The Take-off Process: Initial Internationalization of Small and Medium-sized Enterprises from China

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ABSTRACT

The rapid growth of emerging country markets and their integration into the world economy is drastically re-arranging competitive forces for firms and economies, implying a third wave of globalization, especially increasing the role of smaller firms in internationalization. In this paper the focus is on two major take-off processes from the domestic market to the foreign market, viz. the horizontal take-off process, and the vertical take-off process. "Marketization" is highlighted as a critical factor behind the possibilities to take off. The initial stages of the internationalization process are analyzed inclusive of the indirect and direct export modes. The research is based on an abductive research approach involving case studies with primary data collected through interviews in the Yang-Tse River Region. Six cases are constructed on traditional Chinese family firms run by strong and dominating entrepreneurs, and which represent three major groups of Chinese exporters. Major empirical and theoretical conclusions summarize the article.

Key words: take-off, horizontal and vertical, China, SMEs, direct indirect export

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1 BACKGROUND

Small and medium-sized enterprises (SMEs) seem to play an increasingly large role in the third wave of internationalization of firms. The international business situation at the beginning of the new millennium implies such a third wave, inter alia involving a steep ongoing increase in the international business activities of firms from transition economies such as the P.R.C. The first wave involved firms from Western Europe and North America that internationalized within these continents and between them. In the second wave these firms expanded to East Asia, concomitantly with firms from this region internationalizing to countries there and to Europe and North America. (Jansson, 2007a, b)

The period 1986-2004 is the break through period for the internationalization of large Chinese firms, mainly influenced by the accession of China to WTO and major policy measures. In addition to the state-owned enterprises (SOEs), a number of privately owned enterprises internationalized rapidly. After 2004, a marked increase took place with a rise of 12 billion USD in 2005 and 16 billion in 2006, which rapidly raised the stock of Chinese FDI to 73 billion in 2006. In 2005, up to 75% of outward FDI capital flows had come from SOEs promoted by the Chinese Government (LOCOmonitor, 2006). The FDI stock in 2006 was concentrated to four industries and 77 % of total FDI in 2002/3 was found in developing countries (Buckley et al, 2007b).

Even if the internationalization of Chinese firms more and more involves SMEs (Söderman et al, 2008), it has so far mainly concerned the large corporations. Some studies identify a number of Chinese companies that have become multinational corporations (MNCs) as well as the most successful “internationalizers” so far, e.g. UNCTAD (2006). IBM Going Global (2006) identifies 60 firms with globalization potential. Of the 100 top companies from rapidly developing economies selected by The Boston Consulting Group (2006) to have the potential to change the world, 40 are Chinese. Except for a limited number of firms, the degree of internationalization of Chinese companies is still low, but rapidly increasing, especially after 2004. The dominant motive for investing abroad up to 2004 was to seek new markets, which was increasingly complemented with resource-seeking investments and with asset-seeking investments (Buckley et al, 2007b).

2 PROBLEMS AND PURPOSE

The potential is large for SMEs to internationalize in the third wave of internationalization, which has not yet been used by Chinese smaller firms despite that they have come to the fore in China’s economic development. In 2001, there were about 10 million registered SMEs contributing 55.6 % of the GDP, over 75% of urban job opportunities as well as 60% of the exports and 43 % of the taxation of the country. The private sector accounts for approximately 60% of the country’s GDP. It is the most dynamic sector, growing with around 20 % per year. If this trend continues, SMEs will become the hallmark of the Chinese economy in the future together with the foreign-invested sector. (APEC, 2002; World Bank, 2004).

However, this might not be the case, since too few SMEs expand abroad, a major reason being that too few SMEs grow large enough in the domestic market to develop competitiveness for foreign markets. Judging from research on Chinese firms in Southeast Asia as summarized in Redding (1990) and Jansson et al (2007), this growth problem seems to be a general feature of Chinese firms, especially family firms. Another problem is that already internationalizing SMEs don’t grow enough in foreign markets. Despite high export shares, the firm does not develop much beyond a certain initial stage. The firm exports without internationalizing, getting stuck in the internationalization process.

This article investigates this international growth problem by first studying how firms take-off from the domestic market and how they come further in the internationalization process from indirect to direct exporting: the process for taking off. These aspects concerning

Chinese firms are of general interest due to the rising importance of Chinese firms in the third wave of internationalization. Moreover, the sustainable growth of China's economy as any emerging market economy requires a greater role for SMEs as exporters and the development of various sources of competitiveness. The problem is to make large numbers of firms to internationalize as well as to stimulate their growth so they become midst, and grow further.

