



Target Market Selection Model for E-Commerce Start-Ups exemplified by NewCo

A work project, presented as part of the requirements for the award of a Master's degree in Management from the NOVA – School of Business and Economics.

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Lisbon, 8th January 2016

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Preface

This thesis consummates my Master of Science degree in Management at the Nova School of Business and Economics. This was only possible with the advice and support of a number of people who I want to acknowledge.

First of all, I would like to express my thanks and gratitude to Miguel Duarte who has supervised and supported me through the project. His valuable advice and comments provided me the feedback I needed to continuously improve my work.

I would like to thank the founders of NewCo for the trust and responsibility they gave me in order to enable me to investigate such an important topic.

Furthermore, I would like to thank my fellow students who have strongly supported me during the time I worked on my thesis. Finally, I would like to thank everyone who enabled me to complete this work as well as my master studies successfully.

Lisbon, 08.01.2016

Stephen Wüstel

Abstract

For e-commerce startups (ECSs) international growth has never been more important than today. In order to venture abroad successfully, ECSs need a model which enables them to select the most attractive markets. The current status of theory and literature is rarely applicable to early stage ECSs. Therefore, this research paper provides a model for the systematic selection of new target markets. Based on existing literature as well as primary and secondary research, this thesis develops a generic target market selection model for ECSs. To verify this model, it is applied to a specific online market place called NewCo.

Keywords: internationalization, international market selection, target market selection model, market expansion, e-commerce start-up

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List of Abbreviations

BCG	Boston Consulting Group
CAGR	Compounded annual growth rate
CS	Certainty score
CSC	Country-segment combination
ECS	E-commerce startup
GDP	Gross domestic product
INVs	International New Ventures
KPI	Key Performance Indicator
MPS	Market potential score
MSME	Micro, small and medium enterprises
OS	Overall score
SEO	Search Engine Optimization

1 Introduction and Methodology

This chapter introduces the objective of the thesis, proceeds to provide the profile of the investigated ECS, NewCo, and describes the underlying methodology.

1.1 Background, Problem Definition and Objective

Nowadays, the e-commerce industry faces a period of dizzying growth (McKinsey 2014). Only start-ups which follow this growth with a certain strategy can survive in the long-term (Sherman 2012). One crucial growth strategy for start-ups is internationalization (Anderson 1997). In order to venture abroad successfully, the companies under consideration need a guideline as to how to identify and enter the most attractive markets¹ (McKinsey 2014).

Whereas this selection process is pervasively illuminated for multinational corporations, there is only limited knowledge for start-ups. Existing literature and models, which deal with the selection of new target markets, are often tailor-made for large corporations which distribute physical goods (Le and Rothlauf 2008). This limitation makes it difficult for small business and in particular ECSs to apply these theories. Due to the described reasons as well as the lack of sufficient resources, these companies usually follow a more opportunistic approach. This means that they take advantage of opportunities as they arise (Chell 2000). Bhidé (2000) argues that it is necessary for the management of start-ups to experiment and change when acting in turbulent and uncertain environments. Furthermore, he stresses that opportunistic adaptation to external change is the key to developing a start-up. However, opportunistic behavior bears the risk of operating in a suboptimal market (Chell 2000). Founders who follow opportunistic behavior often tend to enter new markets because of their personal network without considering objective criteria. One example for this is Adwin², an online marketplace which connects brands and customers. Adwin started its operations in Portugal without considering other

¹ According to Wesselmann and Hohn (2012) attractive markets are markets with high market potential and volume, competitor activity, market accessibility, potential market share, sales volume, internal know-how and resources.

² Adwin is an online platform where users can watch videos of their favorite brands in exchange for vouchers and products (Marketeer 2015).

markets but the business did not mature due to a limited market size. To overcome this obstacle, Adwin invested in resources to identify a better fitting market, and selected Brazil as a new market. Adwins' business skyrocketed due to the better market fit (Da Silva 2015).

The objective of the research work that this thesis summarizes is to create a systematic model that prevents other ECSs from facing similar obstacles. It equips them with a target market selection model. Furthermore, it will be applied to a specific ECS which will be called NewCo for confidentiality reasons.

From an academic standpoint, it contributes to the state-of-the-art research in ECSs as well as internationalization strategy, and combines both fields, based on an in-depth literature review and primary research.

From a practical point of view, this thesis is relevant to all ECSs that plan to expand their business internationally. It provides them with a generic model, which allows them to identify and select the most attractive markets for their operations. Thus, this work contributes to the area of the internationalization of ECSs and leads to a more successful internationalization process in the future. Additionally, from NewCo's point of view, this thesis identifies the most attractive markets and enables the formulation of an internationalization strategy. This increases the chance of successful market entry and helps to accelerate NewCo's international growth. The practical usage of the target market selection model developed in this thesis is verified by the application to the ECS described in the following subchapter.

The following research questions will be answered within this thesis:

1. How can ECSs, multi-segment online market places in particular, optimize their target market selection?
2. What is the best methodology to identify, evaluate and select new markets from an ECS perspective?

1.2 Profile of NewCo

NewCo is a Portuguese company, founded in 2012, by an experienced team of three entrepreneurs. Combined, they have more than 45 years of experience in business, sales and software development. They put together a two-sided online market place, which matches clients with professional service providers. This helps clients to find the right professionals for their personal projects. On the other hand, it provides professionals additional customers. NewCo generates profits by charging the professionals commission for each client contact. It mainly targets professional service providers which only have a few employees and whose clients use the internet, Google in particular, to find service providers. Due to their personal network and the relatively low labor costs in Portugal, NewCo started to operate in Lisbon. During the last year, NewCo has increased its market coverage in Portugal and expanded its operations to Spain. Today, their service portfolio covers more than 650 different services. Recently, the founders decided to expand their business further. The objectives are to expand the business in South America and become the market leader in Europe. The competitive situation differs strongly from country to country, but most of their competitors only focus on some specific services. Due to resource constraints, NewCo plans to enter only a small number of new markets in 2016. As a consequence, it is important to identify and enter the most attractive ones.

1.3 Underlying Research Methodology of this Thesis

In existing literature on similar challenges, two research approaches prevail: inductive and deductive. When conducting inductive research, a new model is developed based on actual findings. Deductive research tests the applicability of an existing theory on empirical findings (Bryman and Bell 2003). This paper is based on an inductive approach. It describes the target market selection process from the perspective of ECSs. Furthermore, it provides a generic model which applies to most ECSs. To begin, primary and secondary data were collected and existing internationalization theories reviewed, subsequently followed by the development of a generic target market selection model based on these findings. To validate the model, it was then applied to NewCo's specifications (see Figure 1).

