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RESEARCH

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# Working Paper Series


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# Editorial Comments

Welcome to the Working Paper Series of Business Research group. This issue of the Working Papers Series has been contributed to by staff and Research Higher Degree students of the School of Commerce and Law (previously Commerce and Marketing) the Working Paper Series is being collected under the auspices of the Business Research Group (BRG) which is a research group under CQUniversity's Institute for Resource Industry and Sustainability (IRIS).

At the time of the Call for Papers for the Series papers were called for from any of the disciplines in the School, for example, marketing, human resources management, organisational behaviour, organisational theory, finance, economics, accounting, information technology, strategy or property, particularly where the focus was upon regional issues. This diverse group of potential subjects was (and remains) indicative of the wide range of academic topics that are covered by our school.

As will be seen by the papers contained in the first series the diverse range of topics is also replicated in the research interests of the RHD students being supervised by academics within the School. Relevantly, two of the five papers in the series are RHD students under the supervision of Dr Ho Yin Wong a Senior Lecturer in Marketing.

In terms of those papers:

- Nadia O'Connell, PhD Candidate and Dr Ho Yin Wong examine how productive relationships can be built with international education agents. The paper investigates the role of education agents in the recruitment of international students to a particular university.
- Parves Sultan, PhD Candidate and Dr. Ho Yin Wong explore the perception of students with regard to critical antecedents, dimensions and outcomes of service quality in the context of a university in Australia. The paper reports on the focus group findings conducted by Parves.

Dr Ho Yin Wong has also submitted two papers through which we catch a glimpse of Dr Wong' research interests. The first examines the concept of culture in international marketing. The second paper entitled 'Environmental Business Scanning Literature – Past, Present and Future Research Agenda' makes research propositions that may fill the research gaps identified in the literature.

The final paper examines a totally different topic: retirement savings. Jenny Butler, Lecturer in Tax, in her paper discusses the regulatory system that exists to safeguard the nation's superannuation system and questions whether the regulations that exist are justified given the current superannuation environment.

We thank the authors who have engaged with such a wide range of topics in this series and also the reviewers who have given so generously of their time and expertise. We hope that you, the reader, find this issue as interesting as we have.

The Editors
Professor Sheikh Rahman, Dr Rakesh Gupta and Associate Professor Kristy Richardson

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# Building productive relationships with international education agents

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**Abstract** - The purpose of this paper is to look at a particular university and investigate the role of education agents in the recruitment of international students to this institution. The study highlights limitations of agency theory, having reduced utility for appraising and describing education agent and university relations and looks at relationship marketing as a complimentary method of agent governance and relationship building for enhanced business performance.

A case study approach was adopted for this pilot study, using a single case design with multiple embedded units of analysis. In-depth, one on one interviews were conducted with four industry experts from an educational institution. Additional information was sourced through the internet and from government reports. Data was analysed using Nvivo and manual qualitative data analysis techniques.

This paper fulfils an identified research gap through investigating techniques that institutions could adopt to motivate and improve relationships with education agents. No previous studies have concentrated specifically on the recruitment of international students through this channel.

## Definitions

For the purpose of this paper the following definitions are given for specific terms used throughout the paper.
**International education** - the industry of recruiting international students to study at institutions.
**Education agents** – also commonly referred to as recruitment agents or international education agents, refers to those businesses whose primary mission is to recruit international students into educational institutions, receiving commission for doing so.

## Introduction - Industry Brief

International education is an important industry for the Australian economy. In 2007/08, international education contributed $13.7 billion to the Australian economy, measured through export earnings, including international student expenditure on tuition fees and related living expenses and tourism generated from visiting relatives (Australian Bureau of Statistics, 2008). Education is the second largest services export sector and now the third largest export sector overtaking tourism. Over the last 10 years the industry has achieved 15 per cent average growth per annum (Austrade 2008).

The Australian University's International Directors Forum (AUIDF) benchmarking study (2006) showed that 62.3% of students recruited to study in Australia were recruited by an education agent.

Education agents play an integral role in the industry and have developed as businesses through which international students can be recruited to educational institutions. The number of education agents around the world is unknown, however the Education Agent Training Course (EATC), developed in collaboration between Australian Education International (AEI), the Department of Immigration and Citizenship (DIAC) and Australian international education peak bodies has registered nearly 10,000 education agents since 2005 (PIER 2009). Education agents provide students with an array of advice about studying overseas and receive a commission typically between 10 – 25% from the institution for enrolling students, depending on the sector.

Education agents have established as a business in all countries where international students come from, with a higher prevalence in those countries which have more difficult visa criteria to enter Australia as a students, such as India, Nepal, Bangladesh and China.

Despite high international student recruitment through education agents, little has been written about marketing through this channel or how to build strong relations with them.

**Aims of this study**

Predominantly, this research was driven by the questions:

1. How does *agency theory* lend itself to the education agent/ university relationship and can contributions be made to this theory when examining it from an international education industry perspective?
2. Is a *contract* the most distinct and crucial element in a principal/agent relationship?
3. Is *information asymmetry* an agency problem between education agents and universities or is information sharing between both parties more the norm?
4. What role does *relationship marketing* and *agency theory* play in the relationship between universities and education agents in the recruitment of international students when looked at from the universities point of view?
5. Is *commitment* and *trust* the most distinct variables for building and maintaining a relationship with education agents?

## LITERTURE REVIEW

This paper will look at agency theory and relationship marketing as a theoretical lens to examine business approaches that could be utilised in the management of education agents, including specifically the crucial nature of the contract, information asymmetry and relationship marketing techniques.

## AGENCY THEORY

Agency theory is concerned with the use of contractual terms to control and coordinate the relationship between the principal and their contracted agent (Weitz and Jap 1995; Jensen and Meckling 1976). Agency theory is also concerned with

monitoring behaviour, using power and structuring agent incentives to prevent shirking and the instance of information asymmetry (Fama and Jensen 1983; Tosi, Katz et al. 1997; Garg 2000).
Agency theory has been widely applied in the analysis of principal / agent frameworks, however, appears to have limitations which reduce its functionality as a framework for appraising marketing channel interactions (Vermillion et al. 2002).

**Agency theory and the crucial nature of a contract**

The majority of agency theory literature is concerned with controlling mechanisms such as setting contracts to curtail conflict of interests (Weitz & Jap 1995), monitoring the agents action (Eisenhardt 1988), using power in asymmetric relationships, with the basic axiom of agency theory assuming that agents act opportunistically and the assumption of goal divergence (Jensen and Meckling 1976, Eisenhardt 1989, Garg and Rasheed 2006).

Agency theory was first introduced as a conceptual model to describe the relationship between a principal and an agent where the principal delegates work to an agent (Thompson 1967; Ouchi 1979). Agency theory attempts to describe this relationship using the metaphor of a contract. Jensen and Meckling (1976 p. 6) define "an agency relationship as a contract under which one or more persons (the principal) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent."

Several authors (Fama and Jensen 1983; Tosi, Katz et al. 1997; Garg 2000) state that the most distinct feature and crucial concept of agency theory is the contract, where a system of complex written and unwritten contracts provide an effective disciplinary mechanism for disparate individuals. With the contract aiming to control divergent self-interest of the agent, specifying the rights, obligations, reward structures and monitoring systems between the two parties.

Some authors have already identified limitations, criticising the stressed importance of the contract in agency theory. Mintzberg (1990) states that mathematical models that specify contract conditions, do not truly represent reality, due to the impossibility of capturing all eventualities and the changing nature of the principal-agent relationship. Other authors (Perrow 1986; Eisenhardt 1989) believe that focus on the contract ignores political and interpersonal aspects of the principal-agent relationship.
The above noted studies lack empirical evidence to support their claim, being either conceptual studies or based on laboratory design, not representative of an actual business environment. Research regarding the contract in agency theory literature provides opposing points of view, with the contract being either the critical element in a principal/agent relationship or in contrary not allowing for all eventualities and the personal nature of relationships.

This research will look into the critical nature of the contract between an educational institution and education agents to see if it is deemed to be crucial or if relationship management also plays a strong role in governing and motivating education agents.

The next section will look at another issue as defined in agency theory literature - information asymmetry, firstly looking at conceptual, then empirical research conducted on this topic to provide background research on this topic, with the aim of

later seeing if there is a prevalence of information withholding from both institutions and education agents in the international education industry.

## INFORMATION ASYMMETRY

### Conceptual research into information asymmetry

Information asymmetry is where the agent holds information of value to the principal and the agent will use the incidence of information asymmetry for their own interest (Jensen and Meckling 1976; Huang et. al. 2006; Husted 2007). In the context of this research, the instance of information asymmetry will be viewed not only as the agent withholding information, but the potential withholding or lack of information transferred between both the principal and the agent.

Huang et. al. (2006) provides a conceptual framework of information asymmetry gaps in their bilateral agency relationship model, showing possible instance of information asymmetry in the bank industry. This study states that information asymmetry is an important issue for the sector, but is a very industry specific conceptual paper which provides a model that may not be transferable or relevant to all industries.

Husted (2007) states that many business problems are due to elements of asymmetrical information and analyses this problem using information economics and the principal/agent model, providing possible solutions to instances of information asymmetry. Again this paper provides excellent conceptual ideas, but requires further empirical testing.

### Empirical research into information asymmetry

Several empirical studies have concentrated on the prevalence of information asymmetry in a variety of business settings. Studies of other business structures and settings include shareholder arrangement (Rutheford and Buchholtz, 2007), franchises (Doherty and Quinn, 1999), sales manager and sales employee situations (Sridhar et. al 1997) and incentive contract arrangements (Baker et al. 1994). These studies have highlighted the need to take action to reduce the level of information asymmetry between for example board members and shareholders; franchisee and franchisor; manager and employee; or company and worker. Findings from these studies have verified that information asymmetry is an important issue and the need to implement measures to reduce levels of information asymmetry is warranted.

For example Sridhar et al. (1997) article on information asymmetry between sales managers and sales employees found information asymmetry to be an issue in their empirical research of a Fortune 100 organisation. This study is based on the antecedents of information asymmetry that agency theory stipulates agency problems, including information asymmetry arise between a sales manager and a sales employee either because their goals are incongruent or because performance is difficult to monitor or verify. The construct looked at the degree sales employees perceived they had greater information regarding performance outcomes and methods than their supervisor. The study found the greater the information asymmetry the lower the sales employees performance and the greater the dysfunctional behaviour by subordinates.
Information asymmetry literature is limited in that studies have been of business settings where one party stands to gain from withholding information. Few empirical studies look specifically at the prevalence of information asymmetry in a business

setting where the agent operates as an independent business from the principal, such as education agents and educational institutions. Studies have also concentrated on looking for the prevalence and effect of information asymmetry rather than prevalence of information sharing and cooperation. With relationship marketing becoming a more contemporary style of conducting business, the author believes that organisations are looking for ways to be more cooperative in their approach to information sharing, for the mutual benefit of both parties. This study will looks at the prevalence of information asymmetry and information sharing through interviews with education industry experts and analyse if industry practice contradicts this aspect of agency theory.

Eisenhardt (1989) notes that agency theory could benefit from an additional sociological component and recommends using agency theory in conjunction with complimentary theories. The author of this paper suggests agency theory is limited due to the deemed crucial nature of the contract and the stated prevalence of information asymmetry as a major agency problem and believes that agency theory could benefit from a more holistic and cooperative approach such as relationship marketing, for maximum gain for both parties. While some elements of agency theory are useful in analysing a principal/ agent relationship, a melding of this approach with relationship marketing techniques may prove more useful.

In summary, previous studies have 1) placed too much emphasis on the critical nature of the contract, 2) overstressed the prevalence of information asymmetry and 3) presented contrasting views to contemporary relationship marketing approaches.
The next section will look at relationship marketing to examine whether together with agency theory, governance of education agents by educational institutions can be further enhanced.

**RELATIONSHIP MARKETING**

In the international education industry, agents simultaneously represent more than one institution, creating a conflict of interest between whom the agent should favour. In this situation contracts between institutions are relatively similar, therefore institutions must use things other than the contract to govern and influence education agents to recruit for them. This is where relationship marketing may play an integral role, with as will be shown in the below discussion, institutions could compete more vigorously through forging relationships with education agents and using various relationship marketing techniques.

Agency theory and relationship marketing represent contrasting views about channel relationships, from a focus of transactional exchange to a relational exchange, where value is created through collaboration and commitment (Vermillion et al. 2002).

Relationship marketing is concerned with the notion of being a long term “win-win” situation that is non-adversarial (Ganesan 1994) by developing trust, commitment among other variables to develop and maintain a productive relationship (Dwyer et al. 1987, Morgan and Hunt, 1994; Robicheaux and Coleman, 1994; Doney and Cannon, 1997; Smith and Barclay, 1997; Wilson 1995).

The concept of relationship marketing has been called a major directional change in both marketing theory and practice (Morgan and Hunt 1994) and also a genuine

paradigm shift (Kotler, 1991). Practitioners are placing more emphasis on using relationship strategies such as building trust and commitment to maintain continuity rather than the use of authoritative control mechanisms (Weitz and Jap 1995).

Relationship marketing is "the process of creating, maintaining and enhancing strong, value-laden relationships with customers and other stakeholders." (Armstrong and Kotler 2000 p. 11). In fact, understanding how "to form, maintain and improve relations between customer and service provider has become an essential strategic element in the success of the service enterprise" (Gemunden, Ritter et al. 1997 p. 82). Morgan and Hunt (1994) theorise that the presence of relationship commitment and trust is central to successful relationship marketing and state that commitment and trust are more important than power and its ability to control others.

An extended list of relationship variables which have both theoretical and empirical support include commitment, trust, cooperation, mutual goals, independence/ power imbalance, comparison level of the alternative, adaptation, non-retrievable investments, shared technology, summative constructs, structural bonds and social bonds (Wilson 1995).

Of these commitment and trust are the most commonly included variable in relationship models (Dwyer et al. 1987; Anderson and Weitz 1990; Moorman at al. 1992; Wilson 1995)

Palmatier et al. (2006) meta analysis on factors influencing the effectiveness of relationship marketing found strong support for the fundamental premise of relationship marketing that strong relationships positively affect performance. They found expertise and communication to be the most effective relationship building strategies and commitment and trust ranking the highest variables for service industry exchanges through a channel partner to affect the seller's objective performance.

Although theoretical and empirical research on relationship marketing is extensive, descriptive information about channel relationships in the real world context has not been exploited and much of the qualitative research has focused on consumer behaviour rather than relationship marketing between firms (Weitz and Jap 1995). Trust and commitment are re-occurring prominent variables appearing in research, but further testing of other key elements, particularly extrinsic elements, to build and maintain relationships between a principal and an agent is required. This research will address these limitations, by looking at relationship in a business to business environment and further examine other possible key elements, in addition to trust in commitment, that effect relationships between exchange partners.

**Research methodology/ research methods**

Four marketing and recruitment practitioners from an Australian University were invited to participate in one on one in-depth interviews as part of a pilot study. In-depth interviews were selected for greater control over respondent selection, typically resulting in greater context and flexibility in the inquiry process (Cassell and Symon 2004). Interviews allow for greater depth of information through building a close rapport between interviewer and interviewee (Hedges 1985) (Webb 1995) and are appropriate when interviewees are professional people (Tull and Hawkins 1990).

The case study comprised of sales and marketing practitioners from a University involved in international student recruitment. Each respondent was responsible for agents in a different geographical area including China, India, South East Asia and Europe. The University was selected due to an assumed expertise in recruiting international students, given their high international student population of approximately 30%. This assumed expertise was determined though multiple units of analysis (Yin 2003), including an examination of government statistical reports and the University's annual report. These reports were examined to determine the success in international student recruitment of the University under analysis, with an increase in student recruitment and high proportion of international students reflecting the University's strength and expertise in the field.

Each interview lasted for approximately one hour and was digitally recorded and transcribed verbatim. Semi structured interview questions were followed, allowing for similar questions to be asked of reach respondent, while allowing participants to speak freely and to be probed on certain points raised (Grbich 1999).

Ethical approval was obtained from the participants prior to the interview and authorised in writing. Validity of the data was ensured by using multiple sources of evidence to establish a chain of evidence and through having key informants review draft reports. Strict procedures and protocol for data collection and storage was adopted to ensure the reliability of the data. Data collected was analysed using content analysis techniques using both Nvivo and manual data manipulation. Methods include pattern matching, explanation building, memoing and use of logic models to extract and express the data collected.

## CASE STUDY ANALYSIS AND INTERPRETATION

### Agent contract not most crucial element

*Theme No. 1. All respondents stated that although the contract has a role to play it is not a crucial element in the relationship between education agents and universities.*

As discussed in the literature review section of this paper, several agency theory authors believe that a contract is the most crucial element in a relationship between a principal and agent (Fama and Jensen 1983; Tosi, Katz et al. 1997; Garg 2000). This study aimed to verify if this was also true in the international education industry in a relationship between universities and education agents. Overall, respondents believed that although the contract played an important role, it was not the most crucial aspect and therefore contradicts agency theory.

One industry representative explains "*I guess the contract, in as much detail as it has, can't cover everything that can happen. There are extra things that you have to do and you can never really compensate for those extra things you have to do*."

A second industry representative interviewed explains "*a contract is a piece of paper that isn't personal and the relationship is what gets you the numbers. You can have all the contracts and pay all the commission in the world but if you don't have a relationship, nothing happens.*"

A third industry representative believes that having an onshore presence would be a stronger force than a contract. *"I would think that if we had a representative established offshore this would help in terms of monitoring as well as enforcing what we wanted by more frequent visits. We have a representative offshore in South East Asia. I think that this would be a stronger force than the contract as in most cases once the contract has been signed very few people go back to it."*

Feedback from experts in the international education industry indicates that although the contract has a role to play, especially in setting up initial boundaries under which agents can operate, it is not considered to be the most distinct or crucial concept as other agency theory authors suggest. As seen in the above comments, international education industry experts responses contradict this aspect of agency theory and contrastingly believe that a more cooperative and personal approach to monitoring and working with agents is important.

**Contract seldom referred**

*Theme No. 2. All respondents stated that the contract is seldom referred to.*

Theme two is captured in the experience of one industry expert stating "*I think in reality, a contract is just perceived as a piece of paper, that once it is signed no one is going to look at it and that is probably the reality, so for example having a contract with a particular agent does not mean they are necessarily going to recruit for you. I have discovered when I started working at this institution we had a contract with one of the largest agent in China for five years or so, but they have never recruited a single student for the institution, so to me that is a waste of effort, having a contract in place could mean nothing."*

A second industry expert stated "*the only time we would be referring to it is when there is a dispute about incentives. Incidences arise when an agent think they have sent a lot more students than they have, so they would be disputing the number of students or the level of commission they should be on."*

As shown in comments made by industry experts interviewed, although the contract plays a role, it is not the most crucial element in the relationship between education agents and institutions and once signed the contract is seldom referred to. As will be seen later in comments made by interviewees, strong relations between institutions and agents have far greater influence on recruitment levels than the influence of a contract.

**Information asymmetry vs. information sharing**

*Theme No. 3. All respondents did not believe that information asymmetry was an issue between education agents and their university.*

Information asymmetry is seen in agency theory literature as a major hurdle between principals and agents. This however, does not appear to be the case in the international education industry. This lack of conflict arising from information asymmetry between education agents and institutions is reflected in the below comments by industry experts. One industry expert said "*I haven't really stuck anyone who said they aren't going to give the information."*

A second representative said, "*There is a bit of sharing of information, they are the eyes, they feel what is happening in the market."*

The approach taken by the international education industry appears to be more reciprocal in nature than that defined in agency theory literature. A third industry representative said "*in-country marketing managers work hand in hand with the agents. Good agents want to share because they know they will benefit from it."*

A fourth industry representative said "*the University has more information about courses but we strive to alert the agent in terms of course changes, new products being developed. Also we are trying to involve agents in market research and demand."*

As seen in the comments from industry experts, the problem of information asymmetry, as raised in agency theory literature, is not as prevalent in the relationship between education agents and this University. The common theme from the interviews is that there is a feeling of concerted effort for information sharing and cooperation between education agents and the University, rather than one party trying to keep information from the other.

**Relationship marketing imperative**

*Theme No. 4. All respondents agreed that building a relationship with education agents was of high importance*.

