

Work-in-Progress

**The Internet and Internationalization:  
Nova Scotia SMEs\***

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\*The financial support of the Centre for International Business Studies at Dalhousie University in undertaking the research study is gratefully acknowledged.

**Abstract**

Internationalization processes in the context of the Internet economy are examined. Case study research was conducted with six Nova Scotia SMEs. Findings from this exploratory study include (1) stage-based theories do not reflect company experience, (2) multi-domestic marketing strategies appear dominant, and (3) location and country-of-origin effects persist, in the online environment. Thus, while the Internet may offer global reach, commerce is still conducted locally. The paper also notes a number of challenges faced by Internet-based companies as they expand their business interests, as well as ideas for future research.

## 1. Introduction

Theories of international business generally see companies developing their foreign business operations in a linear pattern, from purely domestic to gradual export development, and ultimately to full global operations. A parallel viewpoint is that companies develop expertise locally, and then seek to exploit this further on an international scale, beginning with exports to close markets or ones with which the entrepreneur has some experience, before expanding more broadly. But these ideas—of orderly and gradual development of foreign business—derive from pre-Internet times. In today's world, some would question these ideas, arguing for example that a company with a web site in effect is immediately a multinational, since customers around the world are just a click away from being able to do business. In this way, smaller companies' resource shortcomings are much less critical than in the past. Research, prospecting, communication and transactions can all be carried out via the Internet. In this respect, the Internet is said to have leveled the playing field between major corporations. Although many would agree that the Internet has such potential, what is the reality for SMEs?

Although considerable professional and popular writing exists on this topic, for the most part, academic researchers have shied away from empirically examining the Internet and international marketing. Given the potentially "liberating" nature of the Internet for smaller companies, it is surprising that few studies have examined its impact on international business expansion among SMEs. More scientific research is warranted in this important area. Key questions that might be tackled include the following. How has this new environment affected companies' international strategy and decision-making? As the Internet appears to change the role of geography, has the process of internationalization changed? Do entrepreneurs see a global marketplace from the beginning?

This paper reports on a modest first examination of some of these questions. It presents findings from an exploratory investigation into the experience of six SMEs as they adjust to take advantage of the opportunities presented by Internet technology. Specific questions addressed include: Are SMEs using the Internet in new ways, and specifically for international activities? How do the international activities of Internet-based companies compare with extant theories of international business? Are there any patterns that emerge at this early stage of business development?

The paper begins with a brief review of the internationalization concept and several process theories. Profiles of the six case companies are then presented and a discussion of their common experiences follows.

## 2. Literature Review

### 2.1 Internationalization Theories

Internationalization theories attempt to explain why companies choose to operate beyond their domestic market and the strategies and structures they develop to do this (Coviello & MacAuley, 1999). Many theories have been advanced to explain the process of internationalization, from Vernon's (1966) international product life cycle to Dunning's (1977) eclectic theory. The Uppsala School's stages theory has been particularly influential since its initial publication in the 1970s.

Derived from case studies of the of internationalization paths taken by a number of Swedish companies, this conceptualization has been influential (Johanson & Wiedersheim-Paul, 1975; Johanson & Valne 1977). The stages theory posits companies as being either (1) a non-exporter, (2) an indirect exporter, or having (3) overseas sales operations, or (4) overseas production units. Companies progress from one stage to another as they gain experience and comfort in dealing with foreign customers and operating in international markets. As company knowledge increases, so too does international commitment. This conception of internationalization has influenced many scholars as well as the design of many government export policies and programs.

In recent years, stages theory has come under increasing scrutiny. Research has revealed companies that have expanded their market interests more quickly than the theory would suggest, as well as taking differing internationalization paths. Trade barrier reductions, the growing importance of high technology sectors, and global market growth all help explain the quickening pace of development and changing approaches (OECD, 1998). As a result of contrary findings, other approaches to internationalization have been widely discussed and examined. Three streams of research focus on business networks, "born global" companies, and international new ventures.

