



Country of origin and network effects on internationalization: A comparative study of SMEs from an emerging and developed economy



Luciano Ciravegna^{a,*}, Luis Lopez^b, Sumit Kundu^c

^a Royal Holloway School of Management, INCAE Business School, Egham Hill, EW20 0EX UK

^b INCAE Business School, Alajuela, Costa Rica

^c Florida International University, Miami, FL 33199, USA

ARTICLE INFO

Article history:

Received 1 June 2012

Received in revised form 1 April 2013

Accepted 1 May 2013

Available online 17 July 2013

Keywords:

Internationalization

Networks

Country-of-origin

International entrepreneurship

High technology small and medium enterprises

Emerging economies

Latin America

ABSTRACT

This study examines the internationalization of high technology small and medium enterprises (HTSMEs). It explores how they develop and use networks to penetrate their first foreign market relying on information collected via direct interviews with the CEOs or founders of 58 high technology small firms that operate internationally. It uses mixed methods to discuss the network building mechanisms identified – client–supplier relationships, existing personal contacts, contacts acquired by chance, and contacts acquired through specific strategies. The findings provide the basis for developing propositions for further comparative analyses of the internationalization of HTSMEs based in emerging and developed markets. The study contributes to the literature on networks, internationalization and international entrepreneurship.

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1. Introduction

The literature on institutions illustrates that emerging markets differ from developed economies because they suffer from institutional weaknesses and market failures (Khanna & Palepu, 2010; North, 1990). Under these conditions, companies leverage relational capital and social networks to achieve their strategic objectives (Nahapiet & Ghoshal, 1998). There is much empirical evidence showing that firms' country-of-origin may affect internationalization strategy (Dunning, 1998; Rugman, Oh, & Lim, 2012; Rugman, Verbeke, & Nguyen, 2011). The use of networks by small enterprises as a means to support internationalization has also received much attention (Coviello, 2006). However, the effect of being based in a developed or an emerging economy on network-supported internationalization is a largely unexplored issue, especially with regard to small entrepreneurial businesses. This study contributes to the development of small firms' internationalization theory by discussing how HTSMEs based in different domestic contexts develop and use their networks to support their first export.

The importance of networks as mechanisms supporting internationalization has been documented at length by the international business

and entrepreneurship literature (Coviello, 2006; Ellis, 2000; Johanson & Vahlne, 2009; Ma, Yao, & Xi, 2009). The internationalization of high technology small and medium enterprises (HTSMEs) has received special attention, with many of the studies of born globals and international new ventures focusing on HTSMEs (Knight & Cavusgil, 2004; Moen, 2002). However, there is still little empirical evidence on the internationalization of HTSMEs based in Latin America (Lopez, Kundu, & Ciravegna, 2009; Nicholls-Nixon, Castilla, Garcia, & Pesquera, 2011). This study responds to calls for the advancement of the research agenda on internationalization through qualitative research exploring different empirical settings, and in particular Latin America (Halinen & Törnroos, 2005; Mort & Weerawardena, 2006; Pérez-Batres, Pisani, & Doh, 2010). The key research questions we address are: How do HTSMEs search for and find their first client in a foreign market? If they use networks, how do they build such networks?

We explore how the country-of-origin affects the internationalization of firms based in Costa Rica, a small emerging economy in Latin America, and Italy, a large developed European economy, using a mixed method approach. We leverage the findings to advance the research agenda by developing a set of propositions for further empirical testing. We chose this unconventional mixed method approach for the following reasons. First, we respond to calls for more diversity in the methods applied to international business and entrepreneurship research (Birkinshaw, 2004). Second, exploratory research and mixed research methods are suited to refine the research agenda on new topics and empirical settings

* Corresponding author at: University of London, INCAE Business School, Alajuela, Costa Rica.

E-mail addresses: luciano.ciravegna@incae.edu (L. Ciravegna), luis.lopez@incae.edu (L. Lopez), kundus@fiu.edu (S. Kundu).

(Bryman, 2006) — there are only a few studies examining the effects of country-of-origin on network-supported internationalization and evidence about Latin American companies is still very scarce (Mort & Weerawardena, 2006; Nicholls-Nixon et al., 2011; Rugman et al., 2011). In the next two sections we review the literature on networks and internationalization and outline our research methods. The following two sections present and discuss the findings, illustrating that both Italian and Costa Rican entrepreneurs relied heavily on networks and social capital to support their first export.

2. Literature review

Several studies have documented that some small and medium enterprises (SMEs) internationalize fast in spite of their size, especially in high technology sectors, such as information technology services and software (Andersson & Wictor, 2003; McDougall, Shane, & Oviatt, 1994). Evidence of fast internationalizing HTSMEs has been the springboard of several new concepts, such as “born globals” (Knight & Cavusgil, 2004; Moen, 2002) and “international new ventures” (Crick, 2009; Oviatt & McDougall, 1994). The debate about the characteristics of “born globals” and “international new ventures” is beyond the scope of this study, though one of its objectives is to contribute to the literature on the internationalization of HTSMEs by providing new comparative evidence of the internationalization mechanisms used by companies based in different economies.