From comments made by industry experts, relationship marketing appears to be the key to increasing student recruitment through education agents.
One industry representative said "*I think some relationships can be built over years of working together to develop into a kind of trust and friendship and you find it is working well and is truly beneficial."*

The importance of relationship marketing is stressed by a second industry representative interviewed, who said "I *think it is all about relationship. With 90% of my agents it is a relationship of trust and dual commitment from both parties and we have got to a point where agents trust me to work for them and I trust 95% of the agents that work for me. The contract is there and they understand what they can and can't do, but I think being in their face saying don't use my logo unless you run it through my office, has a lot more effect than a piece of paper that states what can and can't be done. So it's about relationships, it's about trust and overall being in their face has a lot more weight."*

The respondent goes on to say that "*I think relationships are the single most important part of marketing. It is not how much money you put into marketing. You could put a lot of marketing money in and not recruit students as you don't have a solid relationship with the agent. This business is a relationship business; it is how you manage the relationships with your agents, partners and students. I think my style is 100% relationship building, 90% relationship management, 10% marketing."*

The third industry representative said "*building a strong relationship is probably the most important thing. Honestly if you don't have a relationship I don't think this business works. You have got some people that think they can just walk into an*

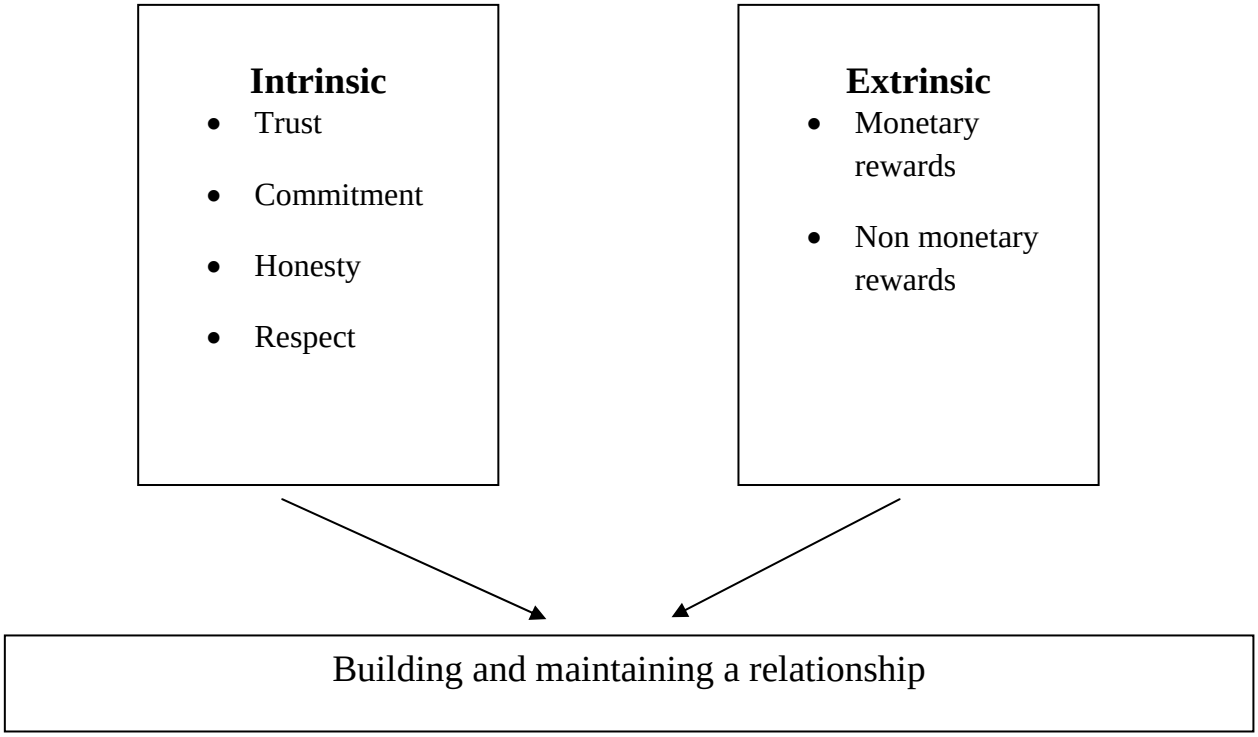
*agent's office and tell them what to do. It doesn't work. I have heard agents complain about it, they say he has just walked in here and told me he wants twenty students; I am not going to give him one. Relationship is the most important thing."*

**Intrinsic and extrinsic elements of relationship marketing**

*Theme No. 5. Key elements to build and maintain a relationship with an education agent.*

The following diagram provides the main clusters of identified responses derived from respondents who were asked a series of questions regarding key elements in building and maintaining a relationship with an education agent. Their responses were grouped into the following intrinsic and extrinsic categories.

**Figure 1. Key elements to build and maintain a relationship with an education agent.**




**Intrinsic elements**

In line with other author's empirical and theoretical research, *trust* and to a lesser extent *commitment* were important relationship development strategies mentioned by respondents in this study with *trust* being mentioned by all respondents as essential in building and maintaining a relationship with an education agent while *honesty* and *respect* were terms mentioned by half of all respondents.

*Commitment* represents a cluster of similar descriptors commonly mentioned by respondents and refers to interaction between education agents and institutions, including such things as the need for regular communication, support, regular contact and visits, reciprocal interactions, essentially engaging a constant relationship between the institution and the agent.

One respondent said "*a good relationship is based on trust in each other, trust that we can support students and deliver things and we have to trust that they can recruit students and aren't recruiting on false promises."*

A second respondent believed the key to building and maintain a relationship with education agents was "*honesty, respect, quality, trust and a willingness to go above and beyond what is required."*

Another industry expert believed the key to developing a good working relationship with an agent is by keeping in constant contact and showing *commitment* to agents. *"I am always emailing or phoning agents pretty much all the time and making sure that there are regular visits and that I participate in their activities. You can't expect a lot of return if you don't do a lot with them."*

**Extrinsic elements**

Monetary and non-monetary r*ewards* are terms clustered around a variety of extrinsic concepts mentioned such as productivity, money, quality, resource allocation, staffing, and training and are the tangible and non-tangible benefits an education agent receives as a result of their relationship with an education institution.

Most industry representative see the main objective of building a strong relationship is to increase student recruitment with the reward for the education agent being a commission payment. A productive relationship with an education agent may take time to develop but as commented by industry experts, it is "*highly important to do so in order to increase student recruitment through this channel."*

Reward in the form of monetary and non monetary benefits were a variable commonly mentioned in this study but stressed in other literature. This may be due to the nature of the international education industry being 1) largely commission driven 2) focused on the sale of a non-tangible, high credence service that cannot be trialled by agents, as a result non monetary items such as familiarisation tours and other non-monetary rewards being one way to entice education agents to recruit students for a particular institutions.

**Relationship benefits**

*Theme No. 6. Good relationships result in increased student recruitment.*

One hundred percent of respondents stated that having a good relationship with education agent's results in increased student recruitment. One respondent stated "*relationship is what gets you numbers."* Another stated that they "*pursue a relationship to increase student numbers. Hopefully by supporting them they will be able to increase the number of students they recruit."* A third respondent stated that "*relationship is the biggest motivator to get an agent to work for you. The agent returns your loyalty. If you have been supportive of an agent, they will go out of their way to recruit for you."*

From numerous comments made by interviewees, relationship marketing and a cooperative approach appears more prevalent than information asymmetry and there is less stated importance placed on the need for a contract to influence the actions of agents. Although elements of agency theory are seen as mandatory, for example

having a contract established between the two parties, relationship marketing appears to be the layer that produces results, providing the interface and developing the trust between the two parties to enable increased numbers of students to be recruited.

## Conclusion

International education to the Australian economy is a multibillion dollar industry (Austrade 2008), with education agents a major distribution channel through which international students are recruited (ACPET 2004). This study was designed to assess the relevance of certain aspects of agency theory to the industry and explore relationship marketing techniques that institutions could adopt to recruit increased international students through this channel.

The case study found that the *contract*, though important was not as critical as discussed in other agency theory literature. The contract was believed to set the boundary between the principal and agent of what can and should be done. In addition *information asymmetry* advocated by agency theory did not appear to pose a major problem for the industry with information sharing being more the norm. An agency relationship between an education agent and a University contradicts the above mentioned studies that found information asymmetry to be an issue, rather than being asymmetrical, the education agents and University have more congruent goals. Both parties strive to recruit increased numbers of international students and performance is easily monitored as it is outcome based. The agent has no gain from shirking as they work on a commission basis, and only stands to increase profits through better performance. These findings suggested the tendency of the adoption of a less rigid or mechanistic approach of handling agents in the university sector.

This research found that *relationship marketing* and the development of a strong relationship with education agents is imperative to recruit increased student numbers through this channel, with *trust, honesty, respect, commitment and developing monetary and non-monetary reward systems* the key to building and maintaining relationships with education agents.

## Limitations and future research

There are four main limitations to this research preventing generalisation to a broader context. First the study currently only provides an analysis of one University. This therefore only provides a perspective of one institution and several marketing employees. Further analysis of additional institutions is required to generalise the findings further. Secondly, this research looks at an Australian based university; the study does not investigate education agents and institutions behaviour in competing nations. Thirdly, education agents were not interviewed as part of this research and therefore their perspective on issues cannot be provided. Fourthly, the study concentrates on recruitment of international students to universities. Interviews were not conducted in other educational sectors such as at English language schools, vocational education centres or at high schools and findings may not apply to these sectors. Further research could be undertaken of additional institutions, in different countries and in different sectors and to overcome these limitations.

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# ANTECEDENTS AND CONSEQUENCES OF SERVICE QUALITY IN A HIGHER EDUCATION CONTEXT: A QUALITATIVE RESEARCH APPROACH

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## Abstract

The study aims to explore the perception of students with regard to critical antecedents, dimensions and outcomes of service quality in the context of a university in Australia. The study used qualitative research method to derive a theoretical model. Three focus group discussions with nineteen students were conducted at the main campus of Central Queensland University (CQUni), Australia. The focus group findings show that the critical antecedents to perceived service quality are information and past experience. Students perceive service quality as a set of attributes and that they evaluate it cognitively. Satisfaction and trust are found to have direct and positive relationships with service quality as consequences. As revealed from focus group discussions, all of the interrelationships among the themes developed are positive. There are several practical implications of this study. Higher education managers should pay particular attention to develop a concrete information structure for potential students through promise and information structure. The authority should also develop and maintain good relationships with present and previous students, local and regional school authorities, and other stakeholders. They should continuously upgrade the performance of the service attributes in order to improve students' experience, spread word-of-mouth, provide satisfaction, and build trust. This study shows that there are two streams to study service quality, antecedent approach and dimensional approach. This study develops a theoretical model, which is the first of its kind, in higher education marketing literature. This research considered three focus group discussions and a single university. Future studies should expand the scope of the research.

**Keywords** – Information, Past Experience, Service Quality, Satisfaction, Trust, Higher Education.

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## Introduction

A number of studies in service quality have enriched the services marketing domain over the last three decades or so. Most of these studies have concentrated their findings on the dimensionalities of service quality across industries, cultures and firms. These studies develop scales to gauge the quality. Amongst these, the widely used scale is the SERVQUAL conceptualized on expectancy–disconfirmation paradigm. However, only a few studies (Dabholkar, Shepherd, & Thorpe, 2000; Gounaris, Stathakopoulos, & Athanassopoulos, 2003) have focused attention on the antecedents to service quality. With regard to consequences of service quality in commercial enterprises, several models are developed in literature (Cassel & Eklöf, 2001; Cronin, Brady, & Hult, 2000; Fornell, Johnson, Anderson, Cha, & Bryant, 1996).

The dimensions of service quality varies by the thoughts of two different schools, Nordic (Grönroos, 1982, 1984) school and American school (Parasuraman, Zeithaml, & Berry, 1985, 1988), by industries (Lee, Lee, & Yoo, 2000), by service types (Babakus & Boller, 1992), by culture (Furrer, Liu, & Sudharshan, 2000) or even by providers or firms in the same industry (Abdullah, 2005; Sureshchandar, Rajendran, & Kamalanabhan, 2001; Zeithaml, Berry, & Parasuraman, 1993). The dimensional approach of service quality provides an understanding of quality dimensions and its relevant attributes. In contrast, the antecedent framework provides an insight of how consumers view service quality as a whole and how this view contribute predicting their behavior (Dabholkar et al., 2000). Consequences of service quality vary across study perspective. For example, economic value may play a significant role as a consequence of service quality for a commercial product. However, this might have little significance as a consequence of service quality for emergency services compared to emotional value.

Although universities and commercial enterprises are two different industries, studies in higher education empirically examine the models that are developed in commercial settings. Therefore, these models do not find cause and effect relationships among some of the variables in the context of higher education sector (see, for example, R. Brown & Mazzarol, 2009; Chitty & Soutar, 2004). As higher education provision is a service and students are expected to fund their educational expenses, it would seem appropriate that universities make a shift from being product-led, i.e. relying on the product to sell, towards a more “customer-led” approach (Angell, Heffernan, & Megicks, 2008). It has been found that when making the uncertain and high-risk decision of choosing a university, the student looks for evidence of service quality (Donaldson & McNicholas, 2004). This confirms the importance of service quality in the university’s functions. Ignorance of the competitive nature of attracting students, along with the importance of measuring the service quality, will ultimately be at the disadvantage of the institution (Angell et al., 2008). Thus, marketing approaches to the higher education domain may provide important outcomes.

This study aims to explore the critical antecedents, dimensions and outcomes of service quality, as perceived by the students, in the context of a higher education institute at Australia. This study is worth doing for several reasons. Firstly, this research is the first attempt of its kind. Second, this study will be contributing not only to the higher education domain in Australia but also to the literature in higher education marketing. Third, we employ qualitative research method in order to

comprehend the insights of the responses with the consequence of establishing a theoretical model.

## Literature Review

*The Dimensional Approach of Service Quality*

Most of the service quality literatures in the last few decades focused on the dimensional approach. As a result, a number of measures evolved; namely Grönroos model (Grönroos, 1982, 1984), SERVQUAL (Parasuraman et al., 1985, 1988) and SERVPERF (Cronin & Taylor, 1992, 1994). Amongst these models, SERVQUAL and SERVPERF scales attempted to find a better measure for service quality from service specific perspective. These models were developed based on commercial services.

Parasuraman et al.'s (1988) SERVQUAL scale defined quality as perception-minus-expectation. There are five dimensions and twenty-two items. These dimensions are reliability, assurance, tangibles, empathy and responsiveness. Although the SERVQUAL has been empirically examined widely, it has also been criticized for a number of reasons. Research demonstrated serious conceptual and operational flaws in perception-minus-expectation measure especially with respect to its theoretical justification and interpretation of the framework (T. J. Brown, Churchill, & Peter, 1993; Cronin & Taylor, 1992, 1994; Lee et al., 2000; Teas, 1993, 1994). Thus, in the revised SERVQUAL scale the authors incorporated 'would' perspective instead of 'should' perspective in all of its expectation instruments to reduce high expectation scores and to make the expectation instruments more relevant to predictive expectations instead of consumers' normative expectations or ideal standards. They also replaced negatively worded items with positive words (see, for example, Parasuraman, Zeithaml, & Berry, 1991c).

The subsequent developments in service quality measures followed the SERVQUAL approach. One of such developments was the SERVPERF scale, also known as performance–only scale (Cronin & Taylor, 1992, 1994). The SERVPERF scale is the unweighted perception components of the SERVQUAL scale, which consists of 22 perception items and excludes any consideration of expectations. The performance–only construct, the SERVPERF, demonstrated its relative superiority over the SERVQUAL scale in terms of statistical analysis (see, for example, Cronin & Taylor, 1992, 1994). Although the SERVPERF scale is based on customer scores evaluating perceived service performance, it seems reasonable to assume that such judgments of customers are formulated with reference to some form of expectations. Expectations, regardless of whether they are measured explicitly or not, are likely to form an anchor for quality assessment (Devlin, Gwynne, & Ennew, 2002).

Empirical studies on service quality in terms of relative superiority between the SERVQUAL scale and the SERVPERF scale are examined. On the one hand, the studies find that the SERVPERF scale is a better alternative than the SERVQUAL scale (Babakus & Boller, 1992; Brady, Cronin, & Brand, 2002; T. J. Brown et al., 1993; Jain & Gupta, 2004; Zhou, 2004). On the other hand, the SERVQUAL has received much attention as a measure of service quality (Chebat, Filiatrault, Gelinas-Chebat, & Vaninsky, 1995; Furrer et al., 2000; Zeithaml & Bitner, 2003). A recent

study suggests that both scales are adequate and equally valid predictors of overall service quality (Carrillat, Jaramillo, & Mulki, 2007).

The dimensional study of service quality still dominates the current literature. There are critical features of the dimensional approach to service quality. Firstly, this approach is a service specific approach, i.e. the direction is from service to consumer. The research instruments are designed considering specific features and natures of the service, and its delivery. Secondly, the resulting dimensions vary based on service types, firms or provider, industry and even culture. Researchers have failed to replicate the five original dimensions of SERVQUAL or SERVPERF scales, namely, reliability, responsiveness, tangibility, assurance and empathy (Carrillat et al., 2007; White & Schneider, 2000). Thirdly, the dimensional approach focuses on service features and ask consumers to rate them considering their expectations and/or perception. As a result, literatures conceptualize service quality based on varied findings of dimensional approach. This underscores that service quality scales need to be adapted to the study context (Carman, 1990; Carrillat et al., 2007). The major benefit of using the dimensional approach is that it gives an understanding of the service features and their relevant dimensions.

Despite the development in service quality literature specially with regard to dimensional approach, one of the dominant review in service quality literature stated that "there does not seem to be a well-accepted conceptual definition and model of service quality nor there is any generally accepted operational definition of how to measure service quality" (Seth, Deshmukh, & Vrat, 2005, p. 933). In the extant literatures, little consensus has been found as to which measure is universally suitable (Angell et al., 2008) and which of the definitions for service quality is appropriate (Wicks & Roethlein, 2009). As a result, there is a scope to examine dimensionalities of service quality across industries. Particularly, this study is designed to capture the antecedents, dimensions and consequences of service quality in the context of a higher education institution at Australia. The following section discusses the antecedent approach to study service quality.

*The Antecedent Approach to Service Quality*

The antecedent approach to study service quality received a little attention in academic literature. For example, one study demonstrated that service quality is influenced by four of its dimensions, namely reliability, personal attention, comfort and features (Dabholkar et al., 2000). This study referred these dimensions as the antecedents to service quality. This longitudinal study used three measures, namely perception-only measure; measured disconfirmation, i.e. explicit comparisons are made in the instruments after the service received; and computed disconfirmation, i.e. expectations (before the service experience)–minus–perceptions (after the service experience). The findings stated that perception measure is superior over computed disconfirmation and measured disconfirmation. Thus, this study recommended that if the objective of the study is to predict service quality or to gauge its determinants, perception-only measure should be used rather than disconfirmation. Although Dabholkar et al. (2000) stated that the four dimensions are the four antecedents to service quality; these findings may not be applicable across service types, firms, service industries and cultures in general. This is because service quality is a contextual issue, its dimensions vary widely. Moreover, the bulk of recent studies still

considers these to be the dimensions of service quality instead of antecedents (see, for example, Bigne, Molinar, & Sanchez, 2003; Kilbourne, Duffy, Duffy, & Giarchi, 2004; Soyoung & Byoungho, 2002; Sureshchandar et al., 2001; Swanson & Davis, 2003).

Research on customer specific antecedents to service quality also received a little attention (Gounaris et al., 2003). The antecedent approach starts from customers. Customers' perception of service quality are affected by factors such as communications from salespeople, social referrals, various types of information collected, and the credence consumers develop towards a service organization (Gounaris et al., 2003; Kangis & Passa, 1997). Gounaris et al. (2003) stated that perceived service quality is a function of customer and company specific antecedents. This study considered word-of-mouth communication as one of the four antecedents consisting of three indicators. However, two of the three indicators of word-of-mouth were seriously lacking from content and face validity. These were 'family bank' and 'get information from advertising campaign'. Therefore, the construct 'word-of-mouth' as an antecedent to service quality might not be conceptually sound. The research on antecedent approach to service quality has been lacking in the context of higher education. However, a number of studies on service quality in higher education context focused on dimensionalities and consequences. In the following, we discuss the critical service quality research in the higher education domain.

*Service Quality Research in Higher Education*

Service quality research in higher education sector is new, at least, compared to that of commercial sector. Most of the quality models that are commonly practiced in the business world have been adapted and used in the education sector (Chua, 2004). Service quality research in higher education develops relevant scales conceptualizing either SERVQUAL scale or SERVPERF scale. One such study reports that SERVQUAL scale is reliable and valid when it is applied to a particular classroom environment (Stodnick & Rogers, 2008). However, a number of studies (see, for example, Cuthbert, 1996a, 1996b; O'Neill, 2003; Oldfield & Baron, 2000; Sahney, Banwet, & Karunes, 2004) examine SERVQUAL scale in university environment and none of those studies are able to replicate five-factor structure of the SERVQUAL scale. Similar to the findings of commercial enterprises, one study finds that the SERVPERF scale outperforms against its counterpart, the SERVQUAL scale, in the context of higher education (Li & Kaye, 1998).

In the context of dimensionalities of service quality in higher education sector, the HEdPERF measure (Abdullah, 2005; 2006a, 2006b, 2006c) and the PHEd measure (Sultan & Wong, 2010) may be considered as comprehensive scales as these measures include a broad range of service attributes in the context of higher education. The HEdPERF measure and the PHEd measure were conceptualized on the performance-only scale. The HEdPERF has 41 attributes loaded on four dimensions, namely, non-academic aspects, academic aspect, reliability and empathy to measure service quality. The PHEd measure has 67 attributes loaded on eight dimensions. These are dependability, effectiveness, capability, efficiency, competencies, assurance, unusual situation management, and semester and syllabus. Both of these measures, the HEdPERF and the PHEd, were developed focusing on the higher education sector of

Malaysia and Japan, respectively. The following table is a brief summary of the dimensionalities of service quality research in higher education.