The *main purpose is therefore to describe and explain the internationalization processes of SMEs from China, focusing on the take-off process*. It is studied how firms start to become international by going abroad. In contrast to most IB research on Chinese firms that are FDI-related studies, the focus is on trade-oriented issues. Moreover, the paper aims to make a contribution to international process theory. Very little is known about the initial steps of the internationalization process, in particular regarding SMEs. This goes for the starting point, the pre-internationalization phase, and how direct and indirect export modes are related to each other (Johanson & Vahlne, 2003; Jansson, 2007b; Tan, Brewer & Liesch, 2007). Regarding the last aspect, exporting is direct to the foreign market or indirect through a representative in the home market, often a trading company. These export modes are more rarely related to each other and the overall process from a theoretical perspective. Indirect exporting, in particular, is not thoroughly researched. The focus of the article is thus on the initiation of the internationalization process or exit issues rather than on entry modes and entry processes.

The traditional definition of SMEs is changed. Only including firms of a size up to 250 employees is too limited for our purpose. Therefore, to cover more of the middle ground between small and large firms, the "M" part is enlarged to include firms of maximum 4.000 employees.

3 HORIZONTAL AND VERTICAL TAKE-OFF

The common focus of the few studies on the start of internationalization is too narrow for our purpose (e.g. Welch, 1977; Tan, Brewer & Liesch, 2007). They concentrate on how the individual decision-maker learns to export rather than on how the organization learns to internationalize, and they relate conditions of foreign markets too little to conditions of the domestic market. Instead, we define this move as a process of transforming an indigenous firm into an international firm, which is usually what internationalization process theory is about. But there is also a reverse process, where the firm starts in the foreign market and later moves into the domestic market. Common names for firms transforming in this way are 'Born globals', 'International new ventures' or 'Technology upstarts'.

We define such a transformation of the firm between domestic and foreign markets as the take-off process, which then occurs in two major ways. Either internationalization starts from the domestic market by building on the competitive advantages established there, or in foreign markets. The former situation is defined as *horizontal take-off* (HTO), while the latter is labelled *vertical take-off* (VTO). The distinction between these two ways to set off is based on a metaphor from aviation. Horizontal take-off then relates to how firms operating in the domestic market are transformed into international firms. This is the traditional internationalization process, which is assumed to occur in a different way in an emerging country market such as China compared to Western mature markets. The main difference is that the firm first establishes itself together with other firms in the local industry to build its competitive strength before it internationalizes. This is the major condition for the HTO (before planes can take-off, an airport must be established). Therefore, internationalization of firms from transition economies such as China is highly influenced by how the "marketization" process from a centrally planned economy to a market economy takes place. These processes involve the transformation of institutions that govern firms, e.g. privatization efforts, property rights regimes, and government intervention and support (World Bank, 2004; Jansson 2007a). In vertical take-off, firms become international from inception without first developing an industry base in the domestic market. Competitiveness is rather developed abroad in the global market place. This way to start to internationalize is defined as the VTO (no airport is needed for helicopters to take off). Factors behind the initiation of the internationalization process or the first export decision are usually defined as external and internal stimuli (Tan, Brewer & Liesch, 2007). Instead, we define them as drivers for taking off.

The article is mainly about indirect exporting through a horizontal take-off, which is compared to direct exporting and to vertical take-off. Since the take-off phase cannot be studied in isolation from the overall internationalization process, the first stages explored in the article are also related to the overall internationalization of the firm.

4 EXTANT THEORY ON THE INTERNATIONALIZATION PROCESS

This section compiles those theories on the internationalization of firms that are relevant for studying the take-off process of SMEs.

Internationalization processes of SMEs from China are assumed to follow the typical patterns found for firms in general (Johanson & Wiedersheim-Paul, 1975; Johanson & Vahlne, 1977) inclusive of SMEs (Hohenthal, 2001). However, ‘International new ventures’ tend to follow another pattern (Oviatt & McDougall, 1994; Madsen & Servais, 1997; Autio, Sapienza & Almeida, 2000; Zahra, 2005). Initial stages of internationalization are also captured in a framework of entrepreneurial and internationalization perspectives known as international entrepreneurial dynamics (Mathews & Zander, 2007).