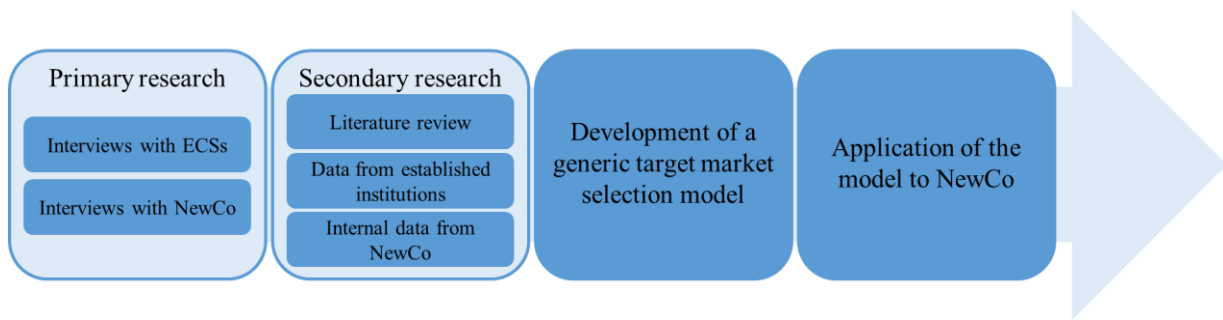


Figure 1: Selected Research Approach

According to Sekaran (1992), it is a useful method to combine qualitative data with quantitative if it is not possible to conduct a strictly quantitative experiment. Therefore, this study incorporates a combination of quantitative and qualitative analysis, beginning with a qualitative approach. In order to learn more about the internationalization of ECSs, it was necessary to conduct interviews with several entrepreneurs, investors and start-up mentors. The heterogeneous peer-group created insights from different perspectives. Sekaran (1992) states that the main advantage of qualitative data collection is that it elaborates a topic from various dimensions. Quinn (2002) argues that qualitative data is necessary to study topics which do not have a single truth. Thus, qualitative data is suitable for this study since NewCo's internationalization strategy is uncertain and depends on a variety of soft factors. The qualitatively identified criteria provide a basis for the development of a target market selection process (see Chapter 3). The process mainly incorporates quantitative criteria from numerous well-established data sources such as the CIA Factbook, Doingbusiness and Eulerhermes. Töpfer (2012) argues that quantitative results are easy to analyze. They also decrease the risk of errors and ensure validity.

The data sources used can be divided into primary and secondary data (Quinn 2002). Primary data was collected via semi-structured interviews (see Appendix A). This type of data has been used to a considerable extent in this study as there is only a limited number of secondary sources which give specific information on the internationalization of ECSs and NewCo in particular. This is based on the novelty of the industry and the lack of literature in this sector (Cofounder A

2015). The secondary data was mainly collected from electronic databases and literature. The developed model compares 170 countries based on a broad range of quantitative criteria. The consideration of various sources helped to examine this topic from different angles. On the other hand the consistency of data is important in order to ensure the comparability between different countries.

2 Literature Review on Internationalization and Target Market Selection

This chapter provides the fundamental theories and models which have been incorporated into this paper. After a thematic demarcation, a discussion of traditional internationalization theories ensues, completed with the theories of International Entrepreneurship and International New Ventures. The introduction of established market analysis as well as Sternad's Target Market Selection Model form a significant part of this chapter as the basis for the developed model (see Chapter 3).

2.1 Thematic Demarcation

Internationalization is “a process, over time, in which a firm develops increasing involvement in operations outside the firm's home country” (Welch and Loustarinen 1988 p. 34). Later, McDougall and Oviatt (1999) complete this definition by adding that involvement can affect the input and output of the firm. The firm can relocate its research department, create new facilities abroad or start exporting products. Grüning and Morschett (2012) describe the phenomenon of internationalization from a process point of view. According to them, a company which wants to enter a new market needs to perform the following process steps: 0. Preparation of the strategy planning project; **1. Evaluation of potential markets and selection the most attractive ones**; 2. Determination of market entry modes for the attractive markets; 3. Development of feasibility studies for entering the attractive country markets; 4. Development of the internationalization strategy; 5. If needed: signing of agreements with partners; 6. Development of the market entry programs.

Defined by the research questions, this thesis mainly focuses on process step 1, **the evaluation and selection of markets**. However, this chapter reviews important theories and models on internationalization in order to build a theoretical foundation for this study. A description of two traditional internationalization models takes place at the beginning as they are both well-established in practice (Blomstermo and Sharma 2003). First it is necessary to introduce the **Uppsala Model** as it is one of the first established internationalization models. The **Network Model** which follows is a later model describing the process of internationalization from a more recent point of view. The main focus of both is on multinational corporations, due to this they cannot explain the rapid internationalization of ECSs. For this reason, the picture is completed with the theories of **International Entrepreneurships** and **International New Ventures (INVs)** which provide insights into the dynamic situation ECSs are facing. There is a brief review session of some of the most influential approaches to market analysis. **Porter's Five Forces**, **PESTLE**, the **Boston Consulting Group (BCG) matrix** and **McKinsey matrix** are fundamental to the understanding of **Sternad's** (2013) systematic **Target Market Selection Model**. Sternad argues that no existing approach considers all factors which are important for market selection. Thereupon, he consolidated several approaches and developed a systematic selection process customized to multinational corporations (Sternad 2013). This process serves as a framework for the model presented in chapter 3.

2.2 Critical Review of Traditional Internationalization Theories

The **Uppsala Model** by Johanson and Vahlne (1977) is the first published internationalization theory. Blomstermo and Sharma (2003) state it as the most established internationalization model. It explains internationalization as a process in which a firm incrementally increases its presence in a foreign market as knowledge of the market grows. It claims that market knowledge, experience and physical distance are the strongest influencers. The model states that companies enter foreign markets with a low level of commitment, e.g. exporting with a sales agent. With growing market knowledge, more resources are invested and the stronger presence results in more market knowledge and further commitment

(Johanson and Vahlne 1977, 2009). The model explains how the experience and learning within a firm influence the firm's decisions on opportunity and risk.

Although the model explains how to solve a lack of market knowledge and experience and how to overcome geographical distance, it is limited to companies with physical goods (Axinn and Matthyssens 2002). For companies with intangible goods it is often not necessary to intensify the international presence to such a large extent (see Chapter 2.4). For this reason, Han and Noller (2009) argue that, for these types of firms an online based and straightforward process would be more beneficial. These arguments show that the Uppsala Model cannot be used to explain the internationalization process of ECSs.

