

The Impact of Network Structure in Internationalisation Process of Small and Medium Sized Enterprises

Case Study: A Finnish-Greek business network

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ABSTRACT

The purpose of this study is to analyse the internationalisation process of small and medium sized companies (SME) and the impact of network environment. The research concentrates on the influence of the relational environment; actor bonds. What kinds of relationships guide the development? What are the critical events and influence factors behind this development? Theoretical and contextual frame is built on interactive network approach (Industrial Marketing and Purchasing Group, IMP) and on incremental internationalisation theory. The study attempts to create a conceptual model for network internationalisation.

The research part is inductive, qualitative and based on case study. The research follows the evolution of one Greek-Finnish business network in paper converting and packaging industry through a focal dyad. The business network is limited to a focal net of relationships. The development is examined through event follow-up and historical reconstruction covering 1994-2004.

According to the preliminary findings accumulation of capabilities and social bonds seem to function as a mechanism for network internationalisation. The study contributes to SME internationalisation both in terms of managerial and policy implications.

1. Introduction

1.1. Objectives of the study and research questions

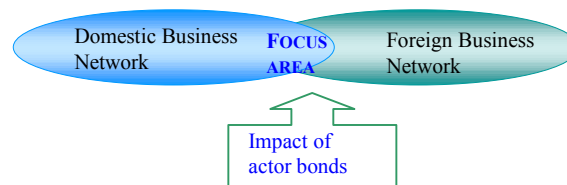
The study attempts to understand “network internationalisation”, network-effect on SME internationalisation (Hertz 2002). It aims at constructing a conceptual model, which

incorporates events and notion of direction; “inward-backward-outward” (Kirpalani and Luostarinen 1999). An implicit objective is to understand evolution process¹ and the hidden configurations of the internationalisation process in terms of actor bonds, relationships. Its explicit objective is to describe a network development process. Critical events and influence factors embedded in the evolution process are explored and identified (Hedaa and Törnroos 1997). The explicit research questions are:

- Identification of the central roles and driving force in SME business network internationalisation
- How actor bonds influence a firm's internationalisation
- How internal development facilitates internationalisation
- What are the critical events in actor bonds from a firm's perspective
- What happens behind the critical events, identification of the influence factors

The research questions originate from the Finnish-Greek trade and its representativeness as a notoriously difficult cultural and geographical combination. The results of this study are expected to contribute to the Finnish-Greek trade, SME export and internationalisation policy and management of cross-cultural business networks.

Figure 1.
Internationalisation
process of SME network:
Focus area of the empirical research



1.2. Research approach, method and data collection

The study attempts to explore business net evolution through critical events and visible/invisible influence factor analysis using a longitudinal case study (Alasuutari 1995; Eisenhardt 1991; Yin 1984; Van de Ven and Poole 1995). It has an idiographic character. Case here refers to a dyad in a focal net.

The study follows a process view, including a historical reconstruction and event follow-up (Mainela 2002; Ring and Van de Ven 1994). The business net evolution is examined from the perspective of critical events and enacted reality (Halinen, Salmi and Havila 1999). The

¹ Including re-and de-internationalisation

events consist of critical events incorporating change forces arising from interaction in the dyad and the network environment.

Case-analysis refers to the method of abstracting the observations, concentrating on the essential characteristics and combining data to solve research questions (Alasuutari 1994). The research problems are approached carrying out several issue-focused, theme research sessions, in order to grasp the richness and the dynamics of time. The researcher's role follows the idea of interactive research (Gummesson 2001). Participant and action research perspective is applied (Alasuutari 1994).

Data collection methods are qualitative; interviews, observations, analysis of archives, correspondence and other written data. Observations are based on field notes. Observation and supporting questionnaires are collected participating in meetings, exhibitions and other business activities. Personal interviews are used having in-depth and semi-structured character (Alasuutari 1995). Some supportive data is quantitative, which is considered appropriate in case study research (Perry 1998). Data gathering takes place 1994-2004. Rich data and good access to information has influenced the selection of the business net and the focal dyad.

The study identifies and establishes a typology of critical events. Actor bonds are analysed from four different aspects: economic, operational, atmospheric² and external. Economic aspect examines the motivation and interest generated by the business and trade potential. Operational aspect examines the communication and cooperation. Atmospheric aspect examines the relationship context such as trust and commitment. External aspect examines the impact of competition both in/outside of the business net as well as the institutional influence of laws, norms and organisations.

In case-analysis it is important to have in-depth analysis to counterbalance the small number of cases selected. Triangulation assists in avoiding erroneous conclusions. Good access, rich

² See Atmosphere, IMP Group, Understanding Business Marketing and Purchasing, Ford, Thomson Learning, 2002, p. 19-34.

data and pre-knowledge diminishes problems concerning validity of the research material and findings.