According to the network approach to internationalization (Jansson, 2007b; Jansson & Hilmersson, 2008; Timlon & Hilmersson, 2008), the more relationships in a foreign country the more established and experienced the firm becomes including a higher degree of internationalization. Relationships are integrated into Cavusgil’s internationalization process model as suggested in Jansson & Sandberg (2008). The reason for this approach is the strong relationship orientation of Chinese firms, usually expressed as ‘guanxi’ and summarized in Redding (1990) and Jansson et al (2007).Relationships being at the core of the entry process follow a similar pattern to the internationalization process as a whole, showing how the gradual build-up of internationalization knowledge takes place through increased network experiential knowledge (Eriksson et al, 1997). The more relationships in a foreign country are developed, the more established and internationally experienced the firm becomes and the higher the degree of internationalization. Also, the more countries the firm has established relationships with, the more internationally experienced it is.

Based on the experiential knowledge process, internationalization processes are often divided into different degrees or stages. A classical grouping of firms in five stages is made by Cavusgil (1980), which has also been found to be valid for small and medium-sized exporters (Gankema et al, 2000). During the first stage, firms have a domestic market focus. Next follows the pre-export stage, when the firm evaluates the possibilities to start exporting. The third stage is experimental involvement, when exporting is a marginal activity. The fourth stage is active involvement, when international business becomes a normal activity, e.g. an important share of the turnover is exported. A suitable organization structure is also now in place for this activity. International business is a regular feature. The company is focusing on key export markets and devotes substantial amounts of time and resources to entering and developing new markets. International business has been integrated into the organization of the firm. Adaptations are increasingly made to markets, customers, and partners. The fifth and last stage involves committed involvement in exporting. The firm can now be called international, since it is heavily dependent on foreign markets. The majority of the turnover is generated through exports and significant amounts of time are spent on this activity. International business is an integral part of strategic management both in the shorter-term and the longer-term.

Organizational learning of experiential knowledge is behind the step character of internationalization models. According to Sharma & Blomstermo (2003), this organizational learning is discontinuous and could be likened to a change of learning platform. New stages of internationalization are established with the firm extending its business from one major type of market to another major type or from one type of foreign environment to another. These foreign country market environments or contexts are defined as institutional settings based on the institutional network approach (Jansson, 2007a). There is an inter-play between network relationships and institutions on the regional emerging market, where institutions are seen as constituting the framework for different relationships, e.g. ”macro rules” such as judicial and penal systems. This constitutes an institutional distance, which is assumed to be large when internationalization processes take place from emerging markets to mature markets. The internationalization process is therefore determined by the institutional distance (Shenkar, 2001; Xu & Shenkar, 2002), which is a broader concept than psychic distance (Johanson & Wiedersheim-Paul, 1975) or cultural distance (Majkgård, 1998).

5 THE TAKE-OFF PROCESS

Based on the extant theory above, the take-off process involves the following initial stages of the internationalization process:

5.1 First Stage: Domestic Market Focus

The first part of the frame assumes that the firm is operating on the domestic market and has no international business, and consequently no internationalization or foreign market knowledge. Still, this stage is important from the internationalization point of view, since the potential for being able to internationalize is developed here. This is especially relevant for firms from emerging country markets, which first develop their sources of competitive advantage at home to be able to compete on foreign markets, especially on more advanced mature markets.

5.2 Second Stage: Pre-export

Here, an awareness of business opportunities on foreign markets emerges within the firm including knowledge of threats from imports to the competitiveness of the home-market (e.g. off-shoring). ‘Wake-up signals’ could be such as international issues become ‘hot’ in the trade, press and politics, or if customers or competitors are internationalizing. At this stage firms also start to passively react to unsolicited orders. Since the focus is still domestic, the firm perceives export markets as very troublesome and risky. The firm might start to carry out research on foreign markets, but do not invest in export promotion campaigns and have little contact with foreign companies. They feel little real need to export and have no plans to do so in the future. There is no internationalization or foreign market knowledge.

5.3 Third Stage: Indirect Exporting

The producer uses a domestic representative, often a trading company, as a sales outlet for the foreign market. The sales usually take place in an international market outlet located in the home market, mainly trade fairs. The producer never leaves home and has no direct relation with the foreign country market. Further internationalization takes place through direct exporting, building on the experience gained through indirect exporting by starting to sell directly to parties on the foreign country market.

