Track 5. SMEs, international new ventures and international entrepreneurship.

Competitive paper.

THE SURVIVAL OF NEW VENTURES IN EXPORTING

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ABSTRACT

Firms that start to internationalize soon after they are established have attracted a lot of research attention. Still, not many studies have analyzed what happens to such firms over time (Cavusgil and Knight, 2015). In this paper, we look at the survival of exporters that start to export from 1 to 7 years after their inception. The data set consists of all companies in Norway established in 2003, which exported goods in the period 2003-2011. The dependent variable is exit from exporting in a specific year. Based upon theory and previous research, in particular Sui and Baum (2014), we hypothesize that profits, firm size, time from inception to export start-up number of export markets and export share of total sales influence the propensity to exit from exporting. Using a semiparametric Cox model the results indicate that only higher profits, a larger firm size, and a higher number of export markets significantly lower the propensity to exit exporting.

INTRODUCTION

The internationalization of firms may follow different patterns. It is a behavioral process, and the behavior manifests itself in a series of actions accumulated over time (Jones and Coviello, 2005). Exporting is the preferred mode of entry into foreign markets by small and medium sized firms, since it requires the least resources and the lowest level of risk compared to foreign direct investment (FDI). The internationalization theory primarily associated with Johannson and Vahlne (1977) envisages the internationalization process as gradual and slow. According to this theory, the managers suffer from a *liability of foreignness* and must gradually acquire more market knowledge by learning from experience. The experiential leaning will facilitate the discovery of new market opportunities as well as reduce the costs involved in operating in a

foreign environment. The liability of foreignness will be higher the larger the psychic distance to the market is, hence exporting will tend to start with the closest countries in terms of psychic distance. The risk of failure as well as the resources needed are lowest in such markets. As more experience is gained, the company will eventually move into more distant export markets and, perhaps, also into more demanding entry modes.

A large number of empirical studies have documented that the internationalization process is not always slow and gradual. Companies that internationalize rapidly after inception are referred to as Born Globals (Knight and Cavusgil, 2004) or sometimes as International New Ventures (Oviatt and McDougall, 1994). The Born Globals concept has been operationalized in different ways in empirical studies as illustrated in a recent review by Eurofund (2012). The variables typically used to define the BG type of company are a) the number of years from the company was established to it starts to export, b) the share of foreign sales as a percentage of total sales, c) the number of markets the company exports to. The typical BG starts to export fairly soon after inception, exports to several countries all over the world and achieves a high export share in a limited number of years. Lopez et al. (2009) has pointed out that many companies start to internationalize shortly after they are established, but only operate in neighboring countries. They refer to such companies as Born Regionals (BR), and they pursue a type of strategy different from both Gradual Internationalizers (GI) and Born Globals (BG).

Recently, research has started to look at the survival of international new ventures compared to the likelihood of survival for companies that follow a gradual approach. Mudambi and Zahra, (2007) used a sample of FDIs into the UK by non-UK companies to explore the topic, while Sui and Baum (2014) compared the survival rates for different internationalization strategies in

exporting using a longitudinal data set of Canadian exporters. The present paper also uses a longitudinal data set to explore to what extent different factors impact the survival rate of companies as exporters. In our case, the data set is obtained from Statistics Norway and it encompasses all companies established in 2003, which export goods at least in one of the years in the period 2003-2011. While Sui and Baum (2014) a priori distinguish between the three strategies IG, BG and BR, we argue that such a categorization is arbitrary and leads to a loss of information. Instead, we use indicators of available resources and experiential knowledge and analyze to what extent the values of such variables have an impact on survival rates. The results show that indicators of available resources like profitability and firm size have a positive effect on the survival rate. The same applies to the number of export markets, which we consider an indicator of experiential knowledge. The results also indicate that the earlier after inception a company starts to export the higher is the survival rate. Export share, on the other hand, did not have a significant impact on the survival rate.