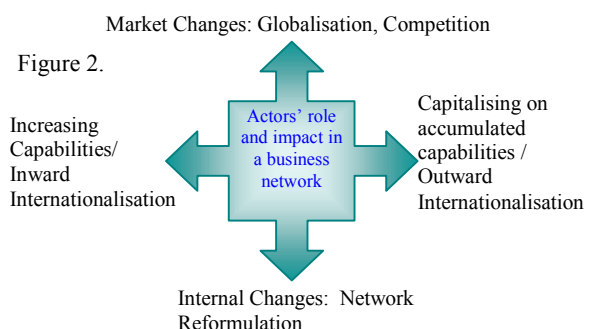
1.3. Internationalisation of SME business networks

Contemporary SME³ internationalisation mechanisms and driving forces have not been discovered to full extent (see Nummela 2002b). Since SME companies form a significant population among SMOPEC⁴ country exporters, their opportunity structure and its potential deserves more attention. These firms have a limited character in terms of autonomy due to their size and resources which stimulates combinations of vertical and horizontal networks.

Being part in a network, having “markets-as-networks” view, indicates that a firm is embedded in a wider, dynamic interconnected network context where strategic actions by firms initiate changes in the network structure (Hertz and Mattson, 2001). The SME internationalisation process is influenced by the network structure and facilitated by the accumulated effect of pull-push forces, learning, tacit knowledge and social contacts. The impact of increased level of internal internationalisation or network competence is a form of network effect on an individual firm (Ritter 1999). It is claimed that this type of network internationalisation process is different from the Uppsala incremental model (Johanson & Vahlne 1977) and more close to the process of born globals (see Johanson and Mattson 1988; Nummela, 2001). A firm can get gradually

involved in international business operations through its input channels, mainly through purchasing and logistical operations (Luostarinen and Welch, 1988). See Figure

2. *Network effect on internationalisation.*

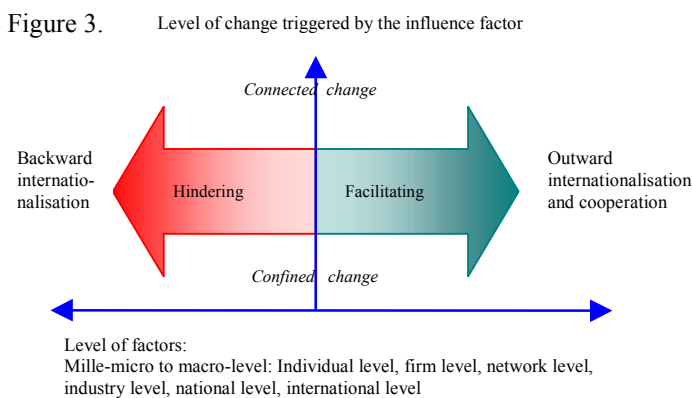


³ The study applies the definition of SME generally accepted until 1996: the size criteria being of 499 or fewer employees as it aims at describing an evolution where the sample exceeds the newer criteria set by EU Official Journal 1996. The qualitative criteria of SME is discussed further in the doctoral thesis.

⁴ SMOPEC, Small and medium sized open economy, see Kirpalani and Luostarinen, 1999

The network approach can also explain why and how firms internationalise (Törnroos, 2002). Johanson and Mattson (1988, p.297-306) assume that a firm's position in the network is a key factor to maintain and develop. Both the degree of internationalisation of the firm as well as the internationalisation of the market influences the process. The study examines domino effect and the degree of internationalisation of the business network (Hertz 2002). The type of inherent dynamics and the "direction" is discussed (Hurmerinta-Peltomäki, 2001, p.31-37).

Figure 3. *Change in internationalisation process. Notion of direction and level- Influence factors*



The hindering or facilitating factors are examined according to change they trigger and the respective level (Nummela 2002a). Critical events are part of the event network that takes place and forms the

opportunity structure (Hedaa and Törnroos 1997)

1.4. Limitations of the study

Theoretically the study is limited to the interactive network paradigm by the Industrial Marketing and Purchasing Group (IMP) and the network perspective on internationalisation (Johanson and Mattson 1988). Uppsala model and Luostarinen's internationalisation view are discussed. Non-economic, behavioural view is emphasised throughout the study.

Empirically the study is limited to research and analysis of *business network's actor bonds* in paper converting and packaging industry focusing on SMEs. Geographically the research is based on two countries, Finland and Greece. Chronologically the study concentrates on the period of 1994-2004.

