (Witter 2004).

Focusing now in Portugal, known as one of the pioneers during the age of discovery, the country owned one of the biggest colonial empires of the world, controlling several colonies around the world. Adding to that, the country participated actively in some historical wars, as it is the case of the World War I. In fact, some of the reasons that dragged Portugal into the war was the fact that the country saw some of its colonies threatened by other European countries, precisely Germany. Given the historical framework of Portugal, analyzing its historical ties with the other countries is imperative for the study.

5.3.1 Colonial Relationship

As it was stated before, Portugal was the owner of one of the biggest colonial empires during several centuries, the famous Portuguese empire. Given this, it's important to know which of the 12 away countries analyzed in this study have actually a colonial relationship with Portugal. This is shown below, in **Table 9**.

Colonial Relationship classification:

- 0: Direct colonial relationship

To be classified with a direct colonial relationship, there are 2 different options. The first happens when the home country is under the authority of another country, by other words is the colony. The second option occurs when the home country is considered the mainland of several other countries, by other words it owns several colonies. Since Portugal was itself one of the biggest colonial empires, only the second option is viable.

- 1: Member of the same empire

This situation only occurs when we behold 2 colonies that belong both to the same empire. Since Portugal was itself the owner of several colonies, it does not share this relation with any other country.

- 2: No colonial relationship

As the name implies, the situation occurs in countries with which Portugal did not have any colonial relationship.

	Colonial relationship with Portugal
Spain	2: No colonial relationship
France	2: No colonial relationship
Italy	2: No colonial relationship
Germany	2: No colonial relationship
UK	2: No colonial relationship
Greece	2: No colonial relationship
Luxembourg	2: No colonial relationship
Croatia	2: No colonial relationship
Brasil	0: Direct colonial relationship
Angola	0: Direct colonial relationship
Mozambique	0: Direct colonial relationship
Australia	2: No colonial relationship

Table 9 Colonial relationship between Portugal and each of the away countries.

Source Ramos et al. (2012) *História De Portugal*.

5.3.2 World War I relationship

World War I relationship:

- 0: Ally
- 1: Neutral
- 2: Enemy

The three different options regarding the relationship of the studied countries with Portugal during the WWI is quite intuitive. Either they were Portuguese allies, enemies or neutral in the case that they didn't participate actively in the war. The relationship can be seen in **Table 10**.

	Relationship between Portugal and away countries during WWI
Spain	1: Neutral
France	0: Ally
Italy	0: Ally
Germany	2: Enemy
UK	0: Ally
Greece	0: Ally
Luxembourg	1: Neutral
Croatia	1: Neutral
Brasil	0: Ally
Angola	0: Ally
Mozambique	0: Ally
Australia	0: Ally

Table 10 Relationship between Portugal and away country during the World War I.
Source Ramos et al. (2012) *História De Portugal*.

5.4 Geographical Ties

As the name implies, in this topic we aim to measure the physical distance between two countries, since it is implicitly related with transportation costs which are imperative when it comes to internationalization. Precisely, we will measure it as the direct distance between cities, home and away, that are known to be strongest with regard to the purchasing power of population.

To this matter, a comparison between the Purchasing Power Parity (PPP) would be ideal, however due to lack of information regarding it, we will have to rely on other indicators. Gross Domestic Product has been so far, a widely used indicator by several authors and organizations, to measure the economic development of a country or region. It is defined by Eurostat, the official statistical office of the European Union as:

“GDP is the central measure of national accounts, summarising the economic position of a country or region. It can be calculated using different approaches: the output approach; the expenditure approach; and the income approach. GDP is used to analyse economic performance and cycles (such as recessions, recoveries and booms). Data in diverse currencies can be converted into a common currency to make it more easily comparable.”

GDP is able to express quite well the levels of macroeconomic activity and economic growth of a region, and is even an accurate way of comparing two different regions. In this specific case, we need a measure that is able to show the living standards of the population in general, thus the indicator used to elect the cities studied will be the GDP per capita. The latter, is obtained by dividing the GDP of a specific region by its population, thus avoiding the trap of cities with high levels of GDP and even higher levels of population, despite the fact that it still doesn't account for income distribution across the population. This way we can have a better perception of living standards.

