

Title: A theoretical perspective on the internationalisation of “born globals”, “traditional SMEs”, “backsourcers”, and “born regionals”

Abstract

Today's research in the SME sector (small and medium-sized enterprises) is lacking a fitting framework of analysis to interpret the recent international activities. Economic internationalization theories explain the existence of international trade and multinational enterprises, process-related internationalization theories try to catch the transformation of organizations across borders. They cannot catch the internationalization processes of small and medium sized enterprises (SMEs) from inception. Modern empirical findings show worldwide that SME internationalization modes are not path-dependent, neither emergent nor incremental. Yet the current SME researchers still use stage models and learning-based stage models or network approaches to explain SME action patterns. But even discontinuous stage models can not cover the range of phenomena such as: “Born Globals” or “Instant Internationals”- traditional SMEs, who enter the international field or are successfully operating in foreign countries -, “Backsourcers”, who re-concentrate their international activities back to the home base, and “Born Regionals”, who gain their force out of the local embeddedness and never shift capacity beyond export activities. This shows an urgent need for a further improvement of internationalization theories.

1 Introduction

While economic internationalization theories explain the existence of international trade and multinational enterprises, process-related internationalization theories try to catch the transformation of organizations across borders. But can they catch the SME internationalization processes, too?

Modern empirical findings worldwide show: SME internationalization modes are not path-dependent, neither emergent nor incremental (Kinkel, Lay & Maloca, 2007; Schulz, 2006; Fernandez & Nieto, 2005; Cutura, 2005; Alon, 2004; Gankema, Snuif & Zwart, 2000). Yet the current SME research field still uses stage models and learning based stage models or network approaches to explain SME action patterns. But even discontinuous stage models can not cover the range of phenomena such as: “Born Globals” or “Instant Internationals” - traditional SMEs, who enter the international field or are successfully operating in foreign countries -, “Backsourcers”, who re-concentrate their international activities back to the home base, “Born Regionals”, who gain their force out of the local embeddedness and never shift capacity beyond export activities. Today's SME research is lacking a fitting framework of analysis to interpret the recent international activities. The SME research field is in urgent need to fill this theoretical gap with an appropriate approach, which focuses on the size of the enterprise. The concentration on an independent theoretical concept of SME and internationalization is essential and indispensable. In the SME research applies, however: “Size does Matter“ (Wincent, 2005; Audretsch & Elston, 2000; Spence, 1999). First

theoretical approaches fail to explain the full range of SME internationalization processes (Schulz 2007; Bell, McNaughton, Young & Crick, 2003; Smolarski & Wilner, 2005).

Structure and aim of this paper is to cover the current state of research on empirical findings of different SME internationalization patterns to show the evidence that they are not covered or only partly explainable by stage models, network approaches or other theoretical frames.

2 Internationalization of “Born Globals”

Knight and Cavusgil (1996) give the following definition of “Born Globals”: “*Born Globals are small, technology-oriented companies that operate in international markets from the earliest day of their establishment*” (p. 11). An “International New Venture” (INV) is defined similar to a born global firm as a “*business organization that, from inception, seeks to derive significant competitive advantage from the use of resources and the sale of outputs in multiple countries*” (Oviatt & McDougall 1994, p. 47). The two expressions “Born Global” and “International New Venture” will be used here as synonyms. Rennie (1993) describes “Born Globals” as competing on quality and value created through innovative technology and product design. Such firms are usually founded in knowledge-intensive industries and tend to be highly specialized. The specialization of SMEs is necessarily associated with a reduction in the size of the available market. The core capability of “Born Globals” must therefore be expected to be narrowed and focused (Madsen & Servais 1997, p. 577). Thus, they may find it necessary to expand overseas to take advantage of the skills already developed in their home market, as well as to finance their significant R&D outlays. It is not surprising that technology appears to be a critical component of the internationalization of newly created high-technology SMEs. For these firms, given the rapid rate of obsolescence of innovations, the drive towards foreign markets to exploit their know-how as quickly as possible emerges as an absolute must (Fujita, 1998, p. 58). Madsen and Servais (1997, p. 580) as well as Borghoff (2005) suppose that the phenomenon of “Born Globals” is not limited to high-technology industries, as it has generally been indicated in literature. Also specialized assortments of low-technology products adapted to homogeneous niche segments in many countries, and even trading companies may be cases for “Born Globals”. On the other hand, the mere participation in a new high-technology industry does not mean that start-ups are international from inception. Especially firms in service industries (like internet firms or software consultants) encounter high barriers to internationalization because of the importance of reputation, ‘front-room activities’, and embeddedness in their personal and business networks that are typically still local (Kotha, Rindova & Rothaermel, 2001; Borghoff & Welge 2000).