2. The Framework - Network Internationalisation Approach

Theoretically the study is constructed on the interactive network paradigm by the Industrial Marketing and Purchasing Group (IMP) and on network approach in internationalisation (Johanson and Mattson 1988). The industrial markets consist of exchange relationships between multiple organisations. Development of industrial networks is a consequence of interaction (Håkansson and Johanson 1992). The IMP model of business network consists of three elements: *actors, activities and resources* (Håkansson and Snehota, 2000). The ARA model (see Ford, 2002, p.162-181) concentrates on the configuration of a business relationship: Activity links, resource ties and actor bonds. Actors are firms or individuals that perform activities and control resources. Actors perform activities, transactions and create value via transformation of resources.

Driving forces for SME internationalisation are discussed (Håkansson 1982; Turnbull and Valla 1986). The concept of different stages (Johansson and Vahlne 1977; Luostarinen 1979) is questioned. The concepts incorporate elements from social network theory (Wellman and Berkowitz 1988; Gulati 1998) and rely on the Nordic network approach, particularly on cooperation and SME internationalisation (Bengtsson and Kock 1999; Törnroos 2002; Nummela 2000; Hurmerinta-Peltomäki 2001).

2.1. Key concepts

The concepts used in analysis of business networks are network horizon, network context and network identity. *Network horizon* explains how extended an actor's view of the network is. Factors influencing the view are experience, structural network features and connectedness.

Network context determines the actors, who they are and how they are related to each other, the activities, what activities are performed and the ways in which they are linked together, and the resources, what resources are used and the pattern of adaptation between them.

Network identities refers to how the firms see themselves in the network and how they are

seen by the other actors. Another aspect in analysis is the network *role of an actor*. Defined roles are: the architect, the lead operator and the caretaker (Anderson and Narus 1999).

Ties, links, bonds, relationships, nodes and actors relate to different forms of connectedness and its elements. Transactions and exchange episodes refer to the interactivity and its time aspect.

2.2. Positioning of the research

The underlying philosophy of science in this thesis is based on realism (Hunt 1991). The study refers to the thoughts of marketing schools on social exchange and systems as well as micro-functional market exchange (Alderson 1965)⁵.

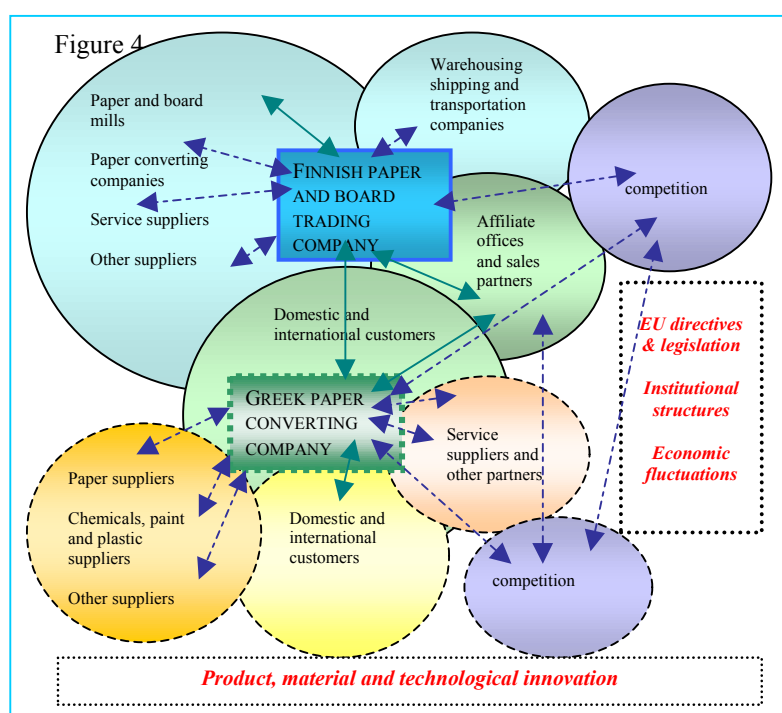
This is a descriptive and explorative study having idiographic characteristics. In spite of that, it is assumed that the research findings may assist in understanding respective cases as many behavioural and situational factors/events have universal characteristics. Longitudinal case analysis on SME business net evolution and internationalisation process may reveal underlying configurations that occur in the flow of events and the respective influence factors. The study has its reference frame mainly in network internationalisation following previous research especially in understanding the role of actor bonds and relational structure. SME nets form the focus as it seems that the significance of the level of internationalisation of individual, firm and its network environment is somewhat neglected although the SME capabilities have been discussed (see Luostarinen 1979; Nummela 2000; Hurmerinta-Peltomäki 2001).

