Value creation by small firm internationalization: a competence-based approach

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This study examines the relationship between the competencies of the small business owner and their interest in international activities. Based on a review of the literature and a quantitative empirical survey among 803 newly founded Austrian companies, the paper identifies the central explanatory variables of internationalization, thus contributing to a theoretically based conceptualization of this phenomenon. Previous conceptualizations of small firm internationalization are extended and specified. This reveals the necessity for a wider inclusion of utilized resources throughout the internationalization process. Moreover, the impact of the structure of social capital of a business owner on the decision to start international activities is examined. The findings elucidate differences between performance drivers with regard to the network, marketing and technology competence of the small business manager. The study repudiates the Uppsala Model in favour of the „born global hypothesis“.

social capital, networking capabilities, exporters, born global, international performance

Being involved in cross-border activities has been increasingly typical for small and medium-sized companies since end of the last century (Fan & Phan, 2007). Internationalization is assumed to be one of the most important sources of economic value creation and development in Europe. Major incentives and means have been implemented to foster, secure and accelerate the creation and the early growth of international new ventures – whatever their origin. However, despite years of experience, the problem of predicting potential growth and profits of future businesses remains highly uncertain (E. Autio, Sapienza, & Almeida, 2000). Actually, internationalization of born global companies seems to entail both high potential future profits and high uncertainty. A major question concerns the possibility to prove, at least partly, the future value of an opportunity before its realization. Recent research showed that international new ventures, those companies that enter foreign markets at inception, often suffer the two liabilities of newness and foreignness, which may increase the odds of their failure (Mudambi & Zahra, 2007).

This calls for a better understanding of the concept of internationalization competencies. This paper proposes to learn from successful international new ventures about the way they represent their opportunity early before its concretization so that both procedural and declarative basic knowledge may be identified.

A significant problem of small firm internationalization seems not to be so much a problem of lacking ideas or products but one of deficits in the resources and assets since international activity requires resources that newly founded firms may find it difficult to acquire. During the last two decades, International Entrepreneurship research has analysed the drivers for SMEs (in particular knowledge-intensive new firms) for international activities and how international new ventures can overcome hindrances such as the liabilities of newness and smallness. New business creation and growth are not autonomous, isolated processes but collective processes that involve the establishment and sustaining of a network of relationships between the new organization and other parties in its environment. A firm needs to interact with customers for and distributors of its outputs, and with the suppliers of inputs the firm requires, such as funds, labour, material resources and knowledge. A young firms’
relationships provide access to external resources which compensate for internal resource constraints.

The phenomenon of companies that commence international activities increasingly early in their existence has elucidated a clear shift in theory building in the field of International Management research. Recent empirical evidence suggests that the symbiosis of internationalization and social capital has the unique ability to impart growth and survival to companies (Arenius, 2002). Autio stated that the role of social capital in an international context could be discussed in terms of an entrepreneurial network that becomes a base for international growth of new ventures (Erkko Autio, 2006), suggesting a strong reciprocal relationship between this type of entrepreneurship and social capital.

Until now, researchers (Oviatt & McDougall, 2005) have found that the pattern of internationalization in technology-based industries differs from that of traditional companies concerning choice of markets and entry modes, which tend to become international in a slow and incremental manner. Although some empirical evidence for the internationalization of the wine business industry exists (Graves & Thomas, 2006), the question of the impact of social capital on the pattern of internationalization has not yet been analysed. Therefore, the primary purpose of this paper is to provide a detailed account of how internationalization was inspired, adopted and managed in companies in the Wine Business Industry, in an attempt to locate the domain and distinctiveness of social capital. The significance of focusing on social capital is due to its unique role as the single common factor in all the three areas of wine business, international new ventures and high-technology companies.

This article differs from other empirical work on international new ventures in three ways. Whereas previous studies in the business field focused on only particular aspects of internationalization (e.g. export, family business etc.), the author examines the internationalization process in its complex form. Besides, the author places internationalization in the context of the SMEs strategic management processes to locate the support and structure of the social capital. Third, the author extends the internationalization theory building by including the concept of competencies in an attempt to define the domain and distinctiveness of the concept of international new ventures.