The **Network Model** describes internationalization in a more modern way. It emphasizes that firms interact with other parties of their network, so called stakeholders, such as competitors, suppliers, customers, regulatory bodies and public agencies. Companies with long lasting partnerships within their network, are able to exchange market knowledge and experience through technical, social and economic links. This bridging mechanism help them to overcome geographical distances and enable a rapid internationalization (Blomstermo and Sharma 2003).

According to Johanson and Mattsson (1988), the advantage of this model is that it explains the strengths and weaknesses of companies in the context to their environment. However, the model is based on the assumption that an individual firm depends on relationships with other companies in order to gain resources. This assumption does not necessarily hold for ECSs due to the fact that the network that start-ups have established is relatively small and the future network is unknown. This makes it hard for them to establish persuasive partnerships and to exploit the advantages of the networking model.

2.3 Established Market Analysis Models

Porter's Five Forces and the PESTLE analysis as well as the Boston Consulting Group (BCG) matrix and McKinsey matrix are well-established models which companies can use to measure the attractiveness of markets (Homburg 1991). In the following, the relevant models will be introduced as

individual techniques from the mentioned analysis are fundamental to the development of a holistic target market selection model within this thesis (see Chapter 3). Although there is extensive and detailed information about these models, this chapter will only provide a high-level introduction which is necessary to understand this paper.

Porter's Five Forces³ analysis determines the balance of power of a company by evaluating the supplier power, buyer power, competitive rivalry, threat of substitutes and threat of new entry. The outcome of this analysis can be used as a first indicator of the attractiveness of a specific market. However, it should not be taken as the only source of information for such an important business decision. The **PESTLE**⁴ analysis explains how an organization is influenced by political, economic, sociocultural, technological, legal and environmental factors. For this reason, it can be used to complete Porter's Five Forces.

The **BCG** and **McKinsey matrix**⁵ can be used to allocate resources in an objective way detached from short-term performance indicators (Wittek 1980). Initially, the frameworks were used to allocate the business units of a company in a two-dimensional matrix. The position in the matrix provides information about the performance of the business units and markets, and recommends options for strategic actions. Usually one dimension of the matrix incorporates company-specific factors which the company can directly affect, and the other one consists of external factors which the company can only influence indirectly (Meffert, Burmann and Kirchgeorg 2012). The BCG matrix uses relative market share as company-specific and market growth as the external dimension (Wittek 1980). McKinsey evaluates the attractiveness of the market as well as the competitive strength of the company with several criteria. These criteria are weighted and rated in order to calculate an overall score for each dimension (Homburg 1991). With these overall scores the business units are allocated within the matrix. The position in the matrix indicates the attractiveness of the market and the competitive strength

³ See Homburg (1991) for more detailed information

⁴ See Homburg (1991) for more detailed information

⁵ See Wittek (1980) for more detailed information

of the investigated business unit (Wittek 1980). Based on this, the strategic management of a company can decide where to invest or divest resources. Besides business units, the portfolio matrix can also be used for the evaluation of products, industries or geographical markets (Meffert, Burmann and Kirchgeorg 2012). Due to this, Sternad (2013) incorporates elements of the previously mentioned methods in his model.

2.4 International Entrepreneurship and International New Ventures

As mentioned before, traditional theories cannot explain the rapid internationalization of ECSs since their applicability is limited to multinational corporations or traditional business models. Traditional theories are based on the assumption that companies start their business in one country and only venture out internationally after a long period of time. The present situation, however, still shows evidence for companies that start their international operation very early (Sherman 2012). A review of the theories of International Entrepreneurship and INVs is necessary to explain this phenomenon.

International Entrepreneurship is “the discovery, enactment, evaluation, and exploitation of opportunities across national borders to create future goods and services” (McDougall and Oviatt 2005 p. 540). **INVs** are “organizations that from inception seek to derive significant competitive advantages from the use of resources and the sale of output in multiple countries” (McDougall, Oviatt and Shane 1994 p. 49). McDougall and Oviatt (1994) conclude from their research that entrepreneurs’ unique competencies and experience enables them to identify opportunities in multiple countries. This helps them to avoid path-dependence on local competencies. For example, an entrepreneur who has a good network in multiple countries is more flexible in expanding his business because he can choose between several new markets. However, not all INVs can overcome this dependence due to passive forces such as the founding team, network and financing. On the other hand technological developments, especially the internet, provide INVs with opportunities to conduct business in new ways and to communicate information faster and cheaper (Weill and Vitale 2001). It empowers small companies to compete with large multinationals. Thus, INVs are able to position themselves around

the world even before they exist. (Loane, McNaughton and Bell 2004). They can extend their operations to other countries without physical expansion or relocation. Promotion and advertisement can be done globally without major costs (Maloff 1995). Lituchy and Rail (2000) state that the internet increases the level of INVs. They internationalize at a higher speed and start global operations instead of expanding to proximate neighbor countries first. Nevertheless, INVs need to select the right market and entry mode in order to overcome entry barriers. According to Brouthers (2002), the most critical entry barriers for INVs are market understanding, cultural and legal issues and legitimacy.

2.5 Sternad's Systematic Target Market Selection Model

Based on the previously discussed theories, there is a need for **Sternad's systematic Target Market Selection Model** to be reviewed because it serves as a framework for the model developed for ECSs. Sternad (2013) argues that the success of a company strongly depends on the ability to identify attractive markets that fit to their own products or services. The consequence of this is the need for the selection process to incorporate the following: company strategy, market potential and risk, competitor situation, availability of resources and access to market information.

In reality, entry in a new market is not always the result of a strategic process. In the e-commerce industry in particular, globalization and word of mouth lead to unplanned requests from other countries (Brouthers and Nakos 2005). However, a systematic target market selection process increases the chance of successful market entry. A systematic process compares objective criteria with transparent methodology (Brouthers and Nakos 2005). According to Sternad (2013), there is no model that considers all important factors for the selection of new target markets. Due to this, he developed a systematic model, mainly based on the previously introduced theories.

The process starts with a pre-selection of countries. Company specific KO criteria are defined to shorten a list of potential countries. The remaining countries are analyzed with regard to their market potential and risk. An attractive market is only accessible if the company has a competitive advantage on the target market (Brewer 2001). Therefore, the market attractiveness is compared to the competitive

strength of the company. Finally, a resource check examines whether sufficient resources are available or acquirable (see Figure 2).

