
Switzerland and Europe: Close Neighbours or Distant Relatives?

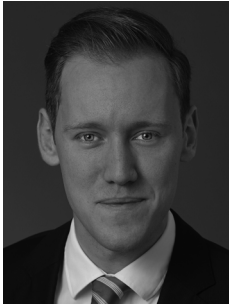


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Psychische Distanz, Globale Wettbewerbsfähigkeit, Handel, Schweiz

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Diese Studie untersucht die psychische Distanz von Schweizer Managern und ihren Handelspartnern. Unsere Daten zeigen, dass die Schweiz und ihre Handelspartner im Ausland sich gegenseitig unterschiedlich weit entfernt wahrnehmen. Diese wahrgenommene psychische Distanz hat einen Einfluss auf ihren Handel. Der Artikel schliesst mit einer Diskussion, wie Schweizer multinationale Unternehmen ihre relative Distanzwahrnehmung nutzen können, indem sie sich als europäischer Hub aufstellen.



This study investigates the distance perceptions of Swiss managers and their European trading partners. Our data demonstrate that perceived distances or similarities between Switzerland and its trading partners often can vary and that these perceived distances influence Swiss trade. The article ends with a discussion of how Swiss multinationals might leverage their relative distances by acting as European hubs.

1. Introduction

International trade has become a keystone for many developed economies (Sachs *et al.* 1995), but trade is not without barriers. Economists have identified a number of factors that either facilitate or inhibit trade. Examples would include administrative barriers such as tariffs as well as the costs that are due to economic, geographic and cultural distances. Beyond these objective factors, recent literature has also hinted that managers perceived distances (or perceived similarities) might significantly influence the likelihood of engaging in international trade or deciding to make international investments. For small and open economies such as that of Switzerland, understanding these factors becomes very important due to their stronger dependence on foreign markets.

In this article, we examine the perceived distances of Switzerland and its two adjacent economies, Germany and France. Switzerland is one of the most integrated economies in the world, which is evident in its high export quota (*Federal Statistics Office* 2014). In addition, Switzerland's integration in global-exchange streams is evident not only in its importance as a financial center but also its impressive number of regional headquarters for both multinational corporations and international organisations (*Federal Department of Foreign Affairs* 2014). This indicates in reverse frequent cross-border interactions, thus rendering the Swiss case as a particularly interesting case study. In a second step we relate

these distances to Swiss trade relations to see whether perceived distances actually affect Switzerland's international trade.

2. Psychic Distance Defined

The role of distance in international business and trade has received a considerable amount of attention over the last six decades. One of the starting premises of this research has been that distance has a cost. Thus, everything else remaining constant, trade will be a negative function of the distance-cost incurred by the exporter (or importer) of a specific product. Although earlier studies primarily focused on geographic distances (and the associated transport costs), more recent attempts enriched these discussions by including cultural distance (the cost of reinterpreting or reformulating ones offerings to account for various cultural preferences and languages), administrative distances (the costs of dealing with other jurisdictions), and economic distances (the costs of adjusting to various levels of development) (*Ghemawat 2001, Berry et al. 2010*). In addition, management scholars have noted that the distance that determines international-trade decisions is driven not only by objective and easily measurable determinants such as Gross Domestic Product (GDP) or geographic distance but also by the managerial perception of these distances (*Beckerman 1956, Johanson & Wiedersheim-Paul 1975, Johanson & Vahlne 1977*). In these studies psychic distance has been defined as “factors preventing or disturbing the flow of information between potential and actual suppliers and customer” (*Vahlne & Wiedersheim-Paul 1973*).

In other words, psychic distance signifies the perceived (rather than the objective) distance of managers towards a foreign country. Research proposed that the perceived psychic distance might govern international business interactions to a larger extent than objective external ones do (*Harzing 2004*). As Harzing argues, it is ultimately managers, who rely on their own perceptions of the external environment, who make international investment and trade decisions. This can be exemplified if we think of a firm in Northern Germany that is probably more likely to source in Denmark than in Poland, for instance, even though, by some objective measures, we should see no significant trade differences.