European scholars have drawn attention to the fact that companies do not exist in a vacuum; rather they exist within business networks which often profoundly influence the domestic and foreign market strategies and operations of single entities (Johanson & Mattson, 1988; Ford, 1997). Research has also focused on those companies that are seemingly "born global"; in other words, companies that operate internationally from the very first day (Knight & Cavusgil, 1996). Related to this is Oviatt and MacDougall's (1994, 1996) research on international new ventures (INV). The nature of the product, industry norms and the orientation of the entrepreneur are primary components of the INV model. High R&D costs and shorter product life cycles force companies to recoup investments quickly and, as a result, market expansion is often rapid. Converging international standards for some products have likewise created a global market where many competent suppliers exist (e.g. computer components). In order to

compete in this market, manufacturers are forced to establish a global marketing and supply capability in short order.

## 2.2 The Internet and International Marketing

The effect of the Internet on company internationalization has yet to be scientifically explored. Quelch and Klein (1996) predicted that companies would become global marketers faster owing to the Internet's low cost communications and ease of access to foreign consumers. Hamill (1997) is of similar mind, seeing improved communication and access as permitting SMEs to overcome many of the traditional barriers they faced in international marketing. Consequently, he expects Internet-enabled companies to pursue international sales at earlier stages in their development. However, access to markets and customers is a double-edged sword. Sawhney and Mandal (2000) argue that the Internet exposes companies to global competition from the beginning. This puts pressure on companies to consider/pursue international sales very early in their development.

As the Internet becomes more international, the opportunities for foreign sales will increasingly become apparent. As in other spheres of business, the conventional wisdom is that first-movers can derive substantial advantages through scaling their operations globally and erecting barriers that will be difficult for latecomers to overcome. However, the dot.com implosion of the last year has demonstrated that being first is no guarantee of success. Many companies have been disappointed with their aggressive expansion strategies—whether at home or in foreign markets. In light of the great potential seen for Internet-enabled businesses, as well as the dearth of writing focusing on international business and marketing among SMEs, an exploratory study seemed merited.

## 3. Methodology

Given the newness of the topic area, case studies were deemed the most appropriate study vehicle. Yin (1994) points out that case studies are best used to evaluate "how" and "why" questions, particularly with current phenomena. Eisenhardt (1989) elaborates on the process of building new theory from case study exploration, and its usefulness in promoting understanding.

The University of Texas at Austin's Center for Research in Electronic Commerce (2000) has devised a four-level schema for classifying and measuring the Internet economy. This schema was used to develop a study sample. The four levels cover infrastructure, applications, intermediaries and commerce. As the focus of this study is on SMEs, companies from the infrastructure layer were not included. Because of the large-scale investment required for this sector, it is almost exclusively the preserve of very large companies. SMEs were categorized as those having fewer than 100 employees and C\$20 million in annual sales.

An initial list of Internet-related companies was compiled from a number of sources, including Industry Canada, the

Information Technology Association of Nova Scotia, and various web directories. After compilation, companies were allocated to one of the four layers and a number selected from each layer for further study and contact. A final list of six companies was compiled and contacts made. All interviews were conducted in November 2000 following a semi-structured format by the first author to ensure consistency and comparability. A short profile of each company follows.

#### 4. The Companies

##### 4.1 Application Level

InfoInerActive Inc. ([www.infointeractive.com](http://www.infointeractive.com)) is a producer of Internet call management software applications that inform Internet users using telephone dial-up connections of incoming calls and allow users to accept or transfer calls to another device. The product is resold primarily through telecommunications companies or large Internet service providers as part of a bundled package of services. Despite the early investment from a local telecommunications company, initial sales were in the US, which continues to be its primary market representing over 80% of sales. Expansion to the United Kingdom and Europe has begun, and there are plans for Asia and South America within the next year.<sup>1</sup>

Clear Picture Inc. ([www.clearpicture.com](http://www.clearpicture.com)) began offering computer diskette-based surveys for corporations and large organizations and has recently migrated to the Internet. It offers its surveying services through application service provider (ASP) agreements where clients purchase use and access to the software which resides on servers in Nova Scotia. The firm operates a remote support office in California and the US represents over 90% of sales. Plans call for expansion to the United Kingdom and Europe within the next year.

##### 4.2 Intermediary Level

Salter New Media Inc. ([www.salternewmedia.com](http://www.salternewmedia.com)) was started as a joint venture between a telecommunications company and a media production company to develop branded proprietary web sites. The first to offer a community-based auction site, the company initially targeted select US cities for inclusion yet had to withdraw given the large investment in promotion required to gain users. The company also produced several specialized content portal web sites. All of the sites are currently targeted solely to a domestic audience, however the company is developing plans to launch foreign sites in the United Kingdom and Australia and is actively seeking partners. All revenues are currently from Canada.<sup>2</sup>

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<sup>1</sup> The company was recently acquired by AOL.

