

**REGIONAL AND FIRM LEVEL DETERMINANTS OF INTERNATIONAL
COMPETITIVENESS: AN EXAMINATION OF SME'S ROLE, CAPABILITY AND
COMPETENCIES**

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Abstract

In our increasingly globalised world, supranational regions, nation states and individual country regions are progressively more in competition with one another. How the nation state and region can become more competitive and how this competitiveness can be measured is open to debate.

This thesis presents work based upon two aspects that have been proffered as to how competitiveness at the country and region level can be explained, that is through investment (via Foreign Direct Investment (FDI)) inflows and through the development of enterprise and in particular the enhancement of the small firm in international markets.

The theme that runs through the thesis is one of competitiveness and competence. The competence of the region to attract FDI and the competence of the entrepreneur and the SME to undertake internationalisation.

The thesis begins by examining the concepts of national and regional competitiveness. Two of the determinants of national and regional competitiveness are then considered - FDI and the level of small firm activity/entrepreneurship. The paper analyses the empirical and theoretical work on FDI and considers how regional competencies/factors can be used to attract FDI. SME internationalisation and its impact on regional competitiveness are then examined, focussing on the resources and competences, at the level of the entrepreneur and the firm, which influence SME internationalisation.

The thesis contributes to the richness of understanding of the complex relationship between the range of explanatory factors at a regional, national and supra-national level that influence inbound FDI. In particular providing a much better understanding of UK regional FDI inflows.

The section on internationalisation of SMEs contributes to the understanding of entrepreneurial and firm competences through the study of small firms at the county level of Northamptonshire. This county is a relatively under-researched area in the study of SMEs and in the study of the county's SME activity in international markets it has been even more sparsely investigated.

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Chapter 1 Introduction

1.1 Overview

The research presented here was conducted over a number of years. The starting point was SMEs in Northamptonshire and their level of export activity. From this strand of research an investigation of export competencies and, in particular foreign language competencies for SMEs in the county, emerged. The research then took the concepts of competencies and resources from the county to the regional level not by examining firm' competencies this time, but in the analysis of the competitiveness (competencies) of a region and its ability to attract inward FDI. Connecting both areas therefore are the themes of competitiveness and competencies and the various barriers that exist that can constrain regional and firm level competitiveness. The thesis is based on thirteen papers between the period 1997 to 2006, with the majority of the core papers published in the last five years.

This introductory chapter presents the research aims, delineates the scope of the research, establishes the main aims and outlines the structure of the thesis.

1.2 Research Aims

This study's prime aim is to gain a better understanding of the regional and firm level competencies that determine regional, national and international competitiveness. More specifically, the aims of this study are to:

- gain a better understanding of the drivers of regional and national competitiveness and their underpinning by both FDI and the level of small firm activity.
- engage with, and develop, theories of foreign direct investment.
- examine the drivers of FDI in the UK regions.
- develop the main theories that determine SME internationalisation.

- examine in detail both entrepreneurial and firm level competencies behind internationalisation and the barriers to internationalisation.

1.3 Research Themes

The thesis explores regional and firm level determinants of international competitiveness. It commences by examining national competitiveness and how regional competitiveness feeds into this. The main determinants of regional competitiveness are then explored and two of these in are investigated in detail. Firstly, the role FDI plays in affecting regional and national competitiveness, and secondly, the role of entrepreneurship or enterprise in stimulating both regional and national competitiveness.

Although there has been a range of studies into the determinants of inbound Foreign Direct Investment (FDI) both at a developed and developing country level there has been less research conducted into the determinants of regional FDI. In particular, there have been a limited number of studies that have examined the regional determinants of FDI in the UK.

The regional determinants of FDI within the United Kingdom are explored through the development of regression models utilising a range of secondary data. The thesis presents findings which show that regional competitiveness and attractiveness factors differ and can be driven by a combination of regional, national and supranational factors including skills levels, education, wage levels, regional funding and tax rates. The third paper in this section takes a broader look at the region, considering countries as part of the East European region. The results suggest that the mix of factors that explain inbound FDI again varies and suggests the "localness" of policy decision-making is required. This part of the thesis contributes to the extant knowledge of the determinants of FDI by drawing out the specific differences between regions, rather than treating them in aggregate or generic terms.

The papers in the second part of thesis lie in the area of the small firm. There is a stream that discusses and analyses firm level factors and their impact on internationalisation. A further section considers skills and competencies of SMEs for their own competitiveness and subsequently for regional and national competitiveness. In particular a number of the papers emphasise foreign language competence as a factor behind internationalisation. Central to the papers in this second part is an

investigation of UK county level SMEs in Northamptonshire a hitherto under-research area. The papers therefore in this section enable a comparison to be made between SME internationalisation and the manner in which SMEs in Northamptonshire fit into this picture.

Collectively the research has provided a fertile picture of the level of competencies and capabilities of regions and firms. It has identified the need to have local policies for local regions and also suggests that FDI might be driven by some factors that are different to those espoused by the development agencies. With regard to internationalising SMEs, the results of the work suggest a number of competencies that local firms are lacking in their attempt to internationalise or need to improve if they wish to increase their international presence.

1.4 Thesis Structure

The thesis comprises ten chapters and two appendices

- Chapter One sets out the aims, objectives and research themes
- Chapter Two lists the published works that comprise this thesis and provides a brief summary of each, cross-referencing to other papers in the thesis.
- Chapter Three examines the concepts of national and regional competitiveness and the factors that are said to determine these. The chapter also includes a discussion of spillovers from FDI and their impact on regional and national competitiveness.
- Chapter Four provides an extensive critical literature review of the theories of FDI
- Chapter Five explores the small and medium sized firm sector in the UK and provides evidence for the growth of the internationalisation of small firms.
- Chapter Six provides a critical analysis of the theories of SME internationalisation including stage theory, the theory of “born globals” and born again globals.
- Chapter Seven explores the capability and competencies of entrepreneurs and entrepreneurial teams for internationalisation. In particular there is a focus on foreign language competence and exporting and a critical analysis of resource base theory.
- Chapter Eight discusses the role of network theory as a means to overcome competency disadvantages faced by the internationalising small firm and the role of firm based factors in the internationalisation process.

- Chapter Nine explores the barriers to internationalisation and suggest areas of competency or resource disadvantage that SMEs face before they enter, or during their involvement in, international markets. The chapter also offers up some limitations with the research and opportunities for further research.
- Chapter Ten explores the research's contribution to knowledge and understanding of the role of SME internationalisation and FDI to regional competitiveness. It evaluates the achievement of the initial aims, some implications for policy makers and both the limitations and further research opportunities in the field of regional competitiveness.

Chapter 2 List of Publications and Paper Summaries

2.1 Introduction

The papers presented here for the award of a PhD by publication constitute only part of the author's output of over 100 published pieces of work including a number of authored books and chapters in other edited works. Although my published output began in the field of labour economics, specifically the teacher labour market whilst at Leicester University, my appointment at the University of Northampton led to the use of my economics training within the context of the economics of leisure/tourism. Looking back, the areas appear unrelated, but an underlying theme was emerging - competencies. The skills and competencies of the newly trained teacher in seeking to find employment and the competencies of a region to attract tourists and delivery tourism services. It was the latter area of research that developed my interest in the study of local economies, and more specifically the Northamptonshire economy.

At this time, the decline of Economics as a subject discipline at Northampton University and the rise of Business Studies led to subsequent changes in both my teaching and research interests. New modules appeared on international business and the small firm in a number of business programmes/awards. This developed my interest, subsequently, in SMEs and the role internationalisation plays in their development.

At the same time Northampton's Business School, began to develop contacts with the local Chamber of Commerce and Business Link and I was asked to be part of the team that worked with them. Out of this liaison, I was part of a team that produced a report that investigated through a range of interviews the FDI that came into Northamptonshire, particularly focussing on the attractiveness factors of the county as a destination for FDI, Cuthbert et al. (1997). It was during this work that I began to realise that the Chamber of Commerce had undertaken, and were undertaking, a number of large surveys in Northamptonshire concerning small firms. Their use of the data from these surveys, however, was fairly superficial. With their agreement I got together a small group of people who began to analyse further some of this data. This produced a number of publications and reports (some of which are included here) and out of this emerged further strands of independent research on foreign languages, ethnicity and skills relating to SMEs all within the context of the local Northamptonshire market. The success of this work within journals and Chamber reports/presentations led to me becoming a research associate for a joint body set up by the Business School at Northampton University and the Chamber

of Commerce, called Matters of Fact. This group commissioned and made bids for research contracts on a competitive basis for a variety of topics - one of which is included here as part of the PhD submission. Additional work for Matters of Fact came through an investigation of the motorsport industry in the county and the up-take of people with disabilities within the Northamptonshire small firm sector - see Cook (2002) and Cook (2004)

The previous work on FDI in Northamptonshire was also developed further in the new millennium when the East Midland Development Agency began to talk to us about FDI in the region. This re-stimulated my interest in FDI and in particular research in the area of regional attractiveness factors that can stimulate FDI. Two of the papers on regional FDI are included in this submission whilst a third is due for publication in *Regional Studies* in 2009 - see Fallon and Cook (2009)

My interest in economics, small firms, FDI and resources/competencies has also lead to a number of published texts that have utilised the previous research work. These include, Cook and Farquharson (1997), Piggott and Cook (1999, 2006) and Cook and Healey (1995). Looking back although the areas of research appear to be diverse, there has been a common thread running through much of the work - local/regional markets and regional and entrepreneurial competencies/resources.

The thirteen papers presented here as part of the submission for a PhD through publication have been published in wide variety of sources and utilise a number of pieces of original contributions investigating Local and Regional markets. A common thread linking the papers together is the broad issue of competitiveness and competencies. The papers are arranged in three sections. Section 1 papers deal with the macro-issue of national and regional competitiveness. The papers concentrate on the competitiveness of regions measured in terms of the attractiveness factors of the regions and their ability to draw-in FDI. Although there has been published work examining country determinants of inbound FDI there has been little work examining UK regional FDI in the context of regional, national and supra-national factors. The research papers provided here indicate that different regions' inbound FDI is determined by diverse factors, such as skill levels, education, wages levels, regional funding and tax rates. Furthermore the mix of the factors varies and this suggests the "localness" of policy decision-making. The work contributes to the extant knowledge by drawing out the specific peculiarities of regions, rather than treating them in aggregate or generic terms.

Section 2 and 3 papers explore competitiveness and competencies in more detail by taking the firm as the unit of analysis. Here the prime focus is on Small and Medium-Sized Enterprises (SMEs), especially in relation to international activity and competitiveness.

Both entrepreneur and firm-level factors are considered as determinants of SME success in internationalisation. Such factors would include skill competencies of the workforce, regional and national support for exporting, access to export experienced and knowledgeable individuals and the resource-based skills, capabilities, networks and competencies of SME entrepreneurs. The papers in sections 2 and 3 indicate that SME competitiveness in export markets, for example, can be enhanced through improved language competence, training and increased knowledge of foreign markets. The papers contribute to present knowledge through the development of models of export behaviour in a hitherto under-explored market comprising SMEs in Northamptonshire. In addition the papers add to the existing knowledge base by drawing-out the extent to which SMEs face specific regional challenges in terms of skills and capabilities for competitiveness both in their local markets and internationally.

2.2 Published Papers and Summaries

A brief summary is provided for each paper and the aim is to inform the reader of the main thrust and findings of the paper whilst also demonstrating the inter-relatedness of the series of papers both to one another and to the thesis.

The thesis is based upon the following publications:

Section 1: Regional SME competitiveness- FDI as determinant

- 1. Fallon, G, Cook, M and Billimoria, A. H. (2003) The Regional Distribution of Inbound FDI in the United Kingdom: Evidence from the West Midlands and Scotland, in Internationalisation: Firm Strategies and Management, Edited by Wheeler, C., McDonald, F. and Greaves, I. Basingstoke, Palgrave MacMillan. pp. 37-59, ISBN 1-4039-0671-8**

This paper focuses on the regional determinants of FDI in two UK regions – The West Midlands and Scotland. Through the use of primary research an econometric model was developed by the authors to explain inbound FDI into the West Midlands and Scotland. The econometric model, based upon the theoretic literature of Dunning and others was developed to explain the attractiveness of regions for inbound FDI. The paper also contrasted those factors the development agencies considered to be important in attracting FDI to their regions with the factors that were found to be significant drivers from the associated regional

econometric models. Although a number of studies have been undertaken to explain national FDI inflows few papers at that time had explored the determinants of regional FDI. The model developed here also used a broader range of explanatory variables to explain inbound FDI than earlier work and it therefore, enhanced further understanding of the regional determinants of FDI. Paper 2 below further develops this model and widens the analysis to further regions.

2. **Fallon, G. and Cook, M. (2004) A Four Regional Approach to Inbound FDI Decisions, in The Process of Internationalisation: Strategic, Cultural and Policy Perspectives, Edited by McDonald, F, Mayer, M and Buck, T., Basingstoke, Palgrave MacMillan, pp. 296-312, ISBN 1-4039-3228-X**

This paper expands on the work of paper 1. The explanatory variables used in the authors' econometric model in paper 1 are further developed and additional explanatory factors are utilised. Two further regions, Wales and the South Eastern region are included in the analysis. The four regions were chosen to explore peripheral, outer-core and inner-core differences in regional determinants of FDI. Although FDI was seen to be determined by the underlying motives of, market-seeking, resource-seeking, efficiency-seeking and strategic asset seeking, the explanatory variables determining FDI within each of these four categories often differed within each region. Regional competencies are therefore not necessarily the same, suggesting different policy objectives are required for each region.

3. **Fallon, G, Jones, A and Cook, M. (2004) The Determinants of FI Location in Central and Eastern Europe: evidence from Hungary and Romania, Managing Economic Transition Network, WP01/04. pp. 1-22, ISSN 1471-9894**

This paper utilises a model developed by Bevan and Estrin (2000) to explore FDI at a larger regional level, that of Eastern Europe. More specifically it examines FDI into Hungary and Romania within the Eastern European region. Using a model developed by Bevan and Estrin (2000) the paper seeks to consider whether the model is appropriate in a different time frame for economies in transition. The model utilises many of the concepts developed in papers 1 and 2 but also considers additional factors that can impact upon country FDI such as the source countries of FDI, gravity principles and risk. The paper still concentrates upon the underlying factors that drive FDI, but on this occasion in the context of relatively new market-based economies. The analysis contrasts an earlier entrant into the EU - Hungary - with a latter entrant - Romania.