By so doing, the author addresses several hitherto unexplored questions: Can social capital embedded in international relationships be leveraged for relationship benefits in a similar manner as in domestic contexts? In this context, the paper attempts to answer the following hitherto unexplored questions: Can competencies and capabilities of the entrepreneur embedded in international relationships be leveraged for relationship benefits in a similar manner as in domestic contexts? Under which conditions is management and network competence advantageous in an international context?

Accordingly to these research questions the author has structured the paper as follows: A literature review is first carried out, in which different views on internationalization are discussed. Thereafter follows a presentation of the conceptual framework, the research model and the sample and choice of variables. The section two the methodology and research design, section three the results and section four will provide concluding remarks.

II. CONCEPTUAL FRAMEWORK
Firms’ internationalization is a well-researched area. Earlier research is discussed here and categorized under different headings.

Internationalization is a complex process over time (Jones & Coviello, 2005). According to Oviatt & McDougall (2005), the phenomenon of early internationalization appeared towards the end of the last century (Oviatt & McDougall, 2005). International Entrepreneurship research occurs at many level of analysis (Barrutia & Echebarria, 2007) and therefore can be described as necessarily interdisciplinary and multi-level (Boojihawon, 2007).

The first level of analysis was the definition of the term international new ventures in order to distinguish exactly from firms with no international activities (Fan & Phan, 2007). Startup companies were the target group of the empirical survey – which requires a clear definition of the measurement concept for international new ventures (Knight, Madsen, & Servais, 2004).

A review of a decade of ‘born global’ firm internationalization observes that the literature remains fragmented with a comprehensive theoretical explanation (Knight et al., 1996; Oviatt & McDougall, 1997; Servais & Rasmussen, 2000) for SME internationalization (Rialp, Rialp, & Knight, 2005). The examination of the existing studies points to the need for a synthesis. Numerous theories have been presented to explain why start-up companies engage in international operations.

Four conceptual perspectives in the literature can be found which are of influence to the theory building in the research field of International Entrepreneurship.

As far as networks are discussed in the theory building process, two basic underlying theoretical perspectives on internationalization are seen as fundamental concepts for this article: on the one hand we find the Uppsala Internationalization Model and on the other hand the International-New-Venture Approach. The main premise behind the Uppsala internationalization model (J. V. Johanson, J.-E., 1990) is that the process of internationalization is gradual and evolutionary. Incremental learning at the firm level is the main factor explaining the firm’s internationalization. A firm increases its commitment to a market incrementally as it learns about the market. Thus, the Uppsala model describes the managerial goals of internationalization in terms of reducing risk and avoiding uncertainty. Nevertheless, the Uppsala internationalization model has been criticized for being too deterministic and unable to explain the “leapfrogging” activities of born-global firms identified in the international-new-venture literature (MacDougall & Oviatt, 1994). The Uppsala model was extended by the network theory of internationalization which emphasises the impact of business relationships upon the development and internationalization process of firms (J. V. Johanson, J.-E., 1990; J. V. Johanson, J., 1992).

There is empirical evidence to suggest that networks are important for born global firms (Coviello & Jones, 2004) because of their resource constraints (Coviello & Martin, 1999). Networks have been argued to contribute to the success of born global firms by helping to identify new market opportunities and contribute to building market knowledge ((Majocchi & Zucchella, 2003). However, only little attention has been drawn to the capability of small
business owners to exploit resources from social capital. Sapienza et al. held a similar view and stated that internationalization theories for new ventures including only two or three variables have limited predictive ability for growth or survival of the company (Sapienza, Autio, George, & Zahra, 2006) Research therefore suggests a broader conceptualization of internationalization which was adopted in this study and which confirms that internationalization is multi-dimensional and complex phenomenon. Extension of network has been discussed by Loane & Bell (2006), suggesting that international new ventures on the one hand rely on the existing network but on the other hand try to expand the network (Loane & Bell, 2006). Moreover, networking capability plays an important role because it enables identification and exploitation of market opportunities, facilitates the development of knowledge-intensive products and firm international market performance in the born global firm is discussed (Mort & Weerawardena, 2006).