THEORY AND HYPOTHESES

The decision to start exporting as well as the decision to exit from it, ultimately depends upon the economic resources available to the company and managers' view regarding future market opportunities. Experiential knowledge will influence the perceived opportunities. According to Shane and Venkataraman (2000) entrepreneurship is concerned with the discovery and exploitation of profitable opportunities. Such opportunities may be the innovation of new products and services, but it may also be the expansion into new foreign markets if managers perceive profitable opportunities. Thus, the initiation of exports into a new foreign market is a type of entrepreneurial activity. In general, a large share of new product innovations are not successful and therefore withdrawn from the market. It is likely that the same happens for new export ventures, especially if the company is recently established. It has been pointed out that

little is known about the ability of Born-global firms to remain active in international markets and the type of resources that determine their survival (Sui and Baum, 2014). According to Kuvalainen et al. (2012) there is limited research in general concerning the impact of different internationalization paths on long-term survival.

Operating in foreign markets incur costs, and may not immediately lead to profits. Still, it is reasonable to assume that the higher the profits of the company as a whole as a percentage of sales, the less likely it is that it will exit from exporting. If the company as a whole is making a profit, it will be able to tolerate a temporary setback in one or more export markets. Our first hypothesis is therefore:

H1: The higher the profitability of the company the lower is the propensity to exit as an exporter

Profitability is a result of factors on the supply side as well as the demand side. Another indicator of available economic resources is firm size. A large number of studies have investigated the relationship between firm size and various aspects of export behavior and performance. Calof (1994) argues that small firms typically concentrate on the home market, while larger firms may need to go abroad to benefit from economies of scale. Small firms will suffer from limited managerial and financial resources while this is less of an impediment for larger firms. His study shows a positive relationship between firm size and propensity to export in line with many earlier studies. Bonaccorsi (1992), on the other hand, underscores the competitiveness of many small firms based on product quality and flexibility and find a negative relationship based on his sample of Italian SMEs. This is in line with the Resource Based View (RBV), which maintains that the competitive advantage of firms resides primarily in a bundle

of heterogeneous tangible and/or intangible resources and not in scale economies. Esteve-Pérez et al. (2011) also found a negative relationship between firm size and propensity to export, while Williams (2011) in his study found the opposite. It seems fair to conclude that the relationship is not clearly in one or the other direction, but depends upon the composition of the sample analyzed.

While the relationship between firm size and the propensity to export is extensively researched, the relationship between firm size and the decision to exit exporting has received less attention. Sui and Baum (2014) found that firm size has a negative effect on exit from exporting, indicating that larger firms with more resources are better able to cope with difficulties that may arise in the export markets. Moreover, the effect of firm size differ depending on the type of export strategy chosen. Firm size has the strongest negative effect on the exit rate for Born Globals, followed by the Born Regionals. The effect of firm size on exit from exporting is the lowest for Gradual Internationalizers. This leads us to the following main hypothesis:

H2: The larger the size of the firm the lower is the propensity to exit as an exporter

Experience is central in most of the research on the internationalisation process. Cavusgil (1984) found that experience (expressed as number of years in international markets) is positively correlated with export commitment. This commitment is an inherent part of the internationalisation process of firms (Johansson and Vahlne 1977). Fletcher (2001, p. 43-44) concludes that “increased internationalisation centre[s] around management characteristics such as commitment and experience of employees with regard to involvement in international activities”. Experience is chiefly gained by actively operating in the market place (Johanson

and Vahlne 1990). Our main assumption concerning experience is that the more international experience, the less likely it is that the firm will exit from exporting. However, the mechanisms are not straightforward. In the following, we will develop arguments pertaining to experience before export market entry, and explore the role depth and variety of the export venture as proxies for experience in explaining exit from exporting.

The timing of international market entry has been studied by a number of researchers (Autio et al., 2000; Hagen & Zucchella, 2014; Zhou & Wu, 2014). The age at international entry is in fact one of the most salient features of INVs or Born Globals. The presumed lack of resources of firms starting to export soon after inception (Knight and Cavusgil, 1998) suggests that they are less prepared to take on the challenges of internationalisation than firms that have built resources and experience from their domestic market (Johanson and Vahlne, 1977). Given the high degree of uncertainty related to new ventures, compounded by the uncertainty of expanding internationally (Johanson and Vahlne, 1977 and 2009) , it is a fair assumption therefore that experience gained at home before export start-up would be beneficial for a late start-up of international expansion. Successful internationalisation concerns learning about markets and about the internationalisation process itself (Eriksson et al., 1997). The capacity to recognise *and* absorb - over a short period of time - new knowledge from overseas markets and to translate this knowledge into viable strategies is likely to be negligible for new ventures (Vermeulen and Barkema 2002). Furthermore, in BCG parlance, one may term the domestic market the “cash cow”, providing funding for expansion in international markets, the latter then representing the ”Question marks” in the BCG matrix (Henderson 1970). The hypothesis would then be that firms that have operated a certain number of years at home would have had time to test the product or service in the home market, and to build resources, experience and networks,