Table 1: Service quality dimensions in higher education

| **Author, Date** | **Items** | **Items and Dimensions** | **Country/University** |
|---|---|---|---|
| (Sultan & Wong, 2010) | 67 Items | Dependability, effectiveness, capability, efficiency, competencies, assurance, unusual situation management and semester–syllabus | Japan |
| (Rojas-Me´ndez, Vasquez-Parraga, Kara, & Cerda-Urrutia, 2009) | 18 Items | Instructors, program director, secretaries, service attitude and competence development. | Chilean University |
| (Stodnick & Rogers, 2008) * | 18 Items | Reliability, Assurance, Tangibles, Empathy and Responsiveness | One course, Southwestern University, USA |
| (Angell et al., 2008) | 18 Items | Academic, leisure, industry links and cost | One university, UK |
| (Smith, Smith, & Clarke, 2007)* | 22 Items | Reliability, Assurance, Tangibles, Empathy and Responsiveness | IT Department, one university, UK |
| (Abdullah, 2006c) | 41 Items | Non-academic, academic, reputation, access, program and understanding | Malaysia |
| (Abdullah, 2005; 2006a, 2006b) | 35 Items | Non-academic, academic, reliability and empathy | Malaysia |
| (Kwan & Ng, 1999) | 31 Items | Course content, concern for students, facilities, assessment, medium of instruction, social activities and people. | China and Hong Kong |
| (Li & Kaye, 1998)* | 27 Items | Reliability, Assurance, Tangibles, Empathy and Responsiveness | One university, UK |
| (Joseph & Joseph, 1997) | — | Program, academic reputation, physical aspects, career opportunities, location, time and other | New Zealand |
| (LeBlanc & Nguyen, 1997) | 38 Items | Contact personnel/faculty, contact personnel/ administration, responsiveness, reputation, curriculum, physical evidence and access to facilities | Business School, one university, Canada |

*Items were not exactly loaded under each of the dimensions as claimed in the SERVQUAL scale.

The findings of these studies show that developing a service quality measure depends on study perspective. In this context, there is a gap in literature with regard to the development of dimensionalities of service quality in the context of Australian higher education sector. Service quality and its predictability in terms of students' satisfaction are examined in the higher education sector (Stodnick & Rogers, 2008). However, a number of studies used the European Customer Satisfaction Index (ECSI) model in the higher education domain (Alves & Raposo, 2007; R. Brown & Mazzarol, 2009; Chitty & Soutar, 2004; Martensen, Grønholdt, Eskildsen, & Kristensen, 2000). The findings of these studies are inconclusive in that the replication of the ECSI model does not produce any decisive results in the context of higher education. This is because the interrelationships among a number of constructs of the ECSI model in the context of higher education appear statistically insignificant and negative. In addition, these empirical studies hypothesized that 'the university image' is in-built with a university and demonstrated that image affects value, satisfaction and loyalty. However, a number of studies argued that image is build mainly by quality (Grönroos, 1984), and is a consequence of value, quality (Nguyen & LeBlanc, 1998) and satisfaction (M. Johnson, Gustafsson, Andreassen, Lervik, & Cha, 2001). Johnson et al. (2001) stated that the effect of customer satisfaction on image reflects both the degree to which consumption experience enhances image and the consistency of customers' experiences over time. Higher education institutes are distinct service organizations compared to other commercial service organizations and thus, implementing the ECSI model in the context of higher education needs a separate attention.

In summary of the above literature review, first, we find that there is a research gap to explore the antecedents of service quality in a higher education context. Second, there is no study that focuses on dimensionalities of service quality in the context of Australian higher education sector. Third, despite the examination of the ECSI model in the higher education domain, there is a further scope to reinvestigate the consequences of service quality in the context of higher education. There is also an unclear understanding between dimensional study of service quality and antecedent approach to study service quality. Thus, there are research potentials to address these critical issues with empirical evidences in the context of higher education service quality. To address these gaps we adopted qualitative research method as a primary approach in order to comprehend the phenomena in terms of CQUni, Australia.

## Research Method

The approach adopted in this research was an exploratory qualitative method and thus, this research employed focus group technique. There were several reasons for employing focus group technique. These include to study the perceptions of students with regard to critical antecedents, natures, consequences of perceived service quality, and their causal relationships with an aim to develop a research model.

### *Selection of focus group members*

The participants for focus group discussions were students studying at the CQUni, Rockhampton, Australia. The participants were divided into distinct segments based on their level of study, for example, undergraduate and postgraduate including masters and doctoral students. This was done in order to minimize the dominance of

senior student over junior student, and to ensure interactive participation among the group members. Research examining students' choice processes of university course selection used 22 students as focus group members (C. Brown, Varley, & Pal, 2009). Although there is no rule of thumb about the number of members in a focus group, one study suggested that "a group consisting of 5–10 respondents is appropriate (Krueger & Casey, 2000, p. 10)." A number of studies also suggested that several (3–4) focus groups are convened depending on distinct population segments (see, for example, Morgan, 1988; Stewart, Shamdasani, & Rook, 2007). Thus, the present study included five, eight and six undergraduate, masters and doctoral students, respectively, in three focus group discussions, and at the main campus due to budget constraints and time limitations. In the present study, all of the students were having at least six months of studying experience with CQUni, and were selected based on convenience and purposive sampling techniques. We ensure representative members of the larger population in each of these groups following the suggestions of several studies (Morgan, 1997; Stewart & Shamdasani, 1990; Stewart et al., 2007).

*Designing the topic for discussion*

The focus group discussions are exploratory in nature. One of the aims of focus group discussion is to generate relevant themes and determining their relationships. Using a facilitator or moderator for this type of investigation may bias the findings in that the cues provided by the moderator, knowingly or unknowingly, inform the group what information is desired and can get group consensus on a particular issue (Stewart et al., 2007). In addition, hiring a moderator is time consuming and increase the cost of the research project substantially (Morgan, 1997). Thus, the focus group interviews were conducted by the principal researcher in a non–directive and unstructured fashion. Broad questions were asked to each of these groups (Zeithaml et al., 1993). First, the respondents were explained about the research aims, and the tasks they would perform during focus group discussion. Second, broad and open-ended questions were posed; including what affects quality of services in terms of the CQUni prior to enrolment? How do they evaluate service quality in terms of their university? What are the critical quality aspects of this university? What are the critical consequences in terms of service quality evaluation in the context of their university? Third, to facilitate the discussion and to keep it compact within the aim of this study, the researcher summarized the discussion when necessary during each of the interviews. This facilitated participants to focus on the content of discussions. The discussions were recorded using an electronic device. On an average, each discussion took one hour duration.

*Data analysis and interpretation*

The analysis of focus group data requires a great deal of judgment and care, and they depend on the research question and the purpose of focus group discussion (Morgan, 1988). For the purpose of this study, a thorough content analysis is employed. Krippendorff (2004, pp. 3-11) stated that "content analysis entails a systematic reading of a body of texts, images and symbolic matters, not necessary from an author's or user's perspective….it is used when verbal data are gathered in the form of answers to open ended interview questions, focus group conversation…".
The content analysis was conducted through manual procedures. The first stage included identifying the recorded information that were important for developing

themes and the interrelationships following the theoretical and conceptual suggestions (Krippendorff, 2004; Neuendorf, 2005). In this stage of analysis, transcriptions were prepared from the recorded focus group discussions onto paper. We cleaned and edited the manuscript by eliminating typographical errors and contradictions in the text that were irrelevant with the central issue of the study. The second stage followed coding and categorizing that included assigning key words suitable for a section of text, giving a particular meaning to or labelling a section of the material (Sarantakos, 1997). Thus, the texts were classified or categorized. The coding process not only involved categorizing the chunks of texts but also included memoing the data. Memo is the notes, backgrounds, ideas or thoughts about coding data (Babbie, 2007; Sarantakos, 1997). The third stage was concept mapping. Concept mapping is the display of concepts and their interrelations to formulate a theory (Babbie, 2007). It also helps strengthening the theoretical model. The theoretical model was purified following a two step procedures. First, each researcher independently reviewed the transcripts and developed a list of constructs, and formulated the interrelationships among them. Second, the researchers shared their inferences and finally developed the theoretical model and key hypotheses.

## Findings and Research Implications

### *Demography of the Respondents*

Demography of the respondents is important in qualitative analyses. This is because it validates the responses collected to achieve research objective. The ages of the undergraduate and postgraduate students were 19–21 and 26–38, respectively. In these discussions, total female to male ratio was 5:14, and they all were studying more than six months at the CQUni.

### *Critical Antecedents to Service Quality*

Information: Studies ascribed that formal communications from various sources, including advertisements, leaflets, and related articles in magazines and newspapers, affect the way customers interpret ambiguous evidence concerning quality (Deighton, 1984; Devlin et al., 2002; Mathews, 1994). Devlin et al. (2002) stated that information provides opportunities to influence assessment of service quality and customer satisfaction. The extant literature is lacking to explore the nexus between information and service quality.

The focus groups were asked to discuss the factors that affect quality of services in terms of their university prior to enrolment. Respondents stated that information affects the level of quality judgment. They also underlined that the information provided by the institution should be true, want satisfying and reliable. The following are the specific quotes of focus groups' participants.

> "If the product is new and there is no set standard, in that case, the level of quality in terms of my needs would be very much influenced by whatever product related promotional materials are being discharged by the supplier" (Doctoral student, age 38).
>
> "The underlying factors affecting quality are adequate information and its genuineness" (Doctoral student, age 34).

> "…delivered promise should be equal to the delivered service" (Undergraduate student, age 21).

The explicit or implicit promises embedded in provided information and/or marketing communication plays a vital role to form and evaluate quality. Perceived quality is based on one's experience and is a function of attitude (Sultan & Wong, 2010). Favourable perceived quality is dependent on the extent of keeping promises and authenticity of provided information. Quality evaluation starts from provided information and promise. Thus, perceived quality is affected by information and promise. Marketers' task is to design the information structure and promise focusing on those service attributes that are most desired by the target group. Based on the focus group discussions, we find information as promise, information communicated through marketing tools, genuineness of information, and desired information in the context of a higher education. Therefore:

> **H1:** There is a positive relationship between information received by the students and their evaluation of service quality.

Unlike the products, services have special characteristics. They are heterogeneity, perishability, intangibility, inseparability (Zeithaml, Parasuraman, & Berry, 1985). Due to the special nature of services, it is imperative to focus on students' pre-enrolment information structure, which can be strengthened through good word-of-mouth of present students and previous alumnae, promise that the institution can keep, adequate and specific information and its genuineness, and above all focusing on what students' desire in terms of educational information. Because quality is affected by reliable information, the marketing communication message should carefully design the promises. Therefore, managers of higher education institute should concentrate their attentions to these particular areas, and allocate available resources in order to strengthen students' information structure prior to enrolment and optimize the outcomes.

Past Experience: Studies find that past experience helps forming service expectations (Devlin et al., 2002; Gounaris et al., 2003; Zeithaml et al., 1993). However, inexperience of service encounter or unrealistic expectations may results to fuzzy prediction of service quality standards. In the extant literature, the relationship between past experience and service quality is unexplored.

The focus group findings stated that past experience of students had been one of the important issues that affect service quality assessment. Students' recent experience of meeting or interacting with staff of a university also affects service quality judgment. Students use previous study experience as a fuzzy input to predict service quality of a potential university due to mainly their lack of experience with that potential university. This may result to build a set of unrealistic expectations about service quality of a university. The following quotes are relevant to past experience and its relationship with perception of service quality.

> "…before coming to this university, I had only high school experience. From that point, it is hard to say. But at least it tells that we would learn some advanced stuff at the university" (Undergraduate student, age 21).
>
> "I've attended three different universities in Australia. Many people would agree that out of these three…University is the prestigious. But why I didn't go back to that university? So, considering location,

> proximity and recent experience with staff, I'm keep going with the Central Queensland University" (Postgraduate student, age 34).

Past experience is one of the key issues that play a vital role to form quality. This is because during service encounter customers' evaluate their past experience of receiving the same service with the present one. They tend to compare similar type of service attributes received from various providers. However, higher education service attributes are different compared to commercial service attributes. It is hard to compare the service delivery processes in a higher education setting. For example, it is fairly common practice that two lecturers would create and deploy teaching techniques, methods and environment for a course in an individualistic manner for the same group of students in an undergraduate program. This signifies that students' experience with various staff would be different and that this is often incomparable. However, the common ground, in this respect, is that students' experience can be improved continuously though there are significant differences among the service personnel. This leads to positive and favourable evaluation of service quality. Referring to focus group findings of the present study, the evidences suggest that past experience is students' previous educational experience, and their interaction and relationships with staff and/or the university prior to enrolment in a higher education context. This leads to the second hypothesis.

> **H2:** There is a positive relationship between past experience of the students and perception of service quality.

The higher education institutions should continuously improve students' experience with the service that they receive, and should focus on maintaining relationships. As the high school students might build a fuzzy set of assumptions about higher education services due to absence of concrete experience, the university should maintain relationships with local and regional high schools, and invite high school teachers and students to participate in short courses, short visits, meetings and symposiums. This might increase enrolments and impact favourably on quality judgment.

*Service Quality*

Service quality is defined as the totality of features and characteristics of a product or service that bears on its ability to satisfy stated or implied needs (R. Johnson & Winchell, 1988). Service quality has also been viewed as a critical determinant of competitiveness (Lewis, 1989), as a source of lasting competitive advantage through service differentiation (Moore, 1987), and as a driver of corporate financial and marketing performance (Buttle, 1996). While in commercial sector ISO certification may assure customers about the standard of a product and/or service, the higher education sector assures students through accreditations of the programs/courses, ranking of the university, students' commendations and career prospects. In order to understand the nature of service quality in a higher education context, the focus groups were asked how they evaluate service quality in terms of their university. As revealed from focus group findings, the assessment of quality of service is a cognitive process. Meaning that service quality assessment is a psychological result of perception, learning, reasoning and understanding of the service attributes. The specific quote is as follows:

> "I think we add-up the issues like recent experience, present performance and our interests in a subconscious manner. This is a psychological process of understanding" (Postgraduate student, age 33).

It is stated earlier that evaluation of service quality is an experience-based norm. Students' past experience, desired attributes and provided information play a vital role to form and evaluate service quality in the context of higher education. Although a number of strategies are undertaken by the universities to assure students about the service performance, these strategies may not be effective unless students' experience with service attributes are favourable. Thus, students' experience (or perception) of service attributes are important for evaluating service quality of a university.

The focus groups were also asked to discuss the critical quality aspects of services of their university in order to fully comprehend the nature of service quality. The previous studies in dimensionalities of service quality in the context of higher education find a number of service quality attributes relevant to academic, administrative, course administration and the like (see Table 1). Based on the findings of the focus group data, the present study mainly classify these into three categories, academic, administrative and support functions. The following are the specific quotes relevant to academic service quality.

> "I think the most important is the quality of lecturers and how entertaining they are. The lecture should not be boring and after lecture availability is also important" (Undergraduate student, age 21).
>
> "...they should have research expertise and intellectual capacity to conduct research and supervise the research students" (Doctoral student, age 35).

The academic service quality refers to those service attributes that are relevant to teaching quality and ability, course development and teacher–student relationships in order to provide core academic values and/or benefits to the students. Students prefer the lecture to be interactive, understandable, practical and entertaining. The consultancies provided by the lecturers are also important to the students. Thus, after lecture availability, responding through email or phone may prove to be caring. The design of each lecture should be such that it can prove to be new in knowledge and effective to the students each day they attend the lecture. The research expertise and supervision capacity, and a track record of publications of the lecturer are also vital for effective postgraduate programs. Thus, these critical service attributes provide the core benefits/values to the students during their enrolment.

The administrative service quality has similar importance in overall assessment of service quality in the context of higher education. The administrative staff should be skilled and be able to answer students' queries effectively. Avoiding one's responsibilities and tasks may result unfavourable overall assessment of service quality. In this regard, one student commented as follows:

> "Sometimes the staff takes time to reply to our query, and send us the common web links to search instead of addressing the queries. They should know what they are doing" (Postgraduate student, age 27).

The extant studies (Abdullah, 2005; 2006a, 2006b, 2006c; Sultan & Wong, 2010) find a number of items to measure non-academic aspects (or administrative aspects) of

service quality without proper definition. In this study, the administrative service quality refers to those service attributes that are relevant to skills and abilities of the administrative and supporting staff, and their relationships with students in order to provide smooth functioning of academic activities at a university. These are critical service attributes for providing the support services to smooth running the programs/courses.

Facilities service quality refers to those service attributes that are required to create a good higher education environment. This refers to library facilities, entertainment facilities, career counselling, transport facilities, dining facilities, access to computer and other resources, and workshops/seminar/conference. Particularly, the following are some of the specific quotes with regard to facilities service quality.

> "I face specific problem with transport services" (Undergraduate student, age 20).
>
> "We do not have a good dining facility here" (Undergraduate student, age 21).
>
> "The other important issues are whether the university holds workshops and conferences, and invites renowned people to deliver speeches" (Postgraduate student, age 26).

Thus, this study finds three categories (or dimensions) of service quality, namely, academic, administrative and facilities, in the context of CQUni. These categories are related to specific attributes of higher educational services that students encounter during their study. The findings also confirm that antecedents to service quality and dimensions of service quality are two distinct thoughts. The antecedent to service quality mainly involves those issues that students consider prior to interacting with the service. In contrast, the dimensions of service quality are related to specific features of services during service encounter.

*Critical Consequences of Service Quality*

Although a number of studies empirically examined the usability of the ECSI model in the higher education domain, none of those studies are able to clearly show the robustness of the ECSI model in the context of higher education (R. Brown & Mazzarol, 2009; Chitty & Soutar, 2004; Martensen et al., 2000). This motivates us to undertake the present study. Thus, the focus groups were asked to discuss the effects of service quality evaluation in the context of their university. Analysing the focus group data, we find that the critical consequences of service quality in a higher education context are satisfaction and trust. Students' trust is important in a higher education context because it is developed through experience and interaction with the university staff. Students' trust may play a vital role to have outcomes favourable to the university. The ECSI model and subsequent empirical studies examined in the higher education domain ignore the role of students' trust. The specific quotes are:

> "...if the university provides quality services the obvious outcome is our satisfaction and the next is our understanding that the University can satisfy us in future" (Undergraduate student, age 21).
>
> "...it is not necessary to be loyal to a university. For example, I may not come to do PhD here even if I am satisfied. Rather, if I find that lecturers moved from this university to another, I may consider that

university for my future study destination. It's all about my belief of lecturers" (Postgraduate student, age 26).

Satisfaction: Studies suggest that the critical determinant of perceived satisfaction is perceived quality (Cronin et al., 2000; Eskildsen, Kristensen, Juhl, & Østergaard, 2004; Fornell et al., 1996). However, service quality literature in higher education demonstrated that dimensions of service quality also affect students' satisfaction (Stodnick & Rogers, 2008). Satisfaction (or dissatisfaction) is not inherent in the product or service instead it is the consumer's perceptions of the attributes of the product or service (Boshoff & Gray, 2004). The focus group findings stated that satisfaction is affected by the performance of service attributes. The students are satisfied if service attributes perform well. Thus, these findings are indifferent to the extant literatures. The concept of satisfaction occupies a central position in marketing thought and practice. Satisfaction has been viewed as having both affective (emotional) and cognitive dimensions (Oliver, 1996). The findings of the present study suggest that satisfaction is a cognitive evaluation of the performance of service attributes in the context of CQUni. The following are the quotes of the focus group discussions.

"Everyone says …. and …. are big and better universities in this state comparative to this university. I have no experience with them. I can't compare. But to me this university fulfils my need. I have never found anything lacking. I have access the resources that I need" (Undergraduate student, age 20).

"If someone is not satisfied with the performance of the university, he has to finish his degree. He can't just be in the middle of no way and do nothing" (Postgraduate student, age 26).

"I think for us satisfaction of a particular incidence of any aspects of this university depends on the performance of several factors, for example, quality of lecturers, counselling, staff's behavior and the like" (Postgraduate student, age 33).

Therefore, satisfaction may be viewed as a psychological state of happiness of the students as a result of performance evaluation of the service attributes. This leads to the following hypothesis.

**H3:** Performance of service quality positively affects students' satisfaction in a higher education context.

Trust: Trust is the drive of customer retention (Doney, Barry, & Abratt, 2007). It has been defined as "one party's believe that its needs will be fulfilled in the future by actions undertaken by the other party" (Anderson & Weitz, 1989, p. 312). Studies find that service quality and satisfaction are the antecedents of trust in a business-to-business service sectors (Delgado-Ballester & Munuera-Aleman, 2001; Horppu, Kuivalainen, Tarkiainen, & Ellonen, 2008; Lau & Lee, 2000; Zboja & Voorkees, 2006). This is because both of them include consumers' consumption experience and evaluation. However, there is no similar evidence in the context of higher education. The trust determines the relationship strength between students and university staff. While higher education institutes are trying to increase student numbers each year, trust of enrolled students and past students may play a vital role to increase the marketability of the university's programs and the brand, itself. The focus group

findings support this notion. The focus groups were asked to contextualize their trust on CQUni. The specific quotes are as follows.