<sup>2</sup> The parent company of Salter New Media has been acquired by Canadian film company Atlantis Alliance.

GenieKnows.com Ltd. ([www.genieknows.com](http://www.genieknows.com)) developed an application that combines the results from the top 26 search engines with its own index and artificial intelligence filtering system to offer users enhanced search capabilities. The company licenses its search technology to small portal sites and corporate web sites, as well as operating its own search portal. The site regularly receives hits from 88 countries, yet 90% of revenues are from the US. The company plans to offer country specific search portals for 12 countries offering local search results.

#### 4.3 Commerce Level

Lobster Direct Ltd. ([www.lobsterdirect.com](http://www.lobsterdirect.com)) was the first company to sell live seafood on the Internet and continues to lead the consumer market. The company uses local third-party seafood suppliers to fill and deliver orders. This arrangement eliminates border problems where delays can prove costly. The company uses country specific web sites offering unique pricing and shipping information for Canadian and American consumers. Canada is currently responsible for approximately 20% of sales, with the rest all coming from the US. There are no plans to service additional countries at this time.

Vintopia.com Ltd. ([www.vintopia.com](http://www.vintopia.com)) is an online retailer of winemaking equipment and supplies developed to solely service the US market. The company operates a bricks-and-mortar retail store and collaborated with an Internet consulting company in developing its virtual presence. The latter company paid for its development and receives revenue based on transactions, significantly lowering the risk of the initiative for the merchant. As a producer and distributor of wine products, the company has recently added a business-to-business site that is produced and managed in-house. There are no plans to expand the service beyond the US.

### 5. Findings and Analysis

The experience of the six companies reveals general patterns that help to illuminate how the Internet sector is developing. It is apparent that small companies are adapting to the new technology and entrepreneurs have embraced the potential of the Internet in reaching and servicing new customers. All of the companies examined are entrepreneurial ventures where the founder has sought to experiment and deliver to a new market. The technical infrastructure and skills have not been obstacles to participating as most have been able to partner with specialized providers or have brought the skills in-house. Entrepreneurs have effectively managed the change and risks involved.

The companies did not share similar histories, though all were relatively young companies. The average age was five years, and all have changed significantly since their founding. Two are public companies, with the remainder all being privately held and only one with plans to go public. Only one company was founded

solely on the Internet, the others were extensions of existing businesses.

Most of the web-sites were produced by professional designers. All have seen extensive revisions and upgrades. Some companies are now developing or hiring the web skills in-house as they look to the next versions of their sites. All sites are simple, without sophisticated components, yet their ease-of-use meets the needs of customers. Difficult functions such as credit card processing and site hosting has all been outsourced to third party providers. This is most effective and permits companies to maximize the use of their scarce capital.

### 5.1 Entrepreneurs

The backgrounds of the founders varied considerably, yet none had a pure technology training or orientation. Some even lacked direct experience in the particular niche they wanted to serve. A strong sense of curiosity and risk taking, along with a desire to experiment led them to the Internet to see what could be done. Partners in both technology and industry were readily available and the combination with managerial expertise and capital has proved successful. Most bring a passion for business and experimentation, along with the desire to try something new. The entrepreneurs confirmed that the Internet has lowered some of the export resource requirements for SMEs, making it easier to embark in this new direction.

All of the entrepreneurs in this study had some business experience prior to their present position, often in other technology fields or similar businesses. They saw the Internet as providing a new environment and infrastructure to service customers and sought out a setting in which to exploit this opportunity. In some cases, this venture was an extension of an existing business whereas in others it was a new creation. Extended businesses offered a new service or explored a new market, taking advantage of the Internet's special properties.

### 5.2 International Marketing

As five of the six companies are actively engaged in international sales, exporting and international marketing are important aspects of their business plans. The Internet was seen as both an entry channel and service platform for companies, greatly enhancing their ability to enter and build foreign markets.

Companies have adopted an international marketing approach rather than a global one. This multi-domestic strategy sees markets as sufficiently different to warrant a unique marketing approach for each. As one informant noted, "The Internet may be global, but commerce is local." At the retail level, this is particularly important, as consumers need to be enticed to trust the company to fulfill orders.