The type of networks with impact on the internationalization process were analysed and the central role of home-based social networks were identified (Zhou, Wu, & Luo, 2007). This leads to the first proposition:

Proposition 1. International involvement is encouraged by the presence of home-based social networks.

As far as internationalization is concerned it is the entrepreneur who has the freedom to choose between different strategic orientations under the same environmental contingencies, which determine firm performance. It is also the entrepreneur who has to decide how to integrate resources from social capital during the internationalization process. In this context, the role of networks can be analysed from a strategic adaption perspective. Social capital is defined by its function. It is not a single entity, but a variety of different entities, with two elements in common: they all consist of some aspects of social structures, and they facilitate certain actions of actors – whether persons or corporate actors – within the structure. (Bruno, McQuarrie, & Torgrimson, 1992; Coviello, 2006). While network relationships have long been recognized to be indispensable for SMEs to achieve international growth (J. M. Johanson, L.-G., 1988) (Lu & Beamish, 2001), a particular focus on social networks has been limited to date (Ellis & Pecotich, 2001). There is evidence to suggest that networks are important for born global firms because of their resource constraints (Freeman, Edwards, & Schroder, 2006). However, the role of the decision maker and the firm’s characteristics in taking up opportunities for international penetration, extension, integration and operations remain unclear (Jones & Coviello, 2005). Networks have been argued to contribute to the success of born global firms by helping to identify new market opportunities and contribute to building market knowledge (Coviello, 2006; Mort & Weerawardena, 2006). Other themes have also been explored (Eriksson, Johanson, Majkgard, & Sharma, 1997). Studies by Ritter et al. (2003) and Chetty et al. (2003) investigated the development of knowledge intensive products through networks. Others (Bell, Crick, & Young, 2004) examined the role of entrepreneur in the developing network relationship. The tentative conceptual model guiding the research leads to four research questions. It is a well-known fact that many small businesses are highly innovative as start-ups but eventually fail to maintain the competitive advantage as they grow, indicating a need to identify how firms can create competitive advantage from the extension of marketing activities to an international level. It has been demonstrated that home-based networks of the entrepreneur can play a mediating role in the relationship between inward and outward internationalization and firm performance. The
A mediating mechanism is attributed to three information benefits of social networks: (1) knowledge of foreign market opportunities; (2) advice and experiential learning; and (3) referral trust and solidarity. (Zhou et al., 2007). Zahra et al. (2007) suggest SMEs’ ownership and governance systems significantly influence the development of knowledge-based resources necessary for internationalization. They found a positive relationship between both the equity held by top management team members and venture capitalists and the development of these important resources (Zahra, Neubaum, & Naldi, 2007). The strategic role of networks in the internationalization process was confirmed. (Mort & Weerawardena, 2006).

Developing a unified framework goes beyond the limits of this study. In this article, the author concentrates on the role of social capital in the internationalization process. In this context a multi-disciplinary approach that includes entrepreneurship and strategic management is applied. From the perspective of the resource-based view the entrepreneur can achieve competitive advantage and niche positioning from social capital. Recently, researchers have reported a strong correspondence between a firm’s strategic decision-making process and internationalization, necessitating that internationalization from SMEs, cannot be examined in isolation. Rather, internationalization should be seen within the context of the firm’s management and its strategic choices. This perspective also considers the primary role of entrepreneurs which implies of the creation of social capital, through innovation and risk-taking, proactiveness and network expansion. The interconnectedness between social capital and the decision for international activities is now obvious. This necessitates that internationalization studies must place social capital in the context of the firm’s strategic management processes.

This leads to the second and to the third proposition:

Proposition 2. International involvement is encouraged by the presence of resources from strategic partners.
Proposition 3. International involvement is encouraged by the presence of resources from social networks (e.g. family, spouse, friends).