5.4 Fourth (or Third) Stage: Experimental Export

The firm either reaches this stage directly from the pre-export stage through direct exporting or indirectly through the indirect exporting stage. The company is actively reacting to the internationalization challenge through a trial and error process, beginning to develop a commitment to foreign customers and markets. Relationships are developed, usually as triads (Jansson & Sandberg, 2008). The more inexperienced direct exporter does this first temporarily and irregular on a small scale and then more permanently on a larger scale. At this stage, the firm starts to build up internationalization knowledge and an export organization by being directly active in the foreign market. Over time, it might get limited internationalization knowledge, and highly focused network experiential and institutional knowledge (Eriksson et al, 1997).

5.5 Drivers for Take-off

In the pre-export stage certain factors drive the SME to leave the safe heaven of the domestic market for the foreign markets or start to export directly to the foreign market. These factors are either externally or internally generated. The reasons originating outside the firm are further divided into push and pull factors.

6 METHODOLOGY

The methodological approach behind this research is mainly abductive, being a mix of deduction and induction (Jansson, 1994a; Jansson & Sandberg, 2008). The purpose is theoretical development, where the empirical support of a theory is continuously assessed, or, inversely, a reality's theoretical support investigated, through the matching of theories with realities (Dubois & Gadde, 2002). The case-study approach is used (e.g. Merriam, 1998; Yin, 1991). Embedded cases are used to integrate qualitative and quantitative knowledge (Scholz & Tietje, 2002).

The cases were selected to represent the HTO group, but with the purpose to contrast them to one case from the VTO group. Primary data was mainly collected from interviewing. A major reason is that secondary data to support SME research in China is still far from sufficient, research on the SMEs mainly being qualitative. Interviews were done 15 July -15 Sept 2006 and conducted by the Chinese native author and his masters students from Shanghai University. The six case companies were visited and at least three representatives from each case company were interviewed between 5 to 20 hours. All interviews were documented in Chinese and in English. Our Chinese collaborators then presented their conclusions on occasions in late June and mid October 2006 in Shanghai. Each discussion included joint interpretations lasting for about 10 hours. The six cases were summarized in written form and the top managers/owners of the companies gave permission to publish the data and the conclusions.

7 THE CASES

Key data are given on the six cases in Table 1.The selection of companies is based on the four types of Chinese internationalizing firms found by Zeng & Williamson (2003), and the three major routes of internationalization identified by Child & Rodrigues (2005). The first route (original equipment manufacturer – OEM) and third route (organic expansion) are relevant for the SMEs studied. Three types are relevant: *Dedicated exporters* are entering international markets based on high quality and low price due to economies of scale. They have developed expertise in crucial technologies and are focusing on a few standard products sold to high-value segments. Competitive strength is based on manufacturing excellence, low costs and high economies of scale. Their main handicap still lies in a lack of experience in servicing markets where product choice or service is critical for success (Zeng & Williamson, 2003). This category is interesting as an export model for the future growth of present day private smaller firms. Three such MEs are included in the study, namely: two in the engineering industry; *Shanghai Ya se lan Advertising Material Co. Ltd*. that make large inkjet printers, and *Far East Cable Co. Ltd*. in Yixing (Jiangsu) and *Shanghai Green Valley* in the pharmaceutical industry.

Becoming a dedicated exporter is also an opportunity for a SME belonging to a competitive network to export large-quantity commodities, such as clothing, toys, kitchen equipment, shoes, and tooth brushes. The companies are often family owned, have organized themselves in networks, and count for very large parts of the world market share in what they are producing. There are many such export clusters in China, each made up of hundreds of small entrepreneurial companies located in one geographical area and operating as a cohesive, interdependent entity. The competitiveness is based on low-cost production and flexible adaptations to quickly changing markets, and their weakness is marketing (Zeng & Williamson, 2003). Two cases belong to this category. One is the *Yangzhou 5A Brush Industrial Co. Ltd*. located in Hangji, the city of the toothbrush in China. Another such mid-sized family firm is the *Suzhou Xing Xin Knitwear Co. Ltd.*, which is also classified as an OEM. Such firms are rather defined as being involved in original design manufacturing (ODM), since it is a better expression for the route as well as their specialization. This route mainly stands for the passive supplier and foreign buyer driven internationalization processes of most Chinese family firms.