Beyond facilitating trade, the Internet has also increased awareness of distant opportunities and provides access to information that was previously unavailable or not affordable.



Entrepreneurs can access information on new markets, industry trends, and supplier details as never before. This may partially level the playing field with larger competitors and all of the companies studied cited this as one of the main benefits of the Internet. Information helps managers to make decisions that are better informed and permits business expansion to be more carefully weighed, and all of the entrepreneurs have readily embraced this aspect.

### 5.3 Internationalization Paths

The companies examined have all sought international sales from the beginning and most view the domestic market as secondary. In some cases, the web site has been created to solely serve foreign customers. In others, an average of 90% of sales is from outside of Canada.<sup>3</sup> Such a level of export intensity goes beyond what is usually found in traditional SMEs. The reduced time-span to achieve foreign sales and heavy dependence on international markets is interesting and results from a combination of the possibilities provided by the new international environment, as well as customer access afforded by Internet technology.

Stage-based theories may be more applicable to traditional companies seeking to expand rather than Internet-based new entrepreneurial ventures. The Internet has reduced the investment and resources required to operate, thus opening many new avenues for companies, which all have tried to exploit. The Internet provides a direct channel to service customers and circumvents costly distributor arrangements. Direct interaction also permits greater potential learning, since intermediaries are not present to impede information flows. While the companies presented here are attracting and servicing foreign customers, it is difficult to characterize them as truly global ventures. International sales may be crucial to their operations, however this is largely confined to the US and few have sought to expand further. In their dependence on the US market, these Internet-enabled companies resemble Canadian SMEs in more traditional fields. The companies have not sought to build global economies or scale as INV theory would suggest. They are responding to perceived foreign opportunities and using the technology to reach these markets, not seeking to build world-class enterprises.

With the technology and application providers, they have structured their businesses such that the technology is compatible worldwide, although at present there are no plans for expansion beyond North America. With international standards and increasing convergence, this is rational and opens the way to additional future opportunities. These companies may be closer to the INV model as they can gain additional economies from new markets. As more people adopt their systems, demand grows.

Given the openness and acceptance of the Internet by American consumers and companies, as well as the advanced technical state

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<sup>3</sup> Similar levels of export intensity were found in another Canadian study of exporting and the Internet (Rosson 2000).

of the US economy, it is not surprising that the US market dominates all companies' sales. Canada is culturally close enough to the US to mean that few marketing mix changes are required. Both technology and cultural factors combine to make the US a particularly strong pull for companies and it is difficult to separate them in analyzing the true effects. Companies have seen a ready market that is open and easy to service from Canada and have acted accordingly. In fact, many do not consider the US a foreign market as North American trade patterns move in a North-South direction.

The B2B companies in the sample have been encouraged to open physical offices and employ people in key markets to be closer to their customers. This adds credibility to their organization and enhances market knowledge through local network participation. The Internet provides tremendous opportunities for efficiencies by allowing virtual interaction and collaboration. However, there still remains a need for human contact and relations.

For B2C companies, order fulfillment is a major challenge and being located close to the market can offer advantages. Customs delays and shipping costs can make it difficult for companies to compete. One of the companies has joined with a US partner to service customers as perishable goods can quickly deteriorate with even short delays. Other companies are currently exploring the possibility of foreign distribution as regional sales increase. This is consistent with even the largest Internet companies like Amazon.com, which offer multi-domestic distribution.

Country-of-origin effects normally are associated with country-specific factors, which provide either absolute or relative trade advantages for companies. The effects of location and nation are difficult to assess in an Internet context as most commentators and reports dismiss it and discuss only the Internet's abrogation of territory. However, consumers still live in a physical world that shapes many of their opinions and tastes. All of the sites have recently reevaluated their corporate information sections and added more explicit information on location. While not emphasizing the fact that they are "Canadian," this is no longer hidden. One participant noted that a delicate balancing act is necessary since too much trumpeting will alert Americans to the foreign nature of the site and many will click away. Yet, focus groups run by one company showed that, for reasons of trust, a remarkable 80% of participants would be more likely to purchase from a Canadian site. This suggests that US consumers hold a positive view of Canada that is extended towards Canadian companies operating on the Internet—an important finding given current security and privacy concerns.

#### 5.4 Challenges

While every company faces individual obstacles, several common challenges emerged in the research. A number of areas of concern

are now highlighted. As the sector continues to evolve these deserve attention by policy makers.

