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The missing link between awareness and use in the uptake of pro-internationalization incentives

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ABSTRACT

We investigate the process by which firms become participants in official programmes of public support designed to promote outward internationalization. This study builds on previous research that has established the distinct factors associated with firms' awareness and use of public support measures. These earlier studies have also shown that deficiencies within programmes manifest in low participation rates. However, scholars have not extended this reasoning to focus on the underlying processes involved, and have paid little attention to the steps through which firms elect to use public support, and how support operates upon, and within, the firm. In particular, the link between awareness of public incentives towards internationalization and the use of these incentives has been overlooked. General failure to understand this link is a potential source of policy inefficiency, reducing the effectiveness of those public programmes that employ incentives. We pose three research questions to examine the concept of such a link: (1) Do firms select public incentives that compensate for a lack of resources or capabilities in their possession? (2) Do firms react primarily to internal or external exigencies, for example, internal financial constraints or, rather, are they responding to unfolding circumstances, such as the more demanding market conditions experienced on internationalization? And (3) do firms use public support to "externalize" the increased risk to which they are exposed as internationalization proceeds, and thereby protect their external activities and investments from loss?

The process that firms go through to apply for any type of public support is normally two-staged. Firms first become aware of incentives and then decide whether or not to use them. This process can be handled empirically using a Heckman Selection Model, which we apply to explore our research questions using survey data collected from a sample of Portuguese firms. We find that the greater are the internal limitations of these firms with respect to resources and capabilities and the more demanding are the conditions in which internationalization takes place, then the greater is the use made of public support. We find that awareness of the availability of support is promoted by firms' in-house resources and capabilities and, at the same time, is positively associated with more demanding conditions of internationalization. The use of public support appears to be associated with the opportunity cost to the firm of public incentives, and with the increased risk inherent with internationalization. These results point to the existence of important sources of inefficiency within the process of application for policy measures, particularly with respect to the link between awareness and use. The use of public support is inversely associated with the opportunity cost to the firm of the resources deployed to apply for public incentives and, for firms with greater resources and capabilities, associated positively with the increased inherent risk of internationalization. We find evidence that it is the firms with greater resources and capabilities that predominate in the application for public incentives, allowing us to infer from the data that the typical recipient pursues more risky modes of entry, or selects locations with higher levels of risk, because of the availability of public support. These results point to the possible existence of important sources of inefficiency within the process of application for policy measures, particularly with respect to the link between awareness and use. This behaviour is quite distinct from the search for return on commercial investments and, therefore, is indicative of the possibility of social loss within this public policy intervention.

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1. Introduction

Dating from Cyert and March (1963) the view of the firm as an information-processing and decision making system has paved the way for exploration of the complex nature of organizational processes that take place within its internal economy. This approach has been employed effectively within the sphere of international business research by scholars such as Aharoni (1961, 1966), Boddewyn (1979a, 1979b), Johanson and Vahlne (1977) and by Vernon (1966a, 1966b). Although the behaviour of the firm, and the firm's relationship with the external environment that it encounters, has encompassed the artefacts of government policy, the interaction of the firm's decision-making with government policy has remained under-explored – specifically with respect to the mechanism within the firm by which it responds to policy. This is nowhere more true than in the case of internationalization and the process through which home country support measures towards internationalization (HCSMIs) exert traction upon the international strategy and behaviour of domestic enterprises. HCSMIs are official home country incentives provided through law to promote the internationalization of domestic firms. While they are widely recognized in academic literature, and in policy circles, the process through which they exert their effects is poorly understood, both by academic researchers and policymakers themselves.

In this study we do not adopt a regulatory perspective on HCSMIs, nor do we consider their effectiveness as a determinant of internationalization per se. Rather, we focus on one of the earliest decisions of firms within the process – that of application for HCSMIs and, in particular, why firms decide to use public support in the first place. This is the first, but necessary, step in understanding how policy to promote internationalization actually works, and how far it can be made to work better. The conventional wisdom prevalent in non-scientific studies invokes, as the causes of firms' uptake of policy measures, the presence of a desire for: the reduction of costs and uncertainty, the increase of sustainable competitive advantages, base opportunism and, in direct contrast to this, alignment with national policies (EU, 2007; UNCTAD, 2012). We restrict our focus to incentives specifically to promote outward internationalization, and pose three principal research questions: (1) Do firms become aware of public incentives on the basis of the experience, resources and capabilities they possess and do they select incentives that compensate for deficiencies in resources or capabilities under their control? (2) Do firms react primarily to internal or external exigencies, for example, financial constraints or, rather, are they responding to unfolding circumstances, such as more demanding market conditions experienced on internationalization, using public incentives according to principles of opportunity cost? And (3) do firms use public support to mitigate through "externalizing" the increased risk of internationalization, and thereby protect their external activities and investments from loss?