3. Swiss Distance Perceptions

In our study we use the European subsample of a dataset collected by Håkanson and Ambos (2010). They originally asked 1,608 managers in the twenty-five largest economies¹ to rate on a scale from 0 to 100 how close or distant they perceive the other twenty four largest economies. The participants were asked to rate the distance to their home country with 0. In addition, they were asked to rate the country that they perceived as farthest away with the score of 100. Using this approach ensured that the results are anchored and comparable (*Håkanson & Ambos 2010*).

1 These data were collected between 2003 and 2008. The twenty five economies, the largest of 2001, are Argentina, Australia, Austria, Belgium, Brazil, Canada, China, Denmark, France, Germany, India, Italy, Japan, Mexico, Netherlands, Norway, Poland, Russia, South Korea, Spain, Sweden, Switzerland, Turkey, United Kingdom and the USA.

The subsample used in this paper focuses on the perception only of Swiss managers² and their European neighbours. The results for Switzerland are displayed in *Figure 1*. We used the map of Europe (in grey) and repositioned countries according to the psychic distance that Swiss managers perceive towards those countries.

The other German speaking countries, Germany and Austria, remain in their geographical positions, while Swiss managers feel slightly closer to Germany at a distance of 9 than to Austria at 10. More surprising are the positions of the other two major economies that border Switzerland. Italy is seen at 19, which locates it somewhere in Libya. The same applies for France that is seen at a distance of 16, which locates it in the Bay of Biscay. Spain is moving further south somewhere near the Canary Islands with a distance of 29, while the United Kingdom, at 23, makes its way further in the North Sea. Interestingly enough, it is joined there by the two continental economies of the Netherlands at 19 and Belgium at 24. Denmark, at 25 joins its Scandinavian neighbours Sweden, at 25 and Norway at 28. Also interesting are the positions of Poland at 50 and Turkey at 57. Although both countries are in geographical terms not that far away from Switzerland, Swiss managers perceive both as remote.



Figure 1: Psychic Distance from Switzerland towards other major European economies

² For the Swiss data, managers living in German-speaking Switzerland were asked. Nevertheless, these managers do not necessarily speak German as their mother tongue.

3.1 Comparing Switzerland to Germany and France

To find out if distance perceptions of Swiss managers are in line with those of managers from other countries, we show the distance perceptions of the two major European economies: France and Germany. Contrasting Switzerland with its two largest neighbours is potentially interesting. France and Germany not only constitute Europe’s two largest economies (*Eurostat 2015*) but also share common languages with Switzerland. *Figure 2.* and *3.* provide a comparable analysis as the one that we provide for Switzerland in *Figure 1.*

Evaluating the findings in *Figure 2.*, we find that French managers see Switzerland at a distance of 18, which is roughly equal to the Swiss distance towards France, which is 16. One finding that is striking is that French managers perceive the Latin part of Europe as closer to France than Swiss managers perceive it as close to Switzerland. This applies for Spain with a distance of 16 (versus Switzerland at 29), Italy with a distance of 16 (versus Switzerland at 19) and Belgium with a distance of 9 (versus Switzerland at 24). A second noticeable finding is that French managers perceive the Germanic³ speaking parts of Europe as farther away than Switzerland. Even though, many countries are in geographic terms