	Strongest cities economically wise
Portugal	Lisbon
Spain	Madrid
France	Paris
Italy	Milan
Germany	Munich
UK	London
Greece	Athens
Luxembourg	Luxembourg city
Croatia	Zagreb
Brasil	São Paulo
Angola	Luanda
Mozambique	Maputo
Australia	Sydney

Table 11 Cities with the highest GDP *per capita* in each away country.

Sources Eurostat 2016, Eurostat Regional Yearbook, edition 2016, Publications office of the European Union, Luxembourg.

Australian Bureau of Statistics 2016, Australian System of National Accounts, cat. No. 5204.0, Australia.

Finally, we have the physical distance between Lisbon, the strongest portuguese city in terms of purchasing power, and its homologous cities:

Route	Linear distance
Lisbon - Madrid	501,83 Km
Lisbon - Paris	1452,99 Km
Lisbon - Milan	1685,06 Km
Lisbon - Munich	1968,35 Km
Lisbon - London	1583,96 Km
Lisbon - Athens	2850,10 Km
Lisbon - Luxembourg city	1707,47 Km
Lisbon - Zagreb	2198,33 Km
Lisbon - São Paulo	7955,30 Km
Lisbon - Luanda	5798,35 Km
Lisbon - Maputo	8392,49 Km
Lisbon - Sydney	18162,49 Km

Table 12 Linear distance between Lisbon and each one of the strongest cities economically wise.

Source Google Maps.

5.5 Development Ties

Higher levels of country development are not only likely to foster information creation but also making it accessible and comprehensive to different users (Brewer, 2007). For this reason, measuring the development of the countries in this study, is certainly a good input for the psychic distance index. It is intuitive that the higher the development of a country the closer it is to all the others (Brewer, 2007).

Regarding this matter, 2 topics are going to be subject of study: The level of development of the foreign country and the level of corruption of the foreign country.

When it comes to analyze a country development we have to take it account different aspects, from an economic to a social perspective, reason why the indicator used, Human Development Index, try to cover all these fields. Precisely, it is built on the basis of other indexes, as it will be further specified.

The second indicator, the Transparency International Corruption Index, is rather more specific. It is also something of major importance, because corruption can become a relevant hidden cost when it comes to do business (Fukuyama 2005; Ghemawat 2001).

5.5.1 Level of development of the foreign country

For a long time, economic measures were used as a proxy to human development, however, this view has changed recently and it is now recognized that human development cannot be accessed through such a simple indicator as GDP per capita. The Human Development Report Office (HDRO), organization that operates under the responsibility of the United Nations, has been one of the main contributors for this new perspective on human development. It introduced its own indicator, the Human Development Index (HDI). The HDI addresses the problem previously stated, measuring the development of a society regarding different dimensions besides monetary standards of living, namely, life expectancy at birth and knowledge levels of the population. In other words, it can be interpreted as an average of a nation's longevity, education and income.

In order to measure the 3 different dimensions, the index is composed by 3 other indexes: The Gross National Income index (GNI index), Life expectancy index and the Education Index.

In Table 13, we can observe the scores of each country on each of the 3 dimensions, as well as the HDI score and their position on the world ranking.

	HDI rank	HDI Value	Life expectancy	Mean years of schooling	GNI per capita
Portugal	41	0.843	81.2	8.9	26,104
Spain	4	0.926	81.1	13.2	45,000
France	22	0.897	82.4	11.6	38,085
Italy	27	0.887	83.3	10.9	33,573
Germany	4	0.926	81.1	13.2	45,000
UK	16	0.909	80.8	13.3	37,931
Greece	29	0.866	81.1	10.5	24,808
Luxembourg	20	0.898	81.9	12.0	62,471
Croatia	46	0.827	77.5	11.2	20,291
Brasil	79	0.754	74.7	7.8	14,145
Angola	150	0.533	52.7	5.0	6,291
Mozambique	181	0.418	55.5	3.5	1,098
Australia	3	0.939	82.5	13,2	42,822

Table 13 Human Development Index (HDI) scores and rankings.