Although technology competence and management competence are well introduced concepts in the literature (Brinkmann, 2006) the network competence dimension as the ability of the small business owner to utilize and extend resources drawn from strategic networks has been neglected so far. This final issue is therefore is linked directly to the personal competencies of the small business owner and highlights a gap in the International Entrepreneurship literature. It has been shown that human capital characteristics of the entrepreneur or of the members of the founding team provide personal abilities that can facilitate small firm growth and performance (Sapienza et al., 2006). While network relationships have long been recognized to be indispensable for SMEs to achieve international growth (Johanson and Mattsson, 1988; Coviello and Munro, 1997; Lu and Beamish, 2001), a particular focus on social networks has been limited to date (Harris & Wheeler, 2005). It has been criticized that the role of the decision maker and the firm’s characteristics in taking up opportunities for international penetration, extension, integration and operations remains unclear although networks have been argued to contribute to the success of born global firms by helping to identify new market opportunities and contribute to building market knowledge (Chetty et al., 2000).
Therefore the following propositions can be stated:
Proposition 4. International involvement is encouraged by the network competence of the small business owner.
Proposition 5. International involvement is encouraged by the technology competence of the small business owner.
Proposition 6. International involvement is encouraged by the management competence of the small business owner.

Three theoretical imperatives were identified which were discussed in the literature as factors influencing growth of the firm. The core of the theories is summarized in the following table.

<table>
<thead>
<tr>
<th>Theoretical Framework</th>
<th>Network Theory</th>
<th>Resource based Theory</th>
<th>Competence Based Approach</th>
</tr>
</thead>
<tbody>
<tr>
<td>Variable</td>
<td>Structure of network</td>
<td>of Internal resources</td>
<td>firm Marketing Competence Network Competence Technology competence</td>
</tr>
<tr>
<td>Literature Level</td>
<td>of Firm</td>
<td>Firm/Entrepreneur</td>
<td>Entrepreneur</td>
</tr>
<tr>
<td>Analysis</td>
<td>Performance</td>
<td>Performance</td>
<td>Performance</td>
</tr>
</tbody>
</table>

Table 1 Causal logic in explaining performance of three theoretical perspectives

A model is by definition a simplification of a complex reality and there is always a trade-off between including certain factors and relationships in the model and disregarding them. Simplicity and complexity need to be balanced. In order to simplify the model, reciprocal effects of the environment were omitted. The author argues that growth of the international new venture is dependent upon: (1) the structure of the network in the pre-seed phase, (2) the ability of the owner/manager to achieve resources from the existing networks, (3) the utilization of resources through the network, dependent upon the marketing, network and technology competencies of the individual entrepreneur.
III. METHODOLOGY

Research design

Individual SMEs are the unit of analysis in this study. To identify an SME, this study adopted the general definition of SME used by the European Union (2005) and focused on the definition of employee numbers. Accordingly to this definition, a business with less than 10 employees is a Micro business, and a business with 10 to 250 employees is a Small and Medium-sized business. In accordance with the support in the literature for quantitative methods, and in order to address the multi-dimensional nature of internationalization as was discussed earlier, a structure questionnaire was used to collect the data for this study. The respondents were informed by email about the survey and asked to fill out the questionnaire within a limited period of time. The author tested the hypotheses using survey data from startup companies in Upper Austria. This study used the Upper Austrian Chamber of Commerce database, which was accessed during February 2007. Usage of the filters, “foundation year (2002, 2003, 2004, 2005, 2006)” and “active member status” as well as exclusion of “business succession”, yielded 3200 firms which was taken as the population frame. During the allocated time-period of 2 weeks for data sourcing, firms were contacted by email of which 803 agreed, translating into a response rate of 25%. Of the 803 returned questionnaires, 294 were excluded because of incomplete answers, leaving 509 usable responses, which relates to a net response rate of 15.9%. This response rate compares favourably with similar mail surveys of entrepreneurial firms: e.g., (McDougall, 1989; McDougall & Oviatt, 1996) had an 11 percent response rate in a study of new technology-based firms. All of the multiple-item constructs achieved Cronbach alphas of 0.71 or higher, indicating strong internal consistency.

IV. FINDINGS

In this section, the author presents the findings of the survey. Firm-level data were derived by counting the scores for internationalization for all respondents from each company. The profile of respondents demonstrated that 33.3% had no international activities at all (Group I),
14.4% of the companies plan international activities (Group II) and 52.3% already had experience in international activities (Group III). The analysing methods for gathered data in this research were divided in two parts. First is Confirmatory Factor Analysis which was implemented to validate the model and respectively compatibility and relativeness of the question to the model, and the second method was discriminant analysis which was implemented to discover the meaningful difference(s) between the theoretical constructs. The individual measurement items for the study’s dependent, independent, and control variables are listed in Table 1; the construction of the measures is explained in the following. All statement-style items were measured on a scale from 1 = do not agree to 4 = completely agree. The SPSS program was used for the data analysis.