Again the paper highlights the differences in the competitiveness factors in attracting FDI, as well as suggesting that models explaining FDI are not static but need to be dynamic responding to levels of market and economic sophistication.

Section 2: Firm-level factors as determinant of SME success in international markets

- 4. Cook, M (2006) Small Business and EU Policy, In International Business Economics: A European Perspective, 3rd edition, Edited by Piggott, J and Cook, M., Basingstoke, Palgrave MacMillan, pp. 346-371, ISBN 13: 978-1-4039-4219-7.**

This chapter explores competitiveness but in the context of SMEs. It reviews the literature on the internationalisation of SMEs with a strong emphasis on the empirical and theoretical work that has been utilised in the study of UK and European SMEs. The chapter analyses the success factors behind SME internationalisation using a range of comparative country studies. The chapter discusses both the theoretical developments of SME internationalisation as well as the factors constraining SME internationalisation.

- 5. Cook, M (2002) Supporting the Internationalisation of Manufacturers: The need for a more tailored approach, Proceedings of The Fifth SMESME International Conference: Stimulating Manufacturing Excellence in Small and Medium Enterprises, Ashcroft Business School, pp.270-277, ISBN 1-900-432-39-0**

This paper together with papers 6, 7, 8, and 9, 10 and 11 of section 3 investigates the export activity of SMEs from a more localised perspective – the SMEs in Northamptonshire. Paper 5 focuses solely on manufacturing SME exporters in Northamptonshire. Using a database provided by Northants Chamber, the manufacturing firms were selected from their sample and the data were further analysed using Chi squared tests. The paper analyses these manufacturing firms using three different dependent variables: the years actively exporting; the destinations of the markets for their exports; and the export/sales ratio of manufacturers. These three ways of defining exporters were analysed in terms of the reasons for entering export markets, the advice they use for this activity and the barriers and challenges they face in export markets. The paper argues that once the manufacturers are disaggregated by their level of export activity and by the years they had been exporting then important differences exist between the internationalising manufacturers and this suggests that a general approach to SME export support for manufacturing SMEs

within the county may not be appropriate. For manufacturing exporters in Northamptonshire a more targeted type and level of support is called for.

6. MacDonald, S and Cook, M (1997) Letters from America: A Lesson for Business Link? International Small Business Journal, Vol. 16, No. 1 pp74-79, ISSN 0266-2426.

SMEs and SME entrepreneurs bring a whole range of resources and competencies to successful ventures yet there are many SMEs that require further support due to their own lack of resources. One way to overcome resource and competency deficiencies is through public support programmes. This paper contrasts the US experience of support for the small business sector with the UK experience in the late 1990s. It evaluates the role of universities, the use of internet resources and small business advisors in the US and the UK as support agents in the ways in which they can improve the competitiveness of SMEs. Using previous studies the paper poses questions for the UK concerning the quality of Business Link advisors, the level of specificity of their skills, their level of past and on-going training, and the perception of Business Links and their advisors by SMEs.

7. Cook, M., Coskeran, T. and Weatherston, J. (2004a) The Northamptonshire Export Survey, Northampton Business School, Northampton, UCN Publications pp. 1-40, ISBN 1-901-547-027

Staying within the Northamptonshire economy, this paper along with paper 8 provides an analysis of SME exporting behaviour within the county. The paper utilises primary data obtained from a postal survey of SMEs undertaken by Northamptonshire Chamber. From this database of 304 respondents, the active exporters and non-exporters were separated out. This paper concentrates on the active exporters and a range of statistical tests were undertaken to consider their export decisions and level of support they received for exporting. The results of the study indicate that the size of the firm was seen as critical in being an exporter. The export decision appeared to be fairly unstructured and unplanned whilst questions were raised about the level of public and private support for exporting. SME resource factors were seen to be important determinants of export growth, in particular foreign language knowledge and the access to individuals who had experience of export markets. The paper also examined the pricing strategies adopted by exporters in both domestic and export markets and the geographical focus of their export activity.

8. Cook, M., Coskeran, T. and Weatherston, J (2004b) The Success and Constraining Factors Behind the Internationalisation of Northamptonshire's Businesses: Lessons from the

Northamptonshire Business Survey 1998, Northampton, UCN Publications, pp. 1-50, ISBN: 1-901-547-019

Whilst paper 7 focused solely on exporters and the issues that they faced in export markets, this paper, utilising a much larger general business survey of SMEs undertaken by Northants Chamber, enabled a better comparison of exporting and non-exporting SMEs in Northamptonshire to be undertaken. The paper uses a range of statistical tests to examine the differences between exporters and non-exporters. The authors then develop a number of bi-variate logistic regression models to examine the differences between exporters and non-exporters. These models found that there were differences between exporters and non-exporters in their use and commitment to training, the difficulties they faced in filling job vacancies, the types of people they recruited, their use of electronic communication and the areas of advice and support they needed in future business operations. The paper confirms the findings suggested in paper 6 concerning business support and the exporting/non-exporting interface and in particular the use of Business Links by SMEs.

Section 3: Skills, Capabilities and SME competences for competitiveness

9. **Cook, M. (2000) Training and Skill Needs for Successful Exporting: An Econometric Approach, Journal of European Business Education, Vol. 10. No. 1, December, pp. 33-47, ISSN 0968-0543**

Paper 9 provides a link to both papers 7 and 8. In this paper the author develops a number of logistic regressions to determine the differences in resource requirements by exporters and non-exporters. Exporters often found it more difficult to find appropriate skilled employees than non-exporters when trying to fill vacancies and this appeared to affect their growth, output and the quality of their output. Exporters pointed to managerial skills and foreign language skills as being most significant in constraining their growth performance and in general terms exporters considered that their resource constraints were greater than non-exporters. Knowledge of public sector providers of information did not appear to be an issue distinguished exporters from non-exporters, but use of the providers was patchy, with overseas trade services a significant priority for exporters. The paper argues that exporters not only required more and varied advice in their current export activity but also needed significantly more advice in the future in the areas of exporting, legislation, management processes and environmental management.

- 10. Cook, M and MacDonald, S. (1999) The Role Of Languages in Organisation Internationalisation, Journal of European Business Education, Vol. 9, No. 1, pp. 49-61, ISSN 0968-0543.**

Whereas papers 7, 8 and 9 highlighted a range of resource-based issues facing SMEs in their internationalisation endeavours, this paper and paper 11 focus on one specific resource question, that of the use of languages and language training and the impact these have on exporting. Paper 10 has an underlying theme that competitiveness and survivability in international markets can be related to foreign language use and foreign language competence. Using a number of case studies the paper explores the training needs and provision that SMEs made for foreign languages. In particular the paper argues that expanding and developing export capability is constrained through the lack of language provision and training.

- 11. MacDonald, S and Cook, M. (1998) An Exploration of the Use of Language Training in Exporting Firms: Case Studies from Northamptonshire, Local Economy, Vol. 13, No. 3, November, pp216-227, ISSN: 0269-0942**

Whilst paper 10 focused upon the role languages played in organisation internationalisation, paper 11 changes the focus to examine the specific area of language training. Based upon 14 case studies of SMEs in Northamptonshire it attempts to develop an understanding, of how firms use languages and access training as part of a competitive strategy. The paper offers some insights as to how firms find solutions to their training needs with larger firms adopting a multifaceted approach. Smaller firms' approach was far less varied and this, therefore, gave uneven outcomes. The paper highlights the need for SMEs to obtain better information on local and national language training support. The lack of resources was clearly an issue for SMEs in these case studies, particularly for smaller SMEs.

- 12. Cook, M. and Jones, J (2002) Labour Market Information to support Wellingborough East Masterplanning, Matters of Fact Consultancy Report, pp1-90.**

Paper 12 widens the discussion of resources from the specifics of foreign language competencies behind internationalisation to the consideration of the skills needs and skills shortages for SMEs within a specific part of Northamptonshire, the Wellingborough area. The study focused on the eastern development of Wellingborough and the desire to develop high value added jobs in the region. The study uses a combination

of secondary data from regional and county development agencies together with a number of face-to-face interviews with key stakeholders in the Wellingborough East development. The results of the analysis provided evidence of a “tight” labour market in the region, a lack of skills in the labour force, a core of poorly motivated workers who were unwilling to be trained and a group of more highly educated and skilled workers who, having greater flexibility in the labour market, chose to work elsewhere. The evidence from the study indicated that even though policy and decision makers would have liked to have developed an entrepreneurial region in Wellingborough based upon high value-added businesses, they may find such an objective difficult as many of the regions "best" resources, although resident in the region, chose to work elsewhere.

- 13. Cook, M., Ekwulugo, F. and Fallon, G (2003) Start-up and Motivation Factors in UK African and Caribbean SMEs: An Exploratory Study, paper presented at the 4th International Academy of African Business and Development Conference, Westminster Business School, London, pp 21-26, ISBN 0-9700504-0-5**

This paper examines SME skills, competencies and constraints within the Northamptonshire economy with a focus on the African and Caribbean business community. The paper makes use of a number of face-to-face interviews with African and Caribbean entrepreneurs to develop a case study approach in the examination of a range of resource questions for SMEs, including: the issues of start-up resources and finance, business growth and planning, business networks and constraints on business performance. The case studies focus on the resource capabilities and resources that these groups have at their disposal. In many respects this was a pioneering study into the African and Caribbean community in Northamptonshire and it illustrated the difficulties that this sector faced. Part of the research was to consider whether the problems/issues faced by the black SME community in Northamptonshire were similar or different to those from London/South East England which has tended to dominate previous studies.

Chapter 3 UK and Regional Competitiveness

3.1 UK competitiveness

In a recent report, (Deloitte, 2005), globalisation has been depicted as one of the most important drivers of UK competitiveness and Deloitte ranked the UK 6th out of 25 world economies in terms of overall competitiveness in 2005 (Deloitte, 2005). The UK government (DTI 2006) has acknowledged that there is no single measure of how well the UK is confronting globalisation, nonetheless, it offers up a wide range of measures that provide the drivers of productivity that have become linked to measures of competitiveness. In its report (DTI, 2006) the government has identified five drivers of productivity and hence competitiveness. These are:

Investment - both private sector (including domestic and overseas) and public sector and the stability of the macroeconomic environment that can encourage this to take place such as, low inflation, low interest rates, the reduced volatility of GDP growth.

Innovation - Publications and citations of scientific papers as a proportion of the population; R&D expenditure; the number of patents, the proportion of innovative active firms involved with networks and collaborations; and the share of firms' turnover linked to new and improved products.

Skills - level of skills at all levels of the economy to include workforce skills and management skills.

Enterprise - measurements of the enterprise culture; barriers to enterprise, such as administrative burdens on small firms and access to finance; the proportion of the labour force that is either starting or running a new business together with SMEs' productivity growth.

Competition - The level of competition in markets; the openness of an economy to international trade; the extent to which product market regulation acts as a restriction on organisations; and the effectiveness of competition regimes.

The above measures of competitiveness, what have been described as macroeconomic competitiveness factors, are not however, universally accepted as the determinants of competitiveness. Martin (2004) argues that without a good formulation of the underlying factors it is dangerous to base economic policy around

these. Countries could be developing the wrong factors. To illustrate the inconsistency in underlying factors the OECD (2001) relates national competitiveness to a different range of factors including: ICT usage; the diffusion of innovation and technology; the quality of human capital; the level of entrepreneurship; and macro-level factors such as: the stability of the economy; the low barriers to competition; and supportive financial systems.

Krugman (1994) argues that the concept of national competitiveness is essentially meaningless and compares the macroeconomic perspective on competitiveness with that of firm microeconomic competitiveness. His criticisms are based on three points:

1. Whereas the firm through lack of competitiveness can go out of business there is no equivalent of this for the Nation
2. When nations compete against one another it is not the same as that at the individual firm level. In the latter there may be winners and losers but in the former the success of one country or a region may create opportunities. It is not a zero-sum game.
3. If competition has any meaning it is an alternative expression of productivity.

National competitiveness also tends to be defined in terms of outcome rather than the factors that determine competitiveness. Therefore, greater interest should be shown in determining the factors that lead to increased competitiveness.

Although it is difficult to pin down, national competitiveness may trickle down to competitiveness at the regional level, whilst at the same time regional competitiveness can feed through to national competitiveness.

3.2 Regional Competitiveness

The EU's Sixth Periodic report on the Regions (1999) defines regional competitiveness as;

"...the ability to produce goods and services which meet the test of international markets, while at the same time maintaining high and sustainable levels of income or, more generally, the ability of (regions) to generate, while being exposed to external competition, relatively high income and employment levels". "In other words, for a region to be competitive, it is important to ensure both quality and quantity of jobs".

Like measures of national competitiveness there is, again, no single theoretical perspective that explains the complex nature and notion of "regional competitiveness". Classical Theory offers up investment in capital which improves productivity and the gains from trade. Neo-Classical theory also argues for the importance of trade as an engine for regional growth. Keynesian Economics considers that the main driving factors are capital intensity, the level of investment and government spending in area of public sector investment and the role of tax cuts/subsidies for enterprise. For countries and regions that are developing, development economics has played its role in explaining regional competitiveness. Although subject to some criticism Rostow's (1960) stage theory has explored the importance of agriculture and the role of investment in improving regional growth (though within the context of the appropriate social and political framework). Myrdal (1957) considers that regional competitiveness is influenced by the move from agriculture to other higher value-added sectors and that factors of production are attracted to regions which have better growth performances. Other key areas in developing regional competitiveness are the region's openness to trade, the level of overseas funding and the extent of foreign direct investment.

Endogenous growth theory has also sought to explain the key driving factors behind regional competitiveness. The theory suggests that the main drivers can be related to: the level of R&D expenditure, innovation (measured as number of patents), education levels, spending on investment in human capital (schooling, training) and the effective dissemination of knowledge.

In addition to the macroeconomic viewpoint regional competitiveness can be partly explained by micro-economy perspectives, such as that of urban growth theory (Jacobs, 1969; Feldman, 2002), transaction cost economics (Williamson, 1975), business strategy economics and most notably the work by Dunning (1993) into the role of FDI in influencing regional competitiveness. The Cluster Theory of Porter (1990) is also deemed to be relevant in regional competitiveness. He argues that geographic clusters encourage the development of regionally based inter-connected assets that are external to the individual firms but which improve their competitive performance. The degree to clustering provides increased competitiveness might rely on the type of cluster to which organisations join and the reasons for them joining the cluster (McCann *et al.* 2002). Clusters can be seen to stimulate levels of new firm formation, (Acs and Armington, 2004; Audretsch and Keilbach, 2004), through agglomeration economies and spill-over effects.