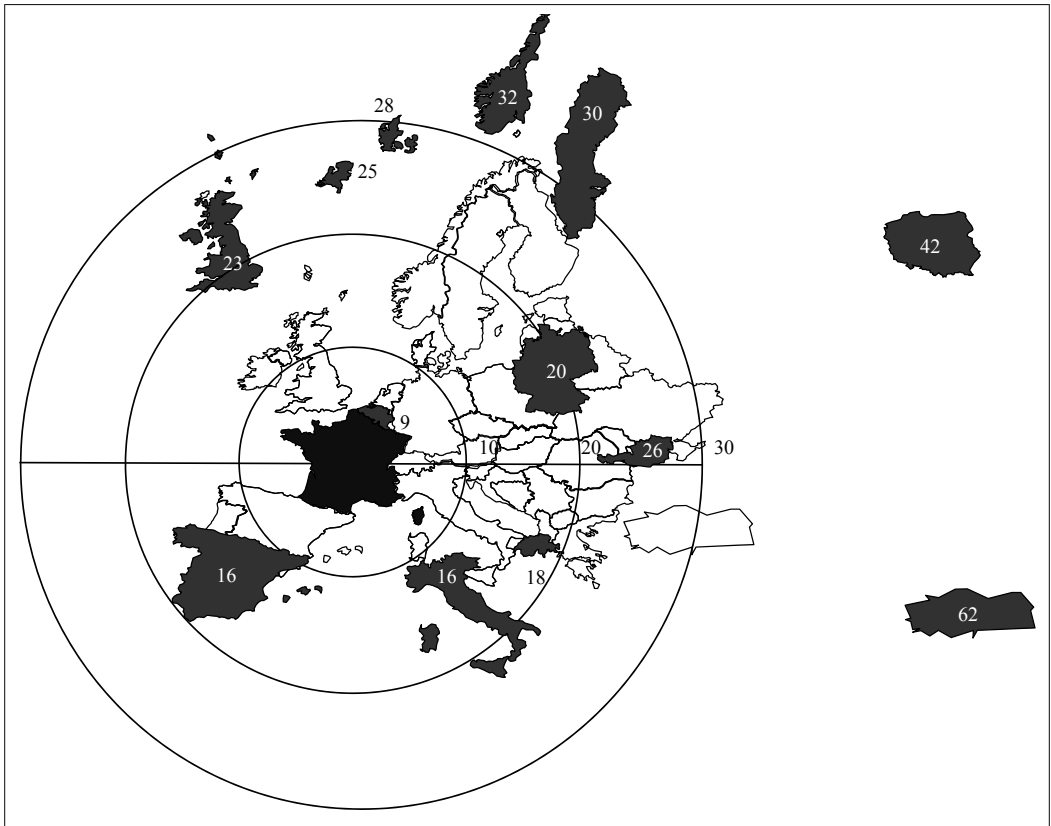


Figure 2: Psychic Distance from France towards other major European economies

3 Under Germanic we cluster Germany, the United Kingdom, the Netherlands, Austria, Denmark, Norway and Sweden.

closer to France than to Switzerland. This finding applies to the Netherlands at a distance of 25 (versus Switzerland at 19), Denmark at 28 (versus Switzerland at 25), Norway at 28 (versus Switzerland at 32), Sweden at 30 (versus Switzerland at 25) and Austria at 26 (versus Switzerland at 10). In addition, even the biggest trading partner (*Insee* 2014) and closest political partner, Germany (*Goldsborough* 1976), is seen at a distance of only 20 (versus Switzerland at 9).

For Germany, the data are as follows. German managers perceive the “Germanic” and Slavic (Poland) speaking areas of Europe as closer to themselves than Swiss managers do. This applies for the Netherlands at 13 (versus Switzerland at 19), the United Kingdom at 19 (versus Switzerland at 23), Denmark at 16 (versus Switzerland at 25), Norway at 22 (versus Switzerland at 28), Sweden at 20 (versus Switzerland at 25), Poland at 37 (versus Switzerland at 50) and Austria at 9 (versus Switzerland at 10). A second finding is, comparable to the French survey: German managers perceive France at a distance of 22, substantially farther away from themselves than Swiss managers, who perceive France at a distance of only 16.

