Learning Through Experience:

The Impact on SME Entry Mode Choice

ABSTRACT

Learning from experience has attracted considerable research attention over the last decades. Yet it is unclear how firms learn from past entry mode choices. In this paper we develop and test theory that suggests that entry mode learning might be non-linear and that firms learn from equity mode, non-equity mode and international experience. Drawing on a sample of 185 German SMEs, we show that non-equity entry mode experience leads to higher resource commitment if firms also possess complementary international experience. In contrast, equity entry mode experience shows signs of decreasing marginal effects. Our study contributes to the SME entry mode literature and offers implications for future research and practice.

Key words: SMEs, entry mode choice, international experience, geographical experience, entry mode experience

INTRODUCTION

Experiential learning is an important business practice that allows firms to develop knowledge, routines and processes and generate a competitive advantage (Haleblian, Kim, & Rajagopalan, 2006; Levinthal & March, 1993; March, 1991; Powell & Rhee, forthcoming). Learning through experience, is critically important for firms expanding abroad as it helps reduce liabilities of foreignness (Zaheer, 1995). This issue is particularly acute for small and medium-sized enterprises (SMEs) as these firms often suffer from resource restrictions (Lu & Beamish, 2001) and are highly sensitive to the challenges arising from differences in institutional context when they enter foreign markets (Cheng & Yu, 2008; Schwens, Eiche, & Kabst, 2011).

Much of the research exploring international experiential learning has focused on the learning that occurs from the number of different countries in which the firm does business (Barkema & Vermeulen, 1998; Slangen & Van Tulder, 2009) and/or the length of time a firm has been active internationally (Brouthers, Brouthers, & Werner, 2003; Cho & Padmanabhan, 2005; Mutinelli & Piscitello, 1998). Learning from the time spent in a target country (Delios & Beamish, 1999) or region (Meyer & Estrin, 1997) has also been investigated. Others have explored the diversity of learning from the repeated adoption of the same entry mode structure in different countries (Dikova & Van Witteloostuijn, 2007; Slangen & Van Tulder, 2009) or the intensity (length of time) a specific mode type has been used (Cho & Padmanabhan, 2005; Padmanabhan & Cho, 1999).

Despite the growing interest in how experiential learning impacts a firm's international operations and especially its entry mode choice, past research suffers from several shortcomings. First, studies investigating mode experience mostly use samples of large MNEs (Madhok, 1998; Sanchez-Peinado, Pla-Barber, & Hébert, 2007; Slangen & Van Tulder, 2009; Vermeulen &

Barkema, 2001). But SMEs are unique and research has shown that they rely on different factors to make mode decisions (Erramilli & D'Souza, 1993; Prater & Ghosh, 2005). Second, prior research focuses on equity modes of entry, i.e. experience from prior joint ventures and wholly owned subsidiaries (e.g., Cho & Padmanabhan, 2005; Guillén, 2003; Padmanabhan & Cho, 1999). Yet, because of resource constraints, SMEs tend to prefer non-equity modes (Zacharakis, 1997). Finally, prior studies often investigate the impact of mode experience *in isolation* neglecting the interaction with other types of international experience. Recent research, however, shows that different types of experience may complement each other (Li & Meyer, 2009; Powell & Rhee, forthcoming), thus potentially resulting in more complex knowledge stocks for the firm (Barkema & Vermeulen, 1998; Powell & Rhee, forthcoming).

In this paper, we build on previous research by theoretically and empirically investigating how entry mode experiential learning and other types of international experience-based learning help explain the entry mode choices made by SMEs. We examine how the learning obtained from the intensity and diversity of equity and non-equity mode experience influence subsequent entry mode choice. In particular, we consider more complex non-linear effects of equity experiential learning. We theorize that high levels of equity mode experience overburden SMEs' ability to identify, value, select, and assimilate these experiences, leading to a non-linear effect with decreasing marginal effects of equity entry mode experience on future mode decisions. We also theorize that learning from non-equity mode experience impacts future mode decisions both in a linear and moderated way. Our theory suggests that non-equity mode experience is moderated by the knowledge a firm can accumulate from its international (target market/region) experience.

Using this approach we make three important contributions to knowledge. First, we expand extant research by including both equity and non-equity entry mode experience in our study. Pre-

vious studies tend to focus on learning through equity modes of entry – joint ventures and wholly owned subsidiaries (e.g., Chang & Rosenzweig, 2001; Dikova & Van Witteloostuijn, 2007; Vermeulen & Barkema, 2001). Yet firms, both large and small use equity and non-equity modes as they expand to foreign markets. By expanding our focus to include non-equity modes we can gain more differentiated insights into the complexities of prior mode experience and how they feed forward into future entry mode decisions. In addition, by considering non-linear relations for the impact of equity entry mode experience on future entry mode choices, we expand existing knowledge by theoretically and empirically showing how the benefits of experiential learning may be limited; there comes a point at which firms have difficulty absorbing and using new knowledge or handling the complexity of higher levels of experiential opportunities. Hence we make a contribution to both the mode choice and experiential learning literatures.

Second, with the recent exception of Powell and Rhee (forthcoming) past international experiential learning studies have tended to look at direct relationships; ignoring any interactions between different types of experiential learning opportunities (e.g., Lu, 2002; Padmanabhan & Cho, 1999). Yet various types of experience-based learning may potentially complement each other (Li & Meyer, 2009; Powell & Rhee, forthcoming). We investigate the link between learning provided by non-equity entry mode experience and international (target market/region) experience. We develop and test theory that suggests that learning obtained through decision-specific experience (gained from non-equity entry mode experience) in tandem with learning generated by more general country- and region-specific international experience influences subsequent entry mode choice. We advance both entry mode and experiential learning literatures by empirically testing this notion and identifying more complex interactions between different types of experiential learning and the effect on entry mode choice.

Finally, we contribute to the small but growing literature exploring SME internationalization (Coviello & McAuley, 1999; Laufs & Schwens, 2014). In most countries around the world SMEs continue to make important contributions to economic growth and prosperity and represent an increasing proportion of international business activities (Coviello & McAuley, 1999; Reynolds, 1997). Yet the experiential learning and mode choice literatures have, for the most part, tended to pay scant attention to these firms; concentrating instead on large MNEs. Because SMEs have unique characteristics how they learn and make international decisions also differ from larger MNEs (Coviello & McAuley, 1999; Erramilli & D'Souza, 1993; Shuman & Seeger, 1986). Thus, by focusing on SMEs we make an important contribution to knowledge.

THEORY AND HYPOTHESES

The process model of internationalization postulates that firms gain experience from foreign operations, and with growing levels of experience they commit increasing amounts of resources to subsequent market entries (Johanson & Vahlne, 1977). Despite its explanatory power the internationalization process model has been criticized for offering an incomplete view of the factors influencing a firm's decision on commitment to foreign markets (Forsgren, 2002). A recent study by Powell and Rhee (forthcoming) therefore calls for shifting research towards the inclusion of more organizational learning aspects and to identify boundary conditions of the internationalization process model. To this end, they suggest "a more exhaustive consideration of various types of experiential learning" (Powell & Rhee, forthcoming, p. 22).

While the focus on experience as the key determinant of firms' internationalization strategies still holds true, the boundary conditions of the internationalization process model have been inadequately specified (cf. Björkman & Forsgren, 2000; Forsgren, 2002). Moreover, Björkman

and Forsgren (2000, p. 12) criticize the model suggesting that "[i]t is not at all clear how experiential knowledge affects organizational behavior". Johanson and Vahlne (1990, 2003, 2009) themselves revised their model several times and admit that various kinds of international experience may affect international entry mode choices. Scholars have therefore recently advocated a broaden of the model by studying wider aspects of learning and including different types of experiential learning (Powell & Rhee, forthcoming).

The impact of learning from experience on the resource commitment of internationalizing firms is a key element of the process theory of internationalization (Johanson & Vahlne, 1977). By gaining experience in international operations, firms develop routines in processing knowledge while simultaneously generating more confidence, which in turn reduces uncertainty. Through these mechanisms, even SMEs are able to increase their resource commitment to foreign operations. Considering different dimensions of learning is important as they may differently impact on a firm's knowledge base and, hence, its strategic decisions. Experience gained from the *number of countries* firms are operating in has been shown to significantly influence entry mode decisions (Barkema & Vermeulen, 1998; Slangen & Van Tulder, 2009). For example, Barkema and Vermeulen (1998) find that the diversity of experience increases the propensity of choosing a greenfield entry as opposed to an acquisition. This effect traces back to the diversity of experience argument; as exposure to a variety of situations and environments fosters learning (Huber, 1991).

Similarly, prior research notes that the *length of time* of international experience may provide a learning opportunity. Measuring firms' years of experience with international business activities, Mutinelli and Piscitello (1998) find that international experience increases the propensity of choosing a higher commitment mode (wholly-owned subsidiary as opposed to joint ven-

ture), although others applying a similar measure do not find a significant effect (e.g., Cho & Padmanabhan, 2005; Lu, 2002). Studies focusing on international experience as years of experience in the host country also provide mixed results. While some of these studies show that host-country experience is associated with higher levels of equity ownership (Delios & Beamish, 1999) others find the exact opposite (Lu, 2002) or do not find a significant influence at all (Cho & Padmanabhan, 2005; Padmanabhan & Cho, 1999).

A related stream of research investigates another type of international experiential learning, i.e. learning from *entry mode experience.* Learning from repeatedly adopting the same entry mode structure represents deep knowledge as accumulated experience can result in specific processes or routines on which the organization can draw upon in subsequent operations (Gao, Pan, Lu, & Tao, 2008).

Below we develop and test theory that suggests SMEs learn from both decision-specific experience (equity and non-equity mode experience) as well as general international (target market/region) experience. We hypothesize that this learning is both linear and non-linear and as such is more complex than previous entry mode or experiential learning research has suggested.

Learning from Equity Modes of Entry

Prior research investigating mode experience concentrates on equity entry modes and finds that prior experience with a specific entry mode increases the propensity of opting for that same entry mode (Cho & Padmanabhan, 2005; Dikova & Van Witteloostuijn, 2007; Padmanabhan & Cho, 1999; Slangen & Hennart, 2008; Slangen & Van Tulder, 2009; Yiu & Makino, 2002). However, some studies show the opposite (Delios & Beamish, 1999; Vermeulen & Barkema, 2001), do not detect a significant effect at all (Kogut & Singh, 1988), or find this effect only applies in

the same line of business (Chang & Rosenzweig, 2001) or in certain industries (Lu, 2002; Sanchez-Peinado et al., 2007).

In contrast to less resource intensive entry modes such as exporting, equity entry modes represent the most comprehensive way of gaining experience abroad (Gao et al., 2008). While non-equity entry modes are associated with comparably few interactions with customers, suppliers and markets (Zahra, Ireland, & Hitt, 2000), firms choosing equity entry modes are directly exposed to customers, institutions, and business partners, allowing for closeness to the market and information collection about competitors. By these means, SMEs potentially gather richer and more complex knowledge (Clarke, Tamaschke, & Liesch, 2013). Equity entry modes even offer the potential for more radical and complex learning (Zahra et al., 2000).

Nevertheless, later entry mode experience can potentially supersede learning effects from earlier experiences (Anand, Glick, & Manz, 2002; Clarke et al., 2013). The value of organizational experiences may thus decrease over time (Gao et al., 2008; Ingram & Baum, 1997; Powell & Rhee, forthcoming). Prior research has shown that the value of more recent entry mode experience is relatively more important for subsequent entry mode choices than older entry mode experience (Cho & Padmanabhan, 2001). For these reasons, we believe that at low to medium intensity levels of equity entry mode experience, SMEs will tend to prefer equity entry modes in the future. However, marginal effects will be decreasing at medium to high intensity levels of equity entry modes shifting the mode decision.

From an administrative perspective, equity operations involve significant financial and managerial resources (Anderson & Gatignon, 1986). Besides the pure effort of setting up an equity operation, more direct and intensive exposure to institutions requires firms to dedicate more financial and managerial resources to equity operations. The more equity operations in different

markets a firm administers, the more complex the organization becomes (Tihanyi, Griffith, & Russell, 2005). Firms then need to allocate their resources to both exploiting established routines as well as exploring new routines gained through new experiences (Ingram & Baum, 1997; March, 1991).

This is particularly relevant for SMEs given that "[t]he nature and the complexity of the internationalization process are clearly different for small and large organizations" (Pla-Barber & Alegre, 2014, p. 1). If the amount of information exceeds an organization's cognitive capacity, the firm suffers from 'information overload' that hampers learning (Barkema & Vermeulen, 1998; Huber, 1991; Yeoh, 2004).

According to Levitt and March (1988), learning through experience is an instrument of intelligence that is subject to organizational limitations. For this reason, we suggest that at low to medium levels of diversity of equity entry mode experience, SMEs are likely to again opt for an equity entry mode. However, at some point, complex and resource-intensive equity operations are likely to attenuate this effect, thereby leading to decreasing marginal effects of equity experience on equity entry mode choice. Organizational learning from a diversity of operations is thus subject to constraints of the organization's cognitive capacity (Barkema & Vermeulen, 1998). Hence we hypothesize that the relationship between an SME's intensity and diversity of equity entry mode experience and its propensity to choose a subsequent equity entry mode is increasing at a decreasing rate. More specifically we hypothesize that:

Hypothesis 1: Equity entry mode experience will increase the probability of subsequent equity entry modes at a decreasing rate.

Learning from Non-equity Modes of Entry

Because of their limited scale, non-equity entry modes provide firms with lower amounts of information and learning opportunities in contrast to equity entry modes (Gao et al., 2008). SMEs that often enter markets through non-equity entry modes may therefore require more time to learn, or a higher diversity of experiences (Zahra et al., 2000). Firms not only need to absorb and integrate new knowledge, but they also need to modify existing routines or create new procedures, as well as spread the knowledge across the organization so as to efficiently make use of it (Martin & Salomon, 2003). This is a gradual process (Eriksson, Johanson, Majkgård, & Sharma, 1997) by which firms become more confident over time and are hence better able to fulfill customer needs (Davidson, 1980). With increasing length of experience firms have more and wider opportunities to gather knowledge and develop processes and routines (Clarke et al., 2013; March, 1991). At high intensity levels of non-equity entry mode experience, SMEs will have accumulated a sufficient knowledge base and have established routines and procedures that enable them to pursue an equity entry mode.

Firms not only learn over time, but also learn from diverse experiences (Levitt & March, 1988; Padmanabhan & Cho, 1999). Most importantly, the efficiency with any particular activity improves with use (Levitt & March, 1988; Penrose, 1959). Through repetition of establishing similar entry mode structures and respective learning effects firms are more likely to subsequently set up similar entry modes in order to reduce implementation costs (Padmanabhan & Cho, 1999). This may be even more important for SMEs that are reliant on limited financial and managerial resources. As such SMEs entering new foreign markets face exposure to a variety of business environments and contexts. They hence interact with a wider range of markets and cultures, which in turn encourages learning (Hitt, Hoskisson, & Hicheon, 1997; Zahra et al., 2000). Differences in demand patterns, industry structures, business partners and suppliers also require firms

to creatively develop new solutions (Barkema & Vermeulen, 1998). A high diversity of non-equity entry mode experience represents a variety of novel experiences, enabling firms to gradually build up a strong knowledge base (Huber, 1991; March, 1991). This in turn allows them to commit higher amounts of resources to foreign operations. We therefore hypothesize:

thesis 2: SMEs with lower levels of non-equity experience (intensity or diversity) opt for non-equity modes while those with more non-equity experience will tend to opt for equity modes.

Besides this decision-specific entry mode experience, SMEs also gather more general internationalization knowledge when operating internationally, especially how to operate in a specific market or region. Such experience helps firms to better estimate potential threats and returns in the respective foreign markets (Anderson & Gatignon, 1986), whereby the overall risk stemming from liabilities of foreignness can be extenuated (Henisz & Delios, 2002; Hymer, 1976). Although experience gained in a particular market may be culture-specific and hence not fully transferrable to another market, firms are likely to become more alert towards potential threats and opportunities deriving from the international environment (Dow & Larimo, 2009, 2011). Dow and Larimo (2009) note the importance of studying regional or cluster-specific experience, rather than including simple measures of host country experience. They argue that firms with prior experience in countries within the same cluster actually have both, more general international experience as well as culture-specific experience. Through familiarity with a particular cluster of countries, its cultures, institutions, and languages, firms are more likely to avoid misunderstandings. Their results confirm that such regional experience is more likely to lead to sub-

sequent high-control modes of entry compared to more general international experience (Dow and Larimo (2009).

We therefore argue that SMEs may benefit from learning from different sources of knowledge as it will increase their knowledge base (Fernhaber, Mcdougall-Covin, & Shepherd, 2009). Especially in combination with non-equity entry mode experience – which is not as comprehensive as experience gained through equity entries – international experience will help SMEs to gain more knowledge about foreign markets and customers, their culture and idiosyncrasies (Henisz & Delios, 2002). We argue that international experience may complement experience derived from non-equity entry mode experience. Hence our final hypothesize states:

Hypothesis 3: The relation between an SME's non-equity entry mode experience and its subsequent entry mode choice is moderated by the level of international (target-market and target-region) experience the firm possesses such that international experience increases the propensity of choosing an equity entry mode.

METHODS

We test our hypotheses on a sample of German SMEs. German SMEs are a good place to test these ideas since they are widely recognized as the 'engine' of the German economy (Schwens et al., 2011; Simon, 1996a, 1996b). More than 99% of all German firms are SMEs; of these at least 36.5% engage in international business activities, thereby contributing to economic stability and growth in Germany (Kay, Holz, & Kranzusch, 2014).

According to the German Institute for SMEs (Institut für Mittelstandsforschung), we define SMEs as firms with up to 500 employees. We accessed the AMADEUS database in order to identify SMEs suitable for our study. To qualify for this study the SME had to be internationally

active and have no more than 500 employees. Based on these criteria we obtain contact details of 2,021 internationally active SMEs. In early 2014, we sent out paper-based questionnaires to the CEOs of these firms as this group of managers exerts decisive influence on strategic decisions (Maekelburger, Schwens, & Kabst, 2012; Mesquita & Lazzarini, 2008) and therefore formed the basis of our survey. After a first wave of questionnaires, we sent out two reminders, after which we made follow-up phone calls. We received 267 responses (13.2% response rate). Because of missing variables, our usable sample includes 185 firms with an average firm size of 163 employees.

Our questionnaire was originally written in English and then translated into German; adhering to back-translation standards ((Brislin, 1970; Hui & Triandis, 1985; Van de Vijver & Hambleton, 1996). All SME CEOs in our sample received the German questionnaire.

Measurements

Our dependent variable, *entry mode choice* was obtained by asking respondents to indicate the type of entry mode for the most recent foreign market entry. Respondents were given a choice of 12 different mode types adapted from Brouthers and Nakos (2004) and Maekelburger et al. (2012). Following Pan and Tse (2000), we created a dichotomous dependent variable *foreign market entry mode choice*, with non-equity entry modes (i.e. exporting, using a distributor, franchising, licensing, or other long-term contractual agreements) coded 0, and equity entry modes (i.e. joint ventures, equity stakes, acquisitions, or wholly-owned subsidiaries) coded 1. This process is similar to that used in past studies (e.g., Brouthers & Nakos, 2004; Maekelburger et al., 2012; Nakos & Brouthers, 2002; Schwens et al., 2011).

We included four independent variables in our analyses: *intensity of equity experience, diversity of equity experience, intensity of non-equity experience,* and *diversity of non-equity experience*. For intensity of equity and non-equity experience we asked respondents to indicate how many years of experience their firm had with each of the 12 different types of entry mode. This measure was adopted from prior studies which measured the count years of experience for each foreign operation (e.g., Cho & Padmanabhan, 2005; Padmanabhan & Cho, 1999). According to the classification offered by Pan and Tse (2000), we added the number of years of experience with the respective types of entry modes to create our aggregate measures of intensity of equity experience and intensity of non-equity experience.

To measure the diversity of equity and non-equity entry modes we asked respondents to indicate the number of countries in which their firm had used each of the 12 different types of entry mode (e.g., Guillén, 2003; Madhok, 1998). Again we summed the number of countries in which the firm used equity modes and the number of countries in which it used non-equity modes to create our diversity of equity and diversity of non-equity mode experience measures.

Our moderator variable *international experience* consists of two items. Respondents were asked to indicate their agreement with the statements "Our company had prior and long standing experience in the target country" and "Our company had prior and long standing experience in the target region". Both items were obtained from Schwens et al. (2011) measured on 5-point Likert scales (1=fully disagree, 5=fully agree) and loaded onto one factor (Cronbach's $\alpha = .84$).

We also included seven control variables that have been shown to influence SME entry mode choices. Previous research shows that younger firms are more restricted in their resources than older firms (Erramilli & D'Souza, 1993). As this may also influence entry mode decisions, we included *firm age* as control variable, calculated as the year of data collection less the firm's

founding year. *Firm size* is often used as a proxy for the resource endowment of a firm which allows larger firms to choose equity entry modes (Contractor, 1984). Firm size was measured as the total number of employees worldwide (e.g., Brouthers & Nakos, 2004). In light of previous findings showing that industry differences may affect entry mode choice (Brouthers & Brouthers, 2003; Erramilli & Rao, 1993), we asked respondents to indicate whether their firm mainly operates in manufacturing or services, and included an *industry* dummy variable (1=manufacturing, 0=services).

Prior research furthermore indicates a strong relation between transaction cost economics (TCE) factors and mode choice (Zhao, Luo, & Suh, 2004). For this reason, we included three TCE variables: Asset specificity, internal uncertainty, and external uncertainty. We adapted *asset specificity* using a multi-item measure (Aulakh & Kotabe, 1997; Brouthers & Brouthers, 2003), that included five items: "Our firm made significant investments that are specific to the needs of the foreign country", "Our products/technologies are tailored to meet the requirements of this foreign country", "Our training program in terms of preparing personnel to provide our service or produce our product is well above average compared to our competitors", "Our firm's potential to create new and creative products or services is well above average compared to our competitors", and "The number of technological resources to handle in international expansion by our firm are well above average compared to our competitors". Respondents indicated their agreement on 5-point Likert scales (1=fully disagree, 5=fully agree). All items loaded onto a single factor (Cronbach's $\alpha = .66$).

Internal uncertainty was captured as international experience (Zhao et al., 2004). We included two measures of international experience. The length of international experience (*IE intensity*) captures the firm's intensity of international experience and was calculated by subtracting

the year of a firm's first foreign market entry from the year of data collection. The diversity of international experience (*IE diversity*) was a single item in our questionnaire asking respondents to indicate the total number of markets in which their products or services are currently marketed. Both measures were obtained from Cavusgil and Zou (1994).

The third TCE variable *external uncertainty* included two items "It was difficult to forecast the sales quotas of our products in the foreign market" and "It was difficult to forecast the competitive advantage of our products in the foreign market" that were again measured on 5-point Likert scales (Cronbach's $\alpha = .76$) and obtained from prior research (Lu, Zhou, Bruton, & Li, 2010).

Finally, we included two motives for internationalization as control variables, i.e. *market exploitation* and *know-how access*. This is in line with prior research (e.g., Maekelburger et al., 2012) and rests on the assumption that strategic motives exert an influence on entry mode decisions (Sarkar & Cavusgil, 1996). We asked respondents to assess the extent to which these two motives influenced their most recent foreign market entry mode decision on a 5-point Likert scale (1=unimportant, 5=important).

Non-response and common method variance

Response bias was assessed following the recommendations of Armstrong and Overton (1977). We compared early and late respondents on a large number of variables. For this purpose, we identified the first and last 10% of all respondents and compared their responses regarding all variables used in our analysis. A t-test as suggested by Miller and Smith (1983) was used to assess response bias but did not produce significant differences between early and late respondents for any of the variables (Foreign market entry mode choice F=1.958, p=.168; IntNEQ F=2.477,

p=.122; DivNEQ F=.289, p=.594; IntEQ F=.558, p=.459; DivEQ F=2.197, p=.145; International experience F=.340, p=.563; IE intensity F=4.004, p=.051; IE diversity F=.278, p=.601; Age F=.065, p=.799; Size F=.000, p=.983; Uncertainty F=1.591; p=.213; Industry F=.310, p=.580; Asset specificity F=.022, p=.883; Motive market exploitation F=1.117, p=.296).

Since most of our measures were self-reported, our data could be subject to common method variance (CMV). We hence took action in order to minimize this risk. First of all, we conducted Harman's single factor test which yielded five factors, with the largest one explaining only 20.34% of the variance (Podsakoff and Organ (1986). Second, Chandler and Lyon (2001) recommend comparing subjective measures with objective measures so as to validate survey measurements. To this end, we compared primary data from our questionnaire with secondary information that we obtained from the firms' websites. A t-test did not produce any significant differences for either firm size (p=.774) or founding year (p=.960). Furthermore, the inclusion of interaction effects presumably reduces CMV, as such interaction terms are likely to go beyond a respondent's cognitive map due to their complexity (Chang, van Witteloostuijn, & Eden, 2010). Finally, the measurement of our dependent variable (capturing entry mode) is more objective than subjective as the respondents were simply asked which entry mode has been used in the most recent foreign expansion. Thus it appears that CMV is not an issue with our data.

RESULTS

We began our analysis by testing for multicollinearity. The correlation results, mean values, standard deviations, and variance inflation factors (VIFs) are displayed in Table 1. With one exception, all correlations are well below .7, indicating that multicollinearity does not constitute a major threat to our results (Anderson, Sweeney, & Williams, 1996). Only the diversity of interna-

tional experience displays high correlations with diversity of non-equity entry mode experience (.76). However, this is not surprising given SMEs' preference for non-equity entry modes from which they gain experience. As we included this variable only for additional moderation tests we do not consider this to be a major threat of multicollinearity. This was further corroborated by calculating the VIFs, which all stayed well below the critical threshold of 2.5 (Allison, 1999).

Insert Table 1 about here

Prior to conducting our analyses, we mean-centered all control and predictor variables in order to facilitate interpretation of our results as well as to reduce the potential threat of multicollinearity (Cohen, Cohen, West, & Aiken, 2013; Comer & Kendall, 2013). Applying hierarchical logistic regression analysis, we tested our hypotheses as shown in Table 2.

Insert Table 2 about here

Model 1 (LR χ^2 = 78.09) includes all control variables, the direct effects of the experience variables, and the moderator variable. Of the control variables, only asset specificity significantly increases SMEs' propensity of choosing an equity entry mode (p=.011), which is consistent with studies applying transaction cost economics (e.g., Brouthers & Nakos, 2004; Maekelburger et al., 2012). Likewise, our moderator international experience significantly increases the probability of a subsequent equity entry mode (p=.076) as a direct effect as is consistent with extant literature (Delios & Beamish, 1999; Maekelburger et al., 2012). In contrast, IE diversity seems to decrease the probability of equity entry modes (p=.049). Furthermore, one of the equity experience variables exerts a direct effect on entry mode choice. The significant positive sign (p=.001) of DivEQ indicates that diversity of equity entry mode experience may lead to further equity entry modes. While DivNEQ does not prove to be significant, the negative sign of IntNEQ hints at an in-

creased likelihood of a subsequent non-equity entry mode (p=.021). This contradicts hypothesis 2 which predicted that non-equity entry mode experience would presumably increase the probability of equity entry mode choices.

Models 2 and 3 test for the non-linear effects of equity mode experiential learning. In hypothesis 1 we hypothesized a nonlinear relation between equity mode experience and mode choice, i.e. an increasing effect at a decreasing rate. We thus expected the linear terms to display a positive sign, while the quadratic terms should have a negative sign. We did not find a significant non-linear effect for intensity of equity experience (model 2, LR $\chi^2 = 78.21$). Yet we do find that diversity of equity experience is significant (model 3, LR $\chi^2 = 81.09$). The linear regression coefficient of DivEQ has a positive significant effect (p=.000), whereas the quadratic term is significantly negative (p=.056). We hence find indication for nonlinear relationship at decreasing rates as displayed in Figure 1. At low to medium levels of DivEQ the probability of further equity entry modes increases. At medium to high levels of DivEQ, however, we find decreasing marginal effects.

Insert Figure 1 about here

In order to develop a deeper understanding of these non-linear effects, we applied a test of the three conditions for the presence of a non-linear effect as suggested by Lind and Mehlum (2010). For the presence of non-linear effects, Lind and Mehlum (2010) Lind and Mehlum (2010) suggest three conditions to be met: First, both the linear and non-linear coefficients must be significant and have the expected signs. Second, the slopes at the extreme points must also be significant with the expected signs. Third, the Fieller method needs to confirm that the confidence interval of the extreme point includes the estimated inflection point. As can be seen from the regression results, the first condition is met for DivEQ and DivEQ². However, the second condition

is only partially fulfilled. While the slope at the extreme left side of the curve is significantly positive (slope = 0.504; p= .001), the slope at the right side is not significant (p=.165). This finding is strongly consistent with our plot as it represents decreasing marginal effects at higher levels of diversity of equity entry mode experience.

We tested hypothesis 3 in models 4 and 5. Model 4 (LR χ^2 = 81.32) shows a significantly positive effect for the interaction of IntNEQ and international experience (p=.092). Similarly in model 5 (LR χ^2 = 84.68) we find a significant and positive effect for the interaction of DivNEQ and international experience (p=.019). This implies that in combination, these different types of experience increase the probability of a subsequent equity entry mode choice, hence supporting hypotheses 3.

Insert Figures 2 and 3 about here

In order to gain a more differentiated understanding of the direction and significance of interaction effects, we computed two sets of plots as suggested by Zelner (2009). The upper set of plots in Figures 2 and 3 displays the predicted probability of an equity entry mode on the y-axis at low to high levels of non-equity entry mode experience on the x-axis. The solid and dashed lines represent low and high levels of international experience, respectively. Given that predicted probabilities are also estimates, we comply with Zelner (2009) by including the second set of plots. Here the y-axis displays the change in predicted probabilities for low to high values of the moderator at different values of non-equity entry mode experience. For intensity of non-equity entry mode experience, the interaction effect is significant at low to medium levels of the independent variable, as the confidence interval (represented by the bars) does not include zero. Except for very low levels of DivNEQ, the effect is entirely sinificant in Figure 3.

DISCUSSION, LIMITATIONS AND CONCLUSION

Our study investigated nonlinear and interactive effects of different types of experience on subsequent entry mode choice of SMEs. We found partial empirical support for our hypotheses, overall stressing the importance of a more differentiated analysis of experiential learning effects in the context of SMEs and under consideration of non-equity entry modes. The following sections discuss our findings.

We hypothesized a nonlinear effect for equity mode experience on subsequent equity entry mode choice but found only partial support. The length of experience with equity operations did not play a role in explaining subsequent entry mode choices. A possible explanation might refer to knowledge losing its value over time, thereby becoming less relevant for further entry mode situations (Gao et al., 2008; Ingram & Baum, 1997; Powell & Rhee, forthcoming). In contrast, our results provide support for the assumption that diverse experiences with equity entry modes will yield further equity operations, yet at a decreasing rate.

There are several possible explanations for this finding. First, a high diversity of equity operations involves a significant amount of information to be absorbed and integrated into the organization (Barkema & Vermeulen, 1998). As SMEs possess only limited resources, they need to exploit these efficiently. At some point, however, SMEs may not have sufficient slack resources to further increase the rate of additional equity operations, which is reflected in decreasing marginal effects in our results. These results highlight the importance of considering resource limitations of SMEs when investigating their internationalization processes (Maekelburger et al., 2012).

Second, any organization is limited by its cognitive capacity (Barkema & Vermeulen, 1998). Because of managerial resource limitations, SMEs might face an overburdening effect on grounds of too many equity operations and the resulting complexity. This is likely to increase the probability of further equity modes at a decreasing rate, as supported by our findings. Third, a possible explanation could be saturation. Once a SME has entered numerous markets via equity operations, the number of relevant markets worth entering will become smaller, thus potentially explaining decreasing marginal effects of diversity of equity entry mode experience. We make an important contribution here by exploring not only the linear effect of equity experience, but also by exploring how this effect can decrease because of firm level constraints on learning. Our findings clearly stress the need for considering the potential of learning over-load when SMEs internationalize (Powell & Rhee, forthcoming; Zollo, 2009).

We also make an important contribution to knowledge by exploring the impact of learning from non-equity modes of entry. Despite our predictions we could not find support for the assumption that high levels of non-equity entry mode experience would lead to subsequent equity entry mode choices. These findings contradict previous studies which empirically supported the internationalization process theory of gradual experience accumulation and increasing market commitment (Cheng, 2008; Hedlund & Kverneland, 1985; Juul & Walters, 1987; Pla-Barber, 2001). Instead, our results show that diversity of non-equity experience does not seem to play a direct role concerning entry mode choice at all. Yet intensity of non-equity experience appears to be a significant predictor of future mode choices. The results corroborate the notion that learning takes time (Brouthers, Nakos, Hadjimarcou, & Brouthers, 2009) and may indeed lead to the establishment of routines (Haleblian et al., 2006; March, 1991; Powell & Rhee, forthcoming). Rather than trying something new, SMEs tend to stick to what they have learned from prior experi-

ences with regard to non-equity entry modes. A possible explanation could be that commonly used procedures are likely be optimized in order to maximize outcomes, which in turn will increase frequency of use. "However, a competency trap can occur when favorable performance with an inferior procedure leads an organization to accumulate more experience with it, thus keeping experience with a superior procedure inadequate to make it rewarding to use" (Levitt & March, 1988, p. 322). This is what Ingram and Baum (1997) call the risk of 'overattention' to short-term experiences which may eventually constrain the organization. It could hence explain why firms with a long history or a wide set of experiences with non-equity modes continued to enter markets via similar modes, instead of advancing to equity entry modes that have higher potential for returns (Anderson & Gatignon, 1986).

Our results also suggest that non-equity mode based learning in combination with international experience is important for future mode decisions. It appears that SMEs are able to benefit from more comprehensive and complementary learning effects. Together with international experience, higher levels of non-equity entry mode experience enable SMEs to acquire enough relevant learning to feel confident in selecting equity entry modes. In this regard, both the intensity and diversity of non-equity entry mode experience can be beneficial. Our findings fully support our third hypothesis and advance prior studies that investigated mode experience and international experience in isolation (e.g., Delios & Beamish, 1999; Dikova & Van Witteloostuijn, 2007). Our results tend to substantiate the notion of "context-specificity of learning experiences" (Søderberg, Vaara, & Nordea, 2003, p. 224). If firms not only possess activity-related experience (i.e. mode experience), but also international experience (i.e. knowledge about the specific context of the new international activity), they may be willing to commit increasing amounts of resources to subsequent operations. Yet this international experience seems to be specific; support-

ing prior research stating that only experience in countries similar to the new host market affects entry mode choice (Dow & Larimo, 2009). Knowledge about local business practices, languages, systems, and political issues seems to be specific to a single country or a particular set of countries (Dow & Larimo, 2011; Eriksson et al., 1997). In combination with either a high intensity or a high diversity of non-equity entry mode experience, such international experience helps firms to correctly apply knowledge from previous experience to new contexts, thereby enabling them to choose equity entry modes.

Limitations

Our study suffers from several limitations. First, our sample includes only SMEs from Germany. In light of the traditional 'German Mittelstand' our results may not be applicable to SMEs from other countries or to larger firms. Future research might want to investigate different types of experience related to entry mode choices of firms in different countries and of different size.

Second, our dependent variable may cause some concern as it is an aggregate measure of different entry modes. While dichotomizing entry modes into equity and non-equity entry modes is consistent with prior research (e.g., Brouthers & Nakos, 2004; Maekelburger et al., 2012; Nakos & Brouthers, 2002; Pan & Tse, 2000), future research may disentangle the constructs further and investigate experience effects on specific entry modes, such as exporting, licensing, or joint ventures.

Third, because our study is cross-sectional, experience effects that vary over time cannot be captured explicitly by our research design. However, we do capture the internationalization modes chosen by SMEs in the past and, hence, offer a valuable contribution towards a better un-

derstanding of how prior experiences feed forward into future entry mode decisions. To further follow this route, we encourage future research to replicate our findings under consideration of time-based effects using longitudinal research designs.

Implications

Our research has important implications for both practitioners and researchers. SMEs have been shown to have a tendency for non-equity entry modes due to their resource limitations (Zacharakis, 1997). Our findings not only confirm this notion, but also advance it by showing that SMEs can only handle limited equity operations. SME managers should therefore be aware that scant resources limit their strategic choices, in particular with increasing numbers of equity operations. With regard to non-equity entry mode experience we suggest based on our findings that managers of smaller firms should be conscious of potential competency traps. The repeated adoption of non-equity entry mode types leads to the establishment of routines, which in turn fosters further adoption of non-equity entry modes. Managers should therefore avoid being stuck in their routines with regard to foreign market entry. Instead, they should actively learn from their experiences and find ways to apply the gathered knowledge in new ways, thereby potentially entering new markets via equity entry modes. A promising way to achieve this could be to enhance a firm's geographical experience. SMEs with non-equity entry mode experience might, for example, hire managers from potential target regions if they wish to establish equity operations abroad. In combination with their non-equity entry mode experience, our results show that this could be a way of entering a new market via equity entry modes.

This study also offers avenues for future research. First, by yielding differentiated results for non-equity entry mode experience and equity entry mode experience, our research shows the

importance of considering SMEs in entry mode research. Future research may therefore advance our study by directly comparing SMEs and MNEs with regard to mode experience and subsequent mode choice. Second, we hypothesized and empirically confirmed the existence of non-linear experience effects on entry mode choices of SMEs. While prior research found a non-linear effect of experience on entry mode choice under consideration of cultural distance (Erramilli, 1991), we suggest a similarly differentiated approach for future studies investigating various types of experience. For example, it would be interesting to investigate possible non-linear effects of experience on subsequent foreign venture performance. Third, we encourage scholars to enhance our findings by studying additional types of experience. For example, future research could investigate the relevance of individual-level experience or industry-related experience in addition to the experience dimensions we offered in our research. Finally and closely related to studying different types of experience, future research could supplement our analysis by studying interactive effects of other types of experience, such as CEO experience or culture-specific experience. Our results clearly show that different types of experience may complement each other, thereby significantly influencing firms' strategies.

Conclusion

In sum, while we found only partial support for our hypotheses, our results clearly demonstrate the importance of a more differentiated investigation of experiential learning effects in relation to the entry mode choice of SMEs. In particular, including non-equity entry modes and related types of experience in our analysis provides new insights into experiential learning and shows how different types of learning enable SMEs to make future mode choice decisions.

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TABLE 1

Mean values, standard deviations, variance inflation factors, and correlations

Variable	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
Mean	44	38 89	27 75	19 50	4 25	2 35	40 45	29 80	48 75	163 14	62	2 19	3 17	4 10	2 32	2 27
SD	50	40 16	29 58	20 15	4 26	1 04	144 27	28 62	40 74	116 56	49	70	1 06	1 10	1 18	1 09
VIF		2 10	2 68	2 11	2 20	1 21	1 13	2 51	1 57	1 37	1 26	1 13	1 25	1 19	1 16	1 17
1 Entry mode	1															
2 Intensity of non-equity experience	- 195 **	1														
3 Diversity of non-equity experience	- 079	464 ***	1													
4 Intensity of equity experience	228	337 ***	250 **	1												
5 Diversity of equity experience	431 ***	057	253 **	632 ***	1											
6 International experience	256 ***	014	134 †	241 **	306 ***	1										
7 IE intensity	- 097	136 †	049	- 046	- 079		1									
8 IE diversity	- 070	403 ***	761 ***	266 **	280 ***	068	043	1								
9 Firm age	038	541 ***	272 **	302 ***	166 *	069	162 *	265 **	1							
10 Firm size	174 *	189 **	202 **	323 ***	342 ***	114	001	201 **	291 ***	1						
12 Asset specificity	272 **	- 124 †	- 089	077	151 *	093	- 085	- 036	013	086	- 088	1				
13 Uncertainty	- 195 **	176 *	017	- 068	- 234 **	- 173 *	052	038	099	- 210 **	047	067	1			
14 Motive market exploitation	155 *	111	040	125 †	220 **	006	- 201 **	118	059	092	063	142 †	123	1		
15 Motive know-how access	050	- 046	- 041	022	020	192 **	099	- 037	079	- 074	- 136 †	185 *	075	020 *	1	
16 Cultural distance (GLOBE)	- 127 †	213 **	152 *	172 *	057	032	- 051	157 *	122 †	- 104	- 020	014	169 *	006 **	152 *	1

TABLE 2

Logistic regression results: foreign market entry mode choice

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Constant	-.583 *	-.476	-.535 *	-.632 *	- 508 †	-.210
Control variables						
Age	.009	.010	.011	.010	.010	.011
Size	.000	.000	.000	.000	.000	.000
Industry	.271	502	.502	.591	519	.550
Asset specificity	.765 **	.751 *	.762 *	.803 **	.743 *	.749 *
Internal uncertainty (cultural distance)	-.250	- 271	-.255	-.279	- 275	-.279
External uncertainty	-.225	- 209	-.196	-.201	- 204	-.212
Motive market exploitation	.182	220	.260	.345 †	217	.207
Motive know-how access	.020	.015	-.001	-.017	.019	.030
International experience (IE)	.324 †	351 †	.577 *	.664 **	351 †	.385 †
IE intensity	-.025	-.004	-.002	-.002	-.002	-.003
IE diversity	-.020 *	-.016	-.010	-.012	-.015	-.021
Direct effects						
Intensity of equity experience (IntEQ)	.001	.021	.017	.017	.018	.016
Diversity of equity experience (DivEQ)	.270 ***	246 ***	.224 **	.218 **	249 ***	.343 ***
Independent variables						
Intensity of non-equity experience (IntNEQ)		-.030 *	-.036 **	-.031 *	-.032 *	-.030 *
Diversity of non-equity experience (DivNEQ)		.000	-.004	-.014	.000	.005
Interaction effects						
IntNEQ x IE			.014 †			
DivNEQ x IE				.026 *		
Nonlinear terms						
$IntEQ^2$					.000	
$DivEQ^2$						-.019 †
Model fit						
LR χ^2	71.602 ***	78.092 ***	81.316 ***	84.679 ***	78 211 ***	81.090 ***
$\Delta LR\chi^2$ (vs. Model 1)	-	-	9.714	13.077	6.609	9.488
R^2 (Cox & Snell)	.321	344	.356	.367	345	.355
R^2 (Nagelkerke)	.430	.461	.476	.492	.462	.475

Note: Dependent variable = Entry mode;
logit coefficients
***$p \leq 0.001$; **$p \leq 0.01$; *$p \leq 0.05$; †$p \leq 0.1$
N=185

FIGURE 1

Non-linear effect of diversity of equity entry mode experience

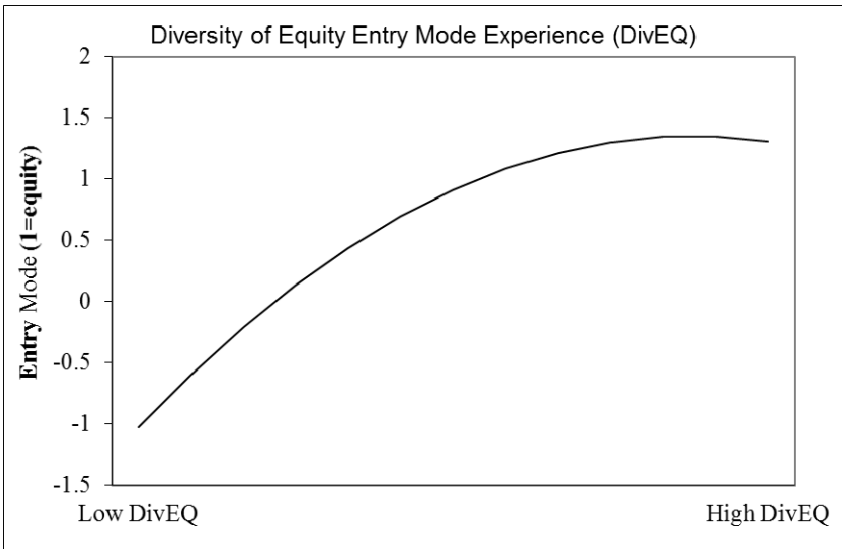
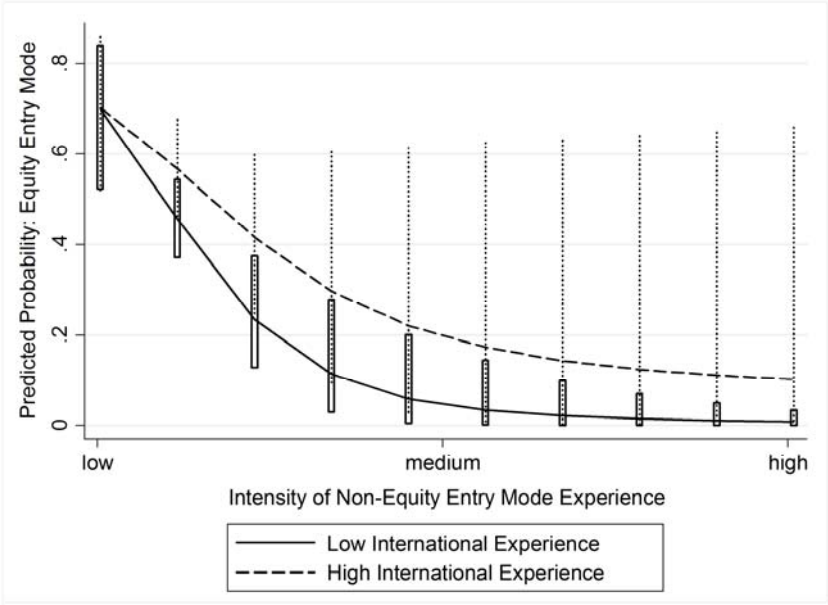


FIGURE 2

Interaction plots: Intensity of non-equity entry mode experience x International experience (a) Predicted probability for low and high levels of international experience; (b) Delta predicted probability for low and high levels of international experience



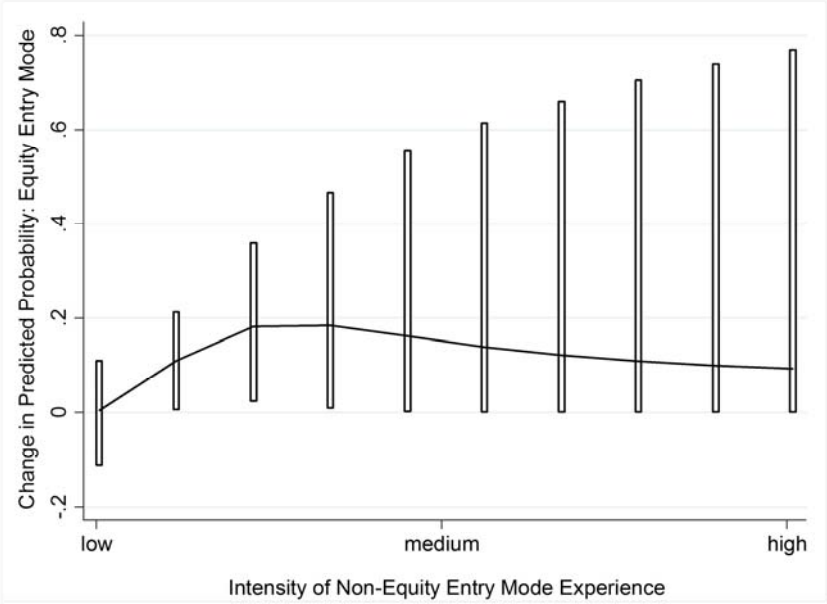
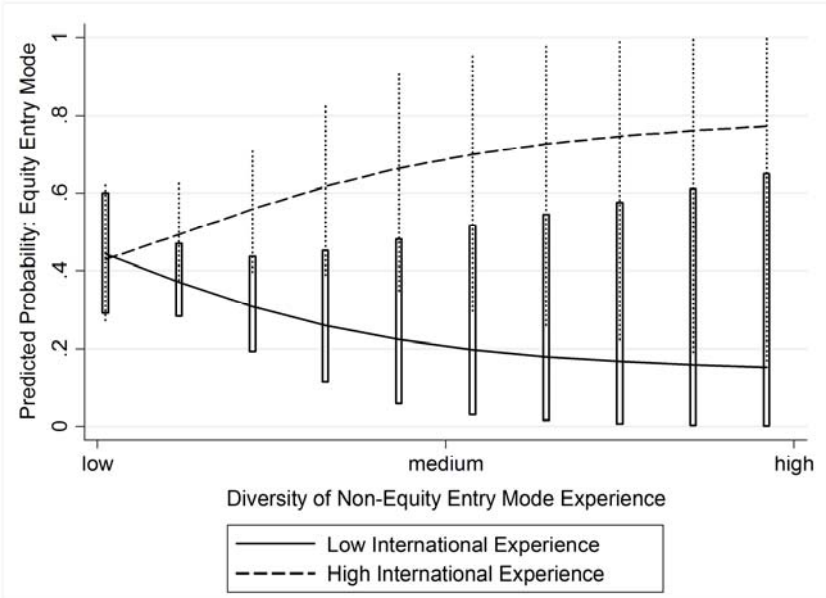
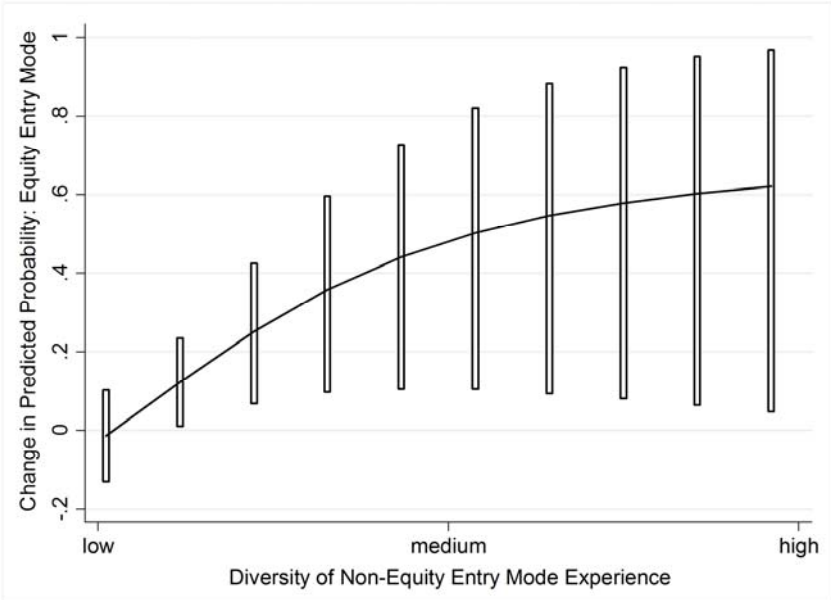


FIGURE 3

Interaction plots: Diversity of non-equity entry mode experience x International experience (a) Predicted probability for low and high levels of international experience; (b) Delta predicted probability for low and high levels of international experience