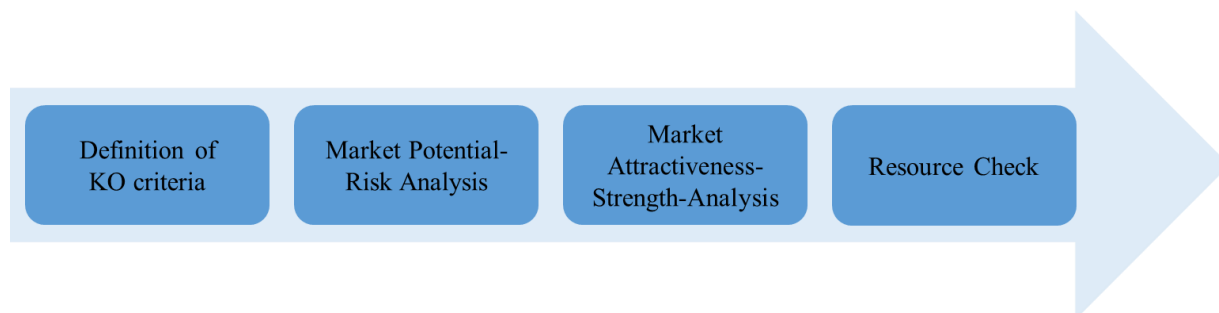


Figure 2: Sternad's Target Market Selection Model (Sternad 2013)

Sternad (2013) states that his approach is an iterative process with multi-phase links and loops. Each process step increases the information on the markets. Thus, it might occur that decisions need to be rethought and process steps repeated.

2.6 Conclusion of Reviewed Literature

Traditional internationalization and market analysis theories cannot explain the rapid internationalization of ECSs seeing as their applicability is limited to multinational corporations. To explain this phenomenon, the theories of International Entrepreneurship and INVs need to be considered. Paired with Sternad's model, these paper built the basis for a target market selection model for ECSs (see Chapter 3).

3 Description of the Target Market Selection Model

3.1 Process Overview

This chapter describes the developed target market selection model. ECSs can use it to identify the most attractive market for their business.

The model is structured in five major process steps (see Figure 3).

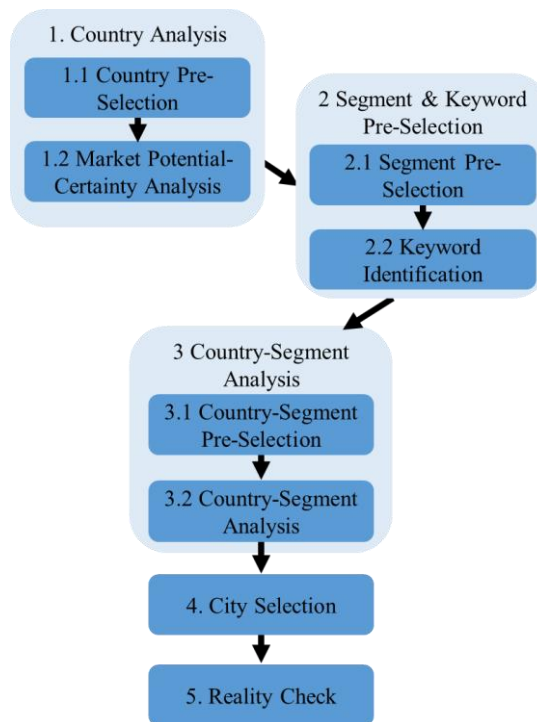


Figure 3: Flowchart - Target Market Selection Model
 based on Sternad's target market selection model
 (Sternad 2013)

The process starts with a country analysis. First, company-specific KO criteria are defined and used to shorten a list of potential target countries. The remaining ones are evaluated in terms of their market potential and certainty. Only the countries with the highest scores in both dimensions are taken on to next process steps. Second, all segments of the business are examined and the ones with the highest chance of success are pre-selected. Depending on the company, segments can represent product or service types, industries, customer types or business sectors. Afterwards, for each pre-selected segment one keyword is identified. These keywords help users to find the offered segments on Google. Third, the pre-selected countries are matched with the pre-selected segments and their demand is tested in the corresponding country. These country-segment combinations (CSCs) can be seen as separate submarkets. Only the ones with the highest demand are further analyzed with a scoring model. The CSCs with the highest scores represent the most attractive markets for market entry. Fourth, the best cities for market entry are identified. Finally, a reality check is performed in order to ensure that the company is capable to enter the selected markets. The following subchapters describe the generic process steps of the model.

3.2 Step 1: Country Analysis

Step 1 aims to identify the most attractive countries for market entry. It is divided into the substeps: 1.1 Country Pre-selection and 1.2 Market Potential-Certainty Analysis.

3.2.1 Step 1.1: Country Pre-Selection

Nowadays, globalization and the internet enable ECSs to enter almost every country in the world (see Chapter 2.4). Thus, ECSs need the ability to compare markets in order to select the most attractive ones. Many ECSs narrow down the list of potential countries by too much. They analyze only the most common countries. This attitude considerably increases the risk of disregarding countries with high potential (Alves 2015). To solve this problem, the present model is capable of comparing the 170 most important countries with a scoring model. The remaining countries are excluded due to the low quality and availability of quantitative data. However, to minimize the time and effort required for the analysis, this step aims to pre-select countries which are worth a deeper analysis. First, the company reviews its internationalization strategy and defines company-specific KO criteria. Commonly used KO criteria are language, psychical distance and existing network (Queimado 2015). These KO criteria are used to shorten the list of 170 potential countries (see Appendix B: Screenshot 1). The remaining ones are evaluated in step 1.2.

3.2.2 Step 1.2: Market Potential-Certainty Analysis

In this process step, the concept of the BCG and McKinsey matrix is used to evaluate the pre-selected countries with regard to their market potential and certainty (see Chapter 2.3). These dimensions indicate the attractiveness of the pre-selected countries (Sternad 2013). Two overall scores (OS) are calculated for each country, one for each dimension. In literature there are many criteria to choose from to determine the dimensions market potential and certainty. Only a specific subset of criteria are applied in the context of this study in order to ensure the practical applicability from an ECS' perspective. The first score indicates the **market potential** of the country (MPS). It is composed of the criteria: population, population growth, urban population, population density, internet usage, smartphone usage, online shopping, human-development index, gross domestic product (GDP), GDP per Capita,

GDP Service Sector, GDP real growth rate, number of micro, small and medium enterprises (MSME) and Ease of Doing Business. The second OS presents the **certainty** score of the country (CS). It incorporates the criteria: inflation, contract certainty, corruption index, unemployment and country risk (see Appendix B: Table 4). The importance of these criteria can be influenced by adapting their weight. Depending on the ECS and its industry characteristics, relevant criteria need to be selected and their weight adapted. The most relevant criteria are weighted with three, the ones with medium relevance with two and the ones with low relevance with one. Irrelevant criteria are excluded by changing their weight to zero. In the following part, the calculation of the OSs are explained based on the criterion population.