Schumpeterian economics through the innovative entrepreneur has also been propounded as a means of improving the competitiveness of regions. In particular the selection of new ideas and products is influenced by the relationship between entrepreneurial competencies and contextual factors.

The theoretical perspectives of regional competitiveness are manifold, but to what extent can they be explained by empirical analysis.

3.3 Empirical studies of regional competitiveness

Of the empirical work undertaken in the area of regional competitiveness, the EU's Second Report on Economic and Social Cohesion (2001) suggests the following factors are more important on influencing regional competitiveness:

1. Level of employment and productivity of those employed
2. The concentration of employment into particular sectors
3. Demographic factors
4. The level of gross fixed capital formation over time (the accumulated stock of capital)
5. Investment in the knowledge economy
6. Level and type of infrastructure
7. The level and nature of education
8. Innovation

An Ernst and Young Study (1997), benchmarking the East and West Midlands against other regions in Europe, suggested that competitiveness at a regional level was due to a combination of the amount of knowledge intensive skills measured in term of education and vocational training attainment levels; innovation capacity measured as the proportion of people in R&D and number of regional patents; the investment in fixed assets and human resources; the proportion of the workforce concentrated in high value-added industries; the strength of the business and financial sector and high levels of FDI. This final factor in the Ernst and Young Report received support from Cantwell and Iammarino (2000) who have argued that inward investment can lead to regional competitiveness through the process of inward innovation and technology.

Given the various theoretic models that have been put forward to explain regional competitiveness Martin (2004) concludes that there is no single theoretic perspective that can explain the phenomenon, but he attempts to develop what he has called "the regional competitiveness hat". Here regional competitiveness is determined by consideration of three elements: regional outcomes; regional outputs and regional determinants.

In competitiveness terms regional outcomes are measured by GDP per head which is decomposed into two parts: GDP per person employed (an approximate measure of labour productivity) and the employment rate. This again indicates why productivity is considered to be central to the discussion of competitiveness. Productivity is seen as an important indicator of competitiveness but not an explanation of it. The aggregate firm activity in a region is important in converting the determinants of regional competitiveness into regional outputs. The degree to which the transfer takes place is considered to be related to the management of the firm and its innovativeness. Moreover, the degree to which this throughput takes place can be related to the sectoral composition of the firms in a region, the levels of specialisation, firm distribution and ownership structure. Some of the latter will be strongly influenced by FDI into the region. What factors can determine the level of regional competitiveness? The determinants are likely to be a combination of local, regional, and national factors. Martin (2004) argues that key factors are the regional investment climate which can be broken down into the following determinants; infrastructure and accessibility; human resources; and the productive environment. These determinants are further influenced by secondary factors such as knowledge infrastructure, the level of innovation, the quantity and quality of technology, demography and migration.

New and Virdee (2006) have also considered the factors at a UK regional level that underlie the differences in competitiveness measured in terms of gross value added per capita. Using the study by Martin above they argue that the components of regional competitiveness (Gross Value Added, GVA) can be explained by sectoral specialisation, average labour productivity, employment rates, the age structure of the population, activity rates and commuting rates. These components they argue can be grouped into two groups. The first group includes natural endowments of the region that cannot be changed or are only subject to long-run change. This would include geographic location, natural resources, urban or rural predominance and demographics. The second group consists of untapped resources within a region that could be used more effectively. Here are included, transportation, general infrastructure, labour market institutions and regulation and human and social capital. When considering the main determinants of GVA per capita, New and Virdee (2006) argue that the main determinants of the differences between regional GVA per capita and that at a UK level are: productivity, the employment rate, commuting rate and activity rate. Of these four, GVA per worker, activity rates and commuting rates appear to be strongly related to GVA per capita, with

employment rates less so. In the report **Cook, M. and Jones, J (2002) Labour Market Information to support Wellingborough East Masterplanning, Matters of Fact Consultancy Report, pp1-90**, commuting was more prevalent for more highly educated, younger people who were attracted to other regions because of more appropriate job opportunities and higher levels of income. Often these job opportunities were not available in the local labour market which did not offer sufficient higher value-added jobs. As these better-skilled people left this served to tighten the local labour market and left behind people with less-skill and lower levels of productivity. The lower level of skills within the Wellingborough labour force affected the area in two ways: reducing the levels of entrepreneurship and influencing the decisions of firms both inside and outside of the region in their location and expansion plans.

New and Virdee (2006) also note that if productivity is measured in terms of GVA per hour worked then its impact on GVA per capita is less marked. Nonetheless, they are persuaded that at a regional level, the transport infrastructure, the sectoral specialisation of the region and the role of FDI, through its knowledge and spillover effects have positive impacts on regional competitiveness.

Regional competitiveness is therefore a complex notion and difficult to pin down. At one level it appears to be related to the individual firms that exist within a region and the interactions and spill-overs that come from these. Nonetheless, as Martin (2004) suggests factors such as the social, economic, institutional and public attributes of the region, such as networks of informal knowledge, trust etc. are important. He also notes that regional competitiveness may be instigated at the local, regional, national and international level. It is not surprising, therefore, that many regions seek overseas investment, particularly because it may bring important spill-overs into the region and because productivity of many of the inbound overseas companies is higher than domestic companies within the region.

3.4 Spillover effects from FDI

The importance of FDI in enhancing regional and national competitiveness through productivity spillovers has been the subject of much research and is one of the arguments for why regions, development agencies and governments have sought to attract overseas investment. The work by Dunning (1981) in his OLI framework regards the move by overseas companies into the host economy as connected to a range of ownership advantages that they possess over domestic firms such as, better knowledge (e.g. patents, technology, and trademarks). Griffiths (1999) notes that MNEs are more R&D-intensive than purely domestic firms whilst Girma *et al.*, (2001) argues that their existence in the local economy raises regional and national productivity. In addition MNEs may drive less efficient domestic firms out of the market and

exert sufficient pressure on those domestic firms that remain so that further productivity increases can be gained. FDI therefore, can be seen as having direct impacts on a region, through investment, employment opportunities and trade. It is through the indirect effect of spillovers that domestic firms can gain access to technology (Blomstrom and Kokko, 1998) and better management practices (Ruane and Ugar, 2004). The spillovers from foreign MNEs to domestic firms can come in a number of ways: They can come along industry lines as foreign affiliates increase a host economy's access to better inputs (Rodriguez-Clare, 1996). It may occur through the networks that are set up between domestic firms and MNEs via supply chain networks. It may arise along regional lines via the process of labour turnover (Song *et al.*, 2001, Moen, 2000) and this may be retained within the region if inter-regional labour mobility is low. Regional labour-market spillovers can be linked to agglomeration economies as both domestic and overseas firms seek to concentrate in one area. (Markusen and Venables, 1999). The negative impact of spillovers is also possible as FDI forces domestic firms to reduce their output and hence lower their productivity (Aitken and Harrison, 1999).

The way these spillovers have been assessed has generally been in three ways. Firstly, they have been analysed through case studies. Here Moran (2001) amongst others has found ample evidence of the positive spillovers in the electronics, machinery and transportation sectors particularly in the area of human resources, productivity enhancement and helping domestic firms to become exporters. Secondly, spillovers have been examined through industry-level studies (Caves, 1974; Blomstrom, 1986; and Driffield, 2000). Generally the view is that there are positive effects on the host country's productivity level. This may come about through the closure of less efficient domestic firms thereby raising aggregate productivity levels. It may come through the positive spillover effect route, and/or it can arise through MNEs having higher productivity levels themselves. A third group of studies considers whether the productivity of domestic plants is correlated with the presence of FDI in the sector/industry within the region. Few studies have been able to confirm this relationship with a number of studies, such as those by Haddad and Harrison (1993), Aitken and Harrison (1999) and Konings (2001) finding the reverse effect, and those by Ruane and Ugar (2004) and Girma *et al.*, (2001) unable to confirm positive productivity spillovers. However, the study by Haskel *et al.* (2004) has confirmed a positive effect at the plant level between overseas FDI and domestic plant's productivity. Furthermore where there are beneficiaries, the level of the technology gap, the degree of skills of the domestic sectors and the level of competition may play an influential role as to whether productivity benefits can be assimilated (Girma *et al.*, 2001)

If such spillovers can be noted it might explain why some governments or development agencies (within the UK) consider it worthwhile offering subsidies to overseas investors. This view is further reinforced when we consider the regional impact of spillovers. Girma *et al.*, (2001) found evidence in their study of the UK

firms for positive spillovers from foreign firms occurring in the same sector and region as the overseas investment. However, these spillovers are only significant for firms that have a low technology gap relative to the MNE. Outside the region there appeared to be negative spillovers at the sectoral level. Even if productivity spillovers cannot be found at the horizontal level, since MNEs may seek to conserve their ownership advantages, Javorcik (2004) argues that the benefits may be provided to the supply chain. In other words there are backward spillovers. Further forward vertical spillovers are also possible as the MNE provides inputs that are technologically superior to those that had been supplied before. Again Javorcik (2004) was unable to find any evidence of intrasectoral spillovers. Finally, it is possible that the reason why spillover effects in some studies have not been in evidence is that the appropriate statistical methods or data sets do not yet exist. Furthermore the spillovers may be heterogeneous and therefore aggregate studies have not been able to detect them (Gorg and Greenaway, 2003).

Although the evidence from spillovers from FDI is mixed, it has not prevented governments actively developing their regional and national environments to attract FDI. It is to these attractiveness factors - perhaps better considered as regional/national competencies - to which the thesis turns in Chapter 4.

Chapter 4 Theories of FDI

4.1 Introduction

Four main groups of theory have emerged seeking to explain the conditions underlying TNC development, focusing on their internal-specific advantages over domestic rivals (Hymer, 1976); oligopolistic rivalry linked to a pattern of imitative international investment (Knickerbocker, 1973; Graham, 1991); product life-cycle theories of trade and investment (Vernon, 1966 and 1979); and the links between high transaction costs and FDI (Williamson, 1975; Buckley and Casson, 1976; Jacobson et al., 1993).

Dunning's 'eclectic paradigm' has brought together these differing theories into a widely accepted framework in which to explore the determinants of FDI location (Dunning, 1998, 2001 and 2002). For FDI to occur, Dunning argues that TNCs must possess distinctive ownership-specific advantages, which they may be best placed to exploit if they can internalise their market transactions. Location is also important if TNCs are to exploit their ownership advantages as fully as possible. They must choose whether to internalise their transactions at home or in a foreign country, and the choice which they make will be heavily influenced by the costs and benefits of locating value-added activities in these different geographical locations.

Scholarly interest has been growing in the locational aspects of FDI, and in how location influences TNCs' competitive advantages and international market entry and development strategies (Dunning, 1998; Driffield and Munday, 2000). Intellectual or know-how capital is becoming increasingly important to the wealth-creation process, leading to a growing emphasis on the need to access spatially immobile assets (such as skilled labour and public infrastructure) in order to exploit firm-specific knowledge-intensive assets (Peck, 1996). TNCs' ability to shift intangible assets across national borders is restricted by the existence of location-specific clusters of complementary activities, leading to the concentration of some industries in particular geographical areas (Storper and Scott, 1995; Markusen, 1996). TNCs are also collaborating increasingly with suppliers, customers and competitors on a global scale, leading to a growth in cross-border alliances, mergers and acquisitions and providing a motive for FDI in particular locations (UNCTAD, 1997 and 2000).

A number of existing studies (Culem, 1988; Guimaraes et al, 2000; Billington, 1999; Hill and Munday, 1995; Yang et al, 2000) have sought to identify the main factors influencing the choice of FDI location in developed countries. Much of the existing empirical literature has explored this issue either at the national

(Wheeler and Mody, 1992; Devereux and Griffith, 1998) or at the regional level (Carlton, 1983; Friedman et al., 1992; Head *et al.*, 1995, 1999). Many researchers have focused on the US context, although some (such as Guimaraes *et al.*, 2000 and Ferrer, 1998) have examined the determinants of FDI location in Europe.

Additional studies are now beginning to emerge, based on the premise that decisions to invest in particular locations are dependent on a hierarchical structure of decision making, linking together international, national and regional elements. Devereux *et al.* (2001) argue that TNCs first choose between locating subsidiaries at the continental level (choosing for example between Europe and the USA), before moving on to decide whether to locate in individual countries (such as France or Germany). This analysis can be taken further by examining the locational determinants of FDI at the regional level, assuming that the decision to invest in a specific host country has already been taken. Loewendahl (2001a) similarly considers that the FDI location decision involves a series of successive stages, in which TNCs managers' attention is drawn initially to a long list of potential host countries, followed by a short list of countries, before focusing ultimately on potential regional and sub-regional sites. Crozet *et al.* (2004) view TNCs' location choices as being guided by a 'learning process', enabling direct investors to invest in locations increasingly remote from their countries of origin as their knowledge of host country and regional business conditions grows.

A number of taxonomies of FDI location have now been developed. Cantwell and Mudambi (2005) put forward a meta-analysis, in which a distinction is drawn between 'competence-exploiting' and 'competence-creating' TNC subsidiaries. The former follow demand-driven strategies, involving the exploitation of competences developed by their parent companies, by market-servicing investment and assembly type production, while the latter pursue more creative, supply driven strategies, involve the generation of new competences in host country locations, together with a range of positive spillover effects for the host economy (such as the dissemination of advanced technologies to local suppliers and competitors, and the upgrading of labour skills). This taxonomy can be related to that of Dunning (1993b, 1998 and 2002), according to whom four main strategic determinants of FDI location can be distinguished, including the search for markets (on the demand side), and the search for efficiency, strategic assets and natural resources (on the supply side). Government factors can also influence the FDI location decision, by facilitating the commitment of FDI and creating a virtuous cycle of investment in particular locations (Stopford and Strange 1991; Dunning, 1993b, 1998 and 2002; Manea and Pearce, 2004; Cantwell and Mudambi, 2005). The determinants of FDI location can in turn be linked to specific motives for direct investment, such as the size of the host economy, its level of per capita income, its population and growth potential, and access to substantial, proximate markets, in the case of market-seeking FDI (Thomsen, 2000; Di Mauro, 1999). FDI

location is also influenced by project type. Recent academic studies (such as Tatoglu and Glaister, 2000) point to six generic project types (IT and software, R&D and high technology, front and back office, manufacturing and assembly, headquarters, and distribution and logistics), each having its own, distinctive key location factors.