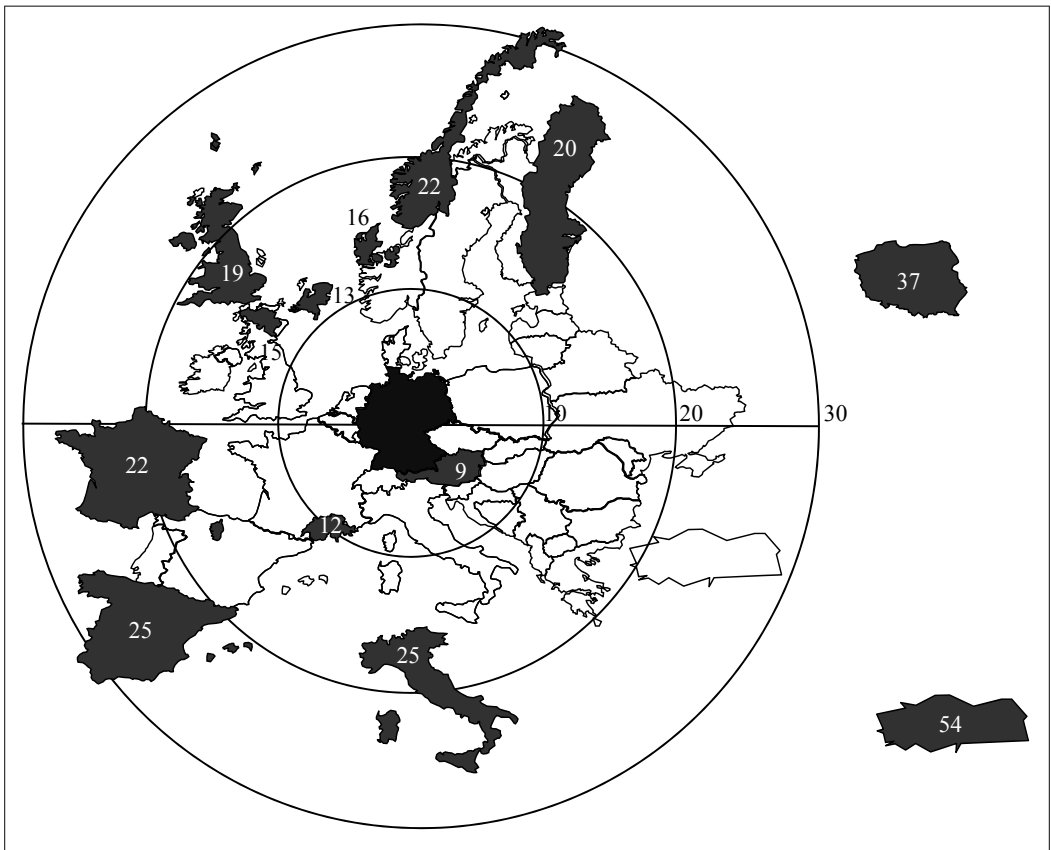


Figure 3. Psychic Distance from Germany towards other major European economies

Comparing the distance perceptions of Swiss, French and German managers, we note some interesting findings. French managers perceive the Latin countries of Europe as much closer than German or Swiss managers perceive the same region. In contrast, German managers perceive the Germanic and Slavic speaking countries as close. The German perception of these regions is substantially closer than the respective French or Swiss perception. Another interesting finding is that both French and German managers perceive Switzerland as close but perceive each other as quite distant. Swiss managers, however, perceive both France and Germany as close.

3.2 How Other Countries See Switzerland

In the preceding argument, we focused on the perceived psychic distance of Swiss managers towards other countries. In this section, we analyse and discuss the perceived psychic distance of foreign managers towards Switzerland. Although the geographic distance between Zurich and London is by definition equal to the distance between London and Zurich, this does not necessarily hold for psychic distance perceptions (*Shenkar 2001, Brewer 2007*).

Due to the fact that psychic distance is shaped by subjective perceptions of managers (*Harzing 2004*), the distance of France as perceived by a Swiss manager can differ from the distance of Switzerland as perceived by a French manager. As a consequence, psychic distance can be asymmetric. Because international trade decisions work both ways, it is also important to know how close or far foreign managers perceive Switzerland. In a second step, therefore, we asked managers in the major European economies how close or far they perceive Switzerland. The results can be seen in *Figure 4*. In addition, to allow comparisons, *Figure 4* shows the scores of Swiss managers. In grey are the perceived psychic distances of foreign countries from Switzerland according to Swiss managers. In black are the perceived psychic distances of Switzerland from their own countries according to managers in foreign countries. Again Germans and Austrians state that they perceive Switzerland as closest (at distances of 12 and 11 respectively). Nevertheless, these managers perceive Switzerland slightly more distant than their Swiss counterparts do.