Smaller firms lack the resources to compete on equal terms with large enterprises. They must rely on their knowledge of specialized, relatively narrowed product niches in order to succeed. Additionally, these companies must internalize the right combination of facilitating technologies, international business know-how, and access to appropriate contacts abroad. Much of the learning associated with this process results from being linked to information networks, both at home and abroad (Knight & Cavusgil, 1996, p. 23). Many entrepreneurial firms, including family businesses, can overcome that disadvantage of small size through their use of technology, such as the internet, to reach consumers beyond their borders. Along with entrepreneurial and managerial characteristics, the application of technology was found to be a key factor to explain internationalization of new ventures (Davis & Harveston, 2000, p. 110; Gallo & Pont, 1996).

“Born Globals” have existed most of the time in economic globalization. Examples are the famous East India Company that was chartered in London in 1600 or the Ford Motor Company that also can be assumed to have been an international new venture at its founding in 1903 (Wilkins & Hills, 1964). Since the late 1980s, however, their number has been continuously increased (Knight, 2000, p. 2; Oviatt & McDougall, 1994, pp. 45-46). Case studies have begun to appear from scholars of entrepreneurship. Some of them have shown that such ventures form because internationally experienced and alert entrepreneurs are able to link resources from multiple countries to meet the demand of markets that are inherently international (Coviello & Munro, 1992; McDougall & Oviatt, 1991). This development can basically be traced to the increase in innovations of information and communication technologies and the resulting decrease in global information and communication costs. Linked with decreasing transport costs, this leads to a shrinking global economic space. For information-based products it leads even to an economic space with zero-time distance. The increasing homogenization of many markets in distant countries has made the conduct of international business easier to understand for everyone (Hedlund & Kverneland, 1985). The conclusion is that increasing numbers of business executives and entrepreneurs have been exposed to international business. International financing opportunities are increasingly available and human capital is more internationally mobile (Oviatt & McDougall, 1994, p. 48).

Madsen and Servais (1997, p. 38) propose that studying “Born Globals” should base on a time perspective which extends beyond their foundation. Probably, many of its “genes” have roots back to firms and networks in which the founder(s) and top managers gained industry experience. Compared to traditional new ventures, “Born Globals” already are instilled with organizational routines, decision rules, and capabilities that are not depending very much on any local or national borders but were gained in the global context. Routines, decision rules, and capabilities can be considered as the ‘genes’ of an organization (McKelvey, 1978). Instead of being tied to geographical markets, these genes may be tied to a certain specialized, value-adding processes, which the firm solves in the particular, internationalized industry. “Born Globals” have direct access to global networks, knowledge and markets right from the start while traditional firms need a development process to explore such global resources.

Oviatt and McDougall (1995) discovered early that the most important characteristic associated with success is probably that the founders of a global start-up develop and communicate a global vision: To become global one must first think globally. Every global start-up they investigated had internationally experienced founders or top managers, and every person interviewed believed that was a necessity. The initial inspiration for many of the ventures studied came from the international experience of its founder. Calof and Beamish (1994) suggest that an individual’s geo-centricity is associated with international experience. Internationally experienced management teams therefore are viewed as a key resource that influences SMEs to engage in behaviors leading to a greater degree of internationalization (Reuber & Fischer, 1997, p. 820).