Source United Nation 2016, Human Development Report, ISBN: 978-92-1-126413-5, Human Developed Report Office.

5.5.2 Level of corruption in foreign countries

To measure the level of corruption in foreign countries, the Corruption Perceptions Index (CPI) was the tool used. This index is elaborated by an independent and international organization that aims to fight corruption around the world, called Transparency International. The data used to build the index is collected from several reports elaborated only by credible institutions (Corruption Perceptions Index 2016: Full Source Description). The index has a special focus on corruption among the public sector and has regards to topics as the “access of civil society to information on public affairs”, “the accountability of the executive to oversight institutions

and of public employees for their performance”, the existence of “Legal, political and public integrity mechanisms effectively prevent public officeholders from abusing their positions”, among many others (Corruption Perceptions Index 2016: Full Source Description). Basically, the index tries to measure the levels of transparency and power abuse across countries. Briefly explaining the statistics behind it, each of the topics analyzed is standardized on a scale from 0 to 100, where a 0 equals the highest level of perceived corruption and 100 equals the lowest level of perceived corruption. Finally, the average of the scores available provided the final score of each country corruption index.

Similarly to the HDI ranking, the lower the level of corruption within a country, the closer it is to all the others in terms of psychic distance.

In Table 14 we have the scores of our countries of interest, as well as their position in the world rank:

	CPI score (0 to 100)	World rank
Portugal	62	29
Spain	58	41
France	69	23
Italy	47	60
Germany	81	10
UK	81	10
Greece	44	69
Luxembourg	81	10
Croatia	49	55
Brasil	40	79
Angola	18	164
Mozambique	27	142
Australia	79	13

Table 14 Corruption Perception Index scores and rankings.
Source Corruption Perception Index report 2016.

5.6 Information Ties

As it has been mentioned before, the role that information plays in International Market Selection (IMS) is critical to improve managers' decision-making process. Although it is indispensable that primary knowledge - knowledge that is created by first-hand experiences - is created when a company goes abroad, secondary information - information acquired through the analysis of primary sources - is usually already existent and is extremely useful for learning purposes. The information available allows managers to acquire and create both institutional and business market knowledge that enables them to understand the market conditions properly. (Johanson and Vahlne, 1977; Brewer, 2007)

The amount of secondary information available with respect to a specific country can vary due to a wide array of factors. Among them we have the size and importance of the country and also the social exchange between a pair of countries, by other words the extent of emigration and immigration between them. (Wiedersheim Paul and Welch 1975) To conclude, the more information respective to a country exists, the closer it is to every other country in terms of psychic distance.

In an attempt to find out how far is each country from Portugal in terms of information available, 2 indicators will be used. The first has regard to the number of Portuguese emigrants in each away country and the number of away country immigrants in Portugal. The second indicator is secondary information availability. Similarly to Brewer (2007), that analyzed this indicator through the number of catalog entries for each away country existent in Queensland University library, I measured it through the number of catalog entries with respect to each away country existent in Católica Lisbon School of Business and Economics library.

5.6.1 Social exchange numbers

Regarding the social exchange matters, it is now clear that it definitely fosters the exchange of information between countries. Thus, it is safe to say that it exists a positive correlation between social exchange numbers, immigration and emigration, and the closeness between two countries in terms of psychic distance.

Concerning the Immigration numbers of Portugal relatively to each of the away countries studied, the Tables 15 and 16 identify the stock of Portuguese born population living abroad by country and the number of immigrants by country of origin living in Portugal respectively.

	Portuguese emigrants abroad
Spain	98975
France	617235
Italy	5241
Germany	75110
UK	92065
Greece	292
Luxembourg	60897
Croatia	51
Brasil	18538
Angola	96203
Mozambique	56891
Australia	1475

Table 15 Portuguese emigrants living abroad, by country of destiny.
Source Portuguese Emigration Factbook 2015.