For Italy, Spain, France, Denmark, Norway and Sweden, the distance towards Switzerland and the distance from Switzerland do not vary too much. But note that managers in all of these countries perceive Switzerland as farther away than the Swiss do. Managers in the United Kingdom, the Netherlands and Belgium perceive Switzerland as substantially farther away. Most remarkable is this gap in own and foreign perception for Poland and Turkey. Managers in both countries perceive Switzerland as substantially closer than the Swiss managers perceive these countries.

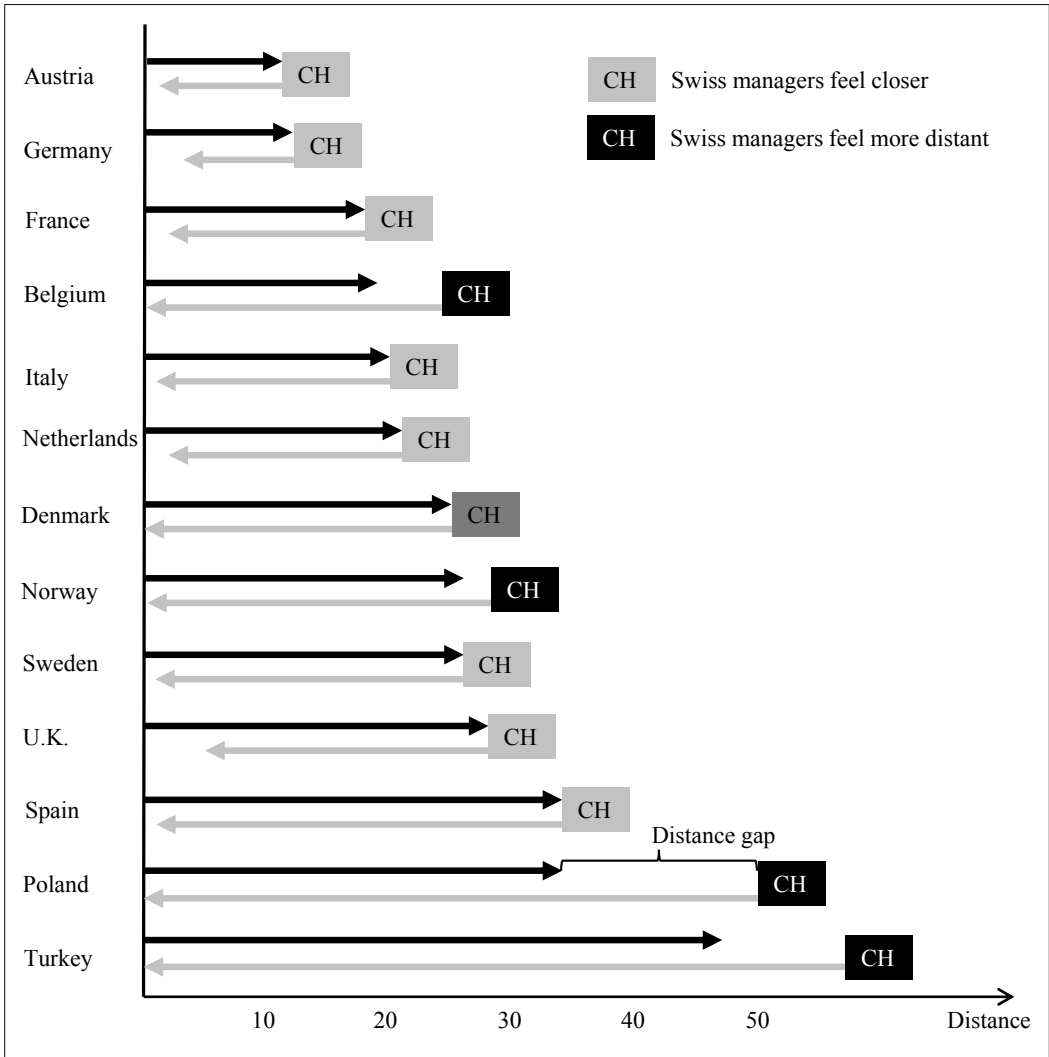


Figure 4. Distance from Switzerland (grey); distance towards Switzerland (black)

4. What Are the Causes of Asymmetric Perceptions?

The asymmetry of distance could pose a risk for international trade and relations. Managers might either overestimate or underestimate the objective distance towards foreign countries. Worse, two firms (or their respective managers) might interact with each other but rely on different assumptions about how close or how far they are to each other. A German manager who trades with the German-speaking part of Switzerland might believe that Switzerland and Germany are close. But the Swiss manager might have a farther distance perception with respect to the differences in culture and administrative business practices. The resulting asymmetry can cause problems for the ease of business through misunderstandings.