A large share of the literature on HTSMEs' internationalization draws from the resource-based view, which considers the firm as a bundle of resources, ranging from human and financial resources to managerial and technological skills (Grant, 1991). The network approach to internationalization argues that through networks (personal contacts and inter-firm networks) HTSMEs can link internal and external resources to pursue strategic aims, such as entering a new market (Blomstermo, Eriksson, Lindstrand, & Sharma, 2004; Coviello & Munro, 1997; Moen, 2002; Sharma & Blomstermo, 2003). Networks can help firms identify business opportunities and support their entry into markets they are unfamiliar with (Chetty & Holm, 2000; Ellis, 2011; Javalgi & Todd, 2011; Madsen & Servais, 1997; McDougall & Oviatt, 2000).

The degree to which firms leverage internal and external resources may be contingent upon country-specific advantages (Rugman et al., 2012). Such firm-specific advantages are primarily derived from the internalization of some asset, for example a network (Rugman et al., 2011). Simultaneously, firms will build on country-specific advantages to decide, given a set of internalized assets, which products and markets to pursue, and, generally speaking, which configuration — part of it being the scope of internationalization — to adopt in terms of these market segments. Rugman et al. (2011) argue that firms build first on country-specific advantages before they start generating firm-specific advantages. Thus, it is plausible that the use of networks to support internationalization may greatly differ by country. Most scholars researching the effects of the country-of-origin on internationalization focus on multinational enterprises, and they rarely examine Latin American firms (Dunning, 1998; Nicholls-Nixon et al., 2011; Rugman et al., 2011). This study furthers the research agenda by exploring the network-supported internationalization of small high technology firms based in an emerging and developed economy through a comparative mixed method approach.

Institutional theory suggests that developing countries' firms face significant challenges in the internationalization process, as there are weak institutions in the form of underdeveloped capital markets, labor markets, and product markets (Fukuyama, 1995; North, 1990). In contexts affected by institutional weaknesses, firms may compensate for market failures by relying more on the personal contacts of the entrepreneur and senior management, often defined as social and relational capital (Ciravegna, 2011; Khanna & Palepu, 2010). Social capital theory explains how firms generate value from the network of relationships in which they are embedded, emphasizing the role of relationship

building and capability building for young firms seeking to go abroad (Nahapiet & Ghoshal, 1998). Yli-Renko, Autio, and Tontti (2002, p. 11) argue, “The social capital of key individuals can be used to solicit trust and reciprocal disclosure of information, to open access to sources of learning, and to obtain informational cues that might be otherwise difficult to obtain.” Many perspectives have been used to examine the international growth of young firms, but an increasingly influential approach is to focus on the relational capital that firms build as a way of creating opportunities and capabilities to grow beyond their home market (Kale, Singh, & Perlmutter, 2000; Prashantham & Dhanaraj, 2010).

In sum, the literature on internationalization illustrates that small firms often use networks to overcome resource constraints (Ciravegna, 2011; Coviello, 2006). Institutional theory suggests that firms based in emerging markets may be more likely to rely on social and relational capital than firms based in developed economies (Khanna & Palepu, 2010). Scholars of multinational enterprises also emphasize the importance of country-of-origin (Dunning, 1998; Rugman et al., 2011). It is unclear whether internationalizing small enterprises based in an emerging economy differ in their use of networks from firms based in a developed economy. In this study we contribute to the development of the internationalization theory by examining HTSMEs based in Costa Rica, a small Latin American economy, and Italy, a large European economy.

Networks to support internationalization may be inherited or actively constructed by entrepreneurs (Harris & Wheeler, 2005). Some authors point out that entrepreneurs may choose their export markets depending on the opportunities that emerge in specific circumstances, for example an unexpected referral from an existing domestic client (Brewer, 2001; Kontinen & Ojala, 2011; O'Farrell & Wood, 1994). Several scholars disagree with this view, suggesting instead that network-supported internationalization is a more active entrepreneurial process (Johanson & Vahlne, 2009; Kim, Basu, Naidu, & Cavusgil, 2011).

Evidence of network building mechanisms and their role in the international business opportunity recognition process remains scarce. For this reason, several scholars call for more qualitative analyses of these processes and for the use of exploratory research to develop the theory (Bryman, 2006; Dominguez & Brenes, 1997; Halinen & Törnroos, 2005; Ojala, 2009; Robson, 2011). Comparing qualitative evidence collected from Italian and Costa Rican HTSMEs, we identify different mechanisms through which the companies acquired the networks they used to support their first international venture. We discuss more in detail each mechanism using case studies. We discover a set of general trends and develop a set of testable propositions to advance the theory of HTSME internationalization (Mort & Weerawardena, 2006; Tashakkori, 1998; Yin, 1994).

3. Methods

This study focuses on the internationalization of a specific type of firm: the high technology entrepreneurial SME. Given that there is very scarce empirical evidence about the internationalization of Latin American HTSMEs, and that research comparing the use of networks by emerging market and developed economy internationalizing HTSMEs is in its initial phase, we adopt an exploratory mixed method approach, as suggested by the research methods literature (Bryman, 2006; Robson, 2011; Tashakkori, 1998).

We include in the sample only firms that have a maximum of 250 employees and whose average annual sales do not exceed Euro 50 million, located in the Central Valley of Costa Rica and the Province of Turin of Italy (European Commission for Enterprise & Industry, 2011). We focus only on producers of software packages or information technology services for other businesses, which have been considered to be “high technology” by previous research (Coviello & Munro, 1997; Spence & Crick, 2006). Only firms that export a minimum of 5% of their average yearly sales are included in the analysis. In order to capture the “entrepreneurial” aspect, we exclude subsidiaries of larger

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