thereby enabling them more effectively to meet the challenges of export initiation and further internationalisation.

H3a: The later the newly established firm enters international markets, the lower is the propensity to exit exporting

On the other hand, the experiential knowledge acquired in the home market may restrain the firm's search for opportunities abroad and makes it less prepared to engage in exporting. More specifically, the longer a firm is operating in its home market the more its resources are committed to this market and the more the learning about idiosyncratic features about this market are being embedded in the organisation – including knowledge, routines and ways of thinking. This is in compliance with Hannan and Freeman's (1984) who state, "once such resources [capital, commitment, entrepreneurial skills, legitimacy] have been invested in building an organizational structure, they are difficult to recover" (p. 152) – or, in our context, to redeploy in other marketing settings. It has indeed been found that late export start-ups will encounter more problems because management is mostly concerned with their on-going domestic business operations, and will therefore not dedicate the same amount of attention or commitment toward the new export venture (Korth ,1991; Shoham and Albaum, 1995). The words of Johanson and Vahlne (1977, p. 28) of the importance of experiential knowledge providing "the framework for perceiving and formulating opportunities" are also valid in the domestic market – in this case constraining the range of opportunities in international markets.

Consequently the less prepared the firm will be in meeting the challenges of operating internationally, leading us to the following competing hypothesis:

H3b: The earlier the newly established firm enters international markets, the lower is the propensity to exit exporting.

Sui and Baum (2014) found that the effect of firm size was moderated by the type of export strategy; the effect of firm size was most pronounced for firms that internationalized early (Born Globals and Born Regionals). Based upon this we hypothesize that such an interaction effect exists in general:

H4: The effect of firm size on the propensity to exit exporting is moderated by the time it takes from the firm is established until it starts to export.

In the same vein, we conjecture that the more markets the firm is active in, the richer is its learning on the internationalisation process. The variety of situations encountered in multiple market settings tends to make perceptible imprints on the organisation and its members. The experiential learning is therefore likely deeper and more resilient. Eriksson et al (1997) found that (local) institutional and business knowledge are critical in the internationalisation process. They observe that the more experience the firm has in the process of internationalisation, the better equipped it is to acquire business and institutional knowledge in individual markets. They furthermore suggest that "it seems reasonable to regard it as a kind of procedural knowledge concerning, for instance, what kind of knowledge a firm needs in different situations" p. (352). Erramilli (1990) finds that number of markets the firm is involved in explains the choice of entry mode into new markets (implying that this choice be more efficient). We infer that the diversity of information and experience gained in multiple markets help the firm to

better approach the challenges posed by international market entry, thereby reducing the risk of exit from exporting.

In addition to the learning aspects, it is reasonable to assume that if the firm is active in many markets it is less likely that a local setback in one or a few markets will make it quit exporting in general. Hence:

H5: The more export markets the newly established firm enters, the less likely it is that it exits exporting.

Export share of total sales has been one of the defining variables of BGs (Oviatt and McDougall, 1993; Knight and Cavusgil, 1996), and has been used as one of several indicators of export success (Cavusgil and Zou, 1994). Whereas export ratio may undeniably convey the message of success of the firm, it may also represent an expression of depth of the firm's experience from, and of commitment to operating abroad. Commitment to the export venture is seen as both an outcome and an integral part of the internationalization process leading to increased market investments, and thereby enhanced market experience and learning (Johanson and Vahlne, 1977, 1990). One may furthermore claim that the greater the part of total sales is devoted to foreign sales, the more attention it will attract from senior management of the firm. The dependence on export markets will therefore instill management to invest further in export operations in order both to safeguard and to develop further the firm's position in the

market place. We believe that such investments make the firm less vulnerable to potential failures in foreign markets. Hence, we posit:

H6: The higher the export share of the firm's sales the less likely it is that the firm will exit exporting.