The literature provides several explanations why two parties have asymmetric views of each other. One that seems to be particularly suited to explain the Swiss case, is grounded in the work on the "mere-exposure" effects (*Schuster 2013*). According to the mere-exposure effect (*Zajonc 1968*), people perceive familiar things as being close. For countries the exposure effect can have different reasons. For one immigrants from a foreign country can explain closer distance perceptions (*Pettigrew & Tropp 2006*). This can contribute to the finding that Swiss managers perceive most European countries as closer than vice-versa. Switzerland as a country with a relative large share of European immigrants (*Federal Statistics Office 2015A*) has a relatively large exposure to people from different countries. Other European countries have absolute and relatively only a marginal number of Swiss immigrants (*Federal Statistics Office 2015B*). A second mechanism that fosters the exposure effect is the relative exposure to the foreign culture via "media spillovers" (*Palich & Gomez-Mejara 1999*). Switzerland, as a relatively small country, relies to a relatively large extent on the mass media of its larger neighbours—that is, those that use languages that are spoken in Switzerland (such as France, Italy, Germany and Austria). In reverse large countries such as Germany, though, have normally such a large number of domestic media services that foreign services are not very widespread. This effect can again contribute to the finding that Swiss managers perceive their European neighbours as closer than the other European managers do.

The same reasoning can explain the asymmetry in the perceived distance among Switzerland, France and Germany. France and Germany are both relatively large countries with a relatively large media sector exposure to German mass media in France and French ones in Germany, therefore, is relatively limited. In contrast, Switzerland has relatively few mass media outlets but shares common languages with both France and Germany. Therefore, Swiss managers have a relatively heavy exposure to the "media-spillover" of the respective other country (*Palich & Gomez-Mejara 1999*). Reinforcing this situation is the fact that Swiss managers can experience cultural productions from other countries in their own languages. Research has shown that a shared mother tongue is one of the main factors that can reduce distance perceptions in an international context, because it substantially reduces uncertainty about some foreign countries (*Evans & Mavondo 2002*).

The second argument that can explain the asymmetry in the Franco-German-Swiss distance perceptions refers to the number of immigrants. Although the numbers of Swiss immigrants in France (0.3% of population) and Germany (0.1% of population) are quite limited (*Eurostat 2014, Federal Statistical Office 2015B*), the opposite is true within Switzerland. Switzerland has many immigrants from both Germany (3.6% of the population) and France (1.4% of the population) (*Eurostat 2014, Federal Statistical Office 2015A*). They increase the exposure of Swiss managers to these countries (*Zajonc 1968*).

5. What are the Implications for Swiss Trade?

We have already argued that managers are the ones who ultimately make decisions on international trade and that these managers have their own personal biases and particular uncertainties that are not necessarily only driven by objective measurable environments. It would be logical for Switzerland to trade more with countries that Swiss managers find familiar. To emphasise this, we examined the trading statistics of Switzerland for the year 2013 (*Swiss Custom Administration 2014*). In particular we compared, in a first step, Swiss exports with the matching psychic distance scores. The results are displayed in *Fig-*

ure 5. Exports have been adjusted according to the size of target economies, by dividing the exports by the GDPs of target countries (*World Bank 2014*). All the countries that we compared are members of the European Union and, except for the United Kingdom, members of the Eurozone. Moreover, all are geographically close enough for us to assume that transportation costs should not play an important role.