Both the papers by **Fallon, G., Cook, M. and Billimoria, A. H. (2003) *The regional distribution of inbound FDI in the United Kingdom: evidence from the West Midlands and Scotland*, In: C. Wheeler, F. McDonald and I. Greaves (Eds.) *Internationalization: firm strategies and management* (Basingstoke: Palgrave MacMillan) pp.37-59** and **Fallon, G. and Cook, M. (2004) *A four regional approach to inbound FDI location decisions*, In: F. McDonald, M. Mayer and T. Buck (Eds.) *The process of internationalisation: strategic, cultural and policy perspectives* (Basingstoke: Palgrave MacMillan) pp. 296-312**, seek to identify the main strategic determinants and specific motives which influence the choice of FDI location by TNC decision-makers at the UK regional level, and to investigate how far regional, national and EU-level factors help to explain the distribution of inbound FDI in the UK regional context. They focus on three of the above strategic determinants of FDI location: the search for markets, efficiency and strategic assets, together with the impact of government influence. Although resource seeking FDI is often discussed as a separate area in FDI theory, this interpretation of resources is becoming historic. Resources have more recently been confined to the area of natural resources. The discussion of the factors under the heading of resource seeking FDI as a category is therefore, excluded from the two papers, since the UK (excepting the continental shelf) is relatively poor in natural resource terms. Following the more recent work by (Manea and Pearce, 2004) the traditional concept of resources such the quantity and quality of labour, labour costs and the like are now considered to be part of other types of FDI, in particular efficiency seeking FDI.

The first paper, **Fallon, G., Cook, M. and Billimoria, A. H. (2003) *The regional distribution of inbound FDI in the United Kingdom: evidence from the West Midlands and Scotland*, In: C. Wheeler, F. McDonald and I. Greaves (Eds.) *Internationalization: firm strategies and management* (Basingstoke: Palgrave MacMillan) pp.37-59**, considers two regions within the UK, the West Midlands and Scotland. The second paper **Fallon, G. and Cook, M. (2004) *A four regional approach to inbound FDI location decisions*, In: F. McDonald, M. Mayer and T. Buck (Eds.) *The process of internationalisation: strategic, cultural and policy perspectives* (Basingstoke: Palgrave MacMillan) pp. 296-312**, widens the study to consider four UK regions and in doing so, makes a greater consideration of inner and outer core regions of the UK, further developing the work of Hill and Munday (1992). Both papers use an econometric model developed by the authors to determine the factors underlying inbound FDI into the regions. In addition the second paper widens the scope of the analysis to cover an increased number of regions, incorporating a greater range of explanatory variables and an increased data period.

The specific motives underlying each of the strategic determinants and government influence (at the regional, national and EU levels) are discussed in the following sections.

4.2 Market-Seeking FDI

Market-seeking (or horizontal) FDI is currently the main global determinant of FDI location, and is motivated by TNCs' continual search for better access to markets, linked to proximity issues, agglomeration and to the desire to minimise distance costs (Thomsen, 2000; Loewendahl, 2001a). It may be driven by the desire to sustain or safeguard existing regional, national or export markets or by the wish to develop new markets for successful existing products (Dunning, 1993a, 1998 and 2002; Culem, 1988; Manea and Pearce, 2004).

Market-seeking FDI can be drawn to particular locations by the population density of regional, national or adjacent markets, together with their per capita income levels, market size and growth prospects (Wheeler and Mody, 1992; Billington, 1999; Ford and Strange, 1999). The size of the market and access to a large proportion of the population was noted by the Advantage West Midlands and Locate Scotland as relevant determinants of FDI in both The West Midlands and Scotland - see the paper by **Fallon, Cook and Billimoria, (2003) The regional distribution of inbound FDI in the United Kingdom: evidence from the West Midlands and Scotland, In: C. Wheeler, F. McDonald and I. Greaves (Eds.) *Internationalization: firm strategies and management* (Basingstoke: Palgrave MacMillan) pp.37-59**. The importance of market size and the level of the population were also confirmed in the regression model for Scotland in this paper. The second paper **Fallon, G. and Cook, M. (2004) A four regional approach to inbound FDI location decisions, In: F. McDonald, M. Mayer and T. Buck (Eds.) *The process of internationalisation: strategic, cultural and policy perspectives* (Basingstoke: Palgrave MacMillan) pp. 296-312**, also confirms the importance again of the size of the population for inbound FDI in both Scotland and the South East region. Market-related agglomeration economies, including service agglomeration and industry-level localisation economies, can also act as important influences on the location of FDI (Guimaraes et al, 2000). The ability of many of the market-related variables to explain the regional location of FDI may be limited, where the markets served by foreign direct investors overlap inter-regional boundaries (Guimaraes et al, 2000). Import-substituting FDI is also more likely to be influenced by the size of local markets than is export-orientated investment (Dunning, 1998). However, market-based agglomeration economies now operate at the national and even at the continental scale (Martin and Sunley, 1996), so helping to draw in the latter type of FDI to regions spatially close to the heart of major supranational markets (such as the Single European Market's so-called 'golden triangle'). An example of this can be found in **Fallon, G. and Cook, M. (2004) A four**

regional approach to inbound FDI location decisions, In: F. McDonald, M. Mayer and T. Buck (Eds.) *The process of internationalisation: strategic, cultural and policy perspectives* (Basingstoke: Palgrave MacMillan) pp. 296-312, for Scotland where UK GDP was found to be an important determinant of inbound FDI. FDI may also be attracted by a self-reinforcing effect, consistent with the impact of agglomeration economies on market-seeking direct investment (Cheng and Kwan, 2000).

Market-seeking direct investment is likely to be attracted to countries or regions with good market access, facilitated by highly-developed transport and communications infrastructures and low transport costs (Hill and Munday, 1992; Arpan and Ricks, 1995; Mudambi, 1995; Yeung and Strange, 2002; Cheng and Kwan, 2000). Market access and good transport links have been specified as important in attracting FDI from the "official viewpoint" for both the West Midlands and Scotland in **The regional distribution of inbound FDI in the United Kingdom: evidence from the West Midlands and Scotland, In: C. Wheeler, F. McDonald and I. Greaves (Eds.) *Internationalization: firm strategies and management* (Basingstoke: Palgrave MacMillan) pp.37-59**, but could not be confirmed in the empirical analysis in this paper. At a more localized level, the paper **Cook, M. and Jones, J (2002) Labour Market Information to support Wellingborough East Masterplanning, Matters of Fact Consultancy Report, pp1-90**, indicated that the Wellingborough area would find it difficult to attract the appropriate inward investment without improving the local infrastructure.

Investment levels may be increased due to the presence of leading suppliers (Dunning, 1998); well-developed service support facilities (Dunning, 1998); and relatively low levels of competition from imports and rival firms (Milner and Pentecost, 1994). Market-seeking FDI location may also be influenced by the need to maximise familiarity with target market conditions (Barkema et al, 1997); and to preserve existing foreign markets established by exporting (Dunning, 1993b); and by the fear of losing potential markets by not engaging in FDI, when competitors are already established in a country or region (Dunning, 1993a; Srinivasan and Mody, 1998).

4.3 Efficiency-Seeking FDI

Efficiency-seeking (or vertical) FDI is driven by the differences in unit costs between geographical locations (Loewendahl, 2001a). It is motivated by the desire to rationalise the geographical structure of FDI in order to take advantage of specialisation (by product or process), of economies of scale and scope, and of potential synergies (Manea and Pearce, 2004). The location of efficiency-seeking FDI can be heavily influenced by TNCs' ability to concentrate production in one, cost-efficient location from which they can supply multiple markets within the same global region (such as the E.U.). The attractions of efficiency-seeking FDI have

therefore increased in recent years, due to the growth of regional integration, political and economic stability (particularly in the EU context) (Di Mauro, 1999; Loewendahl, 2001a).

Differences in local labour markets, trade union strength and regional economic and industrial development all influence the location of efficiency-seeking FDI. Labour market factors, including the supply, cost, skill quality and productivity levels of white and blue collar workers are potentially significant, as is the quality of industrial relations (Arpan and Ricks, 1995; Yeung and Strange, 2002; Manea and Pearce, 2004). The paper **Fallon, Cook and Billimoria (2003), The regional distribution of inbound FDI in the United Kingdom: evidence from the West Midlands and Scotland, In: C. Wheeler, F. McDonald and I. Greaves (Eds.) *Internationalization: firm strategies and management* (Basingstoke: Palgrave MacMillan) pp.37-59** provides evidence of the official view from both Advantage West Midlands and Locate Scotland of the importance of a highly-skilled and well educated labour force as a factor in drawing in FDI to the region. This is later confirmed by **Fallon, Cook and Billimoria (2003)** and in **Fallon and Cook (2004)** in their empirical study for the West Midlands and the South East but not for Scotland. Conversely, at a local level, the paper by **Cook, M. and Jones, J (2002) Labour Market Information to support Wellingborough East Masterplanning, Matters of Fact Consultancy Report, pp1-90**, has highlighted the lack of skills within the Wellingborough workforce and the low proportion of graduates that make up this market leading to a range of “hard-to-fill” vacancies. Thereby indicating the difficulty of attracting the appropriate quality and quantity of FDI to the Wellingborough area of Northamptonshire.

High labour costs and resultant wage differentials are likely to deter FDI (Cheng and Kwan, 2000; Billington, 1999; Aitken et al, 1996) although high and growing levels of labour productivity may offset this effect (Ford and Strange, 1999). Labour costs have declined over time as a proportion of UK companies’ operating costs, leading to a reduction in their importance as a determinant of FDI location. Nonetheless, wage costs were seen as influential in determining FDI in Scotland in **Fallon, Cook and Billimoria (2003), The regional distribution of inbound FDI in the United Kingdom: evidence from the West Midlands and Scotland, In: C. Wheeler, F. McDonald and I. Greaves (Eds.) *Internationalization: firm strategies and management* (Basingstoke: Palgrave MacMillan) pp.37-59**, and for the South East region in **Fallon, G. and Cook, M. (2004) A four regional approach to inbound FDI location decisions, In: F. McDonald, M. Mayer and T. Buck (Eds.) *The process of internationalisation: strategic, cultural and policy perspectives* (Basingstoke: Palgrave MacMillan) pp. 296-312**, However, the positive coefficient attached to the variable for Scotland might be explained by the positive correlation between labour costs and workforce qualifications and skills. This inter-relationship leads to a decline in the significance of labour costs when education variables are also included in regional FDI equations (Hill and Munday, 1992). In

addition the positive wage effect on FDI could be an indication of labour scarcity due to agglomeration economies.

High levels of unemployment may draw in efficiency-seeking FDI, by increasing the availability of labour and the willingness of employees to work harder and for lower wages. They can also however reduce inward investment levels by reducing incomes and spending power in host country locations (Friedman et al, 1992; Billington, 1999). In **Fallon, Cook and Billimoria (2003), The regional distribution of inbound FDI in the United Kingdom: evidence from the West Midlands and Scotland, In: C. Wheeler, F. McDonald and I. Greaves (Eds.) *Internationalization: firm strategies and management* (Basingstoke: Palgrave MacMillan) pp.37-59**, and in **Fallon and Cook (2004) A four regional approach to inbound FDI location decisions, In: F. McDonald, M. Mayer and T. Buck (Eds.) *The process of internationalisation: strategic, cultural and policy perspectives* (Basingstoke: Palgrave MacMillan) pp. 296-312**, the unemployment variable is significant and positive in the Scottish case in both econometric models and for Wales in the four regional model.

The effect of trade union strength on FDI is also unpredictable; high levels of unionisation can attract foreign investors, by raising worker morale and labour productivity (Billington, 1999); it can also deter FDI, however, if it has the effect of raising worker militancy and increasing average wage levels (Ford and Strange, 1999). The study by **Fallon and Cook (2004) A four regional approach to inbound FDI location decisions, In: F. McDonald, M. Mayer and T. Buck (Eds.) *The process of internationalisation: strategic, cultural and policy perspectives* (Basingstoke: Palgrave MacMillan) pp. 296-312**, was unable to confirm that trade union strength was a significant explanatory variable for inbound FDI in any of the four regions in the study.

Regional economic and industrial development, the availability and quality of supporting industries and the resultant potential for cluster development can all influence the location of efficiency-seeking FDI (Porter, 1998; Dunning, 1998 and 2002). Cluster development was also a feature desired by the development agencies in the paper, **Fallon, Cook and Billimoria (2003), The regional distribution of inbound FDI in the United Kingdom: evidence from the West Midlands and Scotland, In: C. Wheeler, F. McDonald and I. Greaves (Eds.) *Internationalization: firm strategies and management* (Basingstoke: Palgrave MacMillan) pp.37-59**. In particular Advantage West Midlands noted the desire to develop its sectors in financial services, soft ware and automotive suppliers, whilst Locate Scotland emphasized its electronics and business services. However, the variable used to measure clusters was not found to be significant for either the West Midlands or Scotland in the empirical analysis and could only be found as significant in one region - the South East - in **Fallon and Cook (2004) A four regional approach to inbound FDI location**

decisions, In: F. McDonald, M. Mayer & T. Buck (Eds.) *The process of internationalisation: strategic, cultural and policy perspectives* (Basingstoke: Palgrave MacMillan) pp. 296-312. High levels of industrial development can act as a stimulus to FDI, as can high geographical concentrations of manufacturing or services activity (as for example in the English West Midlands or the German Ruhr) (Wheeler and Mody, 1992; Billington, 1999). Again a factor highlighted in, **Fallon, Cook and Billimoria (2003), *The regional distribution of inbound FDI in the United Kingdom: evidence from the West Midlands and Scotland, In: C. Wheeler, F. McDonald & I. Greaves (Eds.) *Internationalization: firm strategies and management* (Basingstoke: Palgrave MacMillan) pp.37-59.*** Efficiency-seeking FDI can also be attracted by the presence of specialised clusters of related industries (such as in Silicon Valley, California) (Enright, 1995, 1996 and 1998; Martin and Sunley, 2001). **Fallon, Cook and Billimoria, 2003,** argue that the Silicon glen cluster in Scotland was also a strategic cluster for this region. Industrial park facilities, specialised support services (including training support) and good potential links with local suppliers and buyers can all help draw in FDI (Martin and Sunley, 1996; Srinivasan and Mody, 1998). These conditions can help to create ownership-specific advantages which can be internalised by the TNC as a whole (Birkinshaw and Hood, 1997; Gorg and Ruane, 2001).