McDougall, Shane & Oviatt (1994, p. 479) argue that entrepreneurs are people who “are alert” about potentially profitable resource combinations while others are not. Research has further shown that this alertness to new business opportunity is influenced by previous experience (Casson, 1982; Ronstadt, 1988) because that experience provides a framework for processing information. McDougall et al. (1994, p. 479) assume that founders of INVs are more alert to the possibilities of combining resources from different national markets because

of the capabilities they have developed from earlier activities. These entrepreneurs possess an unusual constellation of capabilities based on international experience and network resources. It is therefore argued further that only an entrepreneur who possesses these capabilities is able to combine a particular set of resources across national borders and form a given INV (McDougall et al., 1994).

For domestic firms, inertia becomes a problem because it inhibits a change to routines appropriate to international environments. International entrepreneurs, however, seem to recognize this, and therefore try to avoid domestic path-dependence by establishing ventures, which, at their inception, have routines for managing multicultural workforces, for co-coordinating resources located in different nations, and for targeting customers in multiple geographic locations simultaneously. In its simplest terms, the founders of INVs believe that ventures will not develop international capabilities except by practicing international business. Successful INVs have been shown to make measurable trade-offs among the risks inherent in the entered countries, the chosen entry modes, and the degree of foreign market dependence (McDougall et al., 1994, p. 481).

Johannisson (1995, p. 38) points to the importance of personal networking in start-up and internationalization processes. Personal networks include both social and business relationships, closely intertwined. In his research project, looking into the networks that young and prospective entrepreneurs build, Johannisson found out that the most important ties in the personal network are considerably older than the venture itself. This, in turn, supports the thesis that “Born Globals” dispose of international experience and networks from inception. Birley’s study (1985) on the role of networks in the entrepreneurial process concludes that entrepreneurs tend to come from smaller for-profit organizations and they tend to start similar businesses in the same location with previous colleagues as partners. The number of “Born Globals” therefore can be expected to rise as more and more professionals are embedded in global business networks. The choice of networks is a key factor in understanding the nature of the subsequent firm, because the elements of the firm are set during the start-up process (p. 115). An empirical study by Eriksson, Majkgard and Sharma (2000) proves that this kind of experiential knowledge develops from the beginning of internationalization activities and leads to the same kind of knowledge which is further developed in any subsequent internationalization. According to this study, experiential knowledge types that have not been developed at an early stage of internationalization are not developed later (Eriksson et al., 2000, p. 323).

Entrepreneurs use their personal contact networks to gain knowledge, and seek out and mobilize new partnerships that help the firm grow and expand into foreign markets. A corollary of the importance of social exchange in accessing and co-coordinating resources is that since face-to-face interaction, and social, cultural, and geographic proximity foster the trust needed to facilitate social exchange relationships. The local resource endowment is also important. This view of firm growth argues that entrepreneurs learn to leverage their capabilities by establishing dynamic linkages to other firms in their local production. In the course of internationalization, these network linkages are then extended to foreign markets (McNaughton & Bell, 1999, p. 66). According to Obrecht (1994, p. 27) it is the interactive combination of the “entrepreneurial resource” with the “network resources” that defines basically the strategic capacity of SMEs. Especially on the international level, the competitive position of SMEs depends on its network resources (Obrecht, 1994).

3 Globalization of traditional SMEs and “Backsourcers”

The traditional SME sector understood as the range of industrial processing branches today proceeds in a highly dynamic economic environment. Characteristics of this sector are the growing uncertainty in planning processes and the steadily increasing pressure of international competition (Kinkel et al. 2007, Schulz, 2006). SME entrepreneurs have to face upcoming uncertainties and adjust to the volatility of market demands. Therefore, many leave their well known export strategies and focus on new forms of internationalization. But the adaptation process is accompanied by essential risks because SME often lack financial and human resources and management know how to handle the global extension of their activities. Limited capabilities are aggravating the first steps into an intensified internationalization (von Behr, 2003). These obstacles may be handled if SME entrepreneurs are able and willing to extend their entrepreneurial, network, and evolutionary capabilities (Borghoff & Schulz, 2005 a & b). The following chapter is based on results of the empirical studies by Schulz (2007) and Schulte (2002) on the internationalization behavior of German SMEs.