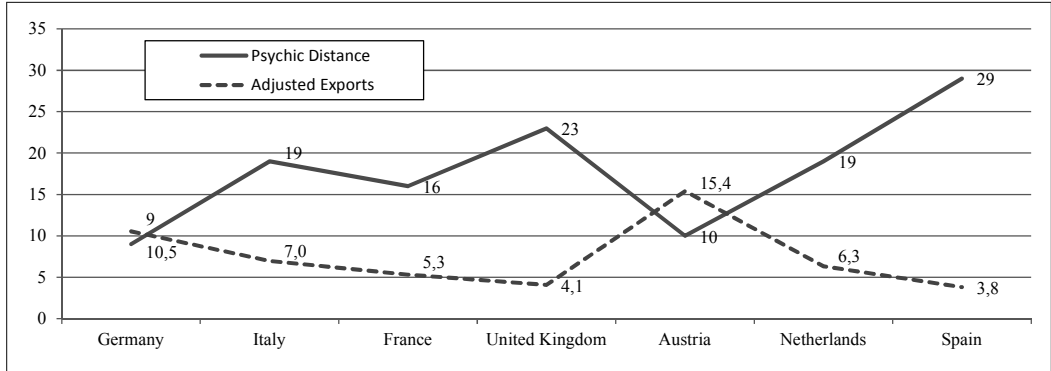


Figure 5: Comparison of adjusted export figures and psychic distance score

Relying on these assumptions, the result should be that the adjusted exports (indicated by the dotted line) have the same value for all target countries. As the graph indicates, though, this is not the case. In contrast, we find a strong negative correlation between adjusted exports and the respective psychic distance scores. Swiss firms exported relatively few goods and services to the psychically distant Spain. While in relative terms the most exports have gone to the psychically close Germany and Austria. These data suggest that psychic distance seems to have a visible impact on the international trade decisions of Swiss firms.

Comparable to our analysis above we can visualise the impact of psychic distance on international trade by comparing the psychic distance scores of foreign countries towards Switzerland with the, by GDP of the origination country adjusted values, of Swiss imports into Switzerland (*Swiss Custom Administration 2014*). The result is displayed in Figure 6.

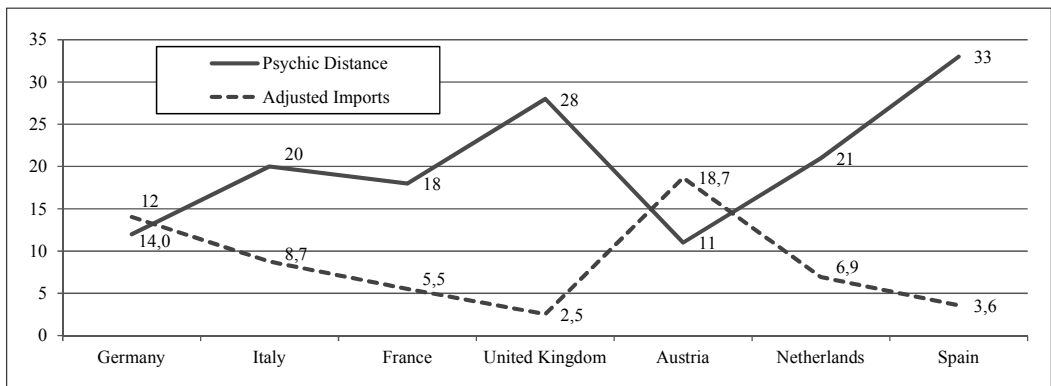


Figure 6: Comparison of adjusted import figures and the psychic distance score

The resulting figures are comparable to those for exports. If the manager of a foreign country perceives Switzerland as quite far away, then imports of Switzerland are quite low. This is e.g. very prevalent in trade relations between Switzerland and the United Kingdom or Spain. In contrast, the two countries with the lowest psychic distance scores (Austria and Germany) are also the countries from which Switzerland sources, in relative terms, most of its imports.

The findings show that the psychic distance perceptions of managers co-vary (inversely) with adjusted⁴ international trade statistics. The fact that we seemingly export (and import) more from countries that managers perceive as psychologically close as opposed to countries that managers perceive as psychologically more distant (irrespective of the objective costs of trading⁵ with those countries) has interesting implications for management. These can be drawn from a possible over or underestimation of the true cost of trade.