> "To me trust is whether the university keeps promises or not..." (Doctoral student, age 34).
>
> "The students have trust on a university if it provides security, satisfaction, value for money and integrity in fulfilling promises" (Postgraduate student, age 33).
>
> "The trust is to provide me something for which I pay the money" (Undergraduate student, age 20).
>
> "How far they can solve any problem without difficulty" (Undergraduate student, age 21).

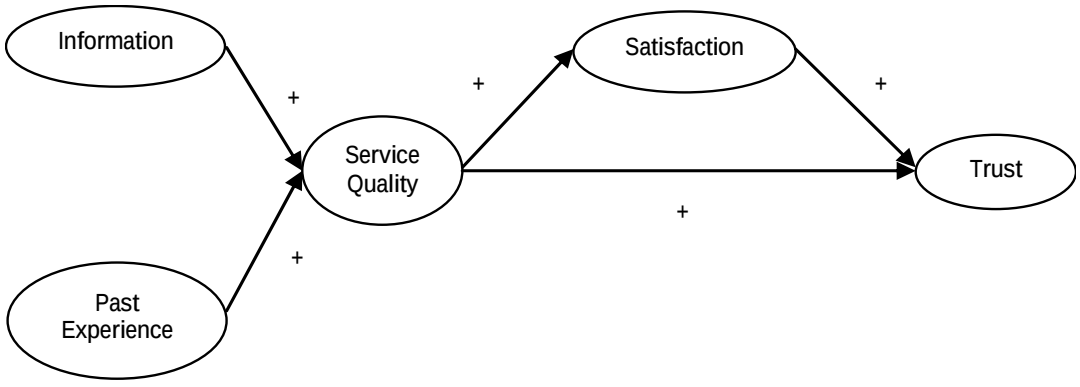
The findings suggest that trust is an important consequence of service quality and satisfaction in the context of higher education. Students perceive trust as the ability to provide satisfaction, secure environment, good value, solution to a problem, and reliable performance of the service attributes. Therefore, trust has significant role in the higher education domain as students build cumulative effects of trust over the years with their teachers, staff, institution, and lastly, with the brand. These lead to the following hypothesis.

> **H4:** Perception of service quality positively affects trust in the context of higher education.
>
> **H5:** Perceived satisfaction positively affects trust in the context of higher education.

Students' trust is the foundation in the higher education services marketing where they have to go through a longitudinal process with their enthusiasm in order to get an outcome at a cost. Thus, achieving students' trust during their course of study has tremendous role in managerial decision making. While implementing the ECSI model in the higher education sector, studies (Alves & Raposo, 2007; R. Brown & Mazzarol, 2009; Chitty & Soutar, 2004; Martensen et al., 2000) have ignored the role of students' trust.

The above discussions signify that perceived service quality in terms of a higher education institute is the focal point for managers. Figure 1 shows the research model. The model shows that information and past experience positively affect service quality, and service quality positively affects satisfaction and trust. The model also shows that satisfaction has a positive and direct relationship with trust in the higher education context.

Figure 1: The Research Model



## Conclusion, Limitations and Future Research

The aims of this study were to explore the perception of students with regard to the critical antecedents, dimensions and consequences of service quality in the context of a university in Australia. We used qualitative method to derive a theoretical model. The focus group findings show that the critical antecedents to service quality in the context of a higher education institute are information and past experience. Students perceive service quality as the performance of a set of attributes relevant to academic, administrative and support functions. As for the consequences of service quality, satisfaction and trust are found to have positive relationships with service quality.

There are several limitations in this study. Although selecting samples from a single university was one of the limitations, previous studies have conducted experiments considering a single university (C. Brown et al., 2009; Douglas, McClelland, & Davies, 2008; Smith et al., 2007; Stodnick & Rogers, 2008). The results of this study were drawn based on three focus group interviews at the main campus of the CQUni, Australia. This was done to comply with the allotted budget and timeframe. However, particular attention was given to select members for each of the focus groups to ensure representativeness of the larger population.

This study considered students studying at undergraduate and postgraduate levels at the CQUni, Rockhampton campus. Future studies should extend the scope of this study including all the campuses and/or universities. It is also recommended that future studies should make two segments, undergraduate students and postgraduate students, to explore some insightful findings. Future study should also validate the model using quantitative research method. A set of research instruments along with statistical validations will be reported in future studies. The validation of the model in the context of higher education industry across various countries should also be contributing to the literature. Future study can also extend this model using similar research methods. The argument of developing a service quality model in a university setting and its subsequent usability in commercial setting may be of interest to some scholars. Studies in the context of higher education service quality have empirically examined the models that are developed in a commercial setting (see, for example, Abdullah, 2005, 2006; Cronin & Taylor, 1992, 1994). Future studies should explore the usability of this model in the commercial service sectors.

The managerial implications of this study have several facets. First, the information designed for the students should contain desired and true messages. Second, continuous improvement of service performance results to good perceived experience of the students, which in turn, publicizes good word-of-mouth. Managers should focus on this issue. Third, managers should be able to develop and to maintain good and long-term relationships with the students. Fourth, managers should be able to maintain good relationships with local and regional high schools. They should invite high school teachers and students to participate in short courses, short visits, fair, meetings and symposiums. This might increase enrolments and impact favourably on quality judgment. Fifth, managers should ensure the performance of quality attributes up to a level where students are satisfied with the service performance and can trust the university.

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# The Concept of Culture in International Marketing: Towards a Relative Measure

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## Abstract

**Purpose** –Previous measures of culture in international business or marketing are constrained by their etic and/or absolute approach. A relative measure of culture is proposed and developed. Such a measure has the potential to be robust across home and host markets.

**Design/methodology/approach** – The conceptual basis for the culture concept is developed from the literature and field work. Next the proposed scale has been tested for reliability and validity using quantitative methods.

**Findings** –The study reinforces the growing disquiet with existing absolute measures, including those of Hofstede. Empirically, the relative scale performs well statistically. The scale is reliable and satisfies face, concept, convergent, discriminant and predictive validity tests.

**Research limitations/implications** –Although the scale works for a given home country (Australia) and over forty host countries, generalization is conditional until the scale is measured using other countries as the home market. There are immediate implications for international marketing practitioners because the subjective nature of the proposed culture measure means that success is up to their own cultural sensing, understanding and responding capabilities.

**Originality/value** –Although the literature has been quite critical of the Hofstede and other absolute measures of culture, there has not been a serious alternative conceptually presented and empirically tested. The current study does provide such an alternative and should facilitate a more consistent future global examination of showing that culture matters.

**Paper type**: research paper

**Keywords:** culture, relative vs. absolute, conceptual, empirical.

## Introduction

Culture is probably one of the most important macro-marketing environments for international marketers to consider when they venture internationally. Culture is considered "the instrument by which each new generation acquires the capacity to bridge the distance that separates one life from another" (Kramer & Herbig, 1994, p.36). The function of culture is to instil the beliefs and values that influence conduct, standards of performance and ways of dealing with interpersonal and environmental relations. In the context of international marketing, the acceptability of a firm's products and services is very much based on culturally bounded social and individual needs and wants (Kramer & Herbig, 1994). If a product is not perceived as being socially acceptable, firms need to revise their offerings (Kim, Forsythe, Gu, & Moon, 2002; Kramer & Herbig, 1994). The logic behind this revision of the offerings corresponds with the fundamental marketing concept – exchange to satisfy customer's needs and wants. In order to facilitate this exchange in the overseas markets, there is a need to understand the culture of the overseas markets.

Culture does matter, but there is a need for more effective measures of culture before we can conclusively demonstrate this point. It will be argued here, as it has elsewhere (for example, Holden, 2004), that the existing international marketing literature has relied on weak measures of culture. The current paper advocates and develops a *relative* rather than an *absolute* measure of culture. The limitations of absolute measures are made as are the benefits of a relative measure. A relative scale of culture is presented and statistical tests have been carried out to show the reliability and validity (including predictive validity) of the scale.

The literature review is presented next, followed by research method, data analysis, findings and discussion.

## Literature Review

In terms of studying culture, Hofstede's (1980) study on the classification of national culture is probably the most quoted work in international management context. He developed a model for classifying national cultures under four main dimensions: power distance, uncertainty avoidance, masculinity and individualism by using data gathered from IBM in the 1960s. However, there are a few limitations associated with the classification. Data are outdated, as they were collected forty years ago (Holden, 2004; Steenkamp, 2001). The study was conducted not from the marketing point of view, but was about work-related values (Holden, 2004; Steenkamp, 2001). The classification does not help international marketers understand their markets or market their products (Holden, 2004). The items measuring the cultural dimensions and the conceptual definition of these dimensions is tenuous and the meaning of the items may not be the same thing in different countries (Steenkamp, 2001). McSweeney (2002) also criticises Hofstede's classification to be a limited characterisation of culture, confined within the territory of states, and has methodological flaws. Empirical studies in recent marketing literature also found that Hofstede's classifications did not hold as expected (Chang, 2006; Garrett, Buisson, & Yap, 2006). All these critiques and recent development of cross-culture studies point to the need for a new measurement that is specifically suited for marketing.

The work from Trompennars (1994) is another popular classification of national culture. Trompennars' research was conducted over a 10-year period during the 1980s and 1990s. Unlike Hofstede who used one company and interviewed only managers in his study, Trompennars surveyed 30 companies and managers and administrative staff in his study. Five dimensions emerged from the research; namely, universalism vs. particularism, individualism vs. communitarianism, neutral vs. emotional, specific vs. diffuse and achievement vs. ascription. Only one of these five dimensions is the same as the Hofstede's classification. While Trompennars' framework has made contributions to the culture literature, the work is not without limitations. Both Trompennars' and Hofstede's approaches possess a limitation of using an etic approach, which is classifying countries based on their fit with a number of alleged cultural discriminators (Fletcher & Brown, 2005). The limitation of these etic studies lies in the fact that culture can be both dynamic and stable (Fletcher & Brown, 2005). Moreover, Trompennars' classification does not offer the next step in applying his model to study marketing issues.

Another classification scheme is based on the World Value Survey organised by the University of Michigan. Based on the values and beliefs of people from 78 countries, two broad dimensions emerged from the results. The first one is concerned about traditional vs. secular values and another is regarding quality of life. The advantage of this study is that it is relatively up to date. The first survey was conducted in the early 1980s and the latest survey took place from 1999-2001. The wide coverage of the world population is another advantage of the World Value Survey scheme. Nevertheless, the shortcomings of this scheme are similar to those of Hofstede's and Trompennars' in that it is an etic approach to view the world. Moreover, it does not provide international marketers with anything concrete to form a base to market their products overseas.

Another recent study on culture was conducted by Schwartz (1994; 1997, 1999). His study examined responses of teachers and students in 63 countries based on Schwartz Values Scale at the country level. The findings suggest that there are seven national-level domains, which are conservatism, intellectual autonomy, affective autonomy, hierarchy, egalitarianism, mastery and harmony. Schwartz's dimensions are valid in the sense that the items reflet the theoretical constructs (Steenkamp, 2001; Usunier, 2005). On the other hand, having possessed the limitations of being an etic approach, Schwartz's work has not been widely tested in the marketing context or has mixed results for the framework in marketing (Watson, Lyonski, Gillan, & Raymore, 2002).

A relative measure of culture provides a better foundation than absolute measures. Previous studies, such as Hofstede (1980) usually use absolute measures of culture. McSweeney (2002) argues that using absolute characteristics of specific national cultures cannot identify differences between national cultures. In other words, comparative measures should be used to examine the national culture differences. Holden (2004, p.568) goes a step further suggesting that "seen in a relational way, culture then becomes a resource, a form of productive knowledge about marketing relationships, about which there is always something new to learn. Culture is a dead resource until its value and utility are recognized as knowledge. In other words, culture is not just an inalienable feature of a market. It is also an element of our perception of it and our participation through marketing activities in it." This argument signifies two main aspects in terms of measuring national culture difference.

Firstly, culture is not set in a stone and can be affected by an individual's perception. Thus, when people's perceptions change, the culture differences change accordingly. Secondly, national culture is a relative concept. The perception of the people in country A have about country C may be completely different to the perception of the people in country B have about country C.

Culture is not fixed or solid, but changes with the marketing relationships across countries and each marketing relationship creates its own culture (Holden, 2004). This dynamic nature of culture makes the measures of culture in a classification manner inappropriate. Any culture is difficult to define in absolute terms. But, people are able to identify the extent to which a foreign culture deviates from their own. That is, the respondents' home country could become a reference norm. Such a scale could be used by research in any home country and applied to any host country, providing the business has experience of both markets, which they do in our study because that is the country all the questions are geared to. The scale is therefore potentially robust, that is, it can be used by any home (domestic) market in relation to any host (foreign) market.

There are few existing empirical studies to use a relative measure of culture. Closely related in what might be termed a quasi-culture rather than culture study, Theodosiou and Constantine (2001) examined the difference of the legal, economic and customer characteristics between the U.K. market and those in which the parent firm was based. Theodosiou and Constantine (2001) do not use the term "culture" but rather "customer characteristics" which is one of four (together with legal, economic and infrastructure) environmental factors that influence the degree of price standardization. The four items included in customer characteristics include:

- Similarity in customers' price sensitivity
- Similarity in the criteria customers use to evaluate the product
- Similarity in customers' requirements and preferences
- Similarity in customer segments targeted.

Importantly, each item was measured on a seven-point scale ranging from "very different" (1) to "very similar" (7) between the U.K. market and that in which the parent firm was based. Such a relative scale was very innovative and therefore noteworthy. Notwithstanding, the details of the scale can be quibbled with slightly. Firstly, the scale is explicitly consumer characteristics rather than culture, which is not a problem in their context, but is in the broader cultural context. Secondly, most of the respondents came from just three countries (USA, Germany and Japan), so the scale is not necessarily robust across a wider range of cultures. Thirdly, the orientation of the study is a single host country (U.K.) and multiple home countries, which is appropriate for their study contrasting manufacturing subsidiaries of MNCs operation in the United Kingdom. However it does not cover the more usual (exporting) orientation of firms from a given single home country (Australia in the research presented soon in our paper) entering among a choice of multiple host countries. The alternative orientation seems more important for countries making ex ante choices across markets rather than a reflection of market differences after the fact of entry. Fourthly, the highest loading item in the Theodosiou and Constantine (2001) consumer characteristic scale, namely price sensitivity, might be better classified as an economic rather than a cultural factor. Fifthly, the fourth item in that scale, similarity in customer segments targeted, might not reflect similarity in culture. For

example, Tiffany the upmarket jewellery retailer could target the same segment (high incomes and sophisticated) in all countries, but this would not mean that all countries had the same culture. Taking points four and five together, these two items may be appropriate for the consumer characteristic scale developed by Theodosiou and Constantine (2001), but these two items would not be appropriate for a cultural scale. More work is needed for such a scale, which represents a major gap in the literature.

In summary, the literature has placed considerable emphasis on the importance of culture in international business. However there is little consensus of a dominant paradigm, creating a vacuum filled temporarily and incompletely by the Hofstede approach. The two main limitations of the existing literature is the over-reliance on an etic approach and absolute measures of culture. Another limitation is that the literature sometimes emphasises a management rather than a marketing orientation in terms of how to apply cultural concepts. An alternative, potentially more effective and powerful direction is the use of *relative* measures of culture. The current study adopts and further develops the relative measurement approach.

**Research Method**

The data collection process had three phases including literature review, in-depth interviews, and quantitative field survey. A mixed method approach was adopted, given the relatively new aspects of culture that were to be explored.

Considering the exploratory nature of this study, it is important to carry out a series of in-depth interviews to establish the items for the culture construct. The objective of in-depth interviews was to identify key factors of culture. Conducting qualitative research is particularly useful for studying the "how" and "why" forms of research questions (Yin, 1994), especially for exploring new constructs. Qualitative input from experts such as managers or consultants using established methods for qualitative research is recommended before modelling to identify the appropriate variables and relationships to include in the model (Laurent, 2000). Quantitative modelling based on qualitative input can also ensure the functional forms and numerical values adequately reflect the real situation (Laurent, 2000). The key feature is that each item in this construct is in *relative* terms, namely the perception of some facet of culture in the foreign market relative to the home market. The measures of the culture construct in relative rather than absolute term are parallel to the literature (McSweeny, 2002; Theodosiou & Katsikeas, 2001).

Four in-depth interviews of international marketing managers were conducted. The interviews allow us to holistically explore and gain insights into the culture issues of firms involved in international marketing. The in-depth personal interviews were semi-structured with closed and open-ended questions with the owners or marketing managers of the businesses. The interviews were focused mainly on the issues of how and why the companies deal with culture issues. The collection of qualitative data, used in the quantitative analysis stage, can enhance external validity of the research (Laurent, 2000). The main themes of the in-depth personal interview protocol were:

1. *Did culture differences play a role in international marketing?*
   (Probe: What are the culture elements? In Asia, did relationship affect your international marketing? Did colour / language affect your branding?)

2. *What other factors of the macro environment played a role in the branding difference?*
   (Probe: Culture / Technology.)
3. *What are the big forces driving the marketing strategy? Are they external forces?*
   (Probe: External forces are beyond your control, such as cultural and economical aspects.)

In summary of the findings from the in-depth interviews, the interviews provided specific ideas and points to develop the survey questions. Below are some of the relevant perspectives emerging from the in-depth interviews.

"Cultural differences are mainly found in communication and ways of doing things. Japanese customers need a lot of explanations during the process of doing business, while the American need much less, maybe the cultural background of Australian and American is closer." (**A health equipment firm)**

"In Middle East countries, we couldn't have pictures of people drinking wine, and we have to take out a lot of female pictures in some of the marketing materials. We can't have any female in any advertising so there are male and male pictures. We have got a new website as well, but it is in different languages." (**A service firm)**

"SMS is not popular in the States, whereas in Europe, people have been using it for decades. We should have started in Europe than in the States or China. Especially those young kids in Europe now grow older and get to higher positions in corporations. They are more open-minded toward advanced technology. It makes us easier to market the product. Radio advertising was done in Cantonese, which most of the Chinese Malaysian speak in the capital – Kaula Lumpur. We outsourced the packaging idea to their agent who redesigned the packaging in Chinese to suit the Malaysia market. For another product, we used a cartoon character instead of a foreigner face as originally planned in the hope that it would not project an image of foreign firm." (**An I.T. development firm)**

"We are aware of the culture in the overseas markets. We would sort of talk to the distributors in those countries and say look is this brand name ok, are these cartoon characters ok? Is the colour of the label ok? Is the size ok? An example could be Malaysia where we export to. A lot of our shampoos will have been made for cats and dogs. There will be a cat and a dog on the label. In Malaysia, if someone owns a cat, they are not to buy a shampoo which also got a dog on the label, because they are Muslim because dogs are dirty animals. They don't like dogs. In the Malaysian market, we make separate labels for the cat shampoos and separate labels for the dogs whereas in Taiwan and HK, they are fine. Dogs and cats are on the same bottle. That's ok. The Taiwanese distributor also puts a Chinese name on the packaging. They have English on the label and Chinese underneath. The same as HK, they have just put a sticker which has got Chinese. In Malaysia, at this stage, we send them with the English labels on. They may put over a sticker on. Otherwise, there is not much culture, but things like size. Different markets like different sizes of bottles. HK distributors like smaller bottles, as they haven't got room to store them. Other countries like bigger bottles. So we are aware of them. There is certain issue such as that." (**A Pet Grooming Manufacturer)**

The findings from the in-depth interviews in combination with the extant literature, which was discussed above, formed the basis to establish the items for the culture construct.

Groeschl and Doherty (2000) argue that there are three layers of a culture; namely, basic assumptions, values and behaviour. The basic assumptions being the core element affect values which in turn influence behaviour that is the outer layer of their culture model. Findings from the in-depth interviews (the service firm, I.T. development firm, health equipment firm and pet grooming firm) also support the idea of values and behaviour being perceived differently between Australia and overseas markets. Thus, the following three items were developed in the international marketing context.

- In relation to the domestic market, customers in this foreign market behave differently.
- In relation to the domestic market, the motivation of customers in the foreign market is harder to understand.
- In relation to the domestic market, the culture in this foreign market is totally different.

Different cultures treat time differently. Time is cultural, subjective and variable, which can cause frustration and friction in cross-cultural business dealings (Hall & Hall, 1990). A number of marketing issues are related to time. For example, new product launches, sales negotiations, and logistics management. The following item was developed to tap into the time dimension.

- In relation to the domestic market, people in this foreign market tend to value individual time more.

Relationship marketing is different to traditional transactional marketing, in that it is based more on mutual cooperation, trust and joint benefits, rather than on competition and self-interest (Morgan & Hunt, 1994). Relationship within marketing involves a reciprocal and dynamic buyer-seller interaction. A single relationship within marketing can later expand to a whole network, which can affect international marketing activities such as market entry strategy. The marketing manager of the pet grooming firm also emphasised the importance of meeting distributors in the overseas in the in-depth interview. An item in relation to relationship was thus developed.

- In relation to the domestic market, interpersonal relationships in this foreign market are more important.

Visual impacts are culture bounded. The white colour commonly used in Western wedding ceremonies is the colour for funerals in China. International marketers need to understand the impact of visual aspects on marketing activities. From the in-depth interviews, visual aspects were raised by the interviewees a number of times (the service firm, I.T. development firm, and pet grooming firm). Thus, an item related to visual aspects was developed.