EMPIRICAL STUDY

Data

To analyze the determinants of a firm's ability to remain active in the export market, we constructed a data set from two of Statistics Norway's existing databases, namely their database containing Structural Business Statistics (St) and the National Register of Establishments and Enterprises (BoF). The structural business statistics describe the economy through the activities of units engaged in economic activities, including the external trade of goods and services. The national register is Norway's index of all enterprises (juridical units) and establishments in the private and public sector in Norway. It contains variables describing each Norwegian enterprise's contact details, legal form, people involved and their managerial roles, their main economic activities, number of employees, etc. For the purpose of this paper, we have decided to focus on goods exporting firms established in 2003. After deleting firms that are only active for one year, we have a sample of 1,112 firms left, which we use in the analysis. These firms are active in different industries, but predominantly in wholesale (55%), manufacturing (18%) and real estate (11%), respectively.

Measures

Dependent variable

The dependent variable in this study measures a firm's exit from exporting. More specifically, this variable is coded 1 in the year a firm stops exporting and 0 otherwise. Each firm is tracked from its year of establishment (2003) to the year in which it exits or to the end of observation period (2011). Observations for firms that stop exporting after 2011 are right censored. The data on export survival is constructed from several databases that are set up and maintained by Statistics Norway (please see the previous section). When a firm is not present in the export statistics this may be because 1) the firm itself ceases to exist (through bankruptcy or acquisition/merger) or 2) the firm stops exporting. Based on the available data, we unfortunately are not able to distinguish between those two types of events and we treat them similarly, namely as an exit form exporting.

Independent variables

Profitability is measured as the ratio of earnings relative to sales. This variable is lagged for one period, meaning that a firm's current ability to remain active as an exporter depends on its profitability one year earlier. *Firm size* is defined as the number of persons (rather than FTEs) a firm employs one-year prior to the observation for the dependent variable. *Time to market* is the number of years that pass until the firm starts exporting after its inception. This variable does is not vary with time and is thus constant over the whole observation period for any particular firm. A firm's *export share* is defined as the sum of sales in all its export markets divided by total sales in the same period one year prior to observing the dependent variable. Finally, the variable *number of countries* indicates the number of markets a firm is exporting to the year before the dependent variable is observed.

Model

We employ a semiparametric Cox model to investigate which variables determine a firm's propensity to stop exporting. This model is one of the most widely used methods for modeling firm survival (see for a recent example Sui and Baum 2014). More specifically, the model estimates a firm's individual hazard or risk of export exit at time *t* as follows:

$$HAZARD_{it} = H_t * \exp(\beta' X_{it}),$$

in which H_t is the baseline hazard at time t (analogous to the intercept in ordinary regression), X_{it} is a vector of independent variables that may affect a firm's export survival and β is a vector of regression coefficients. These coefficients measure the proportional expected change in the hazard rate in response to changes in the independent variables. We estimate the models using the coxph() function in R (currently part of the R package survival), which estimates the model using maximum likelihood.

RESULTS

The pairwise correlations between independent variables do not show high interdependence (Table 1). The highest correlation, between firm size and the number of export countries, is .28. Hence, multicollinearity does not appear to be an issue. The results of regression analysis are reported in Table 2.

Table 1 and 2 about here

Those results indicate that the firm size has a negative effect on the propensity of export exit ($\beta = -.023; p < 0.01$). This means that if a firm is larger, it has a smaller tendency to stop exporting. In addition, we find that if the firm's profitability ratio is high, it is less likely to

leave the export scene ($\beta = -.239; p < 0.001$). Finally, we find a negative effect of the number of export markets ($\beta = -.146; p < 0.001$). This implies that, if a firm is exporting to a larger number of countries, it is less likely that it withdraws from those export markets altogether. Export share of total sales and the time to market did not have any effect on the propensity to exit. Furthermore, we did not find support for an interaction effect between firm size and time to market. Apparently, in this setting, there is no impact of the internationalization strategy as measured by the time it takes from the company is established until it starts to export.