All countries are ranked based on their population. The country with the largest population receives the highest score. The population rank is multiplied by the criteria weight. After repeating this procedure for all criteria, the weighted scores of a country are added up to a MPS and a CS. The arithmetical mean (\bar{x}) and the standard deviation (σ) of the MPS and the CS are then calculated. Based on the Jarque-Bera test, it can be assumed that market potential and certainty are normally distributed (see Appendix B: Screenshot 1 and 2). Therefore the definition of classes is approximated by the normal distribution. Ten classes (C_n) by applying the following formula:

$$C_n = [\bar{x} - (2,5 + \frac{n-1}{2}) \sigma] ; [\bar{x} - (2,0 + \frac{n-1}{2}) \sigma] \quad (1.0)$$

The higher the class, the larger the market potential or certainty. The definition of classes depends on the MPS and CS and consequently on the selected criteria and their weights, so by adapting the criteria weights, the limits of the classes differ and the countries might be assigned to different classes. By using this method, all MPS and CS are translated to a classes from one to ten. This has the advantage that all countries can be allocated in the matrix shown below (see Figure 4 and Appendix B: Screenshot 3) where the x-axis shows the market potential and the y-axis the certainty. Furthermore, the underlying probability distribution assigns only a relatively small number of countries to the highest class. This means that only a small number of very attractive countries need to be evaluated further in the next

process steps. These countries which have a high market potential and high certainty are allocated in the upper right box. All other countries are not taken further in order to reduce the effort involved in the upcoming process steps.

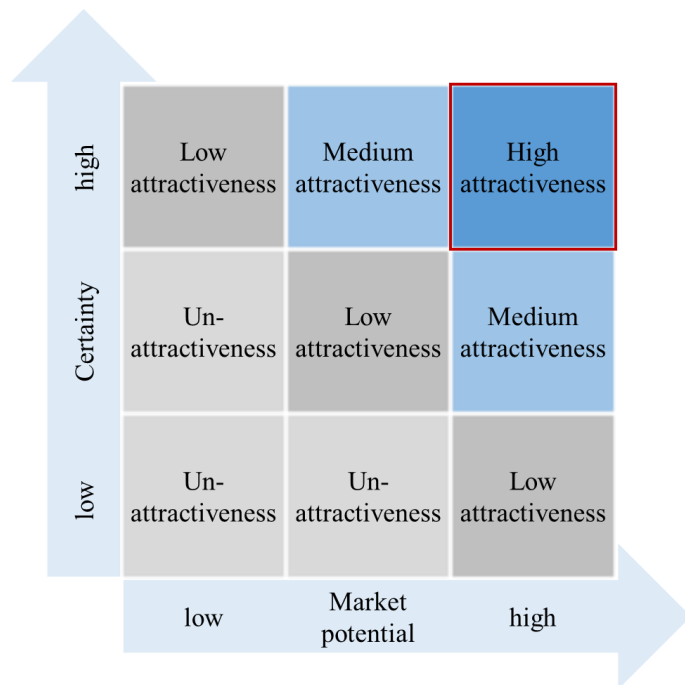


Figure 4: Market Potential-Certainty-Matrix
based on McKinsey matrix (Homburg 1991)

3.3 Step 2: Segment and Keyword Pre-Selection

Step 2 is divided into two substeps. First, all segments of the business are examined in order to identify the ones with the highest chance of successful market entry. Afterwards, a keyword is identified for each segment.

3.3.1 Step 2.1: Segment Pre-Selection

Companies can segment their business in order to monitor and manage it more efficiently. Depending on the business, different segmentation levels are useful. Most companies define the segments according to product or service types, industries, customer types or business sectors. Usually the performance of the segments is heterogeneous. Therefore, it is important to identify the best segments when entering a new market. This step aims to identify the segments which are best for market entry in the pre-selected countries. The pre-selection of segments is based on their performance in the home market measured by the key performance indicators (KPIs) total margin, total volume and margin per

volume. In addition to these, country-specific segments are identified by experts, peer-groups or surveys (Cofounder A). However, the selection of KPIs can vary depending on the characteristics of the ECS (DaSilva 2015).

3.3.2 Step 2.2: Keyword Identification

Acquisition of new customers and business growth are key measures for ECSs (Chen 2014). Andrew Chen (2014) states the four main channels which allow ECSs to scale growth: paid acquisition⁶, virality, search engine optimization (SEO) and direct sales. Except for direct sales, they all strongly depend on web search functions. Google is the most popular search engine in the world with a market share of about 69% in 2015 (netmarketshare 2015). Most ECSs focus mainly on SEO when they enter a new market as it is the acquisition channel with the highest long-term value (Cofounder A 2015). This makes content such as landing pages, articles and reviews as well as backlinks to the strongest enablers (Cofounder A 2015). All of these need to include the keywords which people use as search terms on Google, meaning that this process step aims to identify one suitable keyword for each pre-selected segment. Also the keywords from the basis of the evaluation of the market attractiveness in later process steps, thus requiring cautious selection (Cofounder A 2015). The keyword needs to be localized⁷ and it needs to lead to the pre-selected segment. Furthermore, it needs to have a high search volume. Market knowledge is a prerequisite to selecting the right keyword. The search volume of the keyword can be evaluated with the Google Keyword Planner.

3.4 Step 3: Country-Segment Analysis

Step 3 matches the pre-selected countries and segments in order to identify the most attractive CSCs. The step is further divided into the substeps: 3.1. Country-Segment Pre-Selection and 3.2 Country-Segment Analysis.

⁶ Paid acquisition includes paid online advertisement such as Google Adwords and Facebook Ads (Chen 2014).

⁷ Keyword localization is the adjustment of keywords to accommodate the language, cultural, political and legal differences of a foreign market (Business dictionary 2015).

3.4.1 Step 3.1: Country-Segment Pre-Selection

This step intends to test the demand for the pre-selected segments in the pre-selected countries. Each CSC can be considered as an independent market. This means that the demand of each pre-selected segment is tested in each pre-selected country. To determine this, a company landing page is launched for each country. On these landing pages, visitors can only select the segments they are interested in. A Google Adwords campaign is run in each country to increase the traffic on the landing page. The campaigns are based on the keywords identified in step 2.2. As a result, people who are looking for the segment will enter the landing page and select their preferred service. After a specific period of time the demand can be analyzed by country and segment. Only the CSCs with the highest demand receive further attention (see Figure 5).