	Immigrants in Portugal by country of origin
Spain	10019
France	8440
Italy	6130
Germany	9035
UK	17230
Greece	248
Luxembourg	144
Croatia	174
Brasil	82590
Angola	18247
Mozambique	2809
Australia	269

Table 16 Immigrants living in Portugal, by country of origin.
Source Relatório de Imigração, Fronteiras e Asilo 2015.

5.6.2 Number of catalog entries for each away country in João Paulo II library

The second indicator has respect to secondary information available, precisely the number of catalog entries about each away country in the library João Paulo II, the library of Católica Lisbon School of Business and Economics.

	Nº of catalog entries in the library
Spain	309
France	265
Italy	251
Germany	134
UK	235
Greece	80
Luxembourg	10
Croatia	3
Brasil	1552
Angola	848
Mozambique	456
Australia	47

Table 17 Number of catalog entries regarding each away country, in the digital fund of the library João Paulo II.

Source Library João Paulo II.

5.7 Political Ties

It is clear that the political ties between a pair of countries has a strong impact on the exchange of information between them. Precisely, a closer political relationship tends to foster information flows and thus shorten the psychic distance among them. The distance decreases because there is an increased awareness about market conditions, both by the home government and by home enterprises (Department of Foreign Affairs and Trade 2005; Wiedersheim-Paul and Welch 1975).

The political ties can be measured in several ways, the ones chosen for this study were the quantity of embassies and consulates abroad and hosted, and the number of bilateral trade agreements between Portugal and each away country.

5.7.1 Number of Portuguese embassies and consulates abroad and the number of embassies and consulates hosted

Foreign missions - embassies and consulates - are institutions that represent a country in another country abroad. They represent its country to an extent where the building is considered national soil abroad. In fact, its main goal is to support to citizens abroad, by providing them useful information about their stay, whether it is short or long, and defend them if necessary. Following this, it means that foreign missions are bridging information gaps, which in turn will bring countries together.

A couple of studies also show that foreign missions have a wider impact than it might seem at first sight. Gil-Pareja et al., (2005), studied the impact of embassies and consulates on tourism and concluded that each of them can have an impact varying from 15-30%. Rose (2005), also concluded that for each additional foreign mission, the bilateral exports between 2 countries should increase from 6-10%.

The aforementioned studies support the idea that foreign missions have a key role on information flows, precisely they foster information roles and consequently the interaction between countries.

In the **Tables 18 and 19** you can see the number of Portuguese foreign missions abroad and the number of away foreign missions hosted in Portugal, respectively.

	Nº of Embassies	Nº of Consulates	Nº of honorary consulate
Spain	1	3	10
France	1	5	8
Italy	1	0	12
Germany	1	3	0
UK	1	2	4
Greece	1	0	3
Luxembourg	1	0	0
Croatia	1	0	0
Brasil	1	9	27
Angola	1	2	1
Mozambique	1	2	1
Australia	1	1	5

Table 18 Number of Foreign Missions hosted in Portugal, by type and country of origin.
Source Portal das Comunidades Portuguesas.

	Nº of Embassies	Nº of Consulates	Nº of honorary consulates
Spain	1	3	1
France	1	1	0
Italy	1	0	3
Germany	1	0	3
UK	1	0	1
Greece	1	0	4
Luxembourg	1	0	1
Croatia	1	0	0
Brasil	1	2	1
Angola	1	2	0
Mozambique	1	1	0
Australia	1	0	0

Table 19 Number of Portuguese Foreign Missions abroad, by type and country of origin.
Source Portal das Comunidades Portuguesas.

5.7.2 Bilateral Trade agreements

A bilateral trade agreement represents itself information about a foreign economy, which means that the more exist the closer the psychic distance between 2 countries. They are paramount for the knowledge of market conditions and moreover because they facilitate and encourage the creation of new businesses, as well as the development of existing ones.

In **Table 20** we can access the existent bilateral trade agreements in force between Portugal and each of the studied countries. These agreements have respects to economic matters and were all initiated after 1980.