- In relation to the domestic market, visual aspects such as packaging and colours are more important in this foreign market.

A mail-out quantitative field survey was conducted after the in-depth interviews. 2,880 questionnaires were mailed to Australian firms randomly selected from the

sampling frame “http://www.austrade.gov.au/”. The database containing Australia firm involving international business is maintained by the Australian Government. A total of 315 usable questionnaires were received, giving a response rate of 12.4%, which is comparable with that of the industrial market research - 10% as suggested by Hart (1987) .

Descriptive statistics of the firm characteristics of the sample are displayed in Table 1. There are about 41% of firms in the manufacturing section, 5% in the agriculture section, and 54% in the service sector. In terms of the size of the firms, about 33% of the sample was firms with ten or fewer employees, while 41%, 9% and 12% of the sample were firms with 11 to 50 staff, 51 to 100 staff, and 101 to 500 staff respectively. Approximately 4% of firms employed 500 or more employees. Also about 29 percent of the sample is firms with foreign sales accounted for 10% or less of their total sales. A further 29% have foreign sales between 10 to 30% of total sales while 14% of the sample is firms with 31 to 50% of foreign sales. 5% of firms have 51 to 70%, 12% of firms with 71 to 90%, and 11% of firms with 91 to 100% of foreign sales. 28% of the sample listed their job title as “owner”, 20% as “managing director”, 21% as “marketing manager”, 12% as “general manager”, and 15% as “managers”, with a further 2% stating that they are the CEO. On the whole, the majority of sample respondents appear to represent targeted senior executives. In terms of foreign country entered, a wide range of countries were represented in the sample. A total of 45 countries comprised the sample. The most commonly nominated countries were USA, China, Japan, Malaysia and Singapore. The responses were classified into six regions. The most popular continents were Asia; representing 63% of the sample; followed by North America and Europe, with 17% and 10% respectively. This was expected, given that Asia is geographically close to Australia, and has experienced high economic growth in recent years. In general, the sample represented a mix of firms that were engaged in international business.

**Table 1: Firm Characteristics**

| **Business of Firm** | **N** | **% of firms** |
|---|---|---|
| Services | 172 | 54 |
| Manufacturing | 128 | 41 |
| Agriculture | 15 | 5 |
| Total | 315 | 100 |
| **Number of staff** | **N** | **% of firms** |
| 1 – 10 | 103 | 33 |
| 11 – 50 | 130 | 41 |
| 51 – 100 | 28 | 9 |
| 101 - 200 | 18 | 6 |
| 201 and more | 32 | 10 |
| Missing | 4 | 1 |
| Total | 315 | 100 |
| **Foreign sales as a % of total sales** | **N** | **% of firms** |
| 1 - 10 | 90 | 29 |
| 11 – 30 | 93 | 29 |
| 31 - 50 | 45 | 14 |
| 51 - 70 | 17 | 5 |
| 71 – 90 | 37 | 12 |
| 91 – 100 | 33 | 11 |
| Total | 315 | 100 |
| **Job title of informants** | **N** | **%** |
| Owner | 88 | 28 |
| CEO | 6 | 2 |
| Managing director | 65 | 20 |
| General manager | 39 | 12 |
| Marketing manager | 65 | 21 |
| Manager | 46 | 15 |
| Missing | 6 | 2 |
| Total | 315 | 100 |
| **Region Entered** | **N** | **% of firms** |
| Asia | 198 | 63 |
| North America | 53 | 17 |
| Europe | 30 | 10 |
| Oceania & New Zealand | 18 | 5 |
| Mid/South America | 6 | 2 |
| Africa | 4 | 1 |
| Missing | 6 | 2 |
| Total | 315 | 100 |

## Data Analysis

The following sections will present the results of reliability test based on Cronbach's alpha internal consistent measure, test of sphericity and measure of sampling adequacy, and validity tests. Five validity tests were performed; namely, face validity, discriminant validity, convergent validity, concept validity and predictive validity; to test the items. Each of them will be discussed in turn.

## Reliability

The reliability test result for culture is presented in Table 2. The item "In relation to the domestic market, people in the foreign market tend to value individual time more" was dropped due to a low item-total correlation (0.11). The resulting estimates had an alpha value of 0.73. Thus, further analysis was based on the remaining five variables.

**Table 2: Culture Reliability Test Result**

| **Item** | **Initial Reliability** | **Final Reliability** |
|---|---|---|
| Coefficient alpha | 0.70 | 0.73 |
| | Corrected item-total correlation | Corrected item-total correlation |
| overseas customers behaving differently | 0.51 | 0.54 |
| motivation of overseas customers harder to understand | 0.47 | 0.50 |
| value more individual time (deleted) | 0.16 | n.a. |
| interpersonal relationships more important | 0.51 | 0.50 |
| visual aspects more important | 0..45 | 0.42 |
| culture totally different | 0.51 | 0.54 |

## Test of Sphericity and Measure of Sampling Adequacy

Table 3 presents the results of the Bartlett's test of sphericity and KMO measure of sampling adequacy. The construct achieved a significant p-value, less than 0.001. The results of Bartlett's test of sphericity suggest that the items of the construct are sufficiently correlated, indicating that the data are suitable for factor analysis. The score of KMO measure of sampling adequacy of the construct is 0.78 which is higher than the cut-off, 0.5. The result suggests that there is adequate and high variability in the collected data. In consideration of the satisfactory results of the Bartlett's test of sphericity and KMO measure of sampling adequacy, further analysis based on the tested items in the constructs is deemed to be suitable.

**Table 3: Test of Sphericity and Measure of Sampling Adequacy**

| Constructs | KMO Measure of Sampling Adequacy | Bartlett's Test of Sphericity |
|---|---|---|
| Culture | 0.78 | Approx. Chi-Square = 306.53<br>df = 10<br>sig. < 0.001 |

*Validity*

Face validity refers to the extent to which the items adequately reflect the meaning of the construct under consideration (Churchill, 1979). Expert advice was sought from a professor and business practitioners by presenting the questionnaire for feedbacks. Items and wordings were modified based on their advice with an aim to ensuring that the items are good measures of the designated constructs. Several in-depth interviewees were also used to crosscheck and validate the items to enhance the face validity.

Exploratory factor analysis using principal components with varimax rotation was performed to examine the discriminant validity. Only one component was extracted. Communalities ranged in magnitude from 0.37 to 0.56. A scree test suggested a one-component solution be most appropriate for this sample. Examination of the factor loadings, which is shown in Table 4, led to the conclusion that the five items loaded well on the factor.

**Table 4: Component Matrix of Exploratory Factor Analysis**

| | Component |
|---|---|
| overseas customers behaving differently | 0.74 |
| motivation of overseas customers harder to understand | 0.71 |
| interpersonal relationships more important | 0.70 |
| visual aspects more important | 0.61 |
| culture totally different | 0.75 |

A test of concept validity was conducted by confirmatory factor analysis. The results of the various fit measures from demonstrated satisfactory results of this construct. The indices of the absolute fit measures for culture suggest that the model fits well, with Normed Chi Square statistics being 2.51 and AGFI 0.96. All incremental fit measures also reported acceptable results, all above the 0.90 cut-off (details are shown in Table 5).

**Table 5: Fit Measures for the Confirmatory Factor Analysis Model of Culture**

| Fit indices | Statistics |
|---|---|
| Normed Chi Square (CMIN/DF) | 2.51 |
| Adjusted goodness of fit index (AGFI) | 0.96 |
| Root mean square error of approximation (RMSEA) | 0.07 |
| Incremental fit index (IFI) | 0.98 |
| Normed fit index (NFI) | 0.96 |
| Standardised root mean square residual (SRMR) | 0.03 |

The critical ratio values in confirmatory factor analysis can be used to analyse the convergent validity of the items within the construct, to see whether they are fit together. The critical ratios (c.r.) of all the items were found significant at the 0.05 level (c.r. >1.96, $p<0.05$). The standardised factor loading coefficients (0.67, 0.61, 0.59, 0.48, and 0.68) were well above the acceptable level (0.4). The strongest variable in this construct was "in relation to the domestic market, the culture in the foreign market is totally different" with standardised factor loading of 0.67, followed by "in relation to the domestic market, customers in the foreign market behave differently" and "in relation to the domestic market, the motivation of customers in the foreign market is harder to understand"; and, with standardised factor loadings of 0.67 and 0.61 respectively. These results support the convergent validity of the proposed measurement models.

While various validity and reliability analyses were found satisfactory, it is necessary to examine the predictive validity of the items. The main purpose of predictive validity is to establish an empirical association of the construct under study with some criterion. This study adopted the method used by Dabholkar, Thorpe and Rentz (1996) to examine the predictive validity of the culture scale. Data was collected on four dependent variables related to international marketing strategies in the same study as culture. The variables were measured using a 7-point semantic differential scales with endpoints *strongly disagree* and *strongly agree.* Predictive validity was examined using correlations between the culture scale containing five items and marketing mix adaptation that has four items. These four marketing mix adaptation items are (i) "compared to the domestic market, the approach of promotion/advertising in the foreign market was different" ($r = 0.29$ and adjusted $r^2 = 0.08$, with $F(1,313) = 29.47$, $p <0.001$); (ii) "compared to the domestic market, the product features in the foreign market were different" ($r = 0.40$ and adjusted $r^2 = 0.16$, with $F(1,313) = 60.88$, $p <0.001$); (iii) "our firm carefully develops advertising/promotion message" ($r = 0.26$ and adjusted $r^2 = 0.07$, with $F(1,313) = 22.79$, $p <0.001$); and (iv) "our firm provides a lot of channel support" ($r = 0.21$ and adjusted $r^2 = 0.04$, with $F(1,313) = 14.63$, $p <0.001$). The regression analysis results indicated a statistically significant linear relationship between the culture scale and marketing mix adaptation. That is, a greater perceived difference of culture is associated with marketing mix adaptation. The results indicate predictive validity of the culture construct.

After the proposed items achieving validity and reliability, it is useful to further check the face validity of the culture construct. A categorisation of overseas countries based

on the mean scores using the five items to measure culture scale was performed. The mean score represents the perception with regard to the cultural closeness/distance of overseas markets *in relation to Australia* held by the international marketers of Australian firms. An interval scale of one to seven with endpoints "strongly disagree" to "strongly agree" was used. This scale can examine the perceived cultural closeness/distance deviated from Australia. In other words, the higher the mean score, the higher the perceived cultural distance is from Australia. Three groups of countries/districts emerged. The countries with mean scores from one to five are classified in the first group that has little perceived cultural difference in relation to Australia. The second group, the mean scores ranging from 5.1 to 5.5, contains countries perceived to be moderately close to Australia culture. The third group of countries are with mean scores 5.6 or above and are classified as culturally distant to Australia. The results for three clusters are shown in Figure 1.

The countries in the first group scored relative low in the four questions. That is, they were perceived to have little cultural difference in relation to Australia one. These countries included New Zealand, U.S.A., Canada, the U.K., Switzerland, South Africa and Spain. These countries have similar historical background and/or are at a similar economic standing.

The second group of countries scored about average in the scale. It represents a perceived moderately close culture to Australia. Seven countries in this group are Papua New Guinea, Hong Kong, Philippines, Singapore, South Korea, Taiwan, Saudi Arabia and Macau. Interestingly, all countries in this group are in Asia, including the four little dragons. The increasing economic activities between Australian firms and these countries may minimise the perceived cultural difference, as more understanding and common grounds can be found between them.

The distant culture group scored relative high in the scale. This group comprises China, U.A.E., Thailand, Indonesia, New Caledonia, Malaysia, Japan and India. An interesting finding is that Thailand and Indonesia are geographically close to Australia, but they were perceived to be very different culturally.

Face validity arises because most of the nominated countries are readily associated with a particular category. Based on common understanding, most Australia people would associate New Zealand, U.S.A., Canada and U.K. as having a culture fairly similar to Australia. The same people would, in contrast, associate China, Japan, India and Indonesia as having a more distant culture from Australia.

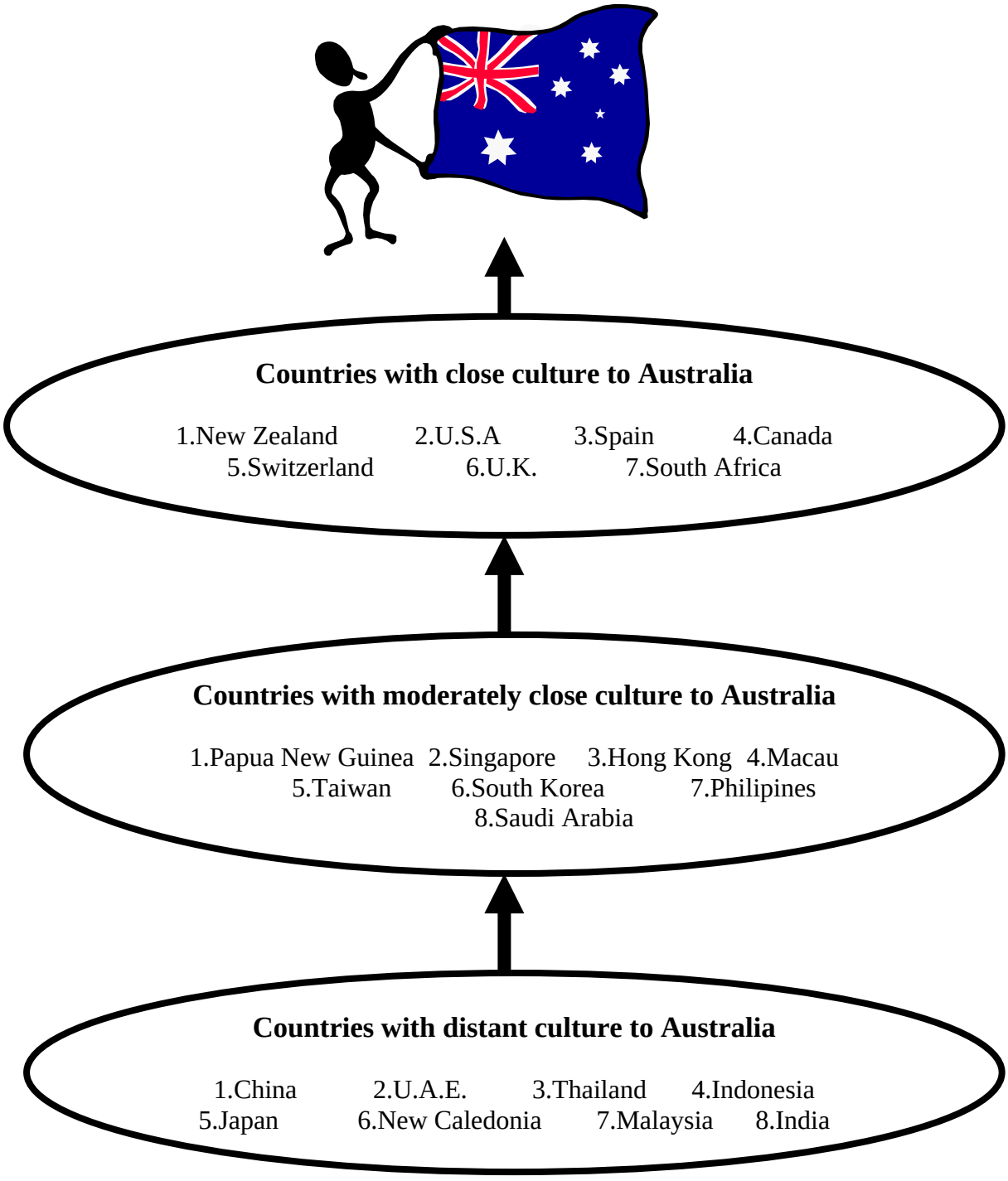


**Figure 1: Categorisation of Perceived Cultural Closeness**

Note that countries with insufficient number were not shown in the table and this classification is based on the mean score of the five cultural aspect items.

A one-way ANOVA analysis was conducted to further validate the above-mentioned three-tiered model. The results of Levene's test was not significant, $F(2,278) = 1.93$, $p>0.05$, so the assumption of homogeneity of variances was considered to have been met. A significant effect was found for the three-tiered cultural model, $F(2,278) =$

67.48, $p<0.001$. Tukey HSD post-hoc comparisons showed that all three groups of countries were statistically significantly different to one another; with distant culture to Australia, M = 5.54, SD = 0.72; moderately close culture to Australia, M = 5.13, SD = 0.75; and close culture to Australia, M = 4.29, SD = 0.90. The one-way ANOVA results support the three-tiered culture model.

**Discussion**

The most critical finding is that the study has developed a *relative* measure of culture, based on how dissimilar the host market is from the home market; a measure that is reliable and valid. Validity includes the commonsense face validity test of comparing three clusters of countries according to cultural distance. Validity also includes tests relating to concept, convergent and discriminant validity.

The scale can potentially be applied to a sample of international marketers in *any* given home market marketing to *any* host country. The scale is potentially robust across home markets, though this is subject to further testing. Of course, the actual scores may vary from country to country. Some countries may shift from one category to another, but we do not expect many such shifts between say two countries in a given category in Figure 1. If for example the study was based in the USA as the home market, one would still expect Canada, U.K. and Australia to be considered culturally close and China and Japan as culturally distant. Future studies are needed to ascertain exactly what variations would occur and the sum of such studies might provide an interesting cultural map of the world of trade. To re-iterate, the *scale* is potentially generalizable, though the *scores* may vary from host country to host country.

Note that the relative scale of culture overrules the notion of an absolute measure in that the score that Americans give China is likely to be different from the score given by British or Australians or any other national (home) sample of international marketers. Further, *within* each country, there is unlikely to be unanimity of scores for a country. The variability of culture within a country can be illustrated with reference to the perception of Australia international marketers of China's culture. The mean score for the five-item cultural scale was 5.5. But actually it ranged from 4.0 to 6.6 with a standard deviation of 0.76. As Holden (2004) noted, culture is a resource and needs to be understood and managed. Culture scores depend on the subjective powers of individual international marketers to sense, understand and respond to the cultural nuances of host countries.

Presenting and developing a more robust measure of culture should enable and facilitate other studies using the relative measure approach. One of the benefits of more robust culture measures that will emerge over time is more consistent empirical findings about the effect of culture on international marketing activity. Already, from the current study, we can point to positive predictive validity findings, especially including the impact of culture on different aspects of marketing mix adaptation from the home to the host country, particularly with respect to advertising and product features. To a lesser extent, there was a slight correlation from culture to more carefully developing advertising messages and providing a lot of channel support. The latter predictions suggest that firms that operate in more culturally distant markets may put more effort into designing the appropriate marketing mix strategies, with the

obverse danger that sometimes culturally similar markets could be taken too complacently.

The initial results suggest that (relative) culture can be robustly measured across different home and host countries, but more research is needed to support this new direction. The predictive validity results so far suggest that culture does matter.

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# ENVIRONMENTAL BUSINESS SCANNING LITERATURE–PAST, PRESENT AND FUTURE RESEARCH AGENDA

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**Abstract**
*The purpose of this paper is to make research propositions that can potentially fill the research gaps in the literature of scanning by businesses about the broader condition that may affect them (environmental scanning) environmental scanning. Major databases such as ABI/INFORM, Elsevier's science direct, and Emerald have been searched. Most of studies were included from published sources. The literature on environmental scanning is reviewed with an aim to identifying the patterns of the extant literature as well as research gaps. Based on the literature review, five propositions are suggested. These propositions are concerned with the antecedents of the environmental scanning behavior and the measurement of firm performance. The contributions of this paper are the identification of the evolution of the environmental scanning literature, research gaps, and the establishment of propositions that future research may further the knowledge of environmental scanning.*

**Keywords: Environmental Scanning, Market Entry Mode Choice, Strategic Planning, Born Global Firms, Firm Performance**

## INTRODUCTION

The contemporary economy is a global economy. Buyers and sellers in every country of the world engage in business transactions that, in one way or another, affect other buyers and sellers worldwide. A critical issue for business is how to best manage the changes currently taking place in the economic world. Global information is a platform to the understanding of the changing global market environment and the development of a successful business strategy. Environmental scanning concerning the activities of acquiring information provides a systematic mechanism to gather global information for managers to make strategic decisions. As such, a need to explore and understand environmental scanning has arisen among academia who look for explanations and try to understand and conceptualize environmental scanning, its nature, its key determinants and predictions, as well as the relationships among environmental scanning set of variables.

This study documents the findings of a literature review of the extant literature in relation to environmental scanning. This study has three main purposes: 1) to document existing literature, 2) to find patterns evolved from the literature, and 3) to make propositions for future research to fill the research gaps.

The research method used in this study is secondary research. The first stage in the research was to collect as much literature related to environmental scanning as possible. Several citation identification methods were utilized. A basic search was performed in ABI/Inform, Elsevier's science direct, and Emerald databases, using key-word search based on the occurrence of the phrases "environmental scanning" and/or "environmental analysis" in the abstract and/or title. A modified approach of content analysis advocated by Baregheh, Rowley and Sambrook (2009) was then employed to categorize the collected literature.

This paper is structured in four main sections. First, a literature review of environmental scanning, reflecting on the development in this area is presented. This is followed by the patterns evolved from the literature. Research gaps are then identified. On this basis, propositions are proposed to fill these gaps.