Several of the larger companies with significant technology investments believed there was insufficient support at the provincial government level. In other areas of Canada, governments have been aggressive in creating the policy infrastructure and tax regime for new economy companies. These are seen as necessary but absent in Nova Scotia at present. In this respect, companies were not seeking more government money but rather more progressive policies.

B2C companies face the challenge of order fulfillment and shipping goods. In a sparsely populated province like Nova Scotia this is a serious problem. Major US centers have large fulfillment houses offering efficient consolidation for often less than US\$1 per order. Companies operating in Nova Scotia incur in-house costs of C\$10 per order or more. This seriously reduces profitability as this must be partially offset by the seller to remain competitive. The lack of such services locally acts as a barrier to further participation yet until the demand grows, it is unlikely to develop. This is one area requiring region-wide industry cooperation. Consolidating efforts would help all but no one SME seems prepared to take the initiative at present.

As most of the companies examined are private, financing has been a challenge; most have decided to stay small and manageable. Being located at some distance from financial centres presents unique challenges for these companies. Participants mentioned the standard rule that venture capitalists will only travel one hour to visit potential investments. Halifax is more than an hour's flight from Toronto and Ottawa, which puts the companies in a difficult situation. Similarly, US-based analysts will not generally cover Canadian public companies unless they are large or offer something unique. Getting attention requires tremendous effort, yet it is important to have this exposure.

Despite widespread coverage of consumer privacy concerns, none of the companies had implemented any privacy policies nor were any planned. Similarly, there was no mention on any of the web sites of appropriate terms of use and legal liability. As most are clearly directed to foreign consumers, this presents a potential liability should a problem arise. Being small, most companies did not have the time or the resources to adequately study the many policy changes currently unfolding internationally. Questions as to jurisdiction, tax policies and warranties were left unanswered. While the federal government has been active in promoting a new policy regime and in bringing in new Internet policies, this does not seem to be reaching this audience.

## **6. Conclusions**

### 6.1 Study Findings

"Access" does not equate to "reach" and the experience of Nova Scotia companies confirms that global Internet commerce is not realistic for SMEs at this time. Opening a web site does not automatically open the door to the world. Bringing people to the site and then encouraging them to buy requires great effort and this has not been sufficiently attractive for the sample companies to pursue. The application layer providers, where common standards have created a global market, are the exception. Yet even with these companies, personal sales efforts are still required to offset the geography. The potential of global Internet commerce is there, yet the practical realities will take some time to realize.

The Nova Scotia SMEs have all adopted a multi-domestic marketing approach, adjusting and adapting their marketing strategies on a market-by-market basis. National and regional differences remain and must be properly addressed with a web site and overarching strategy. Country effects are still seen to exert an influence in decision-making. While there have been obstacles and challenges remain, the companies profiled show that it is possible to conduct international business profitably on the Internet. As Internet technology continues to evolve, it will be instructive to watch how SMEs seize the opportunity to grow their business.

## 6.2 Future research

The present study involved a small sample of companies from one geographic area and therefore any conclusions drawn must be very tentative. However, the findings do provide clues about companies' use of the Internet for international marketing purposes. These results, along with those that are expected from small-scale studies elsewhere, offer some promising avenues for exploration in larger and more quantitative studies.

A few research ideas are suggested by this study. International business theories continue to be challenged and modified as entrepreneurs and companies adjust to changing environments. A larger scale and more diverse investigation of the internationalization process in Internet-based businesses would be beneficial. Another possibility is for research that examines export situations where the market opportunities are less clear-cut than the US market presents to many Canadian companies. For example, how have European companies used the Internet to expand their businesses within the EU? Another possibility would be to compare the experience of companies in similar settings that have pursued different internationalization paths and strategies. In other words, why have some SMEs actively embraced the Internet for export development whereas others have not? What are the various strategies? What results have been achieved? This is bound to provide fertile ground for researchers for some time.

In a changing and rapidly evolving environment, theories of international business are being challenged. Just as INV theories have been advanced to explain high technology markets, new models

focusing on Internet commerce are overdue. The reduced barriers and time to market question extant models, including stages theory. Companies are selling internationally from their inception, often with no direct experience or assistance. Further study and theorizing is called for, so as to inform private sector actions and public sector policy.

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