	Nº of bilateral agreements celebrated
Spain	4
France	1
Italy	1
Germany	4
UK	1
Greece	1
Luxembourg	1
Croatia	4
Brasil	9
Angola	6
Mozambique	7
Australia	1

Table 20 Number of bilateral agreements celebrated between Portugal and each away country.

Source AICEP 2017, *Portugal: Acordos Bilaterais Celebrados na Área Económica*.

5.8 Constructing the Index

Once again, the purpose of the index is to measure how far is each country from Portugal in terms of Psychic Distance. However, in order to do that, it is necessary to run an individual analysis to each of the 7 ties - Commercial, Political, Historic, Geographic, Social, Information and Development – even though the index is only meaningful if all of them are contemplated. To analyze each of the 7 ties, I had to depict them into sub indicators, as it was presented before. In the end, the ties were depicted into 15 sub-indicators, that can be measured and thus allow the comparison between the batch of 12 countries.

Once all the data is collected, it is possible to construct the index. The construction process was essentially based on the globalization index developed by A.T Kearney (2003) and Foreign Policy Journal. Among the 15 indicators, we have different measurement units. For instance, millions of dollars were used for international trade, while kilometers were used to measure geographical distance. For this reason, it was necessary to proceed with a standardization process to ensure that all the variables can be expressed homogeneously. The process used is known as panel normalization of data (Lockwood 2004). It consists in normalizing all the values on a scale from 0 to 1. The absolute numbers at the extremes of each indicator are assigned as 1 and 0, where 1 represents the most distant and 0 the closest in terms of psychic distance. Intermediate values are assigned with relative values between 0 and 1 according to their absolute value.

Once the individual analysis is finished, it is possible to sum up all the values regarding each of the 15 indicators and compute the Psychic Distance Index. Intuitively, the index scores vary on a scale from 0 to 15, where the lower the score, the closer the country is from Portugal. Furthermore, once we have all the scores, it is possible to rank all the 12 countries, with regard to their psychic distance from Portugal.

5.9 Interpreting the Index

The index is definitely a strong tool due to the variety of indicators it comprises. It might turn out that a pair of countries is very similar with regard to one indicator, but very different regarding others. We can see in **Tables 20 and 21**, all the individual scores of each country in the 15 indicators analyzed, and furthermore the final Psychic Distance Index score, as well as the rank within the group.

	International Trade	FDI stocks	Trade Agreements	Foreign Missions	Colonial Ties	Shared Wars	Geography	Culture
Spain	0,000	0,000	0,625	0,531	1,000	0,500	0,000	0,074
France	0,646	0,818	1,000	0,584	1,000	0,000	0,054	0,295
Italy	0,855	0,835	1,000	0,732	1,000	0,000	0,067	0,506
Germany	0,569	0,770	0,625	0,810	1,000	1,000	0,083	0,722
UK	0,820	0,770	1,000	0,820	1,000	0,000	0,061	1,000
Greece	0,993	1,000	1,000	0,875	1,000	0,000	0,133	0
Luxembourg	0,995	0,602	1,000	0,982	1,000	0,500	0,068	0,460
Croatia	0,999	1,000	0,625	1,000	1,000	0,500	0,096	0,011
Brasil	0,957	0,709	0,000	0,000	0,000	0,000	0,422	0,159
Angola	0,889	0,704	0,375	0,800	0,000	0,000	0,300	0,398
Mozambique	0,984	0,955	0,250	0,846	0,000	0,000	0,447	0,500
Australia	0,996	0,997	1,000	0,865	1,000	0,000	1,000	0,801

	Sports	Language	Information	Social exchange	Development	Corruption	PDI	PDI rank
Spain	0,000	0,500	0,701	0,826	0,025	0,365	5,147	2
France	0,619	0,500	0,514	0,000	0,081	0,190	6,303	3
Italy	0,253	0,500	0,799	0,982	0,100	0,540	8,169	6
Germany	0,750	0,250	0,895	0,866	0,025	0,000	8,365	7
UK	0,681	0,250	0,795	0,826	0,058	0,000	8,080	5
Greece	0,772	1,000	0,937	0,999	0,140	0,587	9,437	11
Luxembourg	0,792	0,250	0,990	0,903	0,079	0,000	8,621	9
Croatia	0,844	0,500	1,000	1,000	0,215	0,508	9,299	10
Brazil	0,536	0,000	0,000	0,839	0,355	0,651	4,627	1
Angola	0,958	0,000	0,669	0,817	0,779	1,000	7,691	4
Mozambique	0,939	0,000	0,825	0,905	1,000	0,857	8,508	8
Australia	1,000	0,250	0,984	0,998	0,000	0,032	9,923	12