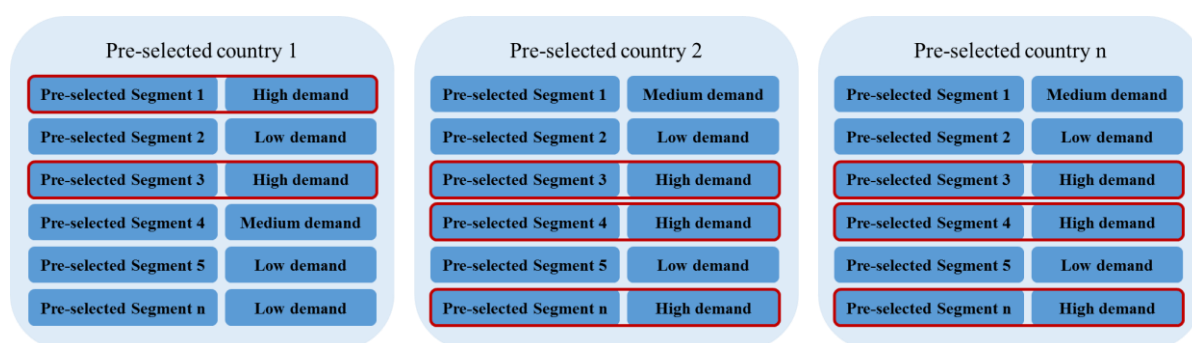


Figure 5: Overview of Selected CSCs

3.4.2 Step 3.2: Country-Segment Analysis

In this step the pre-selected CSCs are evaluated with the same methodology which is used to evaluate the pre-selected countries in process step 1.2. For each CSC an attractiveness score is determined by ranking and weighting the criteria market size, market trend, level of competition and customer acquisition cost (CAC). According to Cofounder A and Hertanu (2015), these criteria are most relevant for the evaluation of target markets (see Appendix D: Table 5 and Screenshots 5 and 6). Afterwards the segments are assigned to ten classes. The higher the class, the more attractive the CSC. In case of limited resources, the selection of CSCs for market entry proceeds from the highest class down.

3.5 Step 4: City Selection

Although most of the ECSs are capable of launching their product nationwide from day one, most of them have a higher chance of succeeding if they first focus on specific areas. This applies in particular for online market places which offer local services to increase the chance of matching demand and supply (Arnd 2015). ECSs for which this assumption does not hold can skip this process step and continue with step 5. Step 4 aims to identify the most attractive cities for local market entry for the previously selected CSCs. In theory, this could be done with the same methodology and criteria which were used to evaluate the pre-selected countries in process step 1.2 (see Chapter 3.2.2). This requires breaking down the country data at city level. However, some of the data is not available on city level and the availability of data also differs from country to country. Due to this, ECSs need to adapt the selection of criteria to their specific situation. For this reason, this paper only provides the criteria used by NewCo (see Chapter 4.4).

3.6 Step 5: Reality Check

Several tasks need to be carried out before entering a market. A reality check list with the following points has been developed on the basis of the literature reviewed and interviews conducted (see Appendix F: Screenshot 9): selected market in line with strategy and market entry mode; sufficient information collected on target market; necessary contacts / existing network; qualified human resources available; sufficient IT capacity; sufficient financing; selected market challenged with industry experts; sub-segment for market entry defined and selected; distribution channel selected; legislation and tax issues clarified and service pre-sold to users. The selected CSCs need to be checked according to this list. The company needs to fulfill all of the listed points in order to be completely prepared to enter the respective CSC. If one task cannot be performed for one CSC, another CSC needs to be selected and the process needs to be repeated from process step 3.2 onwards (see Chapter 3.3).

4 Application of the Target Market Selection Model to NewCo

This chapter applies the target market selection model to NewCo. It describes the company specifics which influence the model, and presents the results of the respective process step.

4.1 Step 1: Country Analysis

4.1.1 Step 1.1: Country Pre-Selection

NewCo aims to become the European leader and expand its business to South America. Based on this, their main consideration is countries on these continents. Australia and South Africa now own wildcard on request of the management team as there are no direct competitors. Currently, the service of NewCo is available in Portuguese, Spanish, English and German. Due to limited resources, Cofounder A decided only to enter countries where one of these languages is broadly understood. By applying language and the continent as the only KO criterion, 20 out of 170 countries have been pre-selected for further analysis (see Appendix B: Table 3 and Figure 8).

4.1.2 Step 1.2: Market Potential-Certainty Analysis

A workshop with the management team of NewCo has been conducted in order to select and weight the relevant criteria for the country analysis. This task is very critical because even a small change in one weight can have a strong impact on the outcome of this process step. Therefore, it is important that each criterion is reviewed separately. Table 1 shows the final outcome of the workshop.

Table 1: Country Criteria Weights

<u>Market potential criteria</u>	<u>Weight</u>	<u>Certainty criteria</u>	<u>Weight</u>
Urban population	2	Contract certainty	2
Population density	2	Corruption index	2
Population growth rate	1	Unemployment	1
Internet user	3	Country risk	1
Smart phone usage	1		
Online shopping	1		
Human-Development Index	2		
GDP Service sector	3		
GDP real growth rate	1		
Number of MSME	1		
Ease of doing business	1		

First, the market potential criteria were discussed. Due to the characteristics of NewCo, both sides of the market place need to be considered when evaluating the market potential. On the one hand, small professional service providers are needed to offer their services and pay NewCo for qualified leads. On the other hand, clients are needed who search for and book service providers online. Furthermore, both sides must be close together because often the physical presence of one party is required. Taking these specifics into account, the number of internet users is weighted with three as it is the strongest indicator for the client side. Urban population and population density are weighted with two as the geographical distance between supply and demand needs to be small. High population density and a large urban population increase the chance of a supply-demand-match. Moreover, the number of smartphone users and online shopper are both weighted with one. Although most of the users use the web version of the marketplace, these criteria are included because they indicate how developed a country is in terms of internet usage. A high manifestation suggests that many internet users are potentially interested in NewCo's service. The new service which NewCo offers results in a large, accessible market. This enables NewCo to grow regardless of the growth of the market size. Due to this population growth is weighted only with one.