5.1 Overestimation of distance

The first case is a situation where the manager perceives a country as more distant than is justifiable by objective distance measures. Although it is prudent to integrate existing cultural, geographic, administrative and economic differences into the assessment of international business activities, a manager should be reflective that his personal distance perception does not differ significantly from objective distance. One particular example to explicate this point can be made with the Swiss perception of Poland. The Swiss managers in the study see Poland at a distance of 50, which is notable much higher than the distance for other Central European countries such as Germany or Austria (at 9 and 10 respectively). The distance of fifty to Poland is comparable to the Swiss distance towards Australia (at 56)⁶. If we take Poland's underlying cultural, administrative, geographic and economic fundamentals into consideration as a fairly stable and growing country (*Eurostat* 2015), it seems to be a fair assessment that the Swiss distance perception of Poland cannot be fully explained by objective distances. Another good example is the case of Turkey. Swiss managers see Turkey at a distance of 57, although if we consider the last two decades of development in Turkey with administrative reforms and quite high growth numbers it offers good conditions for trade and investment activity (*World Bank* 2015). Consequently, overestimating distance can lead Swiss firms to forego potentially profitable trade and investment opportunities.

5.2 Underestimation of distance

The second case is a scenario where the manager underestimates the distance towards a foreign country. A good example would be the manager of a German or Austrian firm, who intends to do business in the German speaking part of Switzerland. Due to the common language, she could assume that cultural, geographical, administrative and economic practises of Germany are similar to those of Switzerland. Nevertheless, this assumption of similarity can create problems. There are subtle differences, after all, in business practices of the two countries. Thus, managers could face the problem that investments and trade relations develop not optimal due these unexpected differences.

4 Swiss exports adjusted by GDP of country of destination. Swiss imports adjusted by country of origin.

5 Costs of trading on this aggregated level can only approximate the actual costs.

6 Data for non-European countries originate from Håkanson and Ambos, 2010.

5.3 Opportunities through Swissness in an asymmetrical world

The asymmetry of psychic distance can present a large opportunity, however, for Swiss firms. We found that Swiss managers perceive France and Germany as substantially closer than the two economies perceive each other. Swiss firms could leverage this reduced distance perception by acting as a hub between these two largest European markets. Through these function Swiss firms could develop a key function in the European economy. The linking effect between Germany and France is in addition fortified because these two countries build, in some way, the key pieces in the whole continental European economic interaction. France perceives the Latin countries of Europe very close, and Germany the Germanic and Slavic speaking countries. Bridging these two key markets, therefore, could generate substantial opportunities for Swiss firms. Swiss firms could take the role that Austrian firms have in regard to the Central-Eastern markets. Austrian firms leverage, in this context, their understanding of the Central-Eastern European markets to function as a hub.

6. Conclusion

In this article, we have highlighted the importance of international trade for countries. Nevertheless, barriers can constrain trade. We have discussed the concept of distance, therefore, as a barrier to Swiss trade. We started by introducing the idea that distance in international trade and investment decisions includes more than merely objective geographic or economic distances. We introduced the concept of psychic distance, therefore, which incorporates the subjective perceptions of managers.

Consequently, we described the distance perceptions of Swiss managers towards other major European economies. To get a differentiated view, we compared Swiss distance perceptions with the distance perceptions of managers from its two neighbouring economies France and Germany. Following, we introduced the idea that psychic distance, unlike geographic distance, can be asymmetric, which explains the varying distance perceptions of other European countries towards Switzerland. In general, we found that Swiss managers feel closer to other countries than managers from these countries feel towards Switzerland. Exposure effects might be one possible explanation of these findings. A relatively open and small economy as Switzerland has more “media-spillover” from foreign countries and a relatively high number of European immigrants. This exposure makes Swiss managers more familiar with other European countries than managers in those countries are with Switzerland.

To investigate the economic significance of psychic distance, we correlated psychic distance scores with the imports and exports of Switzerland. The data showed a strong negative correlation between psychic distance and trade activity, which has implications for the international behaviour of Swiss firms. First, Swiss managers should be careful and reflected not to overestimate or underestimate distance. Otherwise, they can underestimate risks or forego lucrative business opportunities. Second, Swiss managers have the opportunity to function as a hub that links the two major European economies France and Germany, because the Swiss perceive both countries as closer to Switzerland than France and Germany perceive each other.

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