Name of company	**Yangzhou 5A Brush**	**Xing Xin Knitwear SoZhou**	**Far East Cable**	**Green Valley**	**Yesalin Hi Tech Shanghai**	**Sun Tech Wuxi**
Preconception /types	Competitive Network CN HTO	From a cluster. Original Equipment (Design) Manufacturer OEM (or ODM) HTO	Dedicated Exporter HTO	Dedicated Exporter HTO	Dedicated Exporter HTO	Born Globals VTO
Products	Tooth brush	Knitwear	Cables pipes, wires engi-neering	Eastern medical herbs	Printers	Solar cells
No of starters /founders	1	2	2 now 1	1	1	1
Founder´s earlier experience	10 years in tooth brush Business	Ni	From forestry business	Ni	Teacher in mathemati cs	Researc her PhD
No of Employess	1.500	1.500	3.600	4.000 (3.200 on sales)	80	2.000
Turnover mill Yan	90	80	530	Ni	Ni	2.800
Export share	80%	Ni	Ni	3 %	60%	90%
Company age	13	20	10	9	13	4
No patents	180	Ni	Ni	74	Ni	More than 20

Table 1: Basic data on the cases in the summer of 2006. Ni = no information is available

Technology upstarts are mainly using innovations developed by the government’s research institutes to enter emerging sectors such as biotechnology and the computer industry. Scientists are increasingly encouraged to become entrepreneurs, increasing the number of scientists and business managers that come back to China. One such Chinese technology upstart is taken up in this article, namely *Wuxi Suntech*, which is growing rapidly in global markets by selling solar cells. This firm is a well-known success story, e.g. being seen as one

of the most promising start ups in China. The owner and entrepreneur is among the richest individuals in China (The Wall Street Journal, 12-10-2006).
The study is limited to SMEs from the region around Lake Taihu, which is centrally located in-between the three major regions of the Yangtse River Delta Region (YRD): Shanghai, Hangzhou, and Nanjing. The YRD is, along with the Pearl River Delta, the most internationally dependent region in China. It is an important growth engine due to its wide and deep industry structure and very good infrastructure.

8 MAJOR FINDINGS

The take-off process of each of these six cases will now be analyzed. First their development on the local Chinese market or their domestic market focus is discussed to see how their potential for international business emerged with the sources for competitive advantage being developed. This is followed by an analysis of the initial stages of the internationalization process of the firms involved in horizontal take-off. Finally the vertical take-off process is taken up. To illustrate critical parts of the take-off process, suitable examples are included from the case study data bank

8.1 The Horizontal Take-off Process

8.1.1 First stage: Domestic Market Focus

The development of competitiveness in the local Chinese market preceding internationalization takes place in different ways. Three companies selling to firms in business markets represent a more ordinary path of coming from a more nation-wide industry base, viz. *Far East Cable, Shanghai Ya se lan Advertising Material Co. Ltd., and Green Valley*. *Yangzhou Brush and Suzhou Xing Xin Knitwear Co. Ltd*, on the other hand, come from a geographically concentrated base, a local industry cluster or competitive network.

National Industry Base

The development of sources of competitive advantage for international markets in the horizontal take-off process initially takes place on the domestic market inextricably linked to local market development. This is first described for *Far East Cable*, where the industrial market and competitiveness developed in the following way. Cable industry is a key industry in China, since it supplies a strategic component to many industries. The market structure concentration changed from a high level at the end of the 1970’s to a moderate level at the end of the 1980’s.

The key establishment of the market took place in the next stage, which lasted to about 2005. During this expansion stage, the market structure became highly fragmented with a very low concentration ratio. The output share of the SOEs was gradually reduced through privatization. While the share of the SOEs had come down to 4 % at the end of 2004, it increased from 40 % to 70 % for private firms. The big SOEs were broken up, and the number of firms in the market grew to about 5.000, mainly small companies. This resulted in severe overcapacity. The low entry barrier created a disorderly competition with variable quality, fierce price competition and a low business morale including counterfeiting, and rough making.

The next stage started in 2005, being indicated by a stabilization of demand, which is also became more quality oriented. Some companies now rely more on the development of science and technology for their competitiveness. The cost pressure is unprecedented through heavily increasing raw material prices, which causes the very fragmented market structure to start to change. Even if a few local Chinese companies started to export during the former stage, the motivation to go abroad became more real during the stabilization stage. One contributing factor was that the government began to urge and promote firms to internationalize.

Yaselan's market is also found in the beginning of such a more mature stage. Under the pressure of brutal low prices and low profit margins, the core competitiveness of enterprises and barriers were switching to competitiveness being gained from management, scale, brands and services.

8.2.2 Second Stage: Pre-Export Stage

A main window to the world is the Guangzhou Trade Fair, with customers paying in foreign currency. This is how the international business started for all firms except the Technology Upstart Suntech Power. The take-off drivers are analyzed for all cases below.