For many traditional SMEs internationalization beyond export is still a new and unknown stage of business. Wallau (2006, p. 24) as well as Kokalj and Wolff (2001, p. 46) showed that still no more than one third of German SMEs are internationally engaged. And those who are, are mostly engaged through classical trade connections. Less than 20 percent have international experiences gained from co-operations or foreign direct investment projects. Therefore, the majority of SME entrepreneurs must develop innovative strategies to expand their economic performance. Their driving forces are generally motivated by cost reduction, access to foreign markets, follow-the-customer-pressure, and extension of the own knowledge base (Schulz 2006; Lay, Kinkel, Eggers & Schulte, 2001, p. 34). The SME executive level has to choose between different tactics and forms of internationalization to achieve cost advantages, a certain market size, customer favor, and learning.

Following the definition of the European Commission (The European Commission, 2007), an SME business does not include more than 250 employees. Typical for this size of an enterprise is the strong position of the entrepreneur or manager. It is generally the top level of the firm that envisions, prepares, and executes the decisions in the on-going internationalization process. Empirical evidence provided by Schulte (2002) show that the idea and its translation into world wide business activity are normally united in one person - “internationalization made by the boss”. The further engagement into foreign countries goes along with the daily routines of an SME entrepreneur and his or her usual business. This causes an extra load of tasks, which may easily culminate in an overload due to lack of time, experience, and/or international management know how. Other well-known and identified SME shortages in the internationalization process are the lack of language skills, intercultural know how and strategic awareness (Gibb & Scott, 1985; Zündorf, Heitbrede & Kneissle, 1993; Müller & Kornmeier, 2000). Typically, the entrepreneur is not aware of the need to develop new skills and methods but tries to handle the international business like “doing business as usual”. The own operational background and locally bound knowledge is transferred spontaneously to the foreign context without explicit awareness of stepping into radically new fields of work with special demands. This leads into two entailed positions: First, the internationalization process will be perceived as a rising pressure or even a burden, sometimes terminated by the experts because a concentration and intensive focusing on internationalization in terms of an “add-on” activity seems to be impossible. Second, as a way to handle this burden, SME entrepreneurs start to “muddle through” (Schulz 2007; Lay et al., 2001).

The internationalization and location process of traditional SMEs is influenced by (Schulz, 2007; Schulte, 2002):

- Coincidence (often personified as a new acquaintance of a foreign businessman, a new foreign employee with international contacts),
- The main customer (the setting of the planned location site is made by the main customer in case of an international follow-the-customer strategy),
- Supplier contacts (the location process is guided by well-known suppliers which are originated or already settled in the foreign market), and
- Identification of future main markets (location site and main future market are the same).

The traditional SME entrepreneurs often possess little “internationalization capabilities” in the very beginning of internationalization (Borghoff & Schulz, 2005 a & b). In short: The SME system is marked by the extension of the business without full awareness of the upcoming demands to plan and manage worldwide socio-economic relationships. Internationalization is mainly externally motivated by market or customer pressure. The main goal often appears to get along with the pressure and stress caused by an international decision with a minimum expenditure of resources on the analysis of the international conditions. The main objective is to make fast decisions (Schulz, 2007; Schulte, 2002). In this case, SME entrepreneurs take a very pragmatic way of planning and decision making. As emphasized by the interview partners, they “grab a chance”, make a decision mainly “from the guts” or leave the decision to someone else - the main customer, a new partner or an already known partner (Kinkel, Lay & Jung Erceg, 2004). These action patterns can cause severe problems in the emerging management of internationalization. Typical for the pragmatic SME way of globalization management is that the engagement - whether it leads to a successful or non-successful way of internationalization - can only be judged in a retrospective or “ex post” point of view. That does not mean that SMEs cannot internationalize effectively. But SME entrepreneurs take higher risks due to their resource and task situation. Even with growing international expertise the SME entrepreneur sometimes clings to the pragmatic path due to overhauling or missing division of labor. That leads to the assumption that traditional SMEs face a systemic disadvantage in the building-up of global capabilities if they cannot extend the international knowledge base from one person to a internal or external know how net. For final conclusions the roles and types of the SME entrepreneur need therefore further investigation.