Regional clusters and networks of related firms can help to raise productivity, innovation and new business formation at the regional level, leading to lower costs and greater new product development opportunities for TNCs and therefore to greater levels of inbound FDI (Braunerhjelm, and Svensson, 1995; Krugman and Venables, 1995; Ivarsson, 1999). The existence of a business climate conducive to entrepreneurship can also help to promote supply chain linkages and cluster development, thus helping to leverage in additional FDI to particular locations (Dunning, 2002). Regions may also become more entrepreneurial as a response (Atherton and Frith, 2005). However, as the paper by **Cook and Jones (2002)** argues, localised regions with high levels of entrepreneurial activity may overstate an entrepreneurial region if the area is being used as a registered address. In addition, the Wellingborough region of Northampton might not have a long term commitment to the growth in self employment as business starts-ups are more determined by the rise and fall of the level of demand in the general labour market, **Cook and Jones (2002).**

4.4 Strategic Asset -Seeking FDI

Strategic asset-seeking FDI is typically motivated by the desire to sustain or advance TNCs' international competitiveness. It is often based on the exploitation of technological assets in foreign countries, using perhaps collaborative joint ventures, cross-border mergers and outright acquisitions as a means to this end (Dunning, 1993a, 1998 and 2002; Manea and Pearce, 2004).

Strategic asset-seeking FDI can make use of local technology to meet host country consumers' needs and to support local manufacturing facilities in foreign locations. It can also be based on the acquisition of new, location-specific knowledge-related assets, such as regionally – concentrated scientific know-how and technological expertise (Cantwell and Janne, 1999; Enright and Roberts, 2001). The location of FDI in well-chosen countries or regions can therefore help TNCs to become more innovative and technologically advanced, with the result that their global competitiveness can also be improved.

The availability of highly developed skills capital is a key influence on the attraction of strategic asset seeking FDI to particular countries and regions. The existence of know-how intensive clusters and science park facilities can also draw in R&D and innovation-related FDI to particular locations and regions (Crone, 2001; Gorg and Ruane, 2001). This is also a feature of the Silicon Glen attractiveness advocated by Locate Scotland in, **Fallon, Cook and Billimoria (2003), The regional distribution of inbound FDI in the United Kingdom: evidence from the West Midlands and Scotland, In: C. Wheeler, F. McDonald and I. Greaves (Eds.) *Internationalization: firm strategies and management* (Basingstoke: Palgrave MacMillan) pp.37-59.** Advanced industrial countries are generally best placed to offer these kinds of advantages to investors and thus generally enjoy an advantage over less developed countries in attracting strategic asset-seeking FDI (Loewendahl, 2001a).

Strategic asset-seeking FDI is becoming increasingly important over time, as TNCs' depend more on advanced know-how for their competitive advantage, and also become more deeply rooted in host economies. Direct investment in regions with internationally competitive, know-how-intensive clusters can enable TNCs to tap into regionally-based, often cluster-specific, scientific and technological expertise, leading to faster innovation and potentially to global competitive advantage. This can bring benefits for host regions as well as for TNCs, resulting from the deepening of local value chains, as well as from increased levels of locally-based innovation and technology transfer (Grabher, 1993; Dunning, 1998; Porter, 1998; De la Potterie and Lichtenberg, 2001; Neven and Siotis, 1996).

4.5 Government influence on FDI

Investment location decisions are increasingly being driven by the need to access the best economic and institutional conditions, enabling TNCs to exploit their core competencies most effectively and thus maximise the resultant competitive advantages (Woodward, 1992; Dunning, 2002). 'Location tournaments' now take place, involving the use of investment allowances, tax breaks, promotional campaigns and a range

of other measures as a means of luring inward investment into particular locations (Coughlin *et al*, 1991; Hill and Munday, 1992, 1994 and 1995; Wheeler and Mody, 1992; Oman, 2000). Investment promotion can only be truly effective, however, if it goes beyond investment incentives alone to encompass the competitive positioning of individual regions in the market for FDI, sector targeting and cluster development strategies and effective lead generation, project handling and after-care mechanisms, resulting in the attraction and retention of new FDI projects (Loewendahl, 2001b).

Empirical research findings (Hill and Munday, 1992, 1994 and 1995; Brewer and Young, 1995; Phelps, 1997) suggest that governmental and regional policy initiatives, making use of financial and other incentives, can exercise a significant impact on the attractiveness of particular sub-national regions to inward FDI. This was a factor raised by both the development agencies in, **Fallon, Cook and Billimoria (2003), The regional distribution of inbound FDI in the United Kingdom: evidence from the West Midlands and Scotland, In: C. Wheeler, F. McDonald and I. Greaves (Eds.) *Internationalization: firm strategies and management* (Basingstoke: Palgrave MacMillan) pp.37-59**, and the results of the empirical work in this paper confirms the importance of regional preferential assistance in influencing inbound FDI. In their four region study of the UK, **Fallon and Cook (2004) A four regional approach to inbound FDI location decisions, In: F. McDonald, M. Mayer and T. Buck (Eds.) *The process of internationalisation: strategic, cultural and policy perspectives* (Basingstoke: Palgrave MacMillan) pp. 296-312**, show that regional preferential assistance (RPA) was a significant factor in determining FDI inflows in the West Midlands, Scotland and Wales. The insignificance of the variable for the South East region probably reflects the low level of assistance that is available there. The effectiveness of such initiatives differs however between the successive stages of the TNC decision-making process (Loewendahl, 2001a; Oman, 2000). In the first stage, TNCs focus their thinking on global regions such as the EU, drawing up a 'long list' of countries which satisfy their broad location criteria. Market-seeking motives are typically dominant at this initial stage. In stage two, a short list of countries within the global region is compiled, and efficiency-seeking motives now become the dominant criteria governing locational choice. In stage three, TNCs actively consider different locations within particular countries, with the result that national and regional government policies and investment incentives now influence their locational thinking. In stage four, TNC managers often visit a number of rival locations, with a view to taking final decisions over the suitability of infrastructure and premises to their direct investment needs. At this final stage, the quality of the support services offered by national and regional governments and their agencies constitute a highly significant influence on TNCs' FDI location decisions.

National governments also have the ability to influence the regional location of FDI, at least in the advanced industrial country context, by pursuing preferential policies towards foreign investment and trade (Donahue, 1996; Ohmae, 1995). Increasing economic openness, by for example tariff reductions can lead to greater inflows of FDI (Culem, 1988; Veugelers, 1991). Governments' exchange rate policies can also influence FDI, since exchange rate appreciations can reduce the competitiveness of countries and regions as FDI locations, while depreciations can have the opposite effect (Grosse and Trevino, 1996; Blonigen, 1997; Xing and Wan, 2004). The E.U. also has the ability to influence FDI location, by means of its impact on the market performance of member states, and through its competition, industrial and labour market policies (El-Agraa, 2004).

Government actions can also help to increase the attraction of efficiency-seeking FDI to particular countries and regions, by promoting industrial restructuring, the upgrading of human skills capital, regional cluster and supply chains, and small business development (Young and Hood, 1994; Tavares and Young, 2002; Dunning, 1998 and 2002). A broadly-based economic development policy can be followed, including attempts to upgrade the productivity of all competitive clusters rather than merely to shift the regional industrial mix to the most desirable clusters (Porter, 2003). Efforts can also be made to invest in the enhancement of national and regional level research and technological expertise and, specifically, to promote R&D activities as a means of luring in strategic asset-seeking FDI (Adams *et al*, 2003). The ease or difficulty with which institutional and legal arrangements allow strategic assets to be acquired by foreign firms can also be an important influence on inward investment of this type (Dunning, 2002).

Some scholars (for example, Cantwell and Mudambi, 2005) argue however, that government investment incentives may prove to be ineffective in drawing in 'high-technology', R&D-intensive FDI inflows to economically backward regions. Such regions suffer typically from poor infrastructure and labour skills, high unemployment and many other drawbacks, with the result that very few competence-creating MNE subsidiaries may be enticed in or developed from existing, locally based, screwdriver operations. Cantwell and Mudambi do go on to argue however that investment incentives may lead to positive 'pump-priming' effects, encouraging the attraction or development of R&D intensive local subsidiaries, and leading to a 'virtuous cycle' of continuing local investment (associated with local agglomeration effects).

Both of the papers, **Fallon, G., Cook, M. and Billimoria, A. H. (2003) The regional distribution of inbound FDI in the United Kingdom: evidence from the West Midlands and Scotland, In: C. Wheeler, F. McDonald and I. Greaves (Eds.) *Internationalization: firm strategies and management* (Basingstoke: Palgrave MacMillan) pp.37-59 and Fallon and Cook (2004) A four regional approach to inbound FDI**

location decisions, In: F. McDonald, M. Mayer and T. Buck (Eds.) *The process of internationalisation: strategic, cultural and policy perspectives* (Basingstoke: Palgrave MacMillan) pp. 296-312, confirm that the search for markets, efficiency, strategic assets and government factors determine FDI into the UK regions. However, the actual variables within each category often vary by region as does the importance of each of the categories. Policy makers therefore, need to concentrate on specific factors for each region as attractors of FDI rather than following what their neighbouring region does. The two studies above, however, also confirm the consistency of the factors in the West Midlands and Scotland that determine FDI into these two regions.

4.6 FDI in the wider region

The third paper in this section, **Fallon, Jones and Cook (2004) *The determinants of FI location in Central and Eastern Europe: evidence from Hungary and Romania* *Managing Economic Transition Network* WP01/04 pp.1-22**, considers the region in the wider sense, not as part of a country but as countries within a region (Eastern Europe). Again the focus is on inbound FDI and its determinants but in the context of two countries, Hungary and Romania. The countries were chosen to illustrate two parts of Eastern Europe that were at different stages of economic development - Hungary (a more advanced, first wave accession country) and Romania (a less advanced, second wave country). An econometric model is then used to determine the factors that led to FDI entering Eastern Europe and the competitiveness of these countries to attract and retain FDI. FDI is sought by countries in Eastern Europe to promote economic growth and help with the transition process by integrating Eastern European economies into the broader global economy (Hare *et al.*, 1999, Grabbe and Hughes, 1998). It is also a means by which domestic production can be made more efficient, export performance can be improved, there can be a better re-allocation of resources and the means by which innovation and product improvement can take place, (Hunya, 1997; Holland and Pain, 1998; Barrell and Pain, 1999).

The paper by **Fallon, Jones, and Cook (2004)** makes use of a model developed by Bevan and Estrin (2000). Firms engage in FDI where the expected returns exceed the resultant costs. FDI will be more profitable where host country size is greater, the costs of inputs (such as natural resources and labour) are lower and where direct investment is less risky (Sing and Jun, 1995; Culum, 1988). The search for market opportunities is also a reflection of host economy market size (Lankes and Venables, 1996).

Caves, (1996) and Singh and Jun, (1995) have also argued that FDI and economic openness are positively related. A proxy for this in the paper by **Fallon, Jones, and Cook (2004)** is the proportion of Hungary's and Romania's imports sourced from EU member states. Adopting the same approach as Bevan and Estrin

(2000) the country's announcement of EU membership is used as a measure of country risk with Hungary having the lower measure of risk.

The research underlying the paper by **Fallon, Jones, and Cook (2004)** also makes use of bilateral trade flows between donor countries and the two recipient countries. The issue of how best to serve foreign markets is often determined by the trade-off between the incremental costs of direct investment and the costs involved with exporting relating to scale economies (Brainard, 1997). Gravity models have also been used to explain bilateral trade flows and distance between the capitals of Hungary and Romania and the main donor countries was used as a proxy for transaction costs. To take account of the US's greater than expected bilateral trade flows in excess of those predicted by the gravity model (due to economies of scale and scope) a dummy variable was used to reflect its reduced transaction costs. Similarly, a dummy variable was used for Germany since its trade flows might be expected to be greater than those predicted by the gravity model because of its historic geographical closeness with some of the Eastern European countries. One final variable included in the model was the differential bond yields between donor countries and Hungary and Romania. This was used to reflect the impact of supply constraints on FDI (again following the example of Bevan and Estrin, 2000). The results of the study by **Fallon, Jones, and Cook, (2004)** indicate that in the case of Hungary, only the German dummy variable is significant. Market seeking factors do not appear to provide a statistically significant motive for FDI into Hungary. In the case of Romania, market seeking motives are also not significant, though source country GDP, the openness of the Romanian economy (measured as Romania's total imports coming from the EU 15), distance (as a measure of gravity) and unit labour costs are significant. From the paper by **Fallon, Jones, and Cook, (2004)** the results suggest that FDI into Eastern European region of Hungary and Romania can partly be explained by the motives outlined earlier in this thesis, but by considering aggregate data for the whole country hides sectoral influences on inbound FDI. The results from my paper also raise questions as to the validity of the Bevan and Estrin model for countries in the second stage of development. It may be more appropriate for countries in their first stage rather than a more advanced economy such as Hungary, which has made the transition to the next stage of development.

FDI can be an important determinant of regional and national competitiveness. However, the attractiveness factors - what might be called regional or country competences or resources - differ. If, therefore, regions and nation states do not possess the appropriate quantity and quality of resources and competences then inbound FDI, if it comes at all, might by-pass these regions and move onto other resource rich regions.

FDI, however, is only one of a number of factors that can stimulate regional competitiveness. The ability of region to engender a vibrant SME sector has also been established as improving both national and regional

competitiveness (see earlier in this thesis), and it is to this sector of the economy that the thesis now turns. In particular, focus is upon the growth of SME internationalisation and its relationship to the level of regional entrepreneurship and its connection to regional and national competitiveness. SME internationalisation can have important consequences for the growth and sustainability of SMEs and the extent of both domestic and international activity of SMEs in the UK are described in Chapter 5. The thesis then develops the major theoretical perspectives that have been proposed to explain SME internationalisation and in particular the thesis focuses on the resources and competencies that might determine the level of SME internationalisation.