Tables 20 and 21 Individual scores of each country in each one of the 15 indicators analyzed and the final PDI score, composed by all the 15 sub scores.

Source Own calculations, following the panel normalization of data process.

As an example of the previously stated, we can have a look on Mozambique and Germany scores. Mozambique is a former colony of Portugal, given this it would be expected to have a close relationship with Portugal and intense information exchange, because of the historic ties developed between the 2 countries, the fact that they fought besides each other during the first

world war, and even more impactful, the fact that both countries share the same native language, Portuguese. On the other hand, we have Germany who was an enemy of Portugal during the first world war, and with a native language certainly different from Portuguese. Nevertheless, the index scores of these 2 countries, tell us that Germany is closer to Portugal than Mozambique in terms of psychic distance. The latter can be explained by the impact of other indicators, as it is the case of development and commercial ties. Nowadays Germany is one of the most developed countries in the world and has little traces of corruption within the public sector. Furthermore, Germany is a powerful country economy wise, which can be observed through the extent of international trade it has with Portugal. The same cannot be said about Mozambique, since it is considered the less developed country among the 12 and has serious corruption problems within the public sector.

One might be biased to think that some indicators, as for example cultural similarities, are the main driver of information flows between 2 different countries. However, the aforementioned clearly shows us that all the different ties should be taken into consideration, because they all impact the knowledge creation and flow between countries.

As the table shows, Brazil ended up with the lowest Psychic Index Score, 4,627, and so it ranks first among the 12 countries. This can be explained through several indicators combined: a rather strong FDI stock exchange with Portugal, same native language, former Portuguese colony, alliances during the first world war, close political relationships represented through a few trade agreements and a high number of Portuguese foreign missions hosted, and even a fair amount of information available in Portugal.

It is important to bear in mind, that by Brazil ranking first among the 12 countries, it doesn't necessarily mean that it is where Miitik should expand its operations. However, it is the country where it is more likely for Miitik to understand the market conditions and how to operate there.

6. Conclusion

Going back to the genesis of the dissertation, the research has the aim to support Miitik with its International Market Selection. As it was mentioned before, Miitik is in a very early stage of international expansion and according to researchers, a critical resource that companies need during this stage is knowledge (Johansson and Wiedersheim Paul, 1975).

Brewer (2001), states that managers rely heavily on information flows to create and acquire knowledge about foreign markets, by other words, the easier it is to acquire information about a foreign country, the easier it is managers' decision-making process.

The psychic distance concept is the right approach to address Miitik's lack of knowledge, once it clearly states some major factors that actually influence the information flows between countries. The Psychic Distance index was latter designed with the objective of operationalizing the concept. In fact, it tries to cover a wide array of factors that have been proved to influence the flows of information. After choosing the batch of countries with attractive characteristics for Miitik's business, the index enables the company to realize which are the ones that have more information readily available, or at least from which ones it is easier to acquire information. To conclude, the index measures the easiness of managers to get familiar with each foreign market.

Another characteristic that makes the tool so strong, is that it can be applied to companies operating in different industries. Although some changes might be necessary in order to reflect the reality of the company in analysis, it can be used for any industry and to compare any pair of countries in the world, as long as there is data available.

Lastly, the index has the advantage of being nonsymmetrical. For instance, the psychic distance from Portugal to Mozambique is different than the one from Mozambique to Portugal. This characteristic is provided by the fact that some of the indicators that compose the index are nonsymmetrical themselves. It is the case of development and information ties. Indeed, given that Portugal is more developed and has more information available than Mozambique, it is closer to Mozambique than Mozambique is from Portugal.