The most important estimator for the supply side is the GDP of the service sector, weighted with three. It includes services that are not in the portfolio at NewCo but it is a good macroeconomic proxy for the market size. A high GDP indicates that many relevant services are also offered. In addition to that, the number of MSME has to be considered to show the number of potential service providers. It only carries a weight of one because many of NewCo's suppliers are not registered. The GDP growth rate is only weighted with one for the same reason as for the population growth rate. Furthermore, the Ease of Doing Business indicator is included with a weight of one because it is a well-established indicator for market analysis, and helps to understand the effort needed to conduct business in a country. A review of the certainty criteria was carried out after defining the criteria for market potential. For NewCo contract certainty and corruption index are weighted with two because of the high level of trust

needed between NewCo and its clients, as well as between the supply and demand side. The concept of a market place requires both parties to agree on common terms if the legislation of the respective country allows the enforcement of contracts. Unemployment and country risk are considered with a weight of one as they indicate the general stability of the country. The market potential and certainty criteria population, GDP Service Sector, GDP real growth rate, number of MSME and inflation are not relevant for NewCo and are therefore weighted with zero.

After the model has been adjusted with the criteria weights, the scores are calculated, the countries are assigned to classes and the pre-selected countries are allocated in the Market potential-Certainty-Matrix. Figure 6 shows this matrix including the countries with a high market potential and high certainty.

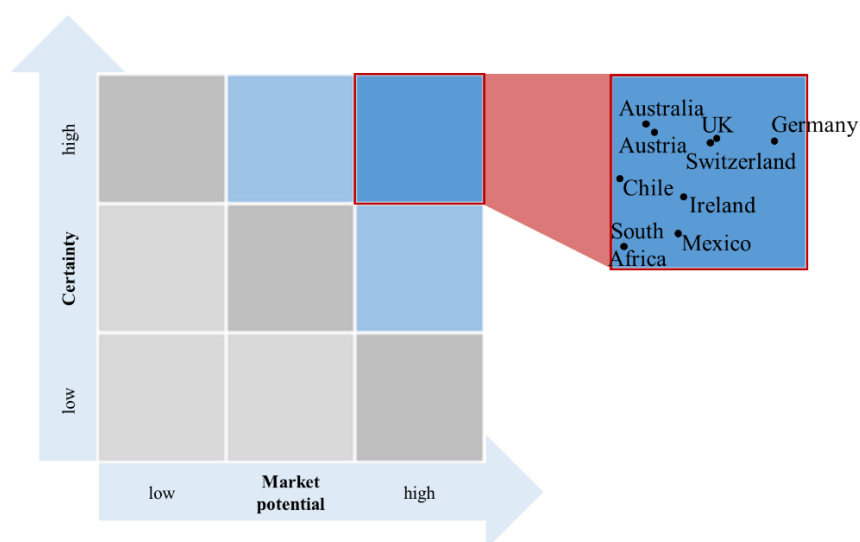


Figure 6: Market Potential-Certainty-Matrix applied to NewCo
based on McKinsey matrix (Homburg 1991)

The management team decided to further analyze Germany (MPS 2487 and CS 879), the United Kingdom (MPS 2369 and CS 826) and Australia (MPS 2079 and CS 875). Switzerland and Austria were not considered due to the fact that most of their market characteristics are too similar to the German market and their market size is smaller compared to Germany. NewCo selected the UK to strengthen their market position in Europe. Australia was selected because there is no direct competitor on the market. The South American countries were not selected because their scores were lower and NewCo decided to analyze only three countries due to limited resources.

4.2 Step 2: Segment and Keyword Pre-Selection

4.2.1 Step 2.1: Segment Pre-Selection

NewCo is present in more than 650 different service industries. Therefore, they structure their business according to segments which consolidate several service industries. During the first years of operation, NewCo collected knowledge about these segments in Portugal and Spain. Based on this, NewCo identified the twenty most successful segments. The main criteria for the selection were total margin, total volume and margin per volume. For example, segment “Service 1” was selected because it is the segment with the highest total margin in Portugal.

Additionally, NewCo identified ten segments with the help of market experts. “Service 28” is an example of one of these. In Portugal this segment is not among any top performing ones. However, this segment is selected because it is average in terms of market size and has no direct competitor in Germany, the UK or Australia (see Figure 7 and Appendix C: Screenshot 4).

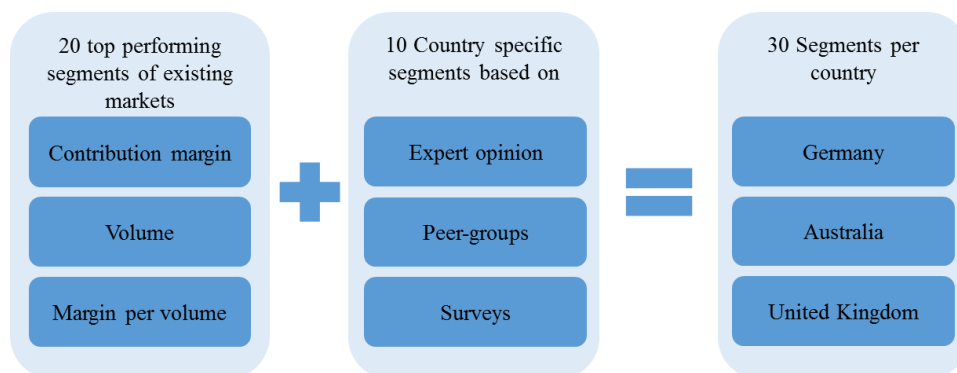


Figure 7: Segment Pre-Selection Method

4.2.2 Step 2.2: Keyword Identification

With the help of experts from Germany and the UK, NewCo identified a keyword for each pre-selected segment. First the Google Keyword Planner was used to identify several keywords per segment. The search results for each keyword were verified. Finally, the keyword with the highest monthly search volume was selected. For example, the keyword for the segment “Service 28” is “keyword DT 28” for Germany (see Appendix C: Screenshot 4).

4.3 Step 3: Country-Segment Analysis

4.3.1 Step 3.1: Country-Segment Pre-Selection

This process step was skipped due to strict budget limitations. All CSCs were examined further in step 3.2 without a demand test. As a consequence, a first validation of the CSCs on the market is missing.

4.3.2 Step 3.2: Country-Segment Analysis

As already mentioned, NewCo considers Google as its only customer acquisition channel. This assumption allows the application of Google-specific tools to indicate market size, market trend and the competitive situation. To estimate the market size, the monthly search volume was taken from Google Adwords, the market trend was indicated by calculating the compounded annual growth rate (CAGR)⁸ based on the 2012 and 2014 value from Google Trends, the level of competition was evaluated with MOZ, an institution which measures the competitiveness of keywords and the CAC is based on NewCo's internal data from Portugal (see Appendix D: Table 5 and 6). Market size and CAC are weighted with three since they are the most important factors when establishing a business with limited resources (Cofounder A 2015). Level of competition is weighted with two due to the fact that more competitiveness makes ranking high on Google more difficult. As in process step 1.2, the market trend is less important for NewCo, the size of accessible market being sufficient for NewCo (Cofounder A 2015). Based on the overall scores, the management at NewCo decided to go on to analyze the following six markets: GER4, GER5, GER20, GER29, AU30 and UK5 (see Appendix D: Table 7 and Screenshots 6 and 7).