8.2.3 Third stage: Indirect Export Stage

Far East Cable is a typical representative of a firm starting its internationalization in the indirect export stage through developing relationships with domestic contractors engaged in power projects abroad, mainly in developing countries. So far, direct exports to middlemen located in foreign markets account for only a small part of the overseas business.

5A Brush also took advantage of the network resources of the Chinese foreign trade companies. Orders were taken in the Guangzhou Fair and exported through Chinese trading firms. The firm communicated with foreign agents and dealers, mainly prior to delivery to settle time, amounts, colours, types, place, and the qualities. Customer relationships were developed by communication at the Fair, mutual visits, and field trips. Business and information support was received from foreign dealers and suppliers. Thus 5A Brush did international business passively and was chosen by the international market.

Suzhou Xing Xin gained its foreign trade operations primarily through the development of friends' and business partners' relationships, i.e. through using the social 'guanxi' network of major individuals within the firm, e.g. the chief managers over 10 years of experience in the industry led to many relationships being established with foreign trade companies.

8.2.4 Fourth (or Third Stage): Experimental Export Stage

Suzhou Xing Xin has partly moved further into the experimental export stage. The leader also had a friend in a local silk company, who knew some foreign trade companies in Hong Kong. In 2004, they together visited four of these companies. Relationships were developed with two, through which the firm came in contact with clients in Europe and America, and which led to Xing Xin developing business with them. Relationships had now been established directly with parties in foreign country markets through its own channel, the firm having begun with direct exporting.

The main reason for developing the international business through direct exporting is the low profitability of indirect exporting. More profits are earned from the simpler models and larger quantities of European and U.S. orders. Between 2004 and 2005, exports to the Japanese market was reduced from 98 to 87 % and increased to U.S.A. from 2 to 13 %. The company has adjusted its organization somewhat to export directly by enlarging the production workshop, and investing 10 million RMB in new workshops and plants.

The *Yaselan* case illustrates how the take-off process occurs in conjunction with increasing sales on the domestic market. The international operations began in 2002, using the Yaselan brand. Many foreign companies established a strong competitive force in China, getting Yaselan to continuously improve its technology. The company establishes new business relations to purchasing traders of foreign countries, and through participating in domestic and foreign professional exhibitions. The chairman of the company goes abroad to visit regularly, mainly to understand the development of overseas market, discuss the sales achievements of the products, help customers solve problems and discuss the direction of future improvement. The company sets up sole agents, most recently in Japan, Australia, and some Asian countries.

Although only so far exporting 3 % of its total turnover, *Shanghai Green Valley* has come further in the internationalization process than the other firms involved in horizontal take-off. Being in one of the most traditional Chinese industries, namely Chinese herbal medicine, it could start to export from a well-established base in the domestic market, and get government support. It mainly exports its herbal medicines and health care products directly to Chinese dealers abroad by using the overseas Chinese business network. One major aim is to spread the culture of Chinese herbal medicine. The international engagement has increased further since 2004 by the establishment of about 30 clinics for diagnosis and treatment, in particular of cancer patients. This has been done in cooperation with local partners and medical workers, mainly being located in places with large Chinese populations. The drug SunRecome is mainly exported abroad, which is a prescription drug used by cancer patients. The expansion plan is to establish an international system for medical treatment and management all over the world, opening 21 new special treatment chains over the next two years.

8.3 The Vertical Take-off Process

The business of *Wuxi Suntech* was first developed in the international market and then on the domestic market. The reason is that this industry did not exist in China at the time of the start of the firm. This is not uncommon in emerging country markets, which are latecomers in hi-tech industries. With China as the production base, most activities of the value chain have been developed internationally in a rather short time: marketing of solar cells and solar moduls, R&D, purchasing, and financing. There is also some foreign ownership. A few critical collaborations even existed long before the company started. The internationalization process follows the pattern described above for the other family firms. However it is direct, faster, and more comprehensive, also involving the two remaining stages of active involvement and committed involvement. For example, a main forum for building networks exists in trade fairs abroad, since no such fairs exist in China. Long-term collaboration agreements have been established with key international suppliers and two Chinese suppliers bought. R&D centres have been established in Australia and China, a sales subsidiary in U.S.A. and a sales network acquired in Japan. After five years of development, Suntech has developed a global brand in the PV solar cell industry. A marketing network and technology network have also been established, each covering the five continents. In 2006, 90 % of the turnover is international sales and 10 % domestic sales.