7. Limitations

There is still some disagreement about the correlation of psychic distance with International Market Selection. For instance, some authors (Andersen 1993) defend that the model is too simplistic and is not explicit enough about the stages of Internationalization that an enterprise should follow.

Another limitation of the model is that although it states that the information flows are facilitated by the extent of ties between 2 countries, and even if a country is considered close to the other, there is still a dependence on the personal characteristics of the manager. He must be

able to understand the information existent in order to acquire the knowledge about a foreign market and thus get familiar with it, otherwise it is likely that the company won't be able to succeed abroad. (Petersen and Pedersen 1996) To sum it up, the firm's success relies of the managers conditions, which is not contemplated by the index.

It is intuitive that some indicators might have different levels of impact on psychic distance than others. If we think about international trade, it is more likely to foster information flows than shared sport interests do. This means that the index would become more accurate if the indicators would have different weights, that actually represent the differences on the impact of each indicator. However, in order to do such change, further research still has to be done in order to understand the exact correlation between each indicator and the extent of information flow.

Lastly, it is important to realize that the index doesn't provide a final recommendation about where the company should go. Since the index is not industry specific, it doesn't account for certain aspects that are imperative when it comes to internationalization. In fact, the results of the index show which are the countries where the company is more like to obtain precise information about market conditions, and understand how it should operate overseas. Nevertheless, the index shouldn't be confused with a PESTEL or a 5 forces analysis. These analyses provide an industry specific analysis that the psychic index doesn't, and is usually paramount when it comes to International Market Selection.

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9. Appendix

Appendix 1 Psychic Distance Index, by Paul Brewer, 2007.

Table 1. National Psychic Distance Indicators		Primary Elements	Formative Indicators	Calculations
Commercial ties	1	Two-way trade	The proportion of total Australian exports going to each country in 2002–2003 (expressed as a decimal fraction) plus the proportion of total Australian imports sourced from each country (expressed as a decimal), normalized.	
	2	Stock of foreign investment	The total Australian outward FDI stock invested in each country in 2001–2002 (expressed as a decimal fraction of the total outward FDI stock) plus the proportion of total inward FDI stock into Australia in 2001–2002 from each country (expressed as a decimal), normalized.	
	Political ties	3	Trade agreements	The number of formal bilateral or regional free-trade treaties in operation between Australia and each country in 2002–2003, normalized.
		4	Value of aid programs	The dollar value of official Australian aid programs to each country in 2004–2005, normalized.
		5	Trade representation offices	The number of Austrade offices in each country in 2003 plus the number of trade offices from each country in Australia, normalized.
	Historic ties	6	Colonial relationship	Direct colonial relationship = 1, membership of the same empire = .5, and no colonial relationship = 0. Values are added for each country and normalized.
		7	Shared wars	World War I: ally = 2, neutral = 1, and enemy = 0; World War II: ally = 2, neutral = 1, and enemy = 0. Values for each war are added for each country and

Geographic ties	8	Geographic proximity	The direct distance between the closest two major port cities in Home and Away in kilometers, normalized.
Social ties	9	Cultural similarities	The cultural distance index that Fletcher and Bohn (1998) developed, normalized.
	10	Sport preferences	A country that regularly plays against Australia in cricket, rugby union, rugby league, and tennis is allocated 1 for each sport. These values are added and normalized.
	11	Language similarities	English is widely spoken = 0, English is widely spoken in business = .25, other languages that use the Roman alphabet are spoken = .5, and other languages that use other alphabets are spoken = 1.
Information ties	12	Secondary information availability	Value equals the number of catalog entries for each country in the University of Queensland library, normalized.

Primary Elements		Formative Indicators	Calculations
	13	Immigration numbers	The number of Australians living in each country plus the number of Australians visiting each country in 2001 plus the number of residents of Australia originating from each country plus the number of visitors to Australia from each country in 2001, normalized.
Development	14	Level of development of the foreign country	The United Nations human development index (normalized)
	15	Level of corruption of the foreign country	Transparency International corruption index (normalized)