## LITERATURE REVIEW

### The first phase

A review of the environmental scanning literature indicates that Aguilar (1967) was the pioneer in identifying the types, sources, and methods of information acquisition frequently utilized by managers. His study found that none of the functional area, hierarchical level or firm size was strongly related to the extent executives scanned different environmental areas. His work was regarded as a micro approach, indicating that the use of environmental analysis was nothing more than a personal engagement of scanning environmental information (Thomas, 1980). The study aroused the interest of and paved a way for studying environmental scanning practices.

In an exploratory study, Kefalas and Schoderbek (1973) found that colleagues and informal meetings were the most important sources of information. Trade magazines and internal reports were of significant written sources. Their findings also showed the relationships between the executive's functional level and specialty and the types of information acquired. Furthermore, the results suggested that production executives spent more time scanning the environment than any other type of executive.

Keegan (1974) found that the executives of U.S. multinational firms relied on external sources of information that written materials from outside the firm were regarded as more important than those from inside. The major sources of this information were the staff of the firm's subsidiaries and affiliates, and those of law and accounting firms, and banks. The results indicated the reliance of the executives on human sources of information than on documentary sources. It showed general tendency that the character of environmental analysis was very subjective at that time. The study also found no computer-based systems for information gathering or retrieval, or significant information flow within the organizations. The contribution of Keegan's study was twofold. First, it provided empirical evidence contrary to a general belief that executives relied primarily on internal sources of information. Second, it

confirmed the Aguilar's (1967) propositions that managers relied chiefly on external human sources of information.

Wall (1974) conducted a longitudinal survey of the U.S. executives' attitudes toward corporate espionage and competitive information gathering. The results showed that published sources were the most frequently relied sources. The findings were contrary to those of Keegan (1974) and Aguilar (1967) that there was a shift in the mid 1970s from the previously relied on personal sources for information acquisition to documentary sources.

With previous research calling for a need for better environmental scanning techniques, Fahey and King (1977) conducted an empirical study centered on environment in both national and global context of social, political, regulatory, economic and technological conditions. They proposed three models to classify firms involved in environmental scanning activities; namely, irregular model, regular model, and continuous model. Their study was pioneer in that it was the first study describing the practice of environmental scanning activities in a diverse range of large firms in a systematically manner. The study substantiated a broad awareness of the importance of environmental scanning, but few of the firms materialized, in fact neglecting, the value of environmental scanning.

A study of U.S. firms found a direct relationship between the size of a firm and the extent of the involvement in environmental scanning activities (Thomas, 1980). It was found that most of the firms had scanning procedures in places with an average of ten years prior to the study. Scanning was thriving among the very largest firms. His study was opposing to Fahey and King's findings that "far from being in a state of neglect or decline, scanning for planning is alive and well, at least in the world's largest corporation." He further argued that "environmental scanning is on the threshold of rapid growth and development (Thomas, 1980, p.21)." However, the key limitation of his study was the research methodology that employed published data as the only source.

O'Connell and Zimmerman (1979) argued that the literature on the subject was too mechanistic, emphasizing purely on scanning systems and tools. Based on the results of the executives from America and Europe in international firms, they found that professional peers, particularly individuals in corporate headquarters, were ranked as the most important source of information. Their finding was different to that of Keegan's (1974). They conclude that firms' members might introduce their own values and needs that biased the ability of the firms to perceive their external environment. It was the first study to introduce human facet in the study of environmental scanning.

The researches on environmental scanning in the 1970's were at the infant stage. The units of the studies were mainly large U.S. firms. Researches focused on scanning systems and tools. In general, the studies were relatively descriptive that stated only the status quo of the environmental scanning behavior.

**The second phase**

During the second phase, interest in environmental scanning started to proliferate. Hambrick (1982) made a significant contribution in investigating the relationship between strategy and environmental scanning practices. The study was the first time of all the environmental scanning research that brought in other organizational variables, while all previous research was mainly concerned with describing the scanning systems. He found that in certain industries, firms with pioneering product or service scanned the entrepreneurial sector more than did firms offering a stable set of products or services. He suggested that executives scanned to reinforce their organizations' competitive strategies. It was this tendency that limited their responsiveness to environmental signals beyond their strategy scope.

Daft and Weick (1984) proposed a conceptual model to explain why organizations interpret the environment in a different way. The two dimensions used by the authors were management's assumptions about the analyzability of the external environment and the extent of organizational intrusiveness into the environment to understand it. These two dimensions form the basis for an interpretation system describing four modes of intrusive organization behavior; namely undirected viewing, enacting, conditioned viewing and discovering. These modes were then related to other organization variables for prediction with regard to strategy and decision processes. The major contribution of the study is the attempt of integrating the environmental scanning theories in the strategic management literature.

Examining the evolutionary process and state of environmental scanning, Jain (1984) found that environmental scanning activities were evolved in a pattern manner which could be distinguished in four phases. These primitive, ad hoc, reactive and proactive phases form a staged model from the primitive to proactive which was the most sophisticated stage of scanning. He further argued that executives' perception about the usefulness of the scanning process and a formalized system of strategic planning are the two prerequisites for firms establishing successful scanning process. He urged executives to change and adapt their perspective to the realities of forthcoming events in order to reap the benefits from environmental scanning.

A three-year-three-phase study surveyed almost 500 of the world's largest firms in three different sections; U.S. industrials, U.S. non-industrials, and foreign corporations showed that about 95 percent of all respondents conducted long-range planning activities Klein and Lineman (1984). Their findings suggested that environmental analysis was emerging as a substantial part of formalized long-range planning process. However, in general, the forecasting tools under environmental scanning were not effectively integrated into planning processes.

Kennedy's (1984) survey tried to find out the firms' approaches to environmental and political risk analysis, methodologies employed, level of integration into strategic planning, and firm characteristics. He found that the scanning activities had developed to a more sophisticated and coordinated state. The existence of SBU was discovered to have a significant relationship with environmental assessment; while the firm characteristics, percentage of sales abroad, and the number of foreign countries were no longer related to environmental scanning activities.

Lenz and Engledow (1986) conducted a field study of 10 firms with the most advanced environmental analysis in place to gain further insights of environmental scanning activities. Results showed that experimentation with alternative administrative structures was persisting. The majority of the firms relied on corporate monitors to initiate environmental analysis. They were usually non-professional personnel involved in scanning activities as volunteers. When potential interest was identified by the corporate monitors, an abstract of the article would be forwarded to the environmental analysis unit. The scanning unit was not tightly linked with strategic planning processes. The authors argued that extending knowledge of design and management of structures and process facilitating strategic adaptation could improve strategic management practice.

Examining the relationship of the perceived level of strategic uncertainty and the frequency and mode of scanning, Daft, Sormunen and Parks (1988) found that customer, economic and competitor sectors generated greater strategic uncertainty than technological, regulatory and sociocultural sectors. When strategic uncertainty increases, executives responded with greater scanning frequency and greater use of personal information sources. The results also indicated that chief executives in high-performing firms scanned more frequently the environment and more broadly when strategic uncertainty was high in comparison to their counterparts in low-performing firms.

Preble, Rau and Reichel (1988) based their study on the recognition that multinational firms were faced with increasing levels of uncertainty and complexity in their multiple and geographically dispersed operating environments. Their study looked at the extent of sophistication of environmental assessment activities, the nature and use of both internal and external sources of information, forecasting techniques, and risk evaluation. The authors concluded that there was an ever-increasing usage, sophistication and integration of international environmental scanning activities. Compared to the Keegan's study (1974), the findings represented substantial progress in terms of sophistication of environmental analysis.

A pioneering study on environmental scanning in this phase was the comparison of the practices of Korean firms and those of the U.S. firms (Ghoshal, 1988). The main areas to examine were the scanning behaviors of individual managers and the structures, roles, and the systems of formal environmental scanning units. The author argued that although scanning behaviors of American and Korean firms were quite similar on average, they differ sharply in the practices. His findings indicated that there was a level of homogeneity in the scanning practices of Korean firm and in their overall approach to the scanning function, which was in sharp contrast to the diversity of scanning practices in U.S. firms. The reason behind this difference was, according to the author, that the scanning practices were the responsibility of one staff in a Korean firm whereas in the United States there were many individuals who contributed to the design and implementation of environmental scanning systems. The author nevertheless indicated that culture might not be the reason for this difference.

In a conceptual paper, Schneider (1989) studied the relationship between strategy formulation; in terms of scanning, selecting, interpreting, and validating information, and national culture. The author suggested two sets of cultural assumptions were

believed to be associated to strategy formulation. They were external adaptation and internal integration, representing relationship with the environment and relationship among people respectively. The assumption made by Schneider is that with confidence on the conditions increases, less time and resources on environmental scanning will be devoted. The major implication of this paper is the author's recognition of the cultural differences in ways of approaching strategic formulation task.

Gilad's work at the end of 80's (1989) criticized the environmental scanning not being able to generate competitive advantage. In order to gain inferior strategic decisions, he proposed that organized intelligence that environmental scanning should be integrated into the overall strategic plan was critical. Organized intelligence should be the coordinated efforts across the whole organization rather than just directed toward familiar and easy-to-obtain information. Gilad further developed a "3E" strategy in terms of competitive intelligence to achieve competitive advantage. The 3Es are Entrepreneurial, Economic and Essential. His study shed light on the use of environmental scanning in relation to strategic management.

The researches on environmental scanning in the 1980s were flourishing. Not only did the studies try to understand what firms did with regard to environmental scanning, but also examined the relationships between the environmental scanning behavior and strategic management. It expanded the knowledge of environmental scanning practices. While most of the studies still focused on the U.S. firms, a comparison study was performed to enlarge the scope of the environmental scanning literature.

**The third phase**

Environmental scanning in the third phase had received continuing recognition in both general management and strategic literature (Ginter & Duncan, 1990; Preble, 1992). Soderlund (1990) proposed that there was a need to have a different approach to the environmental scanning function in the 1990s, which was considered to be a fragmented and confused, irrational and subjective nature of the contemporary society. This post-modern period for business had become increasingly turbulent and dynamic. As a result, the development of the environment scanning system depends on how the firms defined its environment. In respond to these post-modern phenomena, Soderlund (1990, p.9) suggested that "an internal environment based on ad hoc, spontaneous and voluntary interaction which gives rise to a mutual exchange of information. Soderlund's paper provided some insight into the post-modern era of environmental scanning.

A practical guideline of how to tackle macroenvironmental analysis for strategic management was put forward by Ginter and Duncan (1990). The authors proposed managers to ask themselves five questions about macroenvironmental analysis; 1) do we need it (macroenvironmental analysis)? 2) what areas should we analyze? 3) how much information do I need an where do I get it? 4) what techniques can we use to analyze important trends and events? And 5) what procedure and organization structures are most appropriate for analyzing the macroenvironment? It is an integrated framework that allows managers to think about macroenvironmental analysis from the strategic point of view.

Preble (1992) proposed an overall strategic control process to act as a guide for future strategic control systems. Preble's overall strategic control process was based on the use of environmental scanning to provide information for strategic surveillance and premise control. Strategic surveillance and premise control played significant roles in strategy formation, implementation and evaluation feedback control.

Jennings and Lumpkin (1992) conducted an empirical study to determine whether firms employing different strategies based on Porter's (1980) generic strategies would differ their approach to environmental scanning. Their findings confirmed that the type of scanning activity was significant related to strategy. In other words, firms adopting differentiation strategy would tend to scan the environment for opportunities while firms employing a cost leadership strategy would scan the environment in relation to threats. Firms emphasized on differentiation strategy perceive that new acquisitions, market, and investment are more important to their firms while the cost leaders perceive that regulatory and competitive threats were most important to their firms.

Empirical studies found that established firms were more likely to collect macro environmental information such as demographic, population, and socio-cultural trends; and to use formal methods of data collection such as focus groups, structured personal interview and database research than the newer ventures (Mohan-Neill, 1995). Similarly, high performance firms seemed to put more emphasis on a formal and coordinated scanning system (Analoui & Karami, 2002).

A study from Lim, Sharkey and Kim (1996) suggested that high-involvement exporters were involved in greater extent in environmental scanning in terms of export opportunities, competitor activities, and changes in global business conditions than low-involvement exporters that in turn were more involved than non-exporters. Along the line of this study, Yasai-Ardekani and Nystrom (1996) examined the relationships between the scanning design and the organizational context and found that i) the task environment was positively related to the scope design, frequency of scanning, and the top management team responsibility; ii) the general environment was positively related to the top management team responsibility; iii) organizational size was negatively related to the top management team responsibility, iv) inflexibility of technology was positively related to the scope of scanning design, and v) low-cost orientation was positively related to frequency and the top management responsibility. In general, they found that firms with effective scanning systems tended to align their scanning designs with the requirements of their context better than those with ineffective scanning systems.

From the international marketing perspective, Ojah and Han (1997) examined the environmental effects on marketing activity in developing countries. Their study reinforced the importance of environmental scanning when entering a distant and unfamiliar market. Following their idea of learning the role of functional area in environmental scanning, Huffman (2004) proposed that line managers need to play a critical role in feeding the information to the systems. His study shed light on an untouched issue of the role of lower rank staff in environmental scanning. The study suggested that environmental scanning was not only a corporate issue, but also involved line staff. In studying the impacts of environmental scanning on competitive strategy in small manufacturing firms in the U.S., Beal (2000) found that scope of

scanning, but not frequency of scanning, statistically associated with strategy formulation.

Trying to find out the impact of environmental scanning on new product development, Ahituv, Zif and Machlin (1998) found that firms that were more successful in new product development exhibited more frequent formal scanning, had more computer applications in their information system inventory, and possessed more computerized marketing information system than did less successful firms.

A study of Fortune 100 firms, Hough and White (2004) found that scanning increased as the environment increased in uncertainty from stable to moderate and dynamic. Some interesting findings in this study were related to the managers' roles. While the relationships between scanning completeness and environmental dynamism were found in an inverted U shape from vice presidents and product development managers, a positive linear and U shape were found from manufacturing and Sales/Marketing managers respectively. Their study suggested an interaction effect of managers' roles. Kumar, Subramanian and Strandholm (2001) studying the environmental scanning practice of the America health care industry confirmed the moderating role of environmental scanning activities in the strategy/performance relationship.

One of the major themes emerging during this period was the examination of the environmental scanning behavior of firms in different countries. Findings of 55 Hong Kong executives suggested that the executives perceived higher degree of uncertainty in the competitive, customer, and economic sectors than the political (Ebrahimi, 2000). He also found a positive relationship between the degree of perceived strategic uncertainty and scanning frequency and interest of firms in Hong Kong. In addition, the executives also scanned the task environment in terms of competitors, customers, and suppliers of resources sectors more intensely than the remote ones that included political/legal, economic, social/cultural, and technological sectors. Another empirical research studied the sources of information used, environmental scanning practice and organizational performance of Nigerian manufacturing firms (Swayerr, Ebrahimi, & Thibodeaux, 2000). They found that greater scanning frequency in the economic and political sections of the environment than the customer/market and competitor sections. Also, environmental scanning frequency did not affect firm's performance and internal sources of information was preferred in comparison to external ones. May, Stewart and Sweo (2000) studied the environmental scanning behavior of firms in Russia. The empirical results suggested that the Russian executives did not scan more frequently even though the Russian environment was ranked as highest in strategic uncertainty in terms of customer/market, economic and competition. Ogunmokun and Ng (1999) studied the differences between high and low performance of Australian firms in terms of their environmental scanning practices. The results showed that Australian firms with higher performance were significantly different to those lower performance firms in terms of the frequency of use of a systematic method and a fixed policy. Elenkov (1997) studied 141 medium-size Bulgarian firms with regard to the relationship between perceptions of strategic uncertainty and environmental scanning behaviors. The findings suggested that the increase in strategic uncertainty would have a positive impact on managers' reliance on personal modes of scanning and external sources of information. This study further revealed that Bulgarian firms are different to their U.S. counterparts in terms of strategic uncertainty perception and environmental scanning behavior. Another

study using in-depth interviews to examine the environmental scanning behavior of Thailand SMEs found that firms practising environmental scanning were better able to develop appropriate new products (Ngamkroeckjoti, Speece, & Dimmitt, 2005). This finding was in agreement with Ahituv, Zif and Machlin's (1998) study. In a more recent study, an exploratory study of German corporations revealed that environmental scanning would still be an important tool for the German firms in the future (Schwarz, 2008). The findings also suggested that environmental scanning was expected to create alternative pictures of the future, detect change in an organizational environment, and keep track of these changes so that firms can react strategically to them.

In a comparative study of 47 U.S. and 57 Indian entrepreneur firms, Steward, May and Kalia (2008) found that Indian and U.S entrepreneurs are similar in scanning behaviors. Both Indian and U.S. entrepreneurs increased the scanning frequency when they perceived that there were increases in the rate of environmental changes. However, Indian entrepreneurs scanned more frequently than U.S. entrepreneurs due to more discomfort with uncertainty, higher risk avoidance and a greater future orientation in comparison to the U.S.

One of the major contributions in the third phase is the examination of the environmental scanning behavior of the firms in different countries. In addition, various studies were conducted to examine the relationships amount environmental scanning, strategy and firm performance.

A summary of the extant literature is shown in table one.

Table 1: A summary of the extant literature of environmental scanning

| **Author (year)** | **Type of study** | **Findings / Propositions** |
|---|---|---|
| ***Phase One*** | | |
| Aguilar (1967) | Empirical | Types, sources, and methods of information acquisition were frequently utilized by managers. |
| Kefalas and Schoderbek (1973) | Empirical | Colleagues and informal meetings were the most important sources of information. Trade magazines and internal reports were of significant written sources. |
| Keegan (1974) | Empirical | Written materials from outside the firm were regarded as more important than those from inside. The major sources were the staff of the firm's subsidiaries and affiliates, and those of law and accounting firms, and banks. No computer-based system was used. |
| Wall (1974) | Empirical | Published sources were the most frequently relied sources. |
| Fahey and King (1977) | Empirical | Few of the firms materialized, in fact neglecting, the value of environmental scanning |

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|---|---|---|
| Thomas (1980) | Empirical | The size of a firm affected the extent of the involvement in environmental scanning activities. |
| O'Connell and Zimmerman (1979) | Empirical | Professional peers, particularly individuals in corporate headquarters, were ranked as the most important source of information. |
| ***Phase Two*** | | |
| Hambrick (1982) | Empirical | The study found a difference between innovative firms and firms focusing price/quality/service/delivery in the amount of scanning. |
| Daft and Weick (1984) | Conceptual | The study attempted to integrate the environmental scanning theories in the strategic management literature. |
| Jain (1984) | Empirical | Four phases of environmental scanning activities were found; namely primitive, ad hoc, reactive and proactive phases |
| Klein and Lineman (1984) | Empirical | Environmental analysis was part of formalized long-range planning process. But, the forecasting tools were not effectively integrated into planning processes. |
| Kennedy (1984) | Empirical | The existence of SBU had a significant relationship with environmental assessment; while the firm characteristics, percentage of sales abroad, and the number of foreign countries were not related to environmental scanning activities. |
| Lenz and Engledow (1986) | Empirical | Non-professional personnel were involved in scanning activities as volunteers. The scanning unit was not tightly linked with strategic planning processes. |
| Daft, Sormunen and Parks (1988) | Empirical | Strategic uncertainty increases increased scanning frequency and greater use of personal information sources.<br><br>High-performing firms scanned more frequently the environment and more broadly when strategic uncertainty was high in comparison to their counterparts in low-performing firms. |
| Preble, Rau and Reichel | Empirical | Evidence suggested ever-increasing |

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|---|---|---|
| (1988) | | usage, sophistication and integration of international environmental scanning activities. |
| Ghoshal (1988) | Empirical | Scanning behaviors of American and Korean firms were quite similar on average, but they differ sharply in the practices. |
| Schneider (1989) | Conceptual | Two sets of cultural assumptions, external adaptation and internal integration, were conceptualized to be associated to strategy formulation and environmental scanning. |
| Gilad (1989) | Conceptual | A model called "3E" strategy in terms of competitive intelligence to achieve competitive advantage was developed. "3E" stood for Entrepreneurial, Economic and Essential. |
| ***Phase Three*** | | |
| Soderlund (1990) | Conceptual | Mutual exchange of information was based on ad hoc, spontaneous and voluntary interaction. |
| Ginter and Duncan (1990) | conceptual | A five-step guide of how to tackle macroenvironmental analysis for strategic management was developed. |
| Jennings and Lumpkin (1992) | Empirical | Firms adopting differentiation strategy tended to scan the environment for opportunities and perceived that new acquisitions, market, and investment were more important to their firms<br><br>Firms employing a cost leadership strategy scanned the environment in relation to threats and perceived that regulatory and competitive threats were most important to their firms. |
| Preble (1992) | Conceptual | Environmental scanning could provide information for strategic surveillance and premise control. |
| Mohan-Neill (1995) | Empirical | Established firms were more likely to collect macro environmental information; and to use formal methods of data collection than the newer ventures. |
| Analoui and Karami (2002) | Empirical | High performance firms possessed more formal and coordinated scanning system. |

| | | |
|---|---|---|
| Lim, Sharkey and Kim (1996) | Empirical | High-involvement exporters scanned export opportunities, competitor activities, and changes in global business conditions in greater extent than low-involvement exporters which in turn did more than non-exporters. |
| Yasai-Ardekani and Nystrom (1996) | Empirical | Firms with effective scanning systems tended to align their scanning designs with the requirements of their context better than those with ineffective scanning systems. |
| Ojah and Han (1997) | Empirical | The environmental scanning affected marketing activity in developing countries. |
| Huffman (2004) | Empirical | Environmental scanning was not only a corporate issue, but also line staff. |
| Ahituv, Zif and Machlin (1998) | Empirical | Firms more successful in new product development exhibited more frequent formal scanning, had more computer applications in their information system inventory, and possessed more computerized marketing information system. |
| Hough and White (2004) | Empirical | There was an interaction effect of managers' roles in scanning completeness and environmental dynamism. |
| Swayerr, Ebrahimi and Thibodeaux (2000) | Empirical | Nigeria firms showed greater scanning frequency in the economic and political sections than the customer/market and competitor sections. Also, there was no relationship between environmental scanning and firm's performance. Internal sources of information were preferred to external ones. |
| May, Stewart and Sweo (2000) | Empirical | The Russian executives did not scan more frequently even though the Russian environment was highly uncertain. |
| Ogunmokun and Ng (1999) | Empirical | Australian higher performance firms made use of a systematic method more frequent than those lower performance firms. |
| Elenkov (1997) | Empirical | Bulgarian firms tended to rely on manager's personal modes of scanning and external sources of |