Referring to the social capital structure the resource analysis was measured with seven statements regarding the extent to which the firm’s social capital is a source of international competitive advantage for the firm. While previous research has often focused on a single dimension of social capital and measured it indirectly as the number of relationships or network position (Kundu & Katz, 2003). The author found three dimensions of social capital; results indicate that these dimensions are distinct and have differential effects on internationalization for Wine Businesses. These components are personal relations which the owner has, strategic relations with Investors or Strategic partners and intercompany relations (with Industry colleagues, Friends). Staff showed loadings for both components Nr. 1 and Nr. 2. This finding is important because it provides empirical support for propositions in recent research that different social assets may have different effects on relationship outcomes. The standardized factor loadings are all above the recommended minimum in the social sciences of 0.40. Summarizing the findings indicate that propositions 1, 2 and 3 cannot be rejected.

<table>
<thead>
<tr>
<th>Component</th>
<th>1</th>
<th>2</th>
<th>3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Industry colleagues</td>
<td>.783</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Friends</td>
<td>.651</td>
<td>.473</td>
<td></td>
</tr>
<tr>
<td>Staff</td>
<td>.549</td>
<td>.812</td>
<td>.743</td>
</tr>
<tr>
<td>Investors</td>
<td>.812</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Strategic Partner</td>
<td>.743</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Spouse</td>
<td>.872</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Family</td>
<td>.768</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Extraction Method: Principal Component Analysis.
Rotation Method: Varimax with Kaiser Normalization.
Rotation converged in 5 iterations.

Table 2: PCA Resource Analysis

The major purpose of discriminant analysis was to predict membership in two or more mutually exclusive groups from a set of predictors, when there is no natural ordering on the groups. The dependent variable was the Intensity of International Activities (Range: 1…no international activities, 2…planning of international activities, 3…international activities). In this study three categories of independent variables could be found: Technology Competence,
Network Competence and Management Competence. These three categories distinguish the three groups of companies with different levels of international activities.

<table>
<thead>
<tr>
<th>Entered</th>
<th>Wilks' Lambda</th>
<th>Statistic</th>
<th>df2</th>
<th>df3</th>
<th>Exact F</th>
<th>Statistic</th>
<th>df1</th>
<th>df2</th>
<th>Sig.</th>
<th>Statistic</th>
<th>df1</th>
<th>df2</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Management Competence</td>
<td>.84</td>
<td>1</td>
<td>2</td>
<td>114,000</td>
<td>10,558</td>
<td>2</td>
<td>114,000</td>
<td>.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Technology competence</td>
<td>.77</td>
<td>2</td>
<td>2</td>
<td>114,000</td>
<td>7,798</td>
<td>4</td>
<td>226,000</td>
<td>.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Network Competence</td>
<td>.70</td>
<td>3</td>
<td>2</td>
<td>114,000</td>
<td>7,145</td>
<td>6</td>
<td>224,000</td>
<td>.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

At each step, the variable that minimizes the overall Wilks' Lambda is entered.

**Table 3: Discriminant Analysis for Entrepreneurial Competencies**

Summarizing the findings indicate that propositions 4, 5 and 6 can not be rejected.

This article has identified and analysed three distinct streams of research on internationalization: research on (1) the personal networks of the entrepreneur, (2) the use of alliances and external resources by entrepreneurial firms, (3) the relationship between entrepreneurs and investors, (4) regional networks of entrepreneurial firms. The purpose of this paper was to highlight competence dimensions associated with performance variations of international active and non-active companies. Understanding what leads to superior performance is viewed as an important task, which has theoretical as well as practical implications. Rather than trying to maintain separation in theory building, future research should aim at finding ways to consolidate and combine elements from various approaches to form a more comprehensive understand of entrepreneurial exchange relationships. To explore the development and content of exchange, research could focus on questions such as the following.