9. ANALYSIS AND DISCUSSION

Based on the empirical data collected we will now provide some evidence on the features of the six cases. We will start with the take-off process, then analyze the exit strategy, and finish with the drivers of the strategy and take-off process.

One case of vertical take off and five horizontal take offs were found, and where indirect exporting is done by all the firms studied except Suntech Power.

A major condition for HTO is that the firm first *develops competitive advantages in the domestic market*. This indicates that firms in emerging country markets normally first need to develop a better domestic market focus before they can export. How this occurs is highly dependent upon how *local markets* and competition develop. Most SMEs studied belong to industries that have moved through an expansion phase of the market, where a first stage of an oligopoly like situation consisting of a limited number of mostly state-owned enterprises was replaced by a considerably larger number of mostly privately-owned large and small companies, creating and intensifying competition. In the next and third phase, the market is consolidated, resulting in a shake out of firms. The ‘wild’ and fragmented market of the second stage is beginning to be turned into a more adolescent and ‘tamed’ ‘Western’ type of market consisting of a more limited number of competitors of both national and foreign origin. Rivalry is changed from being domestic to being global as well as from being supply driven to being demand driven. Market driven competitive advantages start to develop in the second phase, where intense price competition leads to firms developing strong cost advantages. Differentiation advantages are mainly developed in the third phase, when competition on quality becomes more important, firms investing in more advanced technologies, R&D and brand building. The internationalization of the MEs often takes place in conjunction between increasing sales and development of the domestic market, which is explained by the typically growing market of an emerging country such as China. Internationalization in the first phase is almost entirely driven by government policy.

In the beginning, *the export mode* is indirect. The producer uses a domestic representative, often a trading company, as a sales outlet for the foreign market. The sales usually take place in international market places located in the home market, mainly trade fairs. Most triggers to internationalize in the pre-export stage also come from these fairs. In the indirect export stage, the producer never leaves home and has no direct relation with the foreign country market. Further internationalization takes place through direct exporting, building on the experience gained through indirect exporting by starting to sell directly to parties in the foreign country market. Such firms tend to rapidly pass through the experimental stage, and reach the active involvement stage. The main reason is that these firms already have a large part of their sales abroad and can build on the indirect international contacts created and international knowledge gained in the indirect exporting stage, making it possible to more quickly increase the resources dedicated to international business. Indirect exporting takes place though horizontal take-off, i.e. through a traditional internationalization process. Judging from this study and research on firms that become international from inception, vertical take-offs take place through direct exporting, in this study by *Suntech Power*.

Even that 80% of the tooth brushes from *Yangzhou 5A Brush* goes on export they have not reached further than the indirect export stage, and are moving into the direct export mode. *Far East Cable* is in a similar situation but represents another type of indirect export route, namely piggy-backing. This exporter is riding on the customers’ foreign contacts, being a supplier to them mainly in neighboring countries in Southeast Asia, thus markets with less cultural distance. The firm is internationally small and has not yet many own international contacts. It has had to focus on its survival and manage under high uncertainty. It balances between what the government directs and own intentions by flexibly adapting to various market actors. Skillful leveraging of relationships by using exiting networks to establish new relationships plus the entrepreneurial style of *Xing Xin* have enabled this ODM company to reach a little further into the direct experimental export stage. Lately, one part of the strategy is to create own patents to increase the technological level. The same process also goes for Yaselan. A vital common factor is they are private family firms driven by strong entrepreneurs.

The take off process varies with type of *industry*, which is clearly seen in the case of *Shanghai Green Valley*. Coming from a traditional Chinese industry, it could start to export directly to firms abroad from a well-established base in the domestic market, and getting government support. The firm has also come further in the internationalization process than the other firms involved in horizontal take-off.

To be able to change from indirect to direct exporting and *move further along the internationalization process*, the SMEs need to develop differentiation advantages, their identity, and to re-organize. The firms experience is interpreted to experience high uncertainty during the take-off phase, which is reduced through organizational learning and reduced institutional distance. The problems in changing a domestic to an international learning platform are easy to infer from the study, illustrating the difficulties involved in learning about new and foreign markets in order to break this major institutional barrier. Institutional distance plays a significant role, since firms start with institutionally close markets in Southeast Asia and Japan, and use the Chinese business network as much as possible. In addition, they seem to follow the domestic market behaviour in internationalization, e.g. by relying on networking. This confirms the idiosyncratic foreign investment behaviour of mainland Chinese firms found by Buckley et al (2007b).

The *external push drivers* for going abroad from the pre-export stage were support from government, lack of local funding, overcapacity, low profitability, and intense competition. *The pull drivers* originating abroad were growing global markets, more interested foreign partners, and cooperative local partner companies. The *internal drivers* were asset-seeking (mainly brand building and acquirement of new technology), strong entrepreneurial drive, flexibility, and too low profitability.

The analysis above is summarized in Table 2.

Yangzhou 5A Brush	Only Guangzhi contacts				Global demand for cheap products	Branding and standard setting through patents	Has branded differentiated products
Far East Cable		Domestic clients ref foreign projects				Government stimulates export	Has high quality products and services. Patents
Xing Xin Knitwear SoZhou			Sold via friends to Japan		Global demand for high quality products		Entrepreneurial Spirit. From ODM to ODT
Yeasalen Hi Teck Shanghai				Learnt from many exhibitions	Global demand. Agents and distributors available		Entrepreneurial Spirit
Green Valley				Many own service centers and many end consumers	Chinese diaspora	Government stimulates Chinese herbal medicine	Has drugs for cancer treatment
SunTech Wuxi				R/D centers in Australia	Global Demand	Government funds research	Entrepreneurial Spirit. Own R/D, patents and brand
	First stage: Domestic market focus	**Second stage: PreExport stage**	**Third stage: Indirect exporting**	**Fourth (or Third) stage: Experimental Export**	**External pull drivers**	**External push drivers**	**Internal Drivers**

Table 2: The six cases analyzed

10 MAJOR CONCLUSIONS

1. The empirical results of the study are mainly representative for exporting SMEs belonging to the Chinese family business system or more specifically for dedicated exporters, competitive networks, and technology upstarts. The study therefore complements the previous studies made by Zeng & Williamson (2003) and Child & Rodriguez (2005).
2. The VTO differs a lot from the HTO. E.g. VTO starts with direct exporting, and the firm moves quickly through the other stages to committed involvement.

The remaining conclusions concern SMEs involved in HTO:

3. Various external and internal factors drive the firm to start to export, mainly using the indirect export mode. From here, four SMEs gradually started to go abroad by moving to the experimental stage through selling directly to parties in the foreign market.
4. Exporting started with first developing relationships with firms at home that could re-sell the products on foreign markets, mainly Asian. Movement to the next stage of the internationalization process therefore requires the build up of a critical mass of relationships. This shows that the network approach to the internationalization process is relevant for Chinese firms.
5. The internationalization of the SMEs took mainly place in conjunction with increasing sales on the domestic market, which is explained by the rapidly growing market of an emerging country such as China. This joint foreign and domestic expansion is also typical for later internationalization stages.
6. There is always a unique combination of various drivers in the take-off process to go from the first to the third, as well as going from third to the fourth stage.
7. The lack of internationalization knowledge is a major hurdle in the different stages. E.g. this seems to be the major reason why firms have problems to leave the domestic market by getting out of the indirect exporting stage and start to build direct international relations in the experimental export stage.
8. Chinese diaspora networks and similar cultural factors facilitate internationalization. Again, networks or clusters are key factors of the internationalization process.
9. The horizontal take-off, representing the traditional internationalization process, occurs when institutional distance is reduced, thereby decreasing uncertainty. It mainly takes place within the Chinese business network. The problems to come further in the experimental export stage from the indirect export stage indicate that it is hard to break through the institutional barrier between Chinese and non-Chinese business networks.

11 FURTHER RESEARCH

The last conclusion is similar to the major result found by Buckley et al (2007b) and Deng (2004) about the idiosyncracies of Chinese FDI. The export behaviour of Chinese SMEs also seems to be highly influenced by policy formulation, marketization and political risk considerations. In this paper, it was mainly demonstrated the critical importance of how the domestic markets emerge for the possibilities to develop competitive advantages that hold abroad.

Regarding political risk, we build this study on a broader uncertainty concept based on institutional distance. A further elaboration of the institutional distance as a theoretical construct in internationalization theory therefore seems vital. It is more suitable for developing the institutional aspects of FDI theory to better explain the three major idiosyncratic determinants of Chinese FDI found by Buckley et al (2007). However, even more important is to find better indicators for existing constructs than those used based on official statistics.

Another suggestion for further research is to reformulate the conclusions into testable hypotheses. This would require more studies of institutional determinants of the take-off process and the internationalization process in general such as government, banks, provinces/municipalities, large trading companies, and industry and trade organisations.

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