Our rationale is to add to knowledge on the determinants both of the awareness and of the use of incentives (Crick, 1997; Koksal, 2009), and to explore the link between these two, as we conjecture that it might hold the key to understanding the causes of policy inefficiency. There is evidence to indicate that government actions are liable to fail on account of this missing link in our understanding of the sources of inefficiency (Koksal, 2009; Spence, 2003; Storey, 1999). A case in point is the example of British export promotion, in which a survey by the British Chambers of Commerce, involving eight thousand companies – mainly small and medium sized – concluded that over 65 per cent were unaware of the existence of public support for exports (United Kingdom Parliament, 2013). In the light of evidence such as this, we consider not only the determinants of the decision to use public incentives, but take a step back to examine the antecedents to application for public incentives, including a set of determinants of awareness that firms may have regarding the availability of public incentives. In doing so, we find that, to date, the contributory literature dealing with the internationalization of domestic firms as yet lacks a sound understanding of the effects of firms' characteristics – particularly of firms' resources and capabilities, as well as of the environmental conditions of internationalization – upon the awareness and use of official support by domestic firms.

Investigating policy effectiveness through a two-step model is justified for three main reasons. First, it elucidates the origins of inequality observed in the receipt of government support. It does this is in a manner analogous to research by Heckman and Smith (2004) regarding matters within the context of employment. Such a framework allows us to go beyond a simple, separated, comparison of statistical means for awareness or use of HCSMIs, and so to better explore the role of asymmetrical information across firms in explicating the process efficiency of participation in public incentives. We also aim for a deeper understanding of the parts played by resources, capabilities, and the specificities of risk encountered during internationalization upon firms' behaviour. We posit that it is important to consider whether patterns of firm behaviour towards the use of HCSMIs result from a lack of resources and capabilities necessary to internationalize, from the burden upon the firm of search and screening costs, or from no more than pure opportunism – in which category we include risk externalization.[1] Second, identification of the distributions of awareness and of use can yield practical information about the determinants of participation in public programmes aimed at encouraging activities – particularly those whose motive is, as in the case of internationalization policy, to create impact on economic growth (Keesing, 1967; Kravis, 1970; Penrose, 1956). Indeed, domestic economic growth led by the external sector is recognized as a priority for policy makers (Moran, 1998). Third, new insights into the policy participation process have important implications for strategies towards effective programme evaluation. We know that knowledge accumulated from evaluations can reveal how the determinants of participation vary between firms (Crick, 1995). But, robust scientific understanding promises to inform choices about from where to draw a control group, what variables to collect in a survey, and what targeting strategy should be adopted in differing circumstances (Abelson et al., 2003; Heckman & Smith, 2004).

There is considerable applied research on the promotion of internationalization, notably with respect to exports, for example, Gil, Llorca, and Martinez (2008); Girma and Görg (2007); Greenaway and Kneller (2007); Martincus and Carballo (2008). All of these studies provide evidence to support the existence of a form of 'synchronization' between a firm's resources and capabilities and its use of public incentives. However, there is disagreement over the causal mechanism of this apparent synchronicity. Compounding the lack of evidence on the true nature of the processes through which public incentives are allocated between firms, such evaluations of policy measures to support private investments as there are – be it for internationalization or for other purposes – have focused on the aggregate impact of incentives, so neglecting the question of the "bridge between awareness and use" (Bannò & Piscitello, 2010; Colombo, Grilli, & Verga, 2007; Bergemann & Välimäki, 2002; Heckman, 2010). Our enquiry, although novel in exploring the mechanism within the firm by which it responds to policy, belongs to a small family of evaluative studies that seeks to understand the mechanisms through which public incentives exert traction upon firms' aspirations, strategies and needs. Such

[1] By which we here mean the systematic use of public incentives to defray the cost of engaging in more risky projects.