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International and market-specific social capital effects on international opportunity exploitation in the internationalization process

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ABSTRACT

We develop theory stating that international and market-specific social capital are two distinct forms of social capital which both increase international opportunity exploitation. We also argue that market-specific social capital mediates international social capital. Our theoretical developments are based on internationalization process theory and social network theory. Using data on 239 internationalizing SMEs, our results confirm that the effect of international social capital on opportunity exploitation is only mediated via market-specific social capital. Hence, we identify an internationalization process for social capital development in international business opportunity exploitation. Our contribution adds in several ways to existing international business research.

1. Introduction

Internationalization process (IP) theory and empirical studies on international small and medium-sized enterprises (SMEs) argue that the ability of firms to exploit new international business opportunities determines firm growth and international expansion (Crick & Spence, 2005; Johanson & Vahlne, 1977). However, so far firm exploitation of new business opportunities during internationalization remains an underexplored area within the international business domain (Johanson & Vahlne, 2006; Jones, Coviello, & Tang, 2011; Knight & Liesch, 2016). Within literature on international SMEs, studies have touched on the theme of opportunity exploitation but typically focused on how small, newly started firms access knowledge about initial business opportunities abroad (McDougall, Shane, & Oviatt, 1994; Musteen, Francis, & Datta, 2010). How firms are able to exploit new international business opportunities once an entry abroad has been made remains a largely overlooked question. This deficit in international business research is noteworthy because studies have suggested that a subsequent international expansion can be more challenging than initial expansion (Crick & Spence, 2005; Lindstrand, Melén, & Rovira Nordman, 2011; Prashantham & Young, 2011). To further the understanding of how firms exploit new international business opportunities for continued expansion abroad is thus highly relevant and needed (Knight & Liesch, 2016).

In line with developments in IP theory – namely, the understanding that knowledge of opportunities and foreign markets is obtained through networks of interconnected relationships (Blomstermo,

Eriksson, Lindstrand, & Sharma, 2004; Johanson & Vahlne, 2009) – qualitative findings of international SMEs show that knowledge acquisition through networks is a crucial factor explaining SMEs' abilities to recognize new international opportunities (Coviello, 2006; Loane & Bell, 2006; McDougall et al., 1994). Building on these theoretical and empirical insights, other studies have demonstrated the use of social capital in facilitating SMEs' acquisition of foreign market knowledge (Coviello & Cox, 2006; Presutti, Boari, & Fratocchi, 2007; Yli-Renko, Autio, & Tontti, 2002; Zou & Ghauri, 2010) and international opportunity exploitation (Prashantham & Floyd, 2012; Prashantham & Young, 2011). IP theory further posits that firms' possibilities to exploit business opportunities depend on two forms of foreign market knowledge: market-specific knowledge and internationalization knowledge (Eriksson, Johanson, Majkgård, & Sharma, 1997; Johanson & Vahlne, 1977). Despite the prominence given to SMEs' social capital, empirical studies have not yet investigated international networks in relation to the two critical forms of foreign market knowledge. It is therefore still unclear if an internationalizing firm's network provides these two forms of foreign market knowledge and, if so, how this social capital affects the SME's international opportunity exploitation and continued internationalization. Hence, we argue that to address the deficit in international business literature on the theme of international opportunity exploitation, further theory-building research is needed that investigates the role of social capital on SMEs' abilities to exploit new business opportunities for continued expansion abroad.

We delineate and investigate the role of social capital in SMEs' exploitation of international business opportunities. Our purpose is to

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examine the effects of international social capital and market-specific social capital on SMEs' exploitation of international business opportunities. International social capital is conceptualized as a firm's network of international relationships and the internationalization knowledge accumulated in interactions with these relationships. We conceptualize market-specific social capital as a firm's current network relationships in the host country and the market-specific knowledge acquired in interaction with these relationships (Eriksson et al., 1997; Johanson & Vahlne, 2009). We develop three hypotheses and test them by using structural equation modelling on a data set covering 239 Swedish internationalizing SMEs.

Our research explains the separation of the foreign market knowledge concept and the view of international networks as vessels for knowledge generation in internationalization process theory. In so doing, we identify an internationalization process for social capital development in international business opportunity exploitation. Our contribution adds in several ways to existing international business research. First, we add to internationalization process theory by delineating two forms of firm-level social capital: international social capital and market-specific social capital, and by showing a path dependent effect of the two forms on continued opportunity exploitation. Second, we add to literature on international SMEs and international entrepreneurship research by presenting an in-depth understanding of the effects of social capital on SMEs' abilities to exploit international business opportunities. International entrepreneurship is a strand of international business research that has been associated with research on small, young, resource-constrained firms that identify opportunities abroad from inception. Because previous studies on international SMEs and international entrepreneurship have focused on how small firms generate knowledge about opportunities that enable an initial expansion abroad, this study extends existing literature by providing findings on the effects of social capital for SMEs' abilities to exploit new business opportunities after the firms' initial entry abroad.