Chapter 5 The small Firm Sector in the UK

5.1 Background to the small firm sector in the UK

The Bolton Committee (1971) defined a small firm as an independent business, managed by its owner or part-owners and having a small market share. It also defined small businesses using a number a number of different statistical definitions. It recognised that size was relevant to sector, and offered up definitions based upon number of employees, turnover, and vehicle numbers. Although the Companies Act of 1985 further specified what were "small" and "medium" companies, the Department of Trade and Industry uses the definition shown below.

- Micro-businesses – those with fewer than 10 Full Time Equivalent (FTE) employees
- Small businesses – those with fewer than 50 FTE employees
- Medium-sized businesses – those with fewer than 250 FTE employees
- Large businesses – 250 employees or more

The EU has also adopted a similar categorisation of SMEs since 2003, revising their earlier definition of 1996. As noted below, the EU definition also makes reference to levels of turnover.

Table 1 SME definitions in the European Union

Enterprise Category	Employees	Turnover limit (Euro million)	1996 turnover limit (Euro million)	Balance sheet total (Euro million)	1996 balance sheet total (Euro million)
Micro	<10	2	Not defined	2	Not defined
Small	<50	10	7	10	5
Medium	<250	50	40	43	27

Source: Europa (2003)

Deakins and Freel (1998) argue that a vibrant and healthy economy depends on the competitive advantage that can be obtained from a strong and vibrant SME sector and sustaining and growing these types of businesses has been recognised as being an important element of government policy. In my chapter, **Cook, M. (2006) Small business and EU policy, In: J. Piggott and M. Cook (Eds.) *International business economics: a European perspective* 3rd edition (Basingstoke: Palgrave MacMillan) pp.346-371**, it is argued that:

"SMEs are now considered as important drivers behind the growth and creation of employment, economic growth and increased national and regional competitiveness in a globalised economy" **Cook (2006), p346.**

Furthermore I argue that "The dynamic performance of regions and even entire economies are linked to how well the potential from innovation is used and the extent of entrepreneurial activity" **Cook (2006), p347.**

In international terms, the Global Entrepreneurship Monitor Report (GEM, 2007) suggests that SME activity in the UK, measured in terms of Total Early-Stage Entrepreneurial Activity (TEA), stands up well against the other G7 countries and Russia. However, the UK continues to have a lower TEA rate than the US, Canada, Brazil, India and China, see Table 2. Overall the UK TEA rate has consistently followed the similar trend for the G7 countries.

Table 2, Total Early Stage Entrepreneurial Activity in G7 and BRIC countries

	2002	2003	2004	2005	2006	2007
UK	5.38	6.36	6.25	6.22	5.79	5.56
Canada	8.8	7.99	8.84	9.33	7.1	-
France	3.32	1.62	6.04	5.35	4.4	3.17
Germany	5.16	5.2	5.07	5.39	4.2	-
Italy	5.9	3.18	4.32	4.94	3.5	5.01
Japan	1.81	2.78	1.46	2.2	2.9	4.34
US	10.51	11.94	11.33	12.44	10	9.61
Brazil	13.52	12.89	13.48	11.32	11.7	12.72
Russia	2.51	-	-	-	4.9	2.67
India	17.87	-	-	-	10.4	8.53
China	12.37	10.51	-	13.72	16.2	16.43
G7 average	5.83	5.58	6.19	6.55	5.41	5.54

Source: Global Enterprise Monitor (2007)

Looking more closely at the UK, there are approximately 4.3 million enterprises in the UK, (DTI, 2007), with 72 percent of the businesses in the service sector, 17 per cent in the production industries and 8 per cent

in construction. The remaining firms were in education, social work and public administration. The Small Business Survey SBS (2005) notes that one of the prominent characteristics of SMEs in the UK is the numerical dominance of businesses that have no, or very few, employees. SBS (2005) reveals that 71 per cent had no employees at all, and 24 per cent had fewer than ten. The proportion of small firms without employees varies by sector with education containing the greatest proportion of enterprises with no employees (87.5%) and Hotels and Restaurants having the least (25.3%). Small enterprises and self-employed sole traders represent well over half of private sector jobs (58%) and make up 56% of UK turnover (£1,200bn). In contrast there are only 7000 firms employing more than 250 people, (DTI, 2007). The SBS survey also finds that in their sample 58 per cent of businesses had been operating for more than 10 years, 32 per cent for between four to ten years and 11 per cent less than four years.

At a regional level, 32 per cent of all UK enterprises are to be found in London and the South East. Both these regions have over 675,000 enterprises each. For each region and country in the UK, no more than 0.2 per cent of enterprises are large (250 or more employees), and at least 99.0 per cent of enterprises are small (0 to 49 employees). The proportions of enterprises that are medium-sized (50 to 249 employees) range from 0.5 per cent (in the East of England, South East and South West) to 0.8 per cent (in the North East and Northern Ireland). Part of the difference in employment patterns in SMEs between regions can be explained by differing industry compositions. London has 33 per cent of businesses in sectors J and K (Financial Intermediation and Business Services), the highest proportion of all regions, but less than 1 per cent of businesses in sectors A and B (Agriculture, Hunting, Forestry and Fishing), the lowest of all regions. Northern Ireland conversely has the lowest proportion of businesses in sectors J and K (14 per cent) and the highest proportion of businesses in sectors A and B (16 per cent). On average sectors J and K have higher proportions of their employment in large firms than sectors A and B. In fact in the Agricultural, fishing and forestry sector (AB) 93.8 per cent of employment was in small businesses with financial services having the smallest proportion of small businesses - 14.7 per cent, (National Statistics, 2006). These differences between the level of SME activity within the regions are of great interest to policy makers since they may be a reflection of the difficulty that women, older-aged people, young people, individuals in rural areas and different ethnic groups have in setting up small businesses.

It is also possible to measure the level of small firm activity at the county level as Table 3 indicates for Northamptonshire.

Table 3. The stock of small businesses registered for VAT in Northamptonshire

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
VAT registered Businesses	17915	17820	17885	18120	18560	19020	19615	20120	20560	20895	21260	21565	22035

Source: ONS

Table 3, above, indicates that since 1995 there has been a growth in VAT registered businesses in the county, mirroring the figures at the UK level. The figures however, do not provide an accurate picture of small firm activity in Northamptonshire because they relate only to those firms registered for VAT. Many smaller companies, particularly a large proportion of self-employed businesses will not be included since they lie below the VAT threshold level. However, some businesses do voluntarily register for VAT even though their turnover is below the threshold. Data for 2005 shows that around a fifth of all registrations have turnover below the VAT threshold (DTI, 2005)

Policy-makers may not only be interested in the level of entrepreneurial activity at the regional and national level but also the extent to which SMEs can be seen to grow and thrive and thereby add to the level of economy activity. One aspect of growth that has increasingly become the focus of policy makers is the extent to which SMEs are active in external markets.

5.2 Internationalisation of the small firm

Data from the DTI (DTI 2007) indicates that seventeen per cent of all businesses had some of their business activities outside of the UK and this figure rose to 22 per cent for those with employees. For those businesses that were not current exporters, only 2 per cent planned to start exporting in the next two years.

In the EU a large proportion of the SMEs do not export (Eurobarometer Survey, 2008). Less than one-in-ten export (around 8%) with the highest level of activity in Estonia, 23% and Slovenia 21%). Export activity was less likely in countries such as Spain 3% and France (6%). It might be argued that this type of cross-border activity might be related to the size of the EU country with the bigger the country the smaller the level of export activity by SMEs. However, this is not always the case since a low proportion of Cypriot SMEs – 3%, Bulgarian - 4%, and Maltese SMEs – 6% were involved in exporting. Nonetheless, if the size of the

domestic market is small, then it may not be big enough to support SME activity and some SMEs may be pushed into exporting.

Exporting by the EU's business units is also related to size, with larger organisations more likely to be involved in this activity. The Eurobarometer Survey (2008) also noted that export activity by EU SMEs was sector related. Exporting was more likely by SMEs in the transport/storage/communication sector and by those in manufacturing and less likely in for those SMEs involved in healthcare and hospitality. The great majority of export sales by EU SMEs was into other EU-27 markets, a feature confirmed in the studies of Northamptonshire's SMEs in the following papers, **Cook, M., Coskeran, T. and Weatherston, J. (2004) The Northamptonshire Export Survey, Northampton Business School, Northampton, UCN Publications pp. 1-40** and **Cook, M., Coskeran, T. and Weatherston, J. (2004) The success and constraining factors behind the internationalisation of Northamptonshire's businesses: lessons from the Northamptonshire Business Survey 1998 (Northampton: University College Northampton Publications) pp.1-50.**

Exporting, however, is only one measure of SME internationalisation; there are other forms such as importing from a foreign supplier, the development of foreign partnerships, foreign investments and cross-border clustering. Spigarelli (2003) argues that an international strategy solely based on exporting is a much weaker one than ones that include other forms of internationalisation. To what extent, therefore, are these various forms of internationalisation activities undertaken by SMEs?

ENSR (2003) indicates that 18% of SMEs were internationalised solely through the use of imports, with a further 12% undertaking both imports and export activities. A greater proportion of SMEs had import and export activities than were just exporters which suggest that being an importer is likely to improve the SMEs chances of being an exporter. The ENSR (2003) study also noted that although only 3% of SMEs in the EU had subsidiaries, branches or joint ventures abroad, this type of activity was growing at a faster rate than for large enterprises. Almost one third of the subsidiaries established by SMEs overseas had no exports and this implies that many SMEs were using their subsidiaries as a way to access cheap labour, technology and knowledge. SMEs were using subsidiaries, therefore, as a way of improving their competitiveness.

The localness of export markets is also feature of import markets for SMEs and a similar behavioural pattern can be seen for SMEs who have established subsidiaries or joint ventures. Furthermore, all these activities tend to be located in neighbouring countries or in the larger economies of the global community. As with export activity it is the smaller countries in the EU which are more likely to source imports from overseas markets (Eurobarometer Survey, 2008). This is more of a determining factor than the actual size of the firm.

Once again, the sectoral influence can be seen in the sourcing of imports, with the wholesale and retail trade (21%) and manufacturing (15%) having the highest proportion of importing compared with the hospitality sector which obtained only four percent of their inputs from abroad. This does not include labour for which the hospitality sector has a fairly large demand (Eurobarometer Survey, 2008).

With regard to FDI, the OECD (1997) found that approximately 10% of SMEs were engaged in this type of activity and in terms of quantity of FDI, SMEs accounted for around 10% of this.

5.3 Internationalisation of SMEs and competitiveness

The proportion of sales that are devoted to export markets is often regarded as a measure of the competitive performance of an economy (Buckley *et al.*, 1990) both at the regional and the national level (O'Farrell *et al.*, 1996). Furthermore, the EU (2008) has argued that internationalisation should not be just seen as increased involvement in overseas markets, but that the same drivers of internationalisation are those that affect innovation and the two – internationalisation and innovation - support one another and are key components of both competitiveness and growth. There is a strong relationship between the GDP per capita of a country and its exports of high value-added products. D'Souza and McDougall, (1989) go further by arguing that exporting is a necessary feature for the survival and growth of the small firm. Internationalisation is also considered by some SMEs as a prerequisite of business success and confining their activities to the domestic market disadvantages their businesses in terms of resources, labour costs, the size of their markets and their increasing risk of business failure (Knowles *et al.*, 2006; Bell *et al.*, 2004, Wilson, 2003). The Eurobarometer Survey (2008) concludes that it is not only the level of SME activity into the EU that is important but how the enhancement of SME internationalisation activity can be increased. To this extent government support at both the regional, national and EU level is important. SME internationalisation is subject to market failure and governments are seen as important catalysts of the internationalisation process, dealing with issues such as access to resources (both human and non-human) creating the conditions for an entrepreneurial environment to flourish and removing barriers to growth (see later in this thesis). But even without government help, many SMEs are increasingly active in overseas markets through being pulled into this activity. The OECD (1997) notes that there are few firms that are isolated from the impact of globalisation and even the 40% that appeared to not be affected by globalisation (mostly service based SMEs) are set to fall to 20% during the new millennium.

5.4 Definitional issues and SME internationalisation

Although Buckley (1989) has argued that SMEs face internal constraints to international growth due to scarce quantities of both financial and managerial resources, during the 1990's Oviatt and McDougall (1994, 1999) have shown that there has been a significant increase in the role of SMEs in international markets. Such activity can be expected to grow further as the world economy integrates further, coupled with declines in barriers to globalisation and with improvements in technology. The firm can now use its entrepreneurial competencies together with reduced barriers to trade and improved levels of technology to overcome other barriers to internationalisation (Wright and Etemad, 2001; Fillis, 2002). My chapter, **Cook, M. (2006) Small business and EU policy, In: J. Piggott and M. Cook (Eds.) *International business economics: a European perspective* 3rd edition (Basingstoke: Palgrave MacMillan) pp.346-371** provides an overview of the extent of SME activity within the EU, the main theories of SME internationalisation and EU policy towards SME development.

For many years the more traditional theories of international business, such as monopolistic advantage theory, product cycle theory and internalisation theory were not considered to be important explanations of SME internationalisation. SMEs were not credited with enough managerial expertise, resources and the financial means to internationalise. Moreover young firms were considered to be disadvantaged further because they lack experience and credibility that flows from a domestic track record, (McDougall *et al.* 1994). However, Miesenbock, (1988), Bonaccorsi, (1992), Calof (1994), Bell (1995), McAuley (1999) and Cummins *et al.* (2000) amongst others have indicated the growing international involvement of SMEs in overseas markets. SMEs may have a number of advantages over larger firms such as greater flexibility and operational speed, (Feigenbaum and Karnani, 1991); nonetheless, they face greater management risk and uncertainty. To this extent Manolova *et al.*, (2002) argue that internationalisation might spread the resources of a small firm too thinly or that internationalisation might present internal co-ordination problems.