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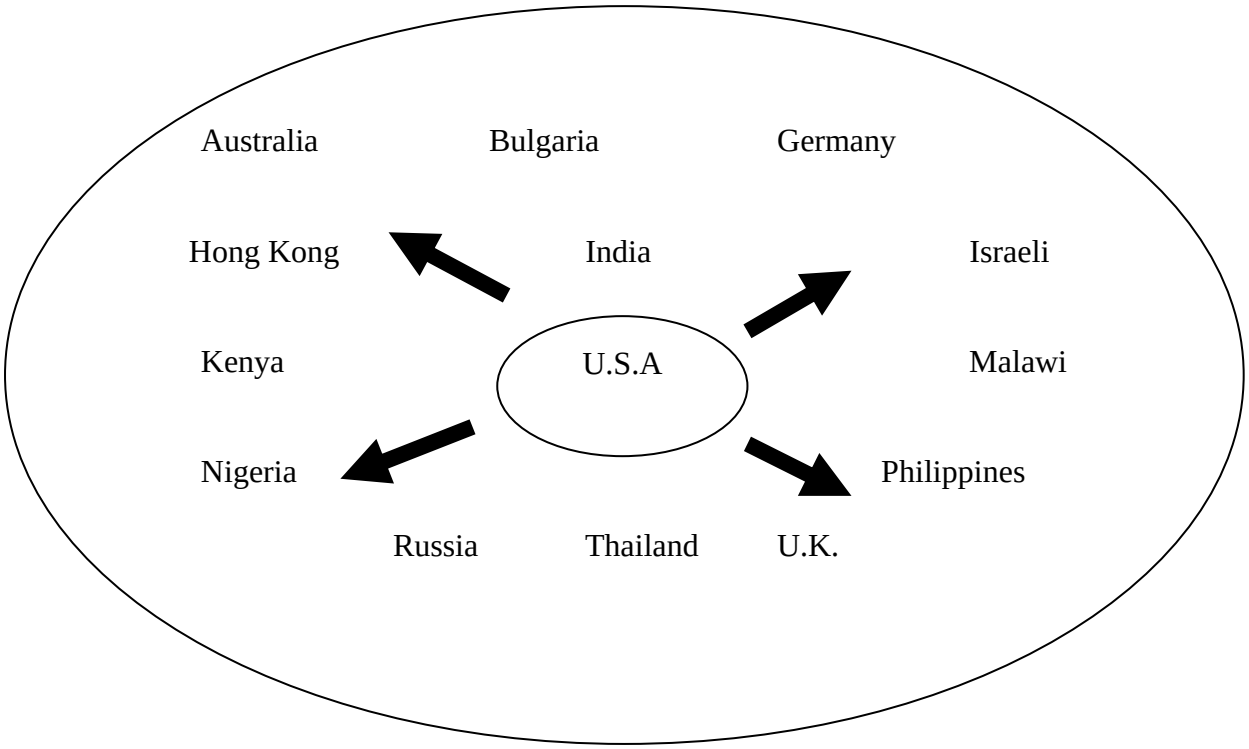
|---|---|---|
| | | information with the increase in strategic uncertainty. |
| Ebrahimi (2000) | Empirical | Hong Kong executives scanned the competitors, customers, and suppliers of resources sectors more intensely than the remote one. There was a positive relationship between the degree of perceived strategic uncertainty and scanning behavior in terms of frequency and interest. |
| Schwarz (2008) | Empirical | Environmental scanning in German firms was expected to create alternative pictures of the future, detect change in an organizational environment, and keep track of these changes for strategic deployment. |
| May and Kalia (2008) | Empirical | Indian entrepreneurs scanned more frequently than U.S. entrepreneurs due to more discomfort with uncertainty, higher risk avoidance and a greater future orientation in comparison to the U.S. |
| Beal (2000) | Empirical | Scope of scanning, but not frequency of scanning, was statistically associated with strategy formulation. |
| Ngamkroeckjoti, Speece, & Dimmitt (2005) | Empirical | Thailand SMEs practising environmental scanning were better able to develop appropriate new products. |
| Kumar, Subramanian and Strandholm (2001) | Empirical | There was a moderating role of environmental scanning activities in the strategy/performance relationship. |

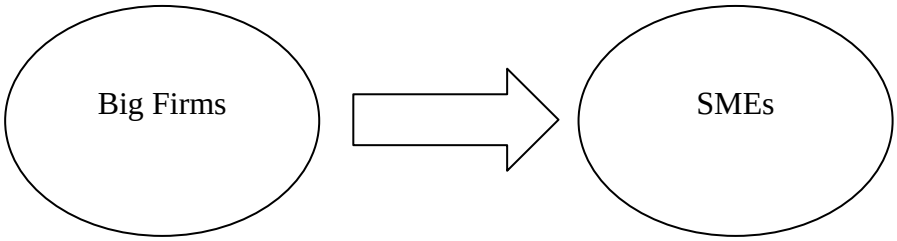
The three-phase evolution of environmental scanning literature shows three distinctive characteristics. The first is the expansion of the country studies, as depicted in figure 1. Most of the studies in the first two phases were based on the U.S. From the third phase, more studies tried to look at the environmental scanning behavior of firms in other countries.

Figure 1: The geographical expansion of the environmental scanning studies



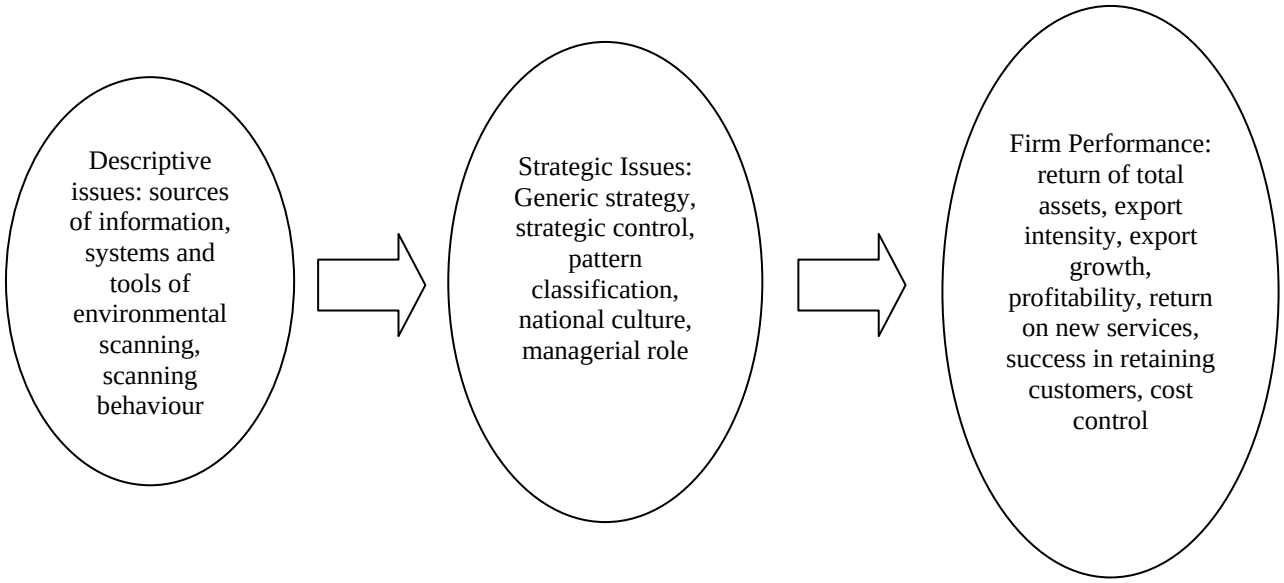

The second characteristic is the extension of the studies from big firms to SMEs. While the studies about the big firms depict what environmental scanning is, how and why they do it, the studies were unable to generalize the environmental scanning practices of smaller firms. Some emerging studies with regard to environmental scanning from the perspective of SMEs have filled this research gap.

Figure 2: The extension of the environmental scanning studies - firm size




The third characteristic identified from the literature is the expansion from descriptive research to correlational research, as shown in figure 3. The expansion spans the knowledge from what environmental scanning is and how it is carried out to what its impacts are. In other words, more empirical studies have examined the consequences of the practices of environmental scanning. In particular, the researches focus on strategic management and financial performance.

Figure 3: The research areas of the environmental scanning studies




While the extant literature on environmental scanning has attracted attention and empirical evidence has grown in the past decades, there exist some research gaps in the literature. Firstly, as suggested by Kumar, Subramanian and Strandholm (2001), the antecedents of environmental scanning behavior are understudied. Secondly, the relationship between environmental scanning and market entry mode choice remains untouched. In consideration of all these issues, the following section will discuss the propositions that can fill these research gaps in the extant literature.

**PROPOSITIONS**

Firm characteristics may affect environmental scanning behavior and practice. Firms that newly enter international markets may have different environmental scanning behavior than those established firms. A set of new firms, which were coined as born global firm, were very successful in the world markets without a strong hold of a domestic market (Rennie, 1993). Born globals have been defined as firms that "as business organizations, from inception seek to derive significant competitive advantage from the use of resources and the sale of outputs in multiple countries" (Oviatt & McDougal, 1994, p.49).

Born global firms are unique in that these firms enter the international market in a relatively short time once the firms have been established. Moreover, born global firms have a relatively high proportion of sales generated from international markets. Born globals challenge the conventional stage theories that emphasize the need to build up the domestic base thoroughly before entering the international arena. The arguments about born global firms are conflicting with the traditional internationalization theories, such as Uppsala model that emphasizes international experience (Johanson & Vahlne, 1977; Johanson & Vahlne, 1990; Johanson & Wiedersheim-Paul, 1975). Moen (2002) argued that born global firms' internal factors such as firm orientation and competitive strategy were different to non-born

global firms. All these works suggest that born global firms are different to other firms in nature and in behavior. Thus,

*Proposition 1: The environmental scanning behavior of born global firms is different to that of non-born global firms.*

The major differences between service marketing and product marketing are generic differences between services and physical goods and the environment within which the marketing task is performed (Cicic, Patterson, & Shoham, 1999). Generic differences are usually referred to in terms of intangibility, inseparability, heterogeneity and perishability (Bradley, 2002). The uniqueness of services suggests that service firms may need different marketing approaches. A number of works provide a solid foundation for developing a new branch of marketing literature for service firms (Bitner, 1990; Eckhardt & Houston, 2002; Vignali, 2001; Wong & Merrilees, 2009; Zeithaml, Parasuraman, & Berry, 1985). When service firms enter overseas markets they have to consider the cultural characteristics with potential adjustment of internal resources and changing marketing strategy. International services are defined as "deeds, performances, efforts, conducted across national boundaries in critical contact with foreign cultures (Clark, Rajaratnam, & Smith, 1996, p.15). This definition suggests that international services pose a couple of unique characteristics compared to domestic services. They are the involvement of cross border activities and the interaction with a foreign culture. Essentially, these studies argue that service firms are different to the product firms in international marketing practices. The information needed for service firms to do business may be different to that for product firms. Thus,

*Proposition 2: The environmental scanning behavior of services firms is different to that of product firms*

The choice of a market entry mode into international markets is a critical decision an international manager must make (Terpstra & Sarathy, 2000). Driscoll (1995) furthered an argument that firms institutionalize their initial mode choice over time as new products are sold through the same, established channels, and new markets are entered using the same entry method. Douglas and Craig (1992) embraced the competitive aspect in the market entry mode selection by suggesting that it is a kind of signal to key competitors and about the firms' intention and determination of the basis for future battles. In this context, the foreign market entry modes become international firms' strategic issue for, which requires proper information and planning efforts to support it.

The selection of the foreign market entry mode is important due to the cost and risk involved. A mistake in selecting a foreign market entry mode could be costly for international firms. When entering international markets, three groupings of foreign market entry modes can be identified; they are export, contractual and investment modes (Driscoll & Paliwoda, 1997). Each of these modes has distinguishing characteristics where different types of information generated from environmental scanning may be needed to make a proper foreign market entry mode choice. For example, since an export entry mode incurs less risk to a firm, the firm may require less information input for its market entry mode choice decision. Thus,

*Proposition 3: Firms with greater environmental scanning efforts tend to prefer a non-exporting entry mode.*

A firm's management orientation can affect how the firm is run with implications for what information is needed. Market orientation is concerned with a business focus paying balanced attention to both customers and competitors to drive the business (Kohli & Jaworski, 1990; Narver & Slater, 1990). In general, the three dimensions of market orientation are organization-wide generation of intelligence generation, sharing and dissemination of such market intelligence and organization-wide market responsiveness. Empirical studies of market orientation have suggested that there is a favourable impact on customer retention rates (Balakrishnan, 1996); it can enhance business profitability (Kim, 2003; Pelendran, Speed, & Widing, 2000); and it can positively affect sponsor trust and sponsor commitment (Farrelly & Quester, 2003). Market orientation is a multifaceted concept that includes intelligence generation, information dissemination and market responsiveness (Farrelly & Quester, 2003). In order to be market oriented, firms need to have sufficient market intelligence that can be generated by environmental scanning. Thus:

*Proposition 4: Firms with greater market orientation tend to have a more sophisticated environmental scanning system.*

A firm's overall international marketing performance indicates "the extent to which a firm's economic and strategic objectives with respect to marketing a product/service to a foreign market are achieved through planning and execution of its international marketing strategy" (Wong & Merrilees, 2007, p.389). A major limitation of extant literature of environmental scanning is that the use of a single dimension of performance (i.e. financial performance) does not adequately represent the performance construct. In another research area such as international marketing, most researchers have advocated a multi-dimensional approach (Calantone & Knight, 2000; Chaudhuri, 1999; Reid, 2002; Shoham & Kropp, 1998).

Multi-dimensional measures of a firm's performance includes financial and strategic aspects. As argued by Cavusgil and Zou (1994, p.4), "a firm usually initiates an export venture with a number of objectives, which can be *financial* (i.e. profits, sales, or costs) and/or *strategic* (i.e. market expansion, competitive response, gaining a foothold in a foreign market, or increasing the awareness of the product/firm)." It is expected that a multidimensional measure of firm performance can provide a more valid picture of the impacts of environmental scanning practices. Thus,

*Proposition 5: The measure of a firm's performance should include strategic performance.*

## CONCLUSION

Research on environmental scanning has expanded in the past 40 years. Various conceptual and empirical studies have advanced the knowledge of environmental scanning. A review of the literature of environmental scanning shows that the literature has evolved in three distinctive phases. The first phase is characterized by studies trying to understand what environment scanning was and how it worked in big American firms. Most of the studies were descriptive in nature, and the primary focus

was on the sources of and the computer usage in environment scanning. During the second phase, interest in environmental scanning started to proliferate. More correlational rather than descriptive studies were performed. Studies were not limited to only what the firms did, but also the impacts of environmental scanning on various strategic management issues. The scanning intensity and cultural issues were also examined. The third phase characterizes the expansion of the literature in terms of the geographical areas into which the studies examined. The scope of correlational study spread out to include firm performance and strategic control. The focus also shifted from big firms to SMEs. However, research gaps still exist in certain areas such as the antecedents of environmental scanning behavior and the link between environmental scanning behavior and market entry mode choice. This paper has made five propositions to fill these research gaps. Three propositions are related to the antecedents of the environmental scanning behavior; one to the market entry mode choice, and one to the measurement of firm performance. Further empirical study to validate these propositions is recommended.

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# Regulation of Superannuation in Australia: An Overview

**Jennifer Butler***

## Abstract

Retirement saving is a topical issue in Australian society today. With longer life expectancy many a debate revolves around whether Australia's retirement savings will be adequate to sustain us for the lengthier periods required without recourse to some form of government funded pension to supplement retirement savings. Hand in hand with that debate is the issue as to whether the superannuation savings that we do have are adequately protected. With increasing superannuation savings so too are the risks that these savings will not be available when the time comes to use them. This paper discusses the regulatory system that exists to safeguard our superannuation system with some consideration given to whether or not the onerous regulations that exist are justified given the current superannuation environment.

## Background

Australia's superannuation system is considered by some to be one of the best in the world.[2] The system addresses the OECD recommendations for a multi-pillar arrangement with the current arrangement constituted by a safety net component, an occupational superannuation component and a private sector component. The safety net component is covered by the Age Pension. The Age Pension is means-tested and available to males aged over 65 and females aged over 63, with the pension age for women rising to 65 by 2014.[3] The level of the Age Pension is indexed to 25% of the Male Total Average Weekly Earnings figure.[4] The low level of income which the Age Pension provides is therefore some significant incentive to contribute to retirement earnings by some other means such as private savings. However, there are some components of the Age Pension that make it an attractive proposition such as the elimination of longevity risk and the ancillary benefits that are provided including subsidisation of prescription medications.[5] The fact that the pension is indexed so that it maintains its real value over time also makes it attractive as compared to some forms of private retirement income streams which are not protected against reductions in real replacement rates.[6] In fact, in 2003 data from the Department of Family and Community Services showed that only 18 per cent of those who are retired were self-funded retirees.[7] Therefore, the Age Pension is still the major form of income support for the majority of those of retirement age and this is expected to be the case for some time into the future.

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[2] Mike Taylor, 'Power in the right hands', *Money Management*, 5 July 2007, 13.

[3] Centrelink,WhoCanGetAgePension,(2008) <http://www.centrelink.gov.au/internet/internet.nsf/payments/qual_how_agepens.htm> at 10 May 2008.

[4] Centrelink, Adjusting Maximum Payment Rates, (2008) http://www.centrelink.gov.au/internet/internet.nsf/payments/pay_cpi.htm at 10 May 2008.

[5] Jon Stanford, 'Long-Term Issues in Superannuation: An Overview' (2004) 37 *The Australian Economic Review* 180, 180.

[6] Ibid.

[7] Department of Family and Community Services, *Inquiries into Retirement and Superannuation*, Occasional Paper no. 11 (2003).

The occupational superannuation component is characterised by compulsion. Employers are required to contribute to superannuation on behalf of most employees at a rate of 9% of the employee's ordinary time earnings. While there is much debate as to whether this rate of contribution is sufficient to adequately fund retirement incomes in the future there is no doubt that at the very least it will reduce the reliance on the Age Pension by those who have had good levels of workforce participation from a young age. There will always be a portion of the community that suffer from lower levels of workforce participation throughout their lifetime for any number of reasons but moving a higher proportion of the ageing community away from Government-funded retirement benefits is expected to be a key outcome of this requirement. In fact, the Government expects that by 2040 only 50% of those who are retired will still be funded by an Age Pension.[8] This rate will gradually increase up to 2020 when the superannuation guarantee amount will be 12%. This is a measure that has been brought in by the Rudd Government in an attempt to address some of these issues. However, it should be noted that this measure is being implemented in direct opposition to the recommendations made by the Henry Review.

The third pillar of the Australia's retirement income system relies on the voluntary provision of private savings and superannuation. There is no real encouragement built into the Australian system to encourage private savings other than a concessional system of superannuation taxation which provides some incentive for those on middle to higher incomes to save through superannuation. By encouraging investment into superannuation rather in some other private capacity the funds are then subject to the preservation requirements which limits the ability to draw on those funds until one of the conditions of release are met. Generally speaking, this will require superannuation savings to be preserved until age 55 although other conditions of release may, in limited circumstances, allow for funds to be paid out earlier.