3. About the Focal Business Net

The focal business net is based in Finland and Greece being involved in a manufacturing process in paper and packaging industry. The Finnish focal company has started as a small size family-owned company in 1973. The company has three fields of business: packaging products, subcontracting and wholesale operations. The company has grown rapidly and has

changed its structure significantly during the past decade though continuous growth via expansion and acquisitions. International activities have increased significantly the last twenty years and today one central business area is international stock lot business.

Today the company is a group of companies with 350 employees and 45 million Euro turnover. After a merger with a competitor in 1999 the group structure changed. Its structure covers six different units, all being wholly-owned independent companies. Many of these

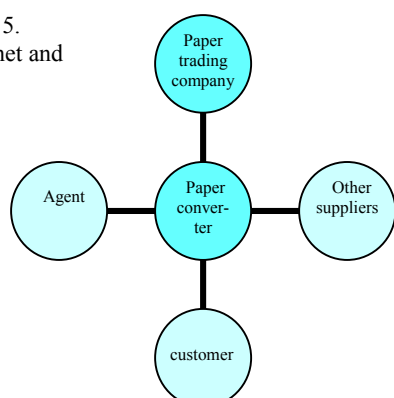


daughter companies and other five cross-owned companies carry on independently international operations and are embedded in their own complex business networks each in its own field of expertise. See Figure 4. *The continuum of the paper trading and converting net - focal*

business net and dyads

The focal dyad is the Finnish export marketing unit for paper and board and the converter

Figure 5.
Focal net and
dyads



partner in target market Greece. See Figure 5.

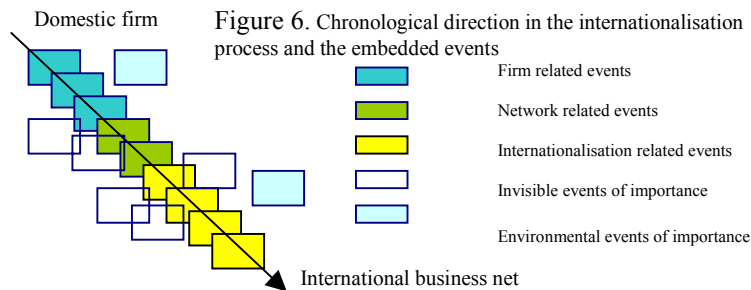
The Greek side of the network evolves drastically during the research period, partner companies have changed but activities continue. Supportive dyads in the manufacturing and business net are included. These relationships

have an essential role in understanding the internationalisation process and business net

⁵ in Sheth, Jagdish N. & Gardner, David M. & Garrett, Dennis E., Marketing Theory: Evolution and Evaluation, John Wiley & Sons, 1988

development concerning the selected market. The selected focal dyad is mapped in time as a follow-up using the concepts of actor bonds, ties, links, roles and network context/horizon.

The study is organised as a chronological process, see Figure 6. It describes the evolution of



the network structure in chronological phases. Stability and change as well as cyclical processes are incorporated in the flow of events.

4. Preliminary Propositions and Conclusions

Despite the inductive nature of the study preliminary propositions are made. They are based on the pre-knowledge and have developed during the research process itself.

1. *Based on the reported activities in the Finnish-Greek business context it seems that SME's efforts have limited success if not tendency to fail compared to the large companies: -Size matters, focus on SMEs.*
2. *If larger companies with strong ties, personal relationships and "historical" commitment seem to perform better, then same fundamentals are assumed to have similar effect on SME's: -Actor bonds essential.*
3. *SME's seem to internationalise through their personal contact network, business net activities and internal processes. Or they react to an external stimulus. They are considerably more reactive/passive and resource-limited and do not have a clear "direction" for growth. - "Actor bond handling and utilisation" needs to be examined.*

Preliminary outcomes concerning the evolution process and its dynamics:

1. *Economic interest is the first stimulus to create a business relationship*
2. *Actor bonds (working relationships) are in often more important than economic interest.*
3. *If economic interest is great enough the problems in actor bonds can be counterbalanced.*
4. *Differences in managing operations are more important than business environment. Culture and business distance have an impact, but the reflections on the operational level are far more important.*
5. *Critical events have either a negative or a positive effect on the business net evolution*
6. *Strong relationships guide the direction of the business net and create driving force*
7. *Environmental/exogenous factors form the setting, but it can be reformulated if bonds are strong enough.*

The expected implications for theory concern the dynamics of a business network and its internationalisation mechanisms. The managerial implications concern the organisation and management of network and its activities and resources in internationalisation process.

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