

Patterns of internationalisation of Finnish SMEs in Estonia: Preliminary survey results

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ABSTRACT

Objective: The objective of this paper is to look at the patterns of the internationalization process of Finnish SMEs and how it fits the internationalization models. Discussions are based on the interrelated theories of internationalization specifically the Uppsala model, Network approach and Models of International Entrepreneurship. This work also presents an intense analysis of the level of internationalization among SMEs, the mode of entry, motives and barriers for internationalization.

Research Design & Methods: The empirical research was carried out in the period of January 2018-August 2018. Data were collected through a mail survey questionnaire and 121 usable responses were received. The data was then analyzed in SPSS software by the cross-tabulation method to achieve the results.

Findings: Findings indicate that the majority of Finnish SMEs that started international operations follow a step-by-step approach of internationalization. Exporting was a major mode of entry into foreign markets, capturing market share was the main motive, and lack of market knowledge was a major barrier for internationalization.

Contribution & Value Added: It is confirmed that Uppsala, Network and Entrepreneurship models are still valid, and majority of Finnish SMEs follow the systematic internationalization process. This study contributes to the internationalization process of SMEs and calls for further comparative research in other markets to validate the results. It is confirmed that there is no single theory, which explains the internationalization process of SMEs and this work provides the threshold for theory development.

Article type: research paper

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INTRODUCTION

Small and medium-sized enterprises (SMEs) play an important role in the economic growth of the countries and consequently, the internationalization process of SMEs has become a subject of academic, political, and governmental attention and research (Oviatt & McDougall, 1994). Due to a reduction in trade barriers and tariffs, regional economic integration and World Trade Organization (WTO), together with the development of information and communication technology provide the opportunity for small and medium enterprises (SMEs) to expand their business into foreign markets and increased their revenues (Ripolles, Blesa, & Monferrer, 2012). Erramilli and D'Souza (1993) argued that what distinguishes SMEs from large multinationals enterprises (MNEs) are their managerial style, ownership, and independence and furthermore, their limited resources may lead them to very different international strategic choices in contrast to large firms (Zacharakis, 1997).

The motives for internationalization are given numerous names by different authors in the wider literature “motives” (Alexander, 1997), “triggering cues” (Wiedersheim-Paul, Olson, & Welch, 1978), “facilitating factors” (Treadgold & Gibson, 1989), “influence of imitation, network position, and international experience” (Oheme & Bort, 2015), “factors influence the choice of internationalization” (Doherty, 2009), “internationalization process” (Oviatt & McDougall, 1995; Wolff & Pett, 2000). These studies examine the characteristics of SMEs, their motivation for international growth; entry mode selection, barriers or obstacles of internationalization. Later, entry mode decision is considered such an important strategic decision and the success of SMEs depends on the preparation and execution of strategy (Knight, 2000). In brief, it remains challenging for many SMEs to internationalize successfully and what are the main factors which affect the entrance of SMEs into foreign markets (Chang & Yu, 2008).

This study sheds the light on the pattern of the internationalization process of Finnish SMEs and how it fits within different models. Hence, the objective of this article is to look at major internationalization theories suggested by numerous researchers (Burgel & Murray, 2000; Oviatt & McDougall, 2005) and to shed the light on which theory or framework explains the internationalization practice of Finnish SMEs in the best way. The second objective is to upsurge the understanding of the behavior of Finnish SMEs in the context of internationalization.

Patterns of internationalization of SMEs must be investigated and, in this investigation, author chooses Finnish SMEs, which have operations in Estonia. We can conclude whether they follow systematic internationalization process or rapid internationalization and what are the motives and barriers of internationalization by examining the behaviour of Finnish SMEs. In order to achieve the main objective of this study following research questions have been formulated:

RQ1: What are the main motives to internationalization for Finnish SMEs?

RQ2: What are most suitable entry modes starting a business in a foreign market?

RQ3: What are the barriers to internationalization for Finnish SMEs to expand the business in foreign markets?

According to Carter and Jones-Evans (2006), there is no single definition of small enterprises. In this study, the European Commission's recommended definition for small and me-

dium-sized enterprises has been followed. According to the European Commission (2003) “enterprises qualify as micro, small and medium-sized enterprises if they fulfil maximum ceilings for staff headcount and either a turnover cap or a balance sheet ceiling” (p. 39).