The focus on superannuation as a key method of encouraging saving for retirement requires there to be a high level of confidence in the ability of superannuation funds to protect the substantial investment in retirement savings. Total estimated superannuation assets have topped the trillion dollar mark and contributions of around $21 billion are made to superannuation funds each quarter.[9] This represents a significant investment by ordinary Australians in saving for retirement which will have the effect of reducing the Government's pension expenditure. Some of the elements of compulsion that characterised the Australian superannuation system have now been rectified. For example, most employees are now able to choose which fund their superannuation is contributed to. However, compulsory superannuation contributions by employers are still the main source of investment in superannuation comprising 65.9% of total contributions.[10] To ensure that these savings are adequately protected a rigorous system of prudential regulation is required. Australia has a system of regulation that has been criticised as being so onerous that it has increased the cost of administration. This is a concern as higher costs will reduce the benefits to members by eroding their account balances. In an ideal world the most influential factor determining account balances would be the performance of investment markets and factors such as management practices of funds would be less

[8] Commonwealth Treasury, *Intergenerational Report 2002-03*, (2003-03).
[9] Australian Prudential Regulation Authority, *Quarterly Superannuation Performance*, December 2007.
[10] Ibid.

significant as adequate regulation will apply to reduce such factors to the level where they will have less of an effect on account balances.

**History of regulatory provisions**

The regulation of superannuation in Australia has been evolving over time as the reliance on superannuation as an alternate means of retirement income has become more important. While superannuation has been available in Australia since the 19th century, regulation of the superannuation industry is a more recent process that reflects the increasing importance of the industry in the Australian economy. Indeed the industry was virtually self-regulating until the mid-1980's at which time regulation was mostly related to the taxation of superannuation and contained in the *Income Tax Assessment Act.* 1987 saw the introduction of specific legislation targeted at regulating superannuation with the *Occupational and Superannuation Standards Act (and Regulations)* being enacted at this time. Along with this legislation came the establishment of a specific industry regulator in the form of the Insurance and Superannuation Commission (ISC) established under the taxing powers of the Commonwealth Government. The use of the taxing powers of the Commonwealth to establish the regulations has produced a situation where any concessions available to a superannuation fund are reliant on that fund meeting the regulatory requirements to obtain any tax concessions available.[11] This is the situation which still exists today.

Substantial changes to the regulatory provisions came about in 1994 with the enactment of *Superannuation Industry (Supervision) Act 1993* (SISA) and associated regulations. The changes under this legislation resulted in the jurisdiction of the ISC being expanded with increased supervision and regulation of superannuation funds.[12] The duties of trustees and service providers were also codified in the legislation. Civil and criminal penalties were also introduced for those trustees failing in their duties under the Act.

Further changes to the regulatory provisions occurred in 1998 following recommendations arising from the Wallis Report. This resulted in a new regulator, the Australian Prudential Regulation Authority (APRA), being established with responsibility for the entire financial system. Other existing regulatory authorities had some of their responsibilities removed while the ISC and the Australian Securities Commission were abolished. The Australian Securities and Investments Commission (ASIC) was also established as an additional regulatory body to oversee consumer and investor protection and regulation of financial markets. Following these changes the responsibility for regulating superannuation is split between APRA (prudential supervision of funds), ASIC and the Australian Taxation Office.[13]

Following substantial growth in the value of assets managed in the superannuation sector and increasing public concern over some high profile corporate collapses further changes to the regulatory regime occurred in the early 2000's. Critical

[11] Hazel Bateman, 'Regulation of Australian Superannuation' (2003) 36 *The Australian Economic Review* 118, 122.
[12] Ibid.
[13] The Australian Taxation Office is responsible for the supervision of the smaller self-managed superannuation funds.

reviews of the industry added further impetus to these changes.[14] Treasury published an Issues Paper in 2001[15] canvassing options for reform leading to submissions to a Superannuation Working Group giving recommendations for reform. The report from the Superannuation Working Group set out the reform objective as being 'to ensure that the regulatory framework for the superannuation industry is robust and provides adequate levels of safety for the retirement savings of the community'.[16] Changes that occurred pursuant to these recommendations and subsequent consultation were the introduction of a universal licensing regime for trustees of regulated superannuation entities, a mandatory risk management framework for trustees and the funds under trusteeship and operating standards covering fitness and propriety, adequacy of resources and outsourcing.[17]

2007 saw some sweeping changes occur in relation to superannuation with the introduction of a raft of reforms designed to simplify the superannuation regime from 1 July 2007. However, these changes related mainly to the taxation of superannuation benefits and the treatment of contributions. The taxation treatment of the superannuation entities themselves is largely unchanged although these provisions have been rewritten and transferred from the *Income Tax Assessment Act 1936* to the *Income Tax Assessment Act 1997*. These changes, while described as 'the greatest reforms to superannuation in Australia's history',[18] did not significantly affect the regulatory provisions relating to superannuation in Australia.

**The current regulatory regime**

The regulatory regime that currently governs superannuation funds in Australia is extremely complicated. As discussed, additional layers of regulatory complexity have been added to the regime over time to add to this complexity. This makes compliance with the regime a complicated issue and has led to an increase in the costs of compliance. Increased compliance costs are a major concern to the industry because even small increases in the administrative costs of a superannuation fund can result in a dramatic reduction in the final balance of the fund. This has been illustrated in research by Bateman[19] showing that a 1 per cent increase in the assets administration cost over a 40 year period of retirement saving would result in a 20 per cent reduction in the final retirement benefit. This is a significant reduction in the final retirement balance which will ultimately affect the adequacy of the benefits to fund a lengthy retirement. This is a particular concern for those with low account balances to which

[14] Critical reviews of the superannuation industry came from the Senate Select Committee on Superannuation and Financial Services, Parliament of the Commonwealth of Australia, *Prudential Supervision and Consumer Protection for Superannuation, Banking and Financial Services, Second Report* (2001) and the Productivity Commission, *Review of the Superannuation Industry (Supervision) Act and Certain Other Superannuation Legislation*, Report no 18, (2002).

[15] Australian Treasury, *Options for Improving the Safety of Superannuation, Issues Paper* (2001).

[16] Superannuation Working Group, *Report of the Superannuation Working Group on Options for Improving the Safety of Superannuation* (2002), 10.

[17] Australian Prudential and Regulatory Authority, *A Recent History of Superannuation in Australia*, APRA Insight, Issue Two 2007.

[18] Commonwealth Treasury, Minister for Revenue and the Assistant Treasurer, 'Super Day – Simplified Superannuation Passes the Senate' (Media Release, 27 February 2007).

[19] Hazel Bateman, 'Retirement income strategy in Australia' (2002) 32 *Economic Analysis and Policy* 49.

higher administration costs have a particularly detrimental effect. This is often those with low workforce participation who are already disadvantaged by the operation of a private retirement system as they have not been able to accumulate assets for retirement to enable them to participate effectively in the superannuation system.

The provisions regulating superannuation funds are contained in SISA and the accompanying regulations. This paper will now explore some of the regulatory provisions governing the current regime to assess how they operate to create complexity within the system and whether this complexity is a necessary evil to adequately protect retirement savings and create an environment where Australians can feel secure that their superannuation monies will be available when the time comes to benefit from them.

**Fund Operation**

The most significant regulation that affects regulated superannuation funds is compliance with the sole purpose test contained in s62 SISA. These provisions require a fund to be maintained solely for one of the core purposes of the Act or for one of the core purposes and one or more of the ancillary purposes. The core purposes relate to the provisions of benefits for the members of funds upon reaching retirement or reaching the age of 65 or provision of benefits upon a member's death. Ancillary purposes are the provision of benefits on termination of employment, the provisions of benefits on cessation of work due to ill health, the provision of death benefits and the provision of other benefits as approved by the Regulator. Additional ancillary benefits that have been approved by APRA are the provision of benefits for the following purposes:

- where benefits are required or permitted under the payment and preservation standards of the *Superannuation Industry (Supervision) Regulations* (SISR) Pt 6
- when a member takes long service leave
- compassionate grounds
- for members of certain superannuation funds affected by the demutualisation of National Mutual Life Association of Australia Ltd and Colonial Mutual Life Assurance Society.

The oft-cited *Swiss Chalet case*[20] illustrates the operation of similar provisions of the *Occupational Superannuation Standards Act 1987* where a superannuation fund purchased, among other things, a Swiss chalet providing funds for the trust fund of one of the fund's members. More recently APRA found the sole purpose test to be breached when the directors of Firezone Protection Services Superannuation Fund used assets of the superannuation fund to secure a loan to provide working capital to the corporate trustee in its capacity as a trading company where the property over which the loan was secured was the major asset of a unit trust held by the superannuation fund.[21]

[20] *Case 43/95*.
[21] Super Review, 'Super fund directors disqualified: Breach of SIS Act prompts action' *Super Review* August 2007, 4.

Contributions which can be accepted by regulated superannuation funds are set out in SISR in reg 7.04. These regulations allow all contributions to be accepted for members under 65 with more restrictive contributions acceptance rules applying to older members. These rules protect the integrity of the superannuation system by reducing the ability to churn contributions through superannuation to take advantage of the concessional tax environment when a member is past the preservation age and should be starting to take benefits out of the system. Recent regulations prevent funds accepting member contributions where no TFN is quoted and apply restrictions on fund-capped contributions. The no TFN regulations allow contributions to be better tracked using the TFN which contributes to the integrity of the system. However, funds are finding that getting members to quote their TFN is not always easy. Restrictions on fund-capped contributions reduce churning of amounts in the concessionally taxed superannuation environment.

Trustees are under obligations to maintain minimum benefits for the benefit of members. Additionally, trustees must ensure that these minimum benefits are maintained until such time as they are able to be cashed by the member or rolled over or transferred as benefits of the member under reg 5.08(1).

Trustees are required to determine the costs that apply to a member account from time to time. Investment returns also need to be determined periodically. Costs and investment returns are required to be distributed in a fair and reasonable manner among all members. Members with small account balances are further protected by provisions preventing administration costs exceeding investment earnings.

Assignment of member's benefits and charges on fund assets will not be allowed unless such assignment and charges are permitted by SIS legislation. Limited charges are allowed under SISR with strict rules in place to manage any associated risk.

Amendments to the governing rules of a superannuation fund will not be allowed where such amendment will have a detrimental effect on member's accrued benefits. However, there are situations in which these rules will not apply where such changes are made pursuant to other legislation, are consented to by the member or the Regulator or where the changes are rectifying mistakes that have been made.

There are a number of rules relating to preservation of benefits set out in the SISR. These rules require trustees to determine which category of benefits a member's benefits belong to and then preserve the benefits accordingly. The categorisation of benefits is only required in relation to pre-July 1999 non-preserved benefits as all contributions and earnings are preserved under the system that was introduced from 1 July 1999.

Most benefits are only able to be accessed once a condition of release specified in SISR Sch 1 is satisfied. The major conditions of release are:

- retirement
- death
- permanent incapacity
- severe financial hardship
- attaining age 65
- attaining preservation age.

Rules relating to portability of benefits are contained in SISR Div 6.4 and 6.5. These rules relate to the roll-over or transfer of member benefits. Generally, for a roll-over to occur the member must give consent or the receiving fund must consent. Portability of benefits has taken on increased importance since 1 July 2004 with members able to request roll-over or transfer of benefits to another fund of the member's choice. Such a roll-over or transfer must occur within the rules contained in Div 6.5. A standard portability form has been introduced from 1 July 2007 which includes standard proof of identity requirements. The standard portability form only applies to requests to transfer the whole amount of a member's benefits. Requests for partial transfer of member benefits may still differ from fund to fund.

Regulations specifying how member benefits are to be paid are contained in SISR Div 6.2. Member benefits can be cashed, rolled over or transferred:

- in accordance with the rules contained in SISR Div 6.3, 6.4 or 6.5, or
- in accordance with the rules contained in SISR Pt 7A where the superannuation interests are subject to a payments split, or
- in accordance with the Family Law (Superannuation) Regulations 2001 reg 14G or 14N where the trustee pays, creates, transfers or rolls over a superannuation interest in satisfaction of a non-member spouse interest on marriage breakdown.

One of the most important discretions to be exercised by a trustee is in relation to the payment of death benefits to the beneficiaries or the estate of a deceased member. Members are able to make a non-binding death nomination to assist the trustee in exercising this discretion. However, the trustee is still able to exercise their discretion in light of all available circumstances at the time of death. Some funds may allow members to make a binding death nomination which requires the trustee to pay the member benefits to those nominated. Such a notice will only be binding on the trustee if stringent conditions are met.

Trustees are also under subject to regulations governing the provision of information to members. These regulations are largely contained in the Corporations Act and Corporations Regulations although SISR still contains some residual disclosure provisions. Dealing with member inquiries is dealt with in s101 SISA requiring trustees to take reasonable steps to ensure that there are arrangements in place to allow members to make inquiries or complaints where required.

There are a number of reporting requirements imposed on trustees under the SIS legislation in including reporting of:

- annual and periodic returns
- lodgement of auditor's reports
- significant adverse events
- change in fund status, and
- any other information requested by the Regulator.

Additional reporting requirements arise under the Superannuation Reporting Standards[22] which require reporting by registrable superannuation entities information in relation to their financial performance, financial position, directly held investments, derivative financial instruments, exposure concentrations, transaction with related parties, profile of fund membership and of the entity, and a trustee statement. Failure to comply with the reporting standards may lead to a fine of up to 50 penalty units as breach of a strict liability provision. A breach may also lead to issuance of an infringement notice by APRA. APRA may impose an administrative penalty in lieu of an offence. Reporting is required in electronic form using the Direct to APRA (D2A) software.

Strict financial management standards apply[23] covering the circumstances in which a fund is considered to be in an unsatisfactory financial position and the requirement for maintaining and monitoring the solvency of a fund. If a fund is considered to be in an unsatisfactory financial position the auditor or actuary is obliged to report the situation to the trustee. The trustee is then required to take remedial action. The solvency of a fund will be determined differently depending on whether the fund is a defined benefit fund or an accumulation fund.

Additional administrative obligations are also set out in SISA relating to appropriate maintenance and retention of records relating to the fund, seeking information from an investment manager so as to determine the investment manager's capability and appointing investment managers. Failure to meet the obligations in relation to correct record-keeping is a strict liability offence. Where such failure occurs with intention to deceive, mislead or provide false and misleading information this will constitute a criminal offence.

Payments to a current or former employer-sponsor are strictly governed and subject to a number of conditions. However, these conditions are subject to the discretion of APRA and can be waived. In addition to the conditions imposed by SISA general trust law provisions may apply. Case law precedents have indicated a number of issues with return of surpluses being ruled invalid. Therefore trustees need to be wary when considering a return of surplus to standard employer-sponsors.

A trustee is under a number of obligations concerning compliance with the superannuation splitting provisions allowed under the Family Law Act 1975 PtVIIIB. There are obligations in relation to the provision of information about the interests that are subject to a split. Trustees have a number of options available to them under SISR Div 7A.1A and Div 7A.2 clarifying different situations that occur under the superannuation splitting provisions. SISR Div 7A.3 further outlines the obligations for non-member spouse entitlements and SISR Div 7A.4 clarifies the creation of new interest for the non-member spouse. While these provisions allow greater equity in the treatment of assets accumulated privately with assets accumulated within the superannuation environment for separating couples they add further work to the already onerous requirements on superannuation funds.

[22] These powers have been determined by APRA under the *Financial Sector (Collection of Data) Act 2001*.
[23] *Superannuation Industry (Supervision) Regulations* reg 9.01 to 9.45.

Unclaimed superannuation benefits and lost members are a continuing problem within the Australian superannuation system. In fact, there is $11.9 billion in lost superannuation accounts.[24] Thus, stringent regulations are in place to direct trustees to deal with unclaimed money and lost members.

The regulations governing fund operation are substantial and can be onerous to comply with. In particular, regulations involving the reporting requirements involve the collection of substantial data which, in some cases, appears not to be utilised in any meaningful way. These regulations could be eased significantly without having any real effect on the actual operation of superannuation funds. This may go some way towards reducing the costs of compliance without any subsequent reduction in the overall safety of superannuation savings.

**Pension Standards**

Minimum standards are in place for complying income streams. Compliance with these minimum standards must occur to enable taxation as a superannuation stream benefit. The minimum standards are contained in SISR reg 1.05(11A) and 1.06(9A). Minimum payments amounts are also specified in Schedule 7.

**Investment Rules**

There are four overriding principles which dictate the investment activities of a fund.[25] The trustee must keep these principles in mind at all times. They are the sole purpose test, the fund's investment strategy, the arm's length rule and the general trustee covenants. In addition to keeping these broad principles in mind the trustee must also abide by the specific regulations dealing with particular investments and investment controls. Regulations dictate the elements to be considered when formulating an investment strategy and when reviewing the fund's investment strategy. A deeming provision exists to deem the governing rules of an entity to contain a covenant requiring the trustee to formulate and give effect to an investment strategy in identical terms to those set out in the regulations. Non-compliance with such a covenant may give rise to a civil liability action where the non-compliance is not reckless or intentional. However, acts of recklessness or intentional non-compliance will give rise to an offence punishable by a fine. Other more general investment controls also exist in SISA as well as specific guidelines issued by the Regulator in relation to particular investments.

As a general rule superannuation funds are prohibited from borrowing. Superannuation funds are only able to borrow money in limited circumstances on a short-term basis. A limited exception to the general rule that prohibits borrowing by superannuation funds exists for investments in instalment warrants. Limitations also apply to the lending of money or financial assistance to fund members or relatives of fund members.

Restrictions apply to acquisition of members assets with acquisitions allowed only in limited circumstances generally requiring that the transaction occur at market value.

[24] Minister for Superannuation and Corporate Law, 'Labor To Act on Lost Super' (Press Release, 20 December 2007).
[25] CCH Australia Limited, *Australian Master Superannuation Guide 11th edition* (2008) 128.

Related to these restrictions are those requiring that transactions occur at arm's length or on terms and conditions that would apply if the transaction was at arm's length. These restrictions operate to prevent misuse of fund assets by the conduct of round-robin arrangements with members and others who are related to the fund. While this has particular application with smaller funds where all fund members are related it also prevents the trustees of larger public funds from engaging in non-arm's length transactions that may not be in the best interests of all members of the fund.

Stringent restrictions are placed on investment in in-house assets[26] imposing a maximum limit on investments with a requirement that where this maximum limit is breached a written plan must be entered into to facilitate disposal of excess in-house assets and no further acquisitions of in-house assets will be allowed. These restrictions also prohibit a superannuation fund from entering into any scheme that would avoid the application of the in-house asset rules.

It is prohibited to offer inducements to employers, or in fact, to refuse to offer goods and services to employers, in return for employers arranging for employees to be members of the fund. These provisions are particularly important given that employees can choose which fund their superannuation contributions are paid into and may be easily persuaded by their employer to choose a particular fund when they are looking for guidance as to which fund to choose.

The relatively light level of regulation surrounding the investments that can be made in superannuation belie the importance of this element of superannuation savings. The returns from superannuation funds are the biggest factor affecting the final balance of the funds and yet there are relatively few rules dictating conduct in this area. Perhaps, if further changes are to be made in the regulation of superannuation additional guidelines as to investment should be considered.

**Registrable Superannuation Entity Licensing and Registration**

Major reforms to the landscape of superannuation regulation occurred in 2004 with the introduction of a licensing regime for trustees and the requirement for registration of registrable superannuation entities (RSE). Subject to these provisions corporate trustees and groups of individual trustees are required to obtain an RSE licence. A risk management strategy is required to fulfil the requirements of licensing. These reforms also require registration of a registrable superannuation entity. While registration is free preparation of a risk management plan is required prior to registration. Apart from the actual cost of the licences required it is the preparation of this risk management strategy and the risk management plans that has contributed significantly to the costs of implementation of the licensing regime.[27] The Association of Superannuation Funds Australia estimates the cost of implementing the licensing regime at $35 - $70 million across the industry.[28] The introduction of the licensing regime has seen some rationalisation in the superannuation industry with many funds assessing the cost of licensing to be too high and winding up and transferring their benefits into larger funds. This has resulted in increased

[26] Sections 69 to 85 *Superannuation Industry (Supervision) Act 1993*.
[27] Zilla Efrat, 'Put to the Test' (August 2005) *SuperFunds* 41, 42.
[28] Association of Superannuation Funds of Australia Limited, ASFA Submission to Taskforce on Reducing the Regulatory Burden on Business (December 2005), 2.

professionalism in the industry. However, it does reduce the number of funds across which the APRA levies can be distributed and may result in higher levies on the remaining funds. The ongoing monitoring of the risk management plan will also contribute to higher ongoing compliance costs as assessment of the risk management plan is being undertaken in conjunction with the fund audit. This has contributed to a 50% increase in audit fees[29] which will again impact on the end balance of the fund's members.

**Conclusion**

There are many layers of complexity that need to be negotiated in the administration of superannuation funds. The regulations put in place by SISA and the associated regulations are many and varied and cover a wide spectrum of the work completed by funds. There is some debate as to whether this work is necessary to adequately safeguard the retirement income of the Australian population. Many of the provisions in place represent good practice and may be put in place by trustees regardless of a legislative compulsion to do so. Indeed, many of the provisions simply legislate what would appear to be common sense. However, there is no doubt that many of the regulatory requirements could be better done without. On the balance, while there are legitimate concerns about the compliance costs it appears that the heavy level of regulation is required to provide some level of confidence within the public that their retirement savings are adequately protected. The consequent increase in compliance costs is a valid industry concern. However, the current economies of scale that are being achieved within the industry following the recent consolidations may contain those costs so that they have less of an effect on the long term outcome of superannuation savings.

[29] Efrat, above n 26, 42.

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