Although the literature on export behaviour of small firms is extensive, there are a number of differences between the studies. For example, one difference arises in the way small exporters are defined. Beamish *et al.*, (1993) chose a cut-off point of \$25 million in sales or less to distinguish between small and medium sized exporting firms; Walters and Samiee (1991) define small exporting firms as those employing between 1 and 99 employees; Kaynak and Kothari (1984) define small export manufacturing firms as those employing 250 people or less; Reid (1984) in his Canadian study defines small exporting firms as those employing between 100 and 500 employees; and Rabino studied exporting firms with less than \$10 million in annual sales. Fillis (2001) has argued in his review of the literature that one of the difficulties facing researchers in considering SME internationalisation is this issue of what defines an SME. Much of the initial

work in the area originated from the US where both perceptual and actual definitions of an SME differ from those adopted in Europe (Cavusgil and Zou, 1994). This makes comparisons between studies problematic. Aside from the issues of defining SMEs in an international context, there is also no agreement as how to measure export performance. Several broad approaches have been advocated (Cavusgil and Zou, 1994; Madsen 1987; Schlegelmilch and Ross, 1987; Walters and Samiee, 1990). These include such things as export sales measured in absolute terms, as a percentage of overall sales and in terms of their growth. Bringing time into the framework, Kleinschmidt (1985) suggests a useful measure would be export intensity over a number of years. In addition he advocates other variables not necessarily correlated with export intensity might be appropriate, such as export success or profitability. Non-financial measure of export success have also been proffered, include the manager's belief that exports contribute to the organisation's overall profitability and reputation (Raven *et al.*, 1994), or the manager's satisfaction with the organisation's overall export performance (Evangelista, 1994). Denis (1990) has also suggested a more qualitative perspective for measuring success in foreign markets - the firm's international reputation. Composites scales of export performance have also been used reflecting a weighted combination of a variety of performance measures. Even though the most frequently cited measures are export sales, profits and composite sales, the lack of consistency between the measures of the dependent variable makes it hard to compare and contrast findings from the different studies (Zou and Stan, 1998). In addition, there have been major differences in the methodologies selected making direct comparison of the results difficult (Calof, 1993). Another difficulty is that some focus on particular sectors, others solely on manufacturing whilst further studies use both manufacturing and service sector firms in their samples (O'Farrell *et al.*, 1996, 1998, Masurel, 2001; Westhead *et al.*, 2001). Some studies use non-random samples which further makes comparison of results difficult (Autio *et al.*, 2000; Westhead *et al.*, 2001) and others have used poorly-developed levels of analysis, relying on univariate cross-tabulations. Further, less attention has been paid as to whether exporting firms perform better than non-exporting firms. Given the difficulties that arise in comparing empirical studies, to what extent has it been possible to develop a theory of SME internationalisation? Chapter 6 addresses this issue.

Chapter 6 The development of a theory of SME internationalisation

6.1 Setting the scene for SME internationalisation studies

The term internationalisation means different things to different people. It has been used to explain the outward movement in an individual firm's international operations (Johanson and Weidersheim-Paul, 1975; Piercy, 1981). However, Welch and Loustarinen (1988) and Johansson and Vahlne (1990) define it as the process of increasing involvement in international activities. Internationalisation combines the development of knowledge of foreign markets and the need to commit further resources to its development. This may include the involvement in importing from a foreign supplier, the development of partnerships, cross-border clustering and foreign investment, as noted in my paper **Cook, M (2006) Small Business and EU Policy, In International Business Economics: A European Perspective, 3rd edition, Edited by Piggott, J and Cook, M., Basingstoke, Palgrave MacMillan, pp. 346-371.** In fact Agndal and Axelson (2004) argue that although international sourcing has received some attention (Deng and Lawrence, 1995; Liang and Parkhe, 1997) such a measure of internationalisation has been less well researched. Johanson and Mattsson (1988) in their study define internationalisation as the manner in which organisations improve both their awareness of the direct and indirect influences of international transactions on their future, and ways in which SMEs develop and construct business transactions with other countries. An alternative definition has been put forward by Ahokangas (1998) who see internationalisation as the means by which resources are mobilised, accumulated and developed for international activities. Calof and Beamish (1995), on the other hand, include in their definition of internationalisation how the organisation adapts its operations to international environments. They also consider the withdrawal from international markets and therefore internationalisation can be viewed not always as a continuous forward progression.

The extant literature holds a relative negative perception of SMEs prospects in international markets (Cavusgil *et al.*, 1979; Cavusgil and Nevin, 1981; Malekzadeh and Nahavandhi, 1985; Cavusgil and Noar, 1987; Christensen *et al.*, 1987). Acs *et al.*, (1997) and Westhead *et al.*, (2002 and 2004) argue that it is only a small proportion of SMEs that are involved with international activities and this type of behaviour is no different within other countries (EIM, 2005). Wright *et al.*, (2007) also note that the size of the country of origin of the SME is also important, in that where domestic markets are small, then to achieve economies of scale requires access to markets overseas. The home economic environment, even without the desire for scale economies, may also impact upon export decisions (O'Farrell *et al.* 1998) In fact the challenges faced by small firms can be very large because they operate in the sectors which can be linked to lower growth rates and slower levels of innovation (Kirchoff, 1994). The SME source of advantage, if it has one, may well be the human capital of the own/founders/management team and these help to overcome the inadequacies of other resource stocks leading to a potential source of differentiated advantage for the SME that is

internationalising, (Brush and Chaganti, 1998; Chandler and Jansen, 1992). In this respect, the work by Joynt and Welch, (1985); Chetty and Hamilton, (1993); Ward, (1993); Kohn, (1997); Zou and Stan, (1998) and Lyndsay *et al.* (2003) provide support for the view that management is the principal force behind the development, growth and success of internationalisation. It has been further argued by Chandler and Hanks (1994) and Bell *et al.* (1998) that the performance of SMEs in international markets is not only related to the accessibility of resources but also to managerial competence and the networks in which the firm is engaged. A view that is supported by Fillis (2004).

As the literature has grown on SME internationalisation, Coombs and Sadrieh, (1997), McDougall and Oviatt (1999), Westhead (1995), and Karagozoglu and Lindell, (1998) argue that there is still insufficient information concerning the international process of small firms, the mechanisms adopted, the steps taken and the factors determining success. In particular studies have failed to distinguish between the needs of small and very small firms compared with larger SMEs, (Nassimbeni, 2001). Calof (1994), Cavusgil (1984b), and Reid (1982, 1983) argue that the use of age and size as measures of international involvement can be criticised and that more direct approaches such as knowledge of foreign markets, general management skill and international selling ability should be measured directly as a means of explaining internationalisation. Further, the determination of the factors behind the internationalisation of SMEs has been approached differently. Studies have often sought to answer different questions and this in itself can lead to conflicting results. It is possible, however, to categorise the study of the factors into four broad approaches: whether the studies consider exporting and non-exporting forms or only exporting firms; whether the studies consider pre-export behaviour and the triggers to exporting; whether the purpose of the studies is descriptive or explanatory; and whether external factors, internal factors, or both are being reflected upon. Given these different approaches there is considerable debate, therefore, as to what factors encourage independent small firms to export their goods and services abroad (McDougal and Oviatt, 1999). The comparison between studies is also made difficult because of differences in methodology relating to differences in definition, sampling and the mis-specification of empirical models (Calof (1993); Coviello and Jones, 2004). Furthermore sectoral studies and non-random samples make generalisations difficult (McDougal and Oviatt, 1996; Westhead *et al.* 2001; Westhead *et al.*, 2002). Nummela (2004) argues that even after thirty years of study there is still no universal theory of SME internationalisation. She argues that it is because researchers have sought to homogenise rather than to heterogenise this group of firms. The desire to incorporate multiple theoretical perspectives into SME internationalisation is a feature of more recent work (Jones and Coviello, 2005) and in particular the integration of the entrepreneur and the package of resources that this person brings.

SME internationalisation can be approached from a number of perspectives. One approach is that of internalisation theory, (Buckley and Casson, 1976), a second would be Dunning's (1977, 1981) eclectic theory and a third transaction costs analysis (Anderson and Gatignon, 1986). In the area of SME internationalisation this would not be the first time that theories developed to explain large firm or multinational enterprise have been utilised to explain small firm activity. This thesis however, concentrates on the specific theories developed for SMEs to explain their activity in external markets in particular the resource based or competency approaches to SME internationalisation. There are, nonetheless, a number of other theories that have been developed to explain SME internationalisation, including: stage theory, transaction cost theory, international entrepreneurship, born global theory, network theory, and it is important, firstly, to consider a number of these theories, to indicate the role that competency or resource-based theory plays in their development.

Out of these theories of SME internationalisation, one theory came to dominate the earlier analysis of SMEs during the 1970s and 1980s and this was process or stage theory (Leonidou and Katsikeas, 1996).

6.2 Stage Theory and the internationalisation of SMEs

Stage theory models developed by Bilkey and Tesar (1977), Cavusgil (1980), Johanson and Vahlne (1977) and Coviello and McAuley (1999) depict the process of internationalisation as an incremental learning process proceeding through a number of stages. Aaby and Slater (1989) in their extensive review of the literature and Andersen (1993) suggest that such models had become generally accepted as explanations of the internationalisation process of SMEs. Andersen (1993) distinguishes between the Uppsala internationalisation model and the innovation-related internationalisation model, though the two models are considered to be inter-related. The former focuses on the acquisition, integration, and use of knowledge about foreign markets, to make increasing commitments and allocation of resources to international activities. Through this process the organisation will begin to commit itself through small incremental steps, gradually building up experience of external markets. By using this approach, risks are reduced and in doing so a larger quantity of resources are committed to overseas markets that are more "psychically" distant (Bilkey and Tesar, 1977, Cavusgil, 1980; Czinkota, 1982). The process can be considered as evolutionary and cyclical: The firm's behaviour is influenced not by the deliberate development of strategy but more through developing internal conditions and making more understating of external conditions. Johanson and Vahlne (1990) suggest that this approach can explain both the stages through which firms become exporters and the decisions by firms (entrepreneurs) to choose successively more psychically distant markets. In the Uppsala model, foreign market commitment is comprised of two elements: the amount of resources committed and the degree of the commitment. The first can be considered in terms of the size of the

investment required, for example, the level of marketing, and firm and human resources that an SME devotes to the activity. The second refers to the complexity of identifying an alternative use for the resources and then the cost of transferring them to this alternative use (sunk costs), Ahokangas, (1998). The Uppsala model is based upon the behavioural theory of the firm (Aharoni, 1966; Cyert and March, 1963). Since internationalisation is based upon a gradual process it can also be seen to be grounded in the growth of the firm, Penrose (1959). Here as the firm begins to operate abroad it learns first hand about the process and gains knowledge. As international knowledge increases so uncertainty decreases and the organisation begins to commit more resources to the activity.

The second approach to stage theory is the innovation-related models. These models consider internationalisation as an innovation for the firm and the approach can be derived from the work by Rogers (1962) and Cavusgil (1980). Management learning is considered as important (Bilkey and Tesar, 1977). The slow nature of this learning process is related to management's aversion to risk taking and a lack of knowledge. Management now take the firm through a variety of stages starting with sales in the domestic market through to experimental involvement in overseas markets on to committed involvement. Because they are behaviourally focused to a large degree, these models treat individual learning and top managers as important aspects of the organisation's international behaviour (Andersson, 2000). The innovation related internationalisation model tends to focus on export behaviour only whilst the Uppsala model places a greater emphasis on the internationalisation process as a whole (Cavusgil, 1980).

However, stage theory as a plausible explanation of SME internationalisation has received increasing levels of criticism. Stage models have been criticised for being mono-directional, they do not take account of non-sequential behaviour, they have an inability to explain step jumps in internationalisation, they put too much emphasis on psychic distance, they understate the importance of social networks and also have difficulty in accounting for born-global firms (Hedlund and Kvarnland, 1993; Rennie, 1993; Oviatt and McDougall, 1994; Holmond and Kock, 1998; Chetty, 1999; Coviello and McAuley, 1999; and Autio et al., 2000). Leonidou and Katsikeas, (1996) in their review of the stage models also note that the number of stages within these models varies, ranging from three up to six. The deterministic nature of stage models is also considered a weakness (Reid, 1981). Once started on the path to internationalisation, individuals appear to have no strategic choices (Andersson, 2000). Ruzzier *et al.* (2006) consider the innovation stage models as lacking theoretical underpinning. In particular it is these models' inability to connect theory and practice that is an issue (Anderson, 1993). There is a lack of demarcation between the stages (Miesenbock, 1988; Andersen, 1993) and not enough attention has been given to the time of the different stages. Furthermore relating each stage to activities within the organisation can be subjective and in doing so the focus shifts away from a real understanding of the differences between the stages (Ahokangas, 1998). Moen and Servais

(2002) and Mugler, (1996) have further suggested that a number of SMEs engage in opportunistic, intermittent export activity. Stage theory needs also to be more dynamic. The time from establishment to the first foray into international markets may be shortening (Luostarinen and Gabrielsson, 2004). In fact the discussion may well have moved on from whether stage models can or cannot be supported to the consideration of a more holistic approach to internationalisation (Bell and Young, 1998; Madsen and Servais, 1997) where internationalisation is seen as being affected by multiple influences within a complex environment. Therefore as Havnes (1998) suggests although an incremental approach may be fine for some SMEs it is not for others, particularly where intermittent and irregular change is often required. Sullivan and Bauerschmidt (1990) suggested that although stage theory had been carefully developed it might be geographically focussed and not representative for SMEs outside of Scandinavia.

It was these difficulties with stage theory that led to Moen and Servais (2002) and Andersson and Wictor (2003) amongst others, to develop an alternative perspective on international SME behaviour, that of the born-global firm. These are firms that appear to internationalise almost from inception. As a way of retaining stage theory they argue that born globals might arise because the stages required to become an exporter are fore-shortened. However, they were unable to support this hypothesis. The concept of born global did appear, therefore, to question the validity of stage theory models of SME internationalisation. The debate still continues as to whether the process view of internationalisation and the born global view offer a more acceptable perspective for SME internationalisation.

6.3 Born global firms

There are many different definitions of the born global firm, but the most common approach is that they consist of small firms where a significant proportion of total sales are in international markets within a short space of time, (Gabrielsson and Kirpalani, 2004; Knight *et al.*, 2001, EIM, 2005). In fact the nomenclature of born globals includes work on global start-ups, high technology start-ups and international new ventures. It has been established earlier that, Andersson and Wictor (2003) are not persuaded that process or stage theory does not explain adequately the internationalisation of born globals. Spence (2003) suggests that born globals do not internationalise in a linear or systematic way as described in process models. This was a view that was supported by the work of Bell *et al.*, (2001), Moen *et al.*, (2002), Littunen (1997) and Saarenketo and Sundqvist (2002). Global evidence of the born global phenomenon can be seen in the studies by Roux, (1979) (France); Gurua and Ranchhod (1999) (UK); Norton, (1994), USA and Garnier (1982) Canada. In the context of management competencies, Gurau and Ranchhod (2006) and Mathews and Zander (2007) argue that the international experience of management teams also affects the both the internationalisation of born global firms and the foreign markets targeted. These competencies include such things as global vision,

how focussed the entrepreneur or the management team is on international markets, the capacity to see the relevance of technological opportunities and then use them, and the insight and understanding of the entrepreneur.