THEORIES OF INTERNATIONALIZATION

Scholars and academics have described the internationalization concept numerous times using many different perceptions and variables. The term ‘internationalization’ is indefinite, and its definitions vary depending on the occurrence they include. According to Penrose’s (1959) internationalization mainly focuses on the firm’s core competencies and opportunities in the foreign environment. Welch and Luostarinen (1988) defined internationalization as the process by which firms increase their involvements in international operations. Afterward, Calof and Beamish (1995) defined internationalization as “the process of adopting firms’ operations (strategy, structure, resource, etc.) to global environments” (115-131). This paper will highlight three frequently cited internationalization theories, known as the Uppsala model, Network theory, and Models of international entrepreneurship.

Uppsala model aimed to clarify how firms expand their operations in foreign markets and meanwhile how their resource commitment increase. The theory describes foreign market choice and explains other foreign direct investment (FDI) choices as well (Johanson & Vahlne, 1977, Luostarinen, 1979). Uppsala model has two dimensions: “market commitment” and “market uncertainty.” Market uncertainty states that there can be several changes in the future due to high competition, industry decline, political stability etc. This framework illustrates that due to the lack of market knowledge firms avoid entering into the foreign market through foreign FDI mode and adopt less risky entry mode (export). A firm may select FDI mode or higher market commitment modes at the time of entry if the foreign market is growing or have a huge potential of growth. (Johanson & Wiedersheim-Paul, 1975). Several academics have initiated it unacceptable in some cases while some others accepted it with amendments. Moreover, this model is predominantly suitable for firms at the early stages of internationalization or have limited resources (Shahzad, & Elenurm, in press). On the other hand, a quick change in technology and today’s level of globalization might have changed this internationalization theory into an inadequate model for the mainstream of today’s firms.

Johanson and Vahlne (2009) reviewed their previous internationalization model by applying a basic networking overlook. The following figure shows the main element and changings in their revised model. Uppsala revised model sheds the light on state and change variables and their impact on each other. The first variable illustrates opportunities, which exist besides the knowledge, and the second variable is inside the model position of the network. The Network position plays a significant role in the internationalization process. There are several activities e.g. learning, trust building, knowledge sharing, creating synergy through cross borders teams and these are the changing aspects of this new version of the Uppsala model (Johanson & Vahlne, 2009). The state and changing dimensions of the model deliver an intense interface contrivance to clarify the internationalization process in a network context. Based on this model, firms, which have business operations in foreign countries, try to overcome on lack of knowledge about the foreign market and make sure their operations run smoothly. (Johanson & Vahlne, 2009).

Moreover, this framework validates the internationalization of firms, in a network context, based on the interface of two dimensions include state and change.

Network theory argues that modern high-technology firms do not follow systematic internationalization process; rather they attain an earlier internationalization through the organizational experience and strong bond with several partners in local and foreign markets. (Mitgwe, 2006). Nowadays firms facing high competition due to the advancement of technology, open borders, ease of doing business, and open trade contract among the nations. Emerson (1981) argues that network is a set of different connected business relationships, in which each interchange relation is between business firms that are intellectualized as cooperative players. Network theorists see the firm's internationalization as a regular expansion from network relationships with foreign individuals and firms (Johansson & Mattson, 1988). The position of the firm in the network (market) is the most significant motive for internationalization. Network position depends on two major elements: Degree of internationalization of the firm, and the degree of internationalization of the network (market). Based on these two elements, four market positions has been introduced for firms: Early Starter, Lonely International, The Late Starter, and International among others (Johanson & Mattsson, 1988). It is established that network-based model's argument quite relevant for born global and international new ventures (INVs) but still Uppsala model is followed by the huge number of firms due to several reasons like limited financial resources, lack of market knowledge, risk and uncertainty, high completion etc. (Shahzad, & Elenurm, in press).

According to Kontinen and Ojala (2011), argue that weak and strong ties and social capital have mainly applied in the context of SMEs. Sharma and Blomstermo (2003) argue that a relationship approaches to focus on network relationship with stakeholders and create synergy for all partners not only for the firms. When firms enter into the foreign market selection of a suitable partner is one of the biggest challenges and therefore, it is used to clarify the selection of foreignmarket and entry mode based on choosing an appropriate partne. Researchers have used them to validate the international opportunity appreciation by entrepreneurial firms, selecting a foreign market by born globalfirms (Prashantham, 2011). Hereafter, network approach provides a narrow down approach specifically in case of SMEs and born globals in order to cope with their limited financial resources, lack of market knowledge, and weak network in foreign market.

The term "*International Entrepreneurship*" (IE) originates from Morrow (1988). He recommended that technological advancements and markets with open borders and cultural awareness provide immense opportunity to firms for global expansion (Oviatt & McDougall &, 2005). Entrepreneurs with a clear global mindset often start born global enterprises and studying them involves appreciative the important transition of procedures, structures, and organizational mindsets at numerous organizational levels (Weerawardena, Mort, Liesch& Knight, 2007). An International new venture has been defined as a "business organization that, from inception pursues to drive substantial competitive advantage from the use of resources and the sale of outputs in several countries" (Oviatt & McDougal, 1994, pp. 45-64). IE research is often regarded as starting with Oviatt and McDougall's (1994) pivotal article on international new ventures (Wach,

2018; Zahra, 2005), which defined the antecedents of as well as the necessary and sufficient conditions for the emergence of born globals (e.g., Madsen & Servais, 1997) or “international new ventures” (INVs)(e.g. Oviatt & McDougall, 1994).

In contrast to the Uppsala model of internationalization, this approach focuses more on rapid internationalization. Also, this theory asserts have described that as internationalization becomes a passion of new entrepreneurs, they possess an immense inclination towards learning and adopting supportive viewpoints, such as innovative ideas, concepts, knowledge, and mechanisms (Collinson & Houlden, 2005). Resource and competency-based theories of internationalization are an important addition to this area of literature. According to IE resources and competencies play an important role in the selection of internationalization strategies. Factors such as financial capability, material capability, and about others, learning capability are determining factors of internationalization. Eventually, the process of internationalization requires the mobilization of resources and competencies in the enterprise (Pantin, 2005; Ruzzier, Hisrich, & Antoncic, 2006). For SMEs to capture the opportunities in the international markets, the entrepreneurial resources, namely the financial and technological resources of the entrepreneur, are important (Dhanaraj & Beamish, 2003). The internationalization process can be influenced by the global vision of the founder, the entrepreneur (Gabrielsson & Pelkonen, 2008). Numerous studies have approved that international entrepreneurial orientation (IEO) is a vital cultural characteristic of born global firms (Knight & Cavusgil, 2004), though there is the second school of thought which believes that IEO is an imminent element of international entrepreneurship theory in general (Wach, 2015). International entrepreneurial orientation is considered a behavioral trait shared by business entities that start out seeking to attain a competitive advantage by expand their business operations in several parts of the world. Table 1 illustrates the comparison view of the above-mentioned models. The table not only sheds the light on main differences of Uppsala, network and IE models but explains main unit of analysis of the models as well.

Table 1. Comparison of theories

| Uppsala View | Network View | IE View |
|--|--|---|
| A development of continuing international engrossment with developing market knowledge and commitment of assets. | Internationalization is the utilization of network benefit. Relationship of a firm can be used as connections to other networks. | Preemptive internationalization procedure and entrepreneurial mind-set and activities in bringing new openings. |

Source: own compilation based on literature review.

ROLE OF SMES IN FINNISH ECONOMY

Historical development shows that Finland’s economy has transformed within a short period from an agricultural economy to a technology-intensive economy (Grönqvist, 2009). Moreover, Nikulainen (2008) argues that Finnish manufacturing and service sectors play a significant role in Finland’s economic development and the manufacturing industry not only evolved with time but introduce highly innovative products. According to Statistics Finland (2016), Finland is much behind in comparison to the other EU Member States with a 239 billion euros GDP rate and ranked 15th out of 28 countries. Finland had 51.8 billion euros of exports and imports were 54.7 billion euros in 2016. According to the Statistics Finland

(2012). SME's contribution was about 385 billion Euros in 2017. Finland has 283,563 enterprises of which 98% are SMEs employing less than 50 people. Moreover, 93.3% of Finnish firms have fewer than 10 employees. Finland's corporate structure has the following composition: 2% are large enterprises and 98% small and medium-sized enterprises. This shows SMEs cover a majestic portion of the corporate structure. The role of SMEs in the Finnish economy and employment is quite significant. SMEs are responsible for more than 36% of Finland's export revenue. As a small and open economy, Finland is very reliant on small and medium-sized enterprises and therefore the role of SMEs in the Finnish economy is crucial.

RESEARCH METHODOLOGY

Data for empirical analysis were collected via a survey questionnaire during the period of January 2018-August 2018. The population of this investigation is Finnish SMEs, which have international activities in Estonia, and the author chooses SMEs according to European Union definition. Data was collected from 550 SMEs from different industries all over the country. The questionnaire was pilot tested with managers in 8 SMEs who were involved during international expansion into foreign markets. It had been found after conducting the pilot test that there was complete appreciative of the theorized questions and supported our expectations of the manager's capability to answer them correctly and comprehensively. In total, initially 550 questionnaires were mailed: 19 were returned as non-deliverable, which compacted the sample size to 531 questionnaires. Overall, 121 usable questionnaires were received which represents an overall 22.78% present response rate. The data was then analyzed in SPSS software by cross-tabulation method to achieve the results.

EMPIRICAL FINDINGS

To characterize the respondents, it is necessary to point out that the target audience for collecting data are, CEOs (50%), Managing Directors (37.6%), Business Development Managers (7.4%) and others (5.0%). The majority of the SMEs came from the field of Engineering 27%, Wood products 22%, ICT 21%, Electrical & Electronics 16%, Health care 12%, Rubber Products 11%, and Plastic Products 11%.

Table 3 lists the frequency of SMEs from different industries, which have foreign operations in Estonia. Engineering with 22.51% on the top and followed by Wood 18.18%, ICT 17.75%, Electrical and Electronics 13.47%, Rubber products 9.09, Plastic products 9.09, and Health care 9.91%. There are 51 SMEs have 7-10 year of operations into foreign markets, 43 have 3-6, 16 have 1-2 and 11 have less than 1 year. Moreover, 15.70% SMEs employee 5 people, 38.01% employee 5-25 people, 19.85% employee 26-50 people, 14.87% employee 51-100, 9.09% employee 101-150, and 2.48% employee more than 150.

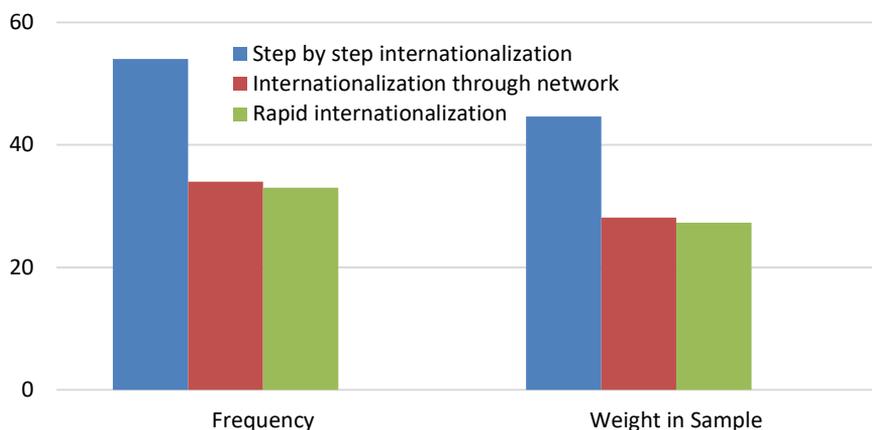
Figure 1 illustrates the internationalization process, where 44.63% highest number of firms used a systematic Uppsala approach for internationalization, while 28.10% of firms mentioned that it utilizes its relations with stakeholders and adapts network approach. On the other hand, 27.27% of firms used rapid internationalization approach.

Figure 2 highlights the key motives of why Finnish SMEs internationalize. It has been found that majestic reason of internationalization was capture market share 42.14% top on the list, which followed by revenue generation/increases in profit 28.11% where 19.85% respondent chose market knowledge, the vision of the owner 9.09% and other reasons are 0.81%.

Table 2. Characterization of SMEs by industry, year of operations and number of employees

| Industry | Frequency | Weight in Sample |
|----------------------------|------------|------------------|
| Engineering | 27 | 22.51 |
| Wood and Wood products | 22 | 18.18 |
| ICT | 21 | 17.75 |
| Electrical and Electronics | 16 | 13.47 |
| Rubber Products | 11 | 9.09 |
| Plastic Products | 11 | 9.09 |
| Healthcare | 12 | 9.91 |
| Total | 121 | 100.00 |
| Years of operations | | |
| Less than 1 year | 11 | 9.09 |
| 1-2 years | 16 | 13.22 |
| 3-6 | 43 | 35.44 |
| 7-10 years | 51 | 42.25 |
| Total | 121 | 100.00 |
| Employees | | |
| Less than 5 people | 19 | 15.70 |
| 5-25 | 46 | 38.01 |
| 26-50 | 24 | 19.85 |
| 51-100 | 18 | 14.87 |
| 101-150 | 11 | 9.09 |
| More than 150 people | 3 | 2.48 |
| Total | 121 | 100.00 |

Source: own elaboration based on the survey.

**Figure 1. Internationalization Process of SMEs**

Source: own elaboration based on the survey.

Figure 3 illustrates the terms of mode of entry into the foreign market, exporting is the most popular mode with 62.80%, while other 14.88% choose joint venture, 10.75% choose wholly owned subsidiary, licensing 9.09% and franchising 2.48%.

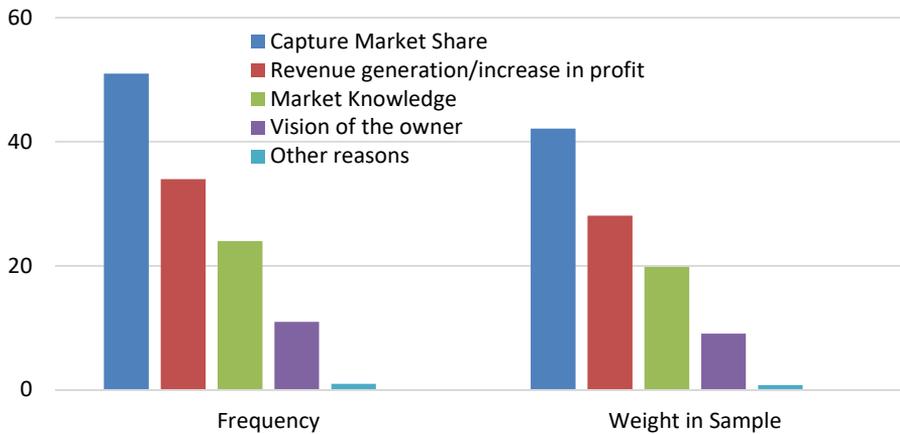


Figure 2. Motives of Internationalization

Source: own elaboration based on the survey.

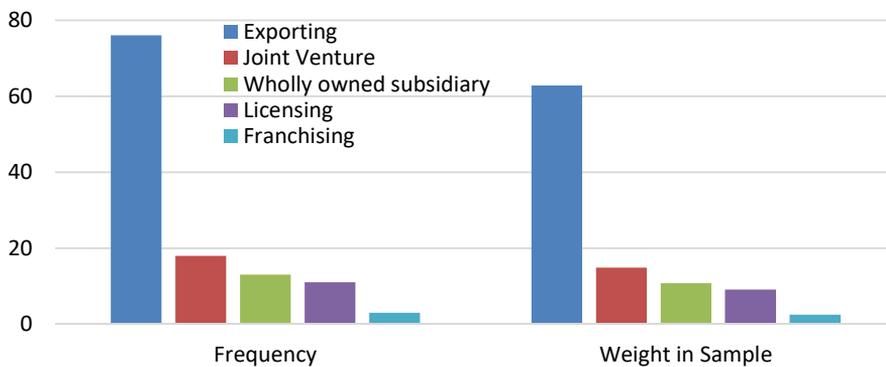


Figure 3. Mode of Entry

Source: own elaboration based on the survey.

Figure 4 list out the barriers to internationalization as indicated by respondents of the SMEs. According to results, lack of market knowledge top of the list with 29.75%, following by weak or lack of network in foreign market 22.33%, risk and uncertainty 15.70%, how to make profit 12.39%, cultural distance 7.43%, high competition 6.62%, and less advanced institutions 5.78%.

Next section sheds the light on conclusion, recommendations and direction for future research.

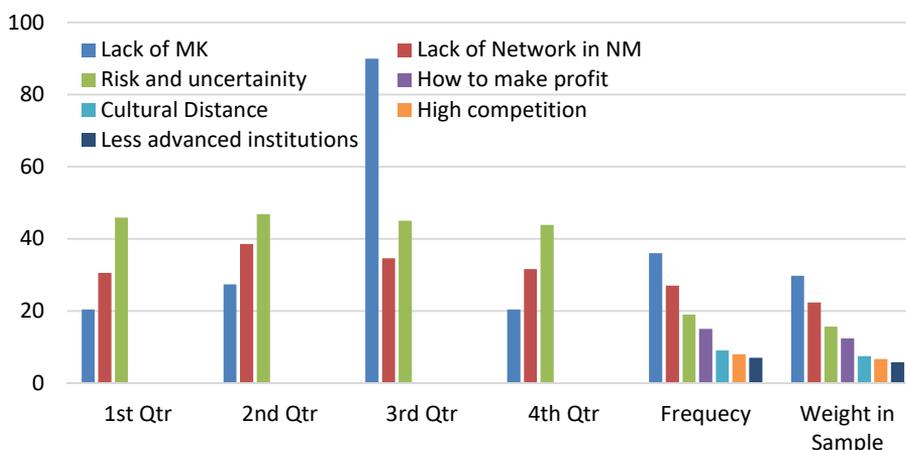


Figure 4. Barriers of Internationalization

Source: own elaboration based on the survey.

CONCLUSIONS

According to data capture, market share was the main reason for internationalization. It is quite clear that the Finnish market is very small and therefore, SMEs must go for other foreign markets for generating more revenues. Finding this investigation is like Abdullah and Zain's (2011) work, which shows that market share and financial success motivate SMEs to internationalize. To obtain this objective SMEs use different methods and strategies when penetrating foreign markets. Shahzad and Elenurm (in press) investigated entry mode strategies of Finnish SMEs and found that firm, country, and industry level variables are significant in the choice of market entry modes. Laufs and Schwens (2014) have conducted a systematic literature review (1986 to 2012) on market entry mode choice of SMEs about explain the theoretical framework applied to explain SME's internationalization. Authors confirm that there is a need to conduct more research on the topic of internationalization of SMEs (e.g., Burgel & Murray, 2000; Jones, 1999; Zacharakis, 1997). Shahzad (2019) investigated Finnish retail SMEs that have an investment in Russia and confirmed that SMEs follow the systematic internationalization process of internationalization. He also argued the main mode of entry was franchises instead of export. The finding of this work differs from the early investigation and provide new insights for an instance, Shahzad and Elenurm (2019), investigated Finnish SME's determinants of market entry mode choice in Estonia and found that firm, country, industry, and institutional environment affect the decision of market entry mode choice. Hessels and Parker (2013) sheds the light on constraints of internationalization for European SMEs and found that having a foreign supplier is a more common internationalization strategy among European SMEs then exporting. Korsakiene and Tvaronavicien (2011) collected the data from 2000 to 2015 on SME internationalization. They have found that the majority of scholars suggested that the main barriers of SMEs internationalization were the unstable legal, political and economic

environment, the lack of knowledge of the foreign market, cultural distance and inappropriate support of the government. Moreover, the important role of the entrepreneur/manager in the internationalization of SMEs has been confirmed by several studies within literature (Reid, 1981) The choice of foreign market entry mode is an important strategic decision for SMEs and complex research issues. According to Calof and Beamish (1995), Chang and Yu (2008,) suggested that SMEs differ their larger counterparts in several ways, which impact important strategic decisions and inappropriate entry mode decision may lead to damages with serious consequences because of their lack of resources.

According to data, a small number of firms adopted greenfield or wholly owned subsidiary as an entry mode due to a highly expensive way to enter into the new market. If we compare the Uppsala model and findings of this investigation then it will be obvious that SMEs use exporting as the first step to enter into the foreign market and it will work as a stepping-stone towards other modes of entry e.g. licensing franchising, joint venture, and wholly-owned subsidiary. The majority of firms pointed out that the reason behind choosing export, as an entry mode, is to avoid risk in the context of financial and market knowledge limitations. On the other hand, there are still many SMEs that adopt the rapid internationalization process instead of systematic expansion due to market knowledge, entrepreneurs experience, abundant financial resources, and product type.

This study sheds the light on a very important element that there is no specific framework or theory, which explains the internationalization process of Finnish SMEs. Uppsala model, Network theory and IE Models are quite relevant when we look into the internationalization process of SMEs, in fact, the Uppsala model is still relevant for SME's context which has been received a lot of criticism recently because not all SMEs are born globals in nature. This study underwrites in a way that it provides significant information for managers of SMEs, entrepreneurs, government institutions, policymakers, through the underlining of vital topics that affect Finnish SME's decision of internationalization. There is very clear evidence that there are several SMEs, which has not started international operations due to a lack of market knowledge, financial resources, and due to weak network connections in a foreign market. These are the areas where Finnish institutions could play a very active role in assisting Finnish SMEs in international expansion. In the present study, efforts have been made to ensure the generalizability of the empirical results, a few limitations of the study must be acknowledged. Overall, this study could not cover all aspects of the internationalization of SMEs. Therefore, the future study may consider investigating the internationalization process of SMEs in specific industries like retail, ICT, manufacturing, wood, etc. in Estonia and then compare the results with other countries as well. Moreover, it would be interesting to investigate the role of different factors in the choice of specific entry modes like culture, institutions, etc. Finally, future studies may investigate why SMEs follow a specific internationalization model and what are the factors, which describe those decisions.

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