Neither national nor international business exists out of itself. It is embedded in the strong network of weak ties (Granovetter, 1973), translated as the complex set of socio-economic relationships, traditions and supporting institutions. The awareness and conscious use of embeddedness in regional or international production networks can cause competitive advantages (Maskell, Eskelinen, Hannibalsson, Malmberg & Vatne, 1998; Hirsch-Kreinsen & Schulte, 2000). The described lack of international entrepreneurial experiences and capabilities often reappears in missing network capabilities of traditional SME leaders in the first steps of their globalization process. The management of production sites in the home country and abroad has to establish, stabilize, and co-ordinate relations and activities of at least two enterprises. It requires the willingness to accept the preconditions of a new set up of an international production chain. Thereby the international management complexity increases rapidly. So does the demand on co-ordination skills, new tools, and methods to build up trust and know how about the new internal and external environments and their special rules.

The management of more than one production site takes up a great deal of entrepreneurial energy. This collides with the conception of several SME managers that the foreign project is self-sufficient as soon as possible and with a minimum amount of effort. The idea often is to organize the necessary co-ordination work 'via telephone' or internet. Like a satellite once brought into space the new site should produce and deliver independently and on a stand alone basis. The international reality is quite different. The SME entrepreneurs have to establish and sustain management capacity abroad not only in the beginning of the new subsidiary and its network building process but constantly. Obstacles for internationalization newcomers are the following categories of management and network problems, which SME entrepreneurs did not consider in their past internationalization activities and thus caused unwelcome "surprises" (Schulte, 2002, p. 156):

- Development of the cost situation abroad (The focus on labor and land costs led to an underestimation of the total sum of direct and indirect costs of an international production net. Costs for substitutions of assets and machinery, qualification costs for employees, traveling expenditures for home staff that are needed abroad, etc. not have been considered.),
- Organisation (of information flow and controlling, processing, quality assurance, etc.),
- Staff situation (lacking management capabilities of foreign executive level, handling of different quality standards, training and working traditions such as absence, fluctuation, gender discrimination etc.),
- Breach of trust (manifested in a lacking perceived fit of business tasks or goals of the foreign management, in the worst case know how diffusion via theft or plagiarism),
- Missing supplier and service network (starting with missing repair services, replacement investment possibilities, suppliers of advance performances and main parts), and
- Non-transparent cultural and political background (of business methods and cultures, working traditions, institutions and administrative machinery).

The known business context of the traditional SME is imprinted by strong regional and national connections, and widened only by export experiences. The beginning international networking opens new space. SME entrepreneurs are foreign to the new environment and clearly perceive this. This demands attention and trust that can be built up and smoothed by proximity, not only spatial closeness but also on a personal basis. Internationally successful SMEs have developed this proximity through the creation of internal and external network interfaces. This means that the entrepreneurs managed to link and expand their business sphere on two levels:

- The business to business level (development of network capabilities between the home and the host country through the exchange of employees, shared trainings, and the creation of responsible interface positions that relieve the SME entrepreneur from the main task of pulling the net together or to build-up trust between the units),
- The local level (acquisition of local and regional knowledge about the embeddedness of the new business, the foreign educational and training system, business methods and routines, supporting institutions, research institutions, unions and employers associations, supplier nets).

Therefore global network capabilities describe a complex set of entrepreneurial competences such as:

- The skill to connect and integrate home and foreign business through trust and division of labor, and
- The ability to integrate in foreign socio-economic environment.

Key factors for the long-term establishment of a solid globalization trajectory are the development of local network positions abroad and of internal business co-ordination mechanisms that are based on a trustful relationship. SMEs, which cannot build up the necessary global networking capabilities, run the permanent risk of losing the control over the value chain and the on-going processes (Hirsch-Kreinsen, 2002). In the worst case scenario the SME runs the risk of insolvency and bankruptcy. The investigated cases provide a deep insight of cases of mismanagement or better expressed “mis-networking” that led to alarming business situations: entrepreneurs closed their eyes for the needs to interlink and make them familiar with the business atmosphere abroad. They fail to understand cultural differences and to adapt to them. Suffering from time pressure, many have not been willing or able to take the time to integrate the different units into one network. Consequences are negative experiences with internationalization that can cause dramatic business results or a retreat and revocation of the international engagement. Surveys show that up to 30 percent of German SMEs internationalization projects are totally or partly relocated to the home base (Schulz, 2006, p. 45; Kinkel et al., 2004, p. 29; Kinkel & Lay, 2000).

All firms, independent of size, have to cope with the evolutionary dynamics inherent in internationalization processes. Traditional SME entrepreneurs have to adjust to these dynamics or otherwise run the risk to miss international or business activities at all (Lay et al., 2001). The capability to be aware of the need to react, to change and to adopt in the adequate way is a matter of survival. Depending on the form and demands of the international dynamics SMEs can follow varying strategies of

- intensification (extension of the international engagement in terms of size, new forms or markets),
- alternation (change of the international engagement in terms of internationalization strategy, form or size), and
- back sourcing (closing down of the international business, temporarily or permanent re-concentration on the home base depending on local and regional production conditions).

SMEs can try to neutralize problems of evolutionary dynamics if they can enhance their entrepreneurial and network abilities. But the economic environment nowadays is turbulent and unpredictable. Traditional SMEs suffer a systemic disadvantage compared to larger enterprises because of their limited resource endowment. They operate with small capacities in management, personnel, and financial dimensions. Nevertheless the number of successful international SMEs is increasing due to the flexibility and innovative power to adapt to global demands. If they pass the critical stage of first internationalization beyond export, and gain experiences through the co-ordination of the cross-border productions chains, an international learning loop is initiated that enables SME entrepreneurs to build up the necessary know how. This learning loop pulls the separated meaning and action systems together, interlinks them strongly and enables to act more than just to react.

4 Conclusion

The development of successful border-crossing business activities can be termed “globalization” or “internationalization” as it is a process in which the firm learns to explore and exploit the differentiated world-wide environment. Path dependence in this context is the incremental process where the behavioral pattern of firms is based on its past international experience. But the traditional focus on “internationalization” in terms of a stepwise and

teleological expansion process beginning in the national and then sequentially in international contexts does not seem to cope with the complexity and reality of small and medium sized enterprises (SMEs). On the one hand, there exist “Born Globals” which are small, technology-oriented companies that operate in international markets from the earliest day of their establishment. On the other hand, traditional SMEs often operate in a worldwide unpredictable way. Empirical findings have shown that SMEs do not follow a common internationalization path or pattern in general. In fact they dislocate to and relocate from foreign basis. In this paper the current need for an internationalization theory targeting especially SMEs was therefore outlined.

“Born Globals” and traditional SMEs possess very different assets of international know how at the beginning of the internationalization process. The entrepreneurial, networking, and evolutionary dynamics capabilities are marked by the former experiences of the entrepreneurs. Whereas the traditional leader is imprinted by regional or national relationships and often lacks an international and intercultural background, the founder of a “Born Global” firm is already connected to the ties of an international network. “Born Globals” may profit from already established learning loops, which traditional SMEs have to set up for themselves. “Born Globals” may gain a time lead in the beginning of internationalization. The suggestion is that this gap will diminish with the on-going collection of experiences. Traditionalist may catch up with “Born Globals” if they do not step in existence threatening traps or are forced out of internationalization by external dynamics.

The latest empirical findings prove strong deviancies from classical international incremental stage models. The global learning loops enhance knowledge and capabilities of SME entrepreneurs via self made experiences and network ties abroad. Consequences are not necessarily an increasing internationalization of SMEs’ further actions. Alternation and also back sourcing can be part of the internationalization process. A higher level of global entrepreneurial, network, and evolutionary dynamics capabilities do not suggest automatically a more advanced stage of international engagement. Learning loops are not geographically directed. Learning and gaining know how opens business spaces without any spatial direction. The dynamic development of global markets can therefore also reopen the space for a local concentration at the home base. The awareness and use of regional business networks instead of global ones can result into newly gained network capabilities. This shows a need for a further improvement of internationalization theories. A central concern is the integration of existing theoretical approaches into a common, commensurable framework in order to cope with the complexity and dynamics of globalization.

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