4.4 Step 4: City Selection

The management team at NewCo agreed on population as the only criterion for city selection. Berlin, Hamburg and Munich were selected for the services GER4, GER5, GER20 and GER29; Sydney, Melbourne and Brisbane for AU30, and London for UK5 (see Appendix E: Table 8 and Screenshot 8). Due to resource constraints, no additional cities are selected for market entry.

⁸ $CAGR = \left(\frac{\text{Ending value}}{\text{Beginning value}} \right)^{\frac{1}{\text{number of years}}} - 1$

4.5 Step 5: Reality Check

The distribution channels are similar for all CSCs. NewCo offers its service online via a localized homepage. The same applies to sub-segment, legislation and IT capacity. The sub-segments are always defined according to cities, which were already selected in process step 4. Furthermore, it is very unlikely that their business model is limited through legislation in other countries. Due to highly developed technology, IT capacity can easily be adopted to new requirements. All CSCs are aligned with the strategy. Germany and the UK are in Europe and Australia owns a wild card. NewCo focus on pre-selling their service to providers and clients in order to validate the demand in the market before starting their operation. For the Australian and English CSCs, the company needs to acquire more market knowledge and qualified resources. Additionally, NewCo must extend its network in Australia and acquire additional financing. Until these tasks are accomplished no pre-sales can be made (see Table 2 and Appendix F: Screenshot 9).

Table 2: Reality Check List

Tasks	Selected market					
	GER4	GER5	GER20	GER29	AU30	UK5
Selected market in line with strategy and market entry mode	✓	✓	✓	✓	✓	✓
Sufficient information collected on target market	✓	✓	✓	✓	■	■
Necessary contacts / existing network	✓	✓	✓	✓	■	✓
Qualified human resources available	✓	✓	✓	✓	■	■
Sufficient IT capacity	✓	✓	✓	✓	✓	✓
Sufficient financing	✓	✓	✓	✓	■	✓
Selected market challenged with industry experts	✓	✓	✓	✓	■	■
Sub-segment for market entry defined and selected	✓	✓	✓	✓	✓	✓
Distribution channel selected	✓	✓	✓	✓	✓	✓
Legislation and tax issues clarified	✓	✓	✓	✓	✓	✓
Service pre-sold to users	■	■	■	■	⊙	⊙

Legend

Yes ✓

In progress ■

On hold ⊙

5 Critical Evaluation of the Target Market Selection Model

The developed Target market selection model (see Chapter 3) can be tailored to most ECSs. Due to the transparent structure of the model, the criteria and their weights can be adopted easily in order to match the specifications of other ECSs and their industries. Nevertheless, caution and know-how is needed to apply the model to other ECSs. The criteria as well as their weights need to be adapted. In order to further improve the accuracy of the model, company and industry specific selection criteria, such as market size, competition and margins must be incorporated. The outcome of the adjusted model should

be challenged with industry experts in order to analyze the accuracy of the model. Therefore, it is important to be aware that even a small change in one criterion weight can change the overall results tremendously. Although the model is mainly based on quantitative data, there is subjectivity when defining the criteria weights.

Considerations must also be made in respect to the characteristics of the ECS. The model is built on the assumption that Google is the most important channel for the acquisition of new customers. According to Cofounder A and Cofounder B (2015), this assumption is valid for NewCo. As a consequence, Google specific tools can be used to approximate market size, market trend and the competitiveness of their markets. ECSs for which this assumption is not valid, need to use other sources of information. Furthermore, the entire process is very keyword sensitive. Process step 3.2 is based on data which strongly depends on the selected keywords. This means that choosing a suboptimal keyword in step 2 distorts the overall results of the model. To overcome this obstacle, several keywords per segment should be selected. An average market size, competitiveness and market trend can be calculated for these keywords. This reduces the keyword sensitivity. Furthermore, an additional measure for the competitiveness could be included since the measure used is strictly limited to Google's organic search and does not consider competitors who use other customer acquisition channels, such as TV or offline marketing. Moreover, for some multi-segment ECSs, geographical markets are not the major structure level. For example Savvy, a marketplace for online teaching, plans its market expansion according to service industries and not countries (Arend 2015). This means that they launch specific services globally from day one instead of focusing on specific countries. Thus, the developed process would need to be changed completely in order to match Savvy's requirements.

6 Conclusion and Outlook

Within the process of this paper, the initial two research questions has been answered. The first research question asked for the main obstacles arising from the target market selection nowadays and where the

highest optimization potential is. This thesis proves that resources and time to market are the most crucial factors for every ECS. Nine out of ten ECSs interviewed stated that they invested only minimum time and effort in the selection of a target market. Their resources are tied to other tasks, such as product development, marketing and sales. Due to this, ECSs often follow an opportunistic approach leveraged by their personal network. Although this behavior entails several advantages, it also risks disregarding highly attractive markets. Hence, the main optimization potential lies in an easy-to-use and quick decision making tool for ECSs. The generic target market selection process developed represents such a tool. It enables ECSs to identify and evaluate the most attractive markets.

This study solves this situation for NewCo. By applying the model, NewCo can internationalize more efficiently and perform better. The target market selection model, allows the management at NewCo to evaluate and select markets in a systematic and objective way. The results of the model can be used to define the internationalization strategy as well as for the acquisition of investors as the reasoning for the international market selection is an important aspect for investors (Alves 2015). Furthermore, other ECSs can tailor the generic model (see Chapter 3) to their company specifics in order to select the most attractive markets. Besides the practical relevance of the model, this paper also expands upon the internationalization theories. It has shown that existing theories and models cannot fully explain the target market selection process of ECSs. The developed model provides one possible explanation for this phenomenon. However, more research is needed to validate the developed model. To achieve more significant results, the model needs to be applied to different types of ECSs, and the sample must be monitored over a longer period of time.

Referring to the initial statement of this thesis that ECSs are challenged by a dizzying growth which requires them to internationalize successfully in order to survive in the long-term (Sherman 2012), the target market selection model developed in this paper allows the management teams of these ECSs to identify the most attractive markets for their business and to internationalize more successfully. It is the first and most important step for ECSs to face this growth challenge and stay competitive in the market.

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