2. Theoretical background

2.1. International opportunity exploitation and foreign market knowledge

The theme of opportunity exploitation has been an underexplored area within the international business domain even though the last decade has seen more attention directed towards the concepts of opportunity recognition and exploitation (Johanson & Vahlne, 2006; Muzychenko & Liesch, 2015). Within literature on international SMEs, qualitative case studies have addressed the question of how small young firms are able to recognize opportunities for doing business abroad and initiate an international expansion (Coviello, 2006; Crick & Jones, 2000; McDougall et al., 1994). The studies have often been positioned within the international entrepreneurship area and given much attention to opportunities related to new venture formation. The study by Ellis (2011) focuses on international entrepreneurship and opportunity recognition but in doing so, this study put forward that the only meaningful opportunity is the one that is actually exploited. For all intents and purposes, it is not until the opportunity actually leads to the formation of a new international exchange (e.g., an exchange with a new foreign intermediary or a new foreign customer) that it can be said to be meaningful. Ellis work, in other words, suggests that the formation of exchange agreements with new partners in new foreign markets constitutes strong evidence of opportunity exploitation. In relation to this literature, IP theory does not explicitly address how firms begin the internationalization process. IP theory instead focuses on the process of recognizing and exploiting new business opportunities once an entry abroad has been made. This process is seen upon as an interactive process, where opportunity recognition and exploitation are interrelated (Johanson & Vahlne, 2006). During internationalization, firms gradually and sequentially increase their recognition (i.e., knowledge about an opportunity) and exploitation (i.e., commitment of

resources) of an opportunity (Johanson & Vahlne, 2009). A business opportunity captures the development of new business with customers and suppliers in existing as well as new foreign markets. In this study, we focus on the concept of international opportunity exploitation and based on IP theory and the reasoning of Ellis (2011), we describe this concept as the formation of and commitment of resources to new business relationships in existing and new foreign markets.

The IP model describes a process where current international operations lead to experiential knowledge accumulation about foreign markets (Johanson & Vahlne, 1990). A firm's continued internationalization is directed by decisions made based on this foreign market knowledge. In their original IP model, Johanson and Vahlne (1977, p. 28) argued that "An important aspect of experiential knowledge is that it provides the framework for perceiving and formulating opportunities." Experiential knowledge enables a firm to identify new business opportunities abroad and take advantage of opportunities by reducing the uncertainty in committing resources to the opportunities (Johanson & Vahlne, 2006; Sharma & Johanson, 1987). International expansion through opportunity exploitation was early on discussed as requiring knowledge of the specific country market as well as more general knowledge of international operations (Andersen, 1993; Johanson & Vahlne, 1977). Later developments separated and operationalized the foreign market knowledge concept into two forms of knowledge: market-specific knowledge and internationalization knowledge (Barkema & Vermeulen, 1998; Eriksson et al., 1997). While prior empirical studies within international entrepreneurship have argued that previous international experiences enhance a firm's ability to recognize new opportunities and expand abroad (Ellis, 2011; McDougall et al., 1994), studies have not investigated opportunity exploitation in relation to the two critical forms of foreign market knowledge which IP theory argues determine possibilities of opportunity exploitation. We believe that linking the theoretical developments of the foreign market knowledge concept to international opportunity exploitation can help in furthering the understanding on how SMEs exploit international business opportunities for continued expansion abroad.

Market-specific knowledge concerns the host country market in which the firm is going to operate or is already operating. It is specific to a market with regard to local market actors, competitors, economy, laws, culture, and the larger society (Makino & Delios, 1996). A firm's current activities in a particular market are the prime source of these experiences. Through business activities, idiosyncratic experiences of partners as well as knowledge of the specific market's organization are obtained by the firm. Market-specific knowledge supports firm understanding of partner preferences as well as business practices in the market. It supplies a multilayered understanding of the local market. Eriksson et al. (1997, p. 7) stated that market-specific knowledge demands "presence abroad, exposure to the situation abroad, and interaction with specific customers, intermediaries and other firms" to be useful. Market-specific knowledge can thus be difficult and costly to obtain, but is critical for successful development of international operations (Barkema, Bell, & Pennings, 1996; Lord & Ranft, 2000).

The other type of knowledge, internationalization knowledge represents a firm's accumulated knowledge about how to internationalize, including how to organize and develop foreign business operations. It is a general type of knowledge that does not relate to a specific market or country (Delios & Beamish, 1999; Fletcher, Harris, & Richey, 2013; Zahra, Ireland, & Hitt, 2000). It is acquired by the firm through exposure "to different country and product markets, clients, and networks, as well as to diverse sets of institutional rules" (Blomstermo et al., 2004, p. 5). Internationalization knowledge is a firm-specific experience of organizing internationalization, accumulated over time. As such, this type of knowledge is applicable and useful in developing international opportunities and operations in different markets. Internationalization knowledge also involves a firm's experiences with its own capability and resources in engaging in international

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