DISCUSSION AND CONCLUSIONS

The starting point of this paper was the observation that there has been little research concerning the future of International New Ventures (INV) and Born Globals after they have started the internationalization process. We have analyzed one particular aspect of this, namely the survival of exporters after they have started exporting. The data set includes all companies in Norway established in 2003 that exported goods in more than year in the period 2003-2011. We hypothesized that available resources and experiential knowledge would be important determinants of survival. We found clear support for the importance of resources, as both profitability (H1) and firm size (H2) were significant predictors. The higher the profitability and the larger the company, the lower the propensity to exit from exporting. In this context it should be noted that exit from exporting include companies that close down completely, but we cannot distinguish those from the cases where they only discontinue exporting.

As for the effect of experiential knowledge, the results are less clear. We argued that the time from the company was established until it started to export might have two opposite effects. On the one hand, the longer the time before export start-up the more prepared may the company

be for entering a foreign market. This indicates that the later the newly established firm enters an international market, the lower is the propensity to exit (H3a). On the other hand, it may be argued that the longer the firm stays in the home market the more preoccupied will the managers be with that market, and the less prepared for the opportunities abroad (H3b). The empirical results indicate no significant effect on the propensity to exit for time to market. The reason may be that both the contrasting effects exist but cancel each other out

Sui and Baum (2014) found that the effect of firm size on the propensity to exit from exporting was moderated by choice of strategy. In particular, the effect of firm size was highest for Born Globals, lowest for companies with gradual internationalization, and medium for Born Regionals. Based upon this we hypothesized that there might be an interaction effect between firm size and time to market (H4). The results showed that the interaction effect was not significant, however. The reason may be that in our data set the variation in time to market is very limited, since the maximum value from inception to export start-up is 7 years. As can be seen from Table 1 the average value is actually 1.09 years. One reason the average is so low is that firms that internationalize early will tend to have more observations registered in the data set. Those that start to export late in the time period will generate fewer annual observations.

The number of export markets is a measure that captures the diversity of experiential knowledge. The results showed that the more markets a firm exports to the lower is the propensity to exit completely from exporting the following year (H5). In addition to diversity of experiential knowledge, the number of export markets is related to the vulnerability of a company. If one is active in many markets, the probability of running into problems in all markets is lower. This is similar to the proverb that you should not put all the eggs in one basket

Our hypothesis 6 concerning the effect of export share is not supported. The beta value goes in the expected direction, but it is not significant. We notice that the negative (but insignificant) correlation between profitability and export share is in stark contradiction to the large body of literature (Cavusgil and Zou 1994, Styles 1998, Zou et al 1998, Francis and Collins Dodd 2000., Gertner et al 2006). One possible explanation is the young age of the firms, the exporting activity still being in its formation stage. Furthermore, the export share varies markedly in our sample (mean 0.13; standard deviation 0.52). Also, we see a relatively strong correlation between export share and number of countries served. This latter strongly correlates with export survival. One interpretation of this finding is that variety or width of experience is more valuable than depth in just one or a few markets. Alternatively, diversity of market presence makes the exporter less vulnerable to the development in just one market, and thereby less likely to exit exporting all together.

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Table 1: Correlation matrix and Descriptive Statistics

	Firm size	Export share	Profitability	Export countries	Time_to_market	Mean	St.dev
firm size	1.00	.03	.01	.28***	-.08***	12.97	33.46
export_share	.03	1.00	-.05	.21***	-.06**	.13	.52
profitability	.01	-.05	1.00	.01	-.02	-.01	.52
exp_countries	.28***	.21***	.01	1.00	-.24***	3.55	5.36
time_to_market	-.08***	-.06***	-.02	-.24***	1.00	1.09	1.14

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

Table 2: Estimates of the Influences on the Propensity of Export Exit

firm size	-.023* (.010)
export_share	-.005 (.116)
profitability	-.239*** (.062)
exp_countries	-.146*** (.039)
time_to_market	.072 (.069)
time_to_market:firm_size	.006 (.005)
n	2180
R square	.034

Standard errors in parentheses
* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$