This is not to suggest that all is lost for stage theory. The process view of internationalisation has received some support from McDonald *et al.*, (2003), and Macnaughton (2003). Furthermore, Chetty and Campbell-Hunt (2004) in comparing firms that internationalise in a “traditional” way with born globals find many similarities between both types of firms, particularly in the psychic distance element of the process model. There have also been attempts to unify the two theories. Autio *et al.* (2000) argue that the born global perspective might be more useful in the earlier stages of internationalisation whilst the process related theory is more associated with the later. Bell *et al.*, (2001) argue that the process theory may apply more to some sectors or types of firms whilst the born global view may be more associated with others. Luostarinen and Gabrielson (2002) also suggest that if born globals are SMEs that exhibit exceptional behaviour then their success is generated from exceptional resources, capabilities and skills. These skills, particularly previous managerial and professional experience in international markets, may compensate for the firm's lack of organisational experience of dealing with international markets (Saarenketo, 2002). Further, they argue that in many cases born globals have non-existent or small domestic markets which suggest that these SMEs are forced into internationalisation.

Born global theory is not without its weaknesses, however. There are questions as to the length of the time period before the first international foray takes place. Chetty and Hunt (2004) define them as organisations that have internationalised within two years of inception, others argue for up to a six year period before internationalisation commences. McDougal *et al.* (1994) have an eight-year time frame. An alternative perspective is also to relate the time to a particular proportion of export sales. Knight and Cavusgil (1996) define born globals as SMEs that export more than 25% of total sales within three years of start-up. However, Reuber and Fischer (1997); Madsen and Servais (1997), Oviatt and McDougall (1994) and Andall and Fischer (2005) point out it is important to consider the managers' previous experience in born global firms. In other words one of the criticisms of international process models is the failure to look at the previous experience of managers and this appears to be the case with born global firms.

6.4 Born again global firms

Bell *et al.* (2003) have suggested that there is another type of firm to consider - born-again globals. These are firms that may not have internationalised but have been in existence for some time. Following some critical incident such as a change in management they quickly enter overseas markets and behave in the same way that born-globals do. Such a critical incident may be because of the availability of new human or

financial resources. These resources may lead to access to different networks. Once again a criticism of the extant literature on born again globals is the lack of a well-defined time frame for the born-global activity to occur after the critical incident. Fry and Freeman (2005) suggest that it should be two years after the incident, using the same definition as Chetty and Campbell-Hunt (2004) use for born globals.

Bell *et al.*, (2004) argue that the differences between the various theoretical and empirical studies of SME internationalisation may be better understood if we do not view internationalisation as being described by conflicting theories and ideas but in a much more holistic way. One approach may be to consider the resources and competencies of the entrepreneur and the firm and how these impact on the stages approach to internationalisation, the decision to become a born global or a born-again global.

Chapter 7 SME capability and competencies for internationalisation

7.1 Internal and external factor approaches to internationalisation

SME internationalisation may be influenced by the internal characteristics of the firm and the entrepreneur and also external forces on the organisation, (Olson and Weidersheim-Paul, 1978; Cavusgil and Nevin, 1981; Brooks and Rossen, 1982). Ford and Leonidou (1991) have classified these into three broad groups:

1. Decision-makers characteristics;
2. Firm-specific characteristics, and;
3. The firm's environmental characteristics

External factors and their influence on export performance have received extensive study (Diamantopoulos and Inglis, 1988, and Rao *et al.*, 1989). Nonetheless, Kirpalani and MacIntosh (1980) and Madsen (1989) argue that the relationship between environmental factors and export success is weak, especially when compared with internal factors. Secondly, external factors could be considered as a constraint, and the ability of SMEs to influence these is only small, (Philip, 1998; Ibeh, 2003). Nonetheless, industrial organisation theory argues that the external factors determine the organisation's strategy, which then influences economic performance (Scherer and Ross, 1990). It follows from this line of argument that the external factors and the organisation's export strategy are prime determinants of export performance.

The influence of internal factors, however, on exporting has received increasing attention (Aaby and Slater, 1989; Cavusgil and Nevin, 1981; and Donthu and Kim, 1993). Aaby and Slater (1989) categories these internal factors into one of three groups: firm competence – technology, market knowledge, planning, export policy, management control and communication; firm characteristics – firm size, management commitment and management attitudes to exporting; and export strategy – market selection, product and product line, pricing, promotion and distribution; They also include a limited number of external factors in determining export performance, but the emphasis is placed on the internal factors. Other authors have been more selective or specific as to the internal or external determining factors. For example, Garnier, (1982) and Rao *et al.*, (1989) considered external environment-related factors, organisation or firm-specific factors were looked at by Wiedersheim-Paul *et al.*, (1978) and Cavusgil and Nevin, (1981); and decision-maker factors were investigated by Simmonds and Smith, (1968) and Cavusgil and Nevin, (1981). The Aaby and Slater model with its concentration on the internal factors that influence SME internationalisation has nevertheless, been the subject of criticism by Bijmolt and Zwart (1994), firstly in the way the variables are categorised into the various factors and secondly in terms of the relationship between the three internal factors and export success.

So what has been advocated as the range of internal level factors that influence SME internationalisation? At the firm level, SME competitiveness and competencies have been suggested as important determinants of

firm internationalisation. Cavusgil and Zou (1994) found that a firm's international competence influences export performance whilst Jantunen *et al.*, (2005) also suggest that it is the internal capabilities of the firm that are important not only for born-global firms but also for other types of SMEs that operate in overseas markets.

The role of management/management competencies in internationalisation have also been identified in a number of studies (Brooks and Rosson, 1982; Cavusgil, 1984a; Miesenbock, 1988; Aaby and Slater, 1989; Leonidou and Katsikeas, 1996; Zou and Stan, 1998; Chetty, 1999; Apfelthaler, 2000; Fillis, 2001; Lloyd-Reason and Mughan, 2002; Gurau and Ranchhod, 2006 amongst others). Management is also responsible for the mode, direction and speed of internationalisation (Leonidou *et al.* 1998) and Reid (1981). Holmund and Koch (1998) and Andersson (2000) also consider that it is the decision maker who is the most important in the progression from domestic markets sales to sales overseas, whilst management networks, Coviello and Munro (1997) also influences the direction and pattern of overseas activity.

7.2 Management and Decision-maker's characteristics and internationalisation

Management or decision-maker characteristics and competencies have been linked with export performance and overseas activity (Brooks and Rosson, 1982; Lloyd-Reason and Mughan, 2002; Ibeh, 2003a; Kunda and Katz, 2003; Manolova and Manev, 2004). This view is supported and shared by some of the major work on export research (Miesenbock, 1988; Aaby and Slater, 1989; Chetty and Hamilton, 1993; and Zou and Stan, 1998). Seringhaus (1993) and Cavusgil and Zou (1994) argue that a firm's export competencies influence greatly the firm's capacity and ability to make use of information which can lead to export activity. In fact Seringhaus (1993) goes further by arguing that the greater information competencies exporting SMEs have, the better they perform. These competencies include such features as technology intensity (McGuinness and Little, 1981; Cavusgil and Nevin, 1981; Burton and Schlegelmilch, 1987); distribution, delivery and service quality, and channel relationships (Brooks and Rosson, 1982; Styles and Ambler, 1994); export cooperation and networking (Hansen *et al.*, 1994); and R&D (McGuinness and Little, 1981; Burton and Schlegelmilch, 1987). Although Storey (1994) strongly linked the resource base of the entrepreneur with firm performance, there is no clear consensus as to which of these characteristics/resources provides the greatest explanation between successful and unsuccessful internationalisation. Nonetheless for small firms the key variable will be the entrepreneur. Reid, (1981), Cavusgil, (1984a), Bloodgood *et al.* (1996) and Chetty (1999), argue that it is the decision maker's characteristics such as knowledge, attitudes and motivation that are critical in the move towards internationalisation. To this was added creativity and innovative thinking, the ability to see and act upon opportunities, network and relationship building (Carson *et al.*, 1995, Fillis and McAuley, 2000). Westhead *et al.*, (2001) argue that independent businesses with older entrepreneurs who have a

greater resource base, better networks and have good management knowledge are more likely to be exporters - (contrast this with the work of Dichtl *et al.*(1990) later). Internationalisation was also more likely in businesses where the entrepreneur had considerable industry knowledge and who have been involved in organisations that had exported before. Fillis (2000a and b) has also suggested that there is some congruence between entrepreneurial and marketing competencies such that the synergy permits some SMEs to get competitive advantages both in the domestic and foreign markets. This type of firm can then enter and expand international activity much faster than was previously thought possible.

Commitment to internationalisation and the expectation that internationalisation would have a significant impact on the growth of the firm were seen as important by Cavusgil and Nevin (1981), whilst Calof and Beamish (1995) considered that the attitudes of the entrepreneur were more important than any environmental factors. These attitudes were seen to be influenced by the past experiences of decision-makers, (Welch and Luostarinen, 1988). This was particularly the case in small firms, when the entrepreneur is seen to wield decision-making powers or where decisions belong in the hands of a few individuals (Reid, 1981). The skills of top managers were considered to be important determinants of exporting by Kaynak and Kuan (1993) and Koh (1991). In particular the international orientation and competencies of these individuals provide the background to the organisation's stance on trade with foreign partners and their ability to explore and develop overseas opportunities. Dichtl *et al.*, (1990) found that foreign market-orientation was less visible if entrepreneurs were older, less well educated and where the entrepreneur had lower levels of foreign language skills and if the entrepreneur considered they faced more barriers to exporting.

So what are these entrepreneurial characteristics/competencies that are so important to internationalisation?

The literature suggests that the decision-maker characteristics that have impacted upon internationalisation can be divided into objective characteristics (language skills, experience abroad etc.) and subjective factors (perceptions of risks, costs of internationalisation etc) (Morgan, 1997). Manolova and Manev (2004), however, place language proficiency in their category of uncontrollable factors along with other management characteristics. Whilst the training of managers in international business (Koh, 1986; De Luz, 1993; CILT, 2003) has been a prominent feature of increasing international trade, knowledge of foreign languages (Bilkey and Tesar, 1977) has been advocated as having positive impacts on exporting by SMEs through enhanced availability of market information, improved negotiation skills and extending the entrepreneur's knowledge of trade partners' business culture (Clarke, 1999). However, Knowles *et al.*, (2006) go further. They argue that languages are often treated separately in the literature and the lack of these is often considered as a major factor in the lack of success in internationalisation in the way that other characteristics are not. Let us examine the foreign language issue and SME internationalisation in more detail.

7.3 Entrepreneur Language competence and Internationalisation

Work by Schlegelmilch and Crook (1988), Lautanen, (2000), Turnbull and Welham, (1985), Usic and Czinkota (1989) and Williams and Chaston (2004) amongst others has investigated the link between linguistic ability and exporting. One view expressed by Clarke (1999) is that because the business world is dominated by the English Language then knowledge of a foreign language is not essential for international dealings. A fact confirmed in my paper, **MacDonald, S and Cook, M. (1998) An Exploration of the Use of Language Training in Exporting Firms: Case Studies from Northamptonshire, Local Economy, Vol. 13, No. 3, November, pp216-227**. In this paper a number of the interviewees noted that because many business people speak English there is little need to learn a foreign language. A number of empirical studies have questioned this view (Pearson, 1989; Swift, 1990, 1991; Enderwick and Akoorie 1994; Lloyd-Reason and Mughan, 2002; Knowles *et al.* 2006) as does my paper **MacDonald and Cook, 1998**. In fact the work by **Cook, M. and MacDonald, S. (1999) The role of languages in organisation internationalisation *Journal of European Business Education* 9(1) pp.49-61** investigating SMEs in Northamptonshire who had undertaken language training for their employees, confirmed that language difficulties acted as a barrier to exporting even for this more “enlightened group”. Foreign language knowledge, however, was considered as a relatively less important barrier to exporting compared with highly competitive markets or bureaucratic obstacles. Nonetheless, improved foreign language skills were also ranked highly as ways that organisations in Northamptonshire could improve their presence in export markets (**Cook, M., Coskeran, T. and Weatherston, J. (2004) *The Northamptonshire export survey Northampton Business School (Northampton: University College Northampton Publications) pp.1-40***) Language training has also been a fairly prominent element of government policy used as a stimulant for international trade (CILT, 2003; Clarke, 1999; Hagen, 1999; Morgan, 1997; Wright and Wright, 1994).

Although both the papers, **Cook, M. and MacDonald, S. (1999) The role of languages in organisation internationalisation *Journal of European Business Education* 9(1) pp.49-61** and **MacDonald, S and Cook, M. (1998) An Exploration of the Use of Language Training in Exporting Firms: Case Studies from Northamptonshire, Local Economy, Vol. 13, No. 3, November, pp216-227** considered the role and importance of foreign language for Northamptonshire’s exporting SMEs, the two papers extend the analysis into how Northamptonshire's SME's have responded to their foreign language difficulties. Organisations knew they needed foreign language training for a variety of reasons such as dealing with customers. They also realised that poor foreign language knowledge hampered negotiations, slowed down the translation of documents and realised that a better knowledge of languages would help them in dealing with joint venture partners. Nonetheless, their overall level of foreign language training was relatively weak and decision

makers were uncertain as to which levels of employee within the organisation, having received language training, would best benefit the organisation. For those SMEs in Northamptonshire that had undertaken language training a variety of training approaches to overcome their poor language knowledge had been used, these included: individual trainers, off-site and on-site courses, language tapes and sending people to countries to assimilate the language. As a more "quick fix" solution, Northamptonshire's SMEs argued that barriers to language could be overcome through their use of foreign nationals in the host country and in their employment of foreign language speakers. However, resource-based constraints dictated whether organisations undertook the training of their employees or sought to employ people with language skills. In the paper **MacDonald, S and Cook, M. (1998) An Exploration of the Use of Language Training in Exporting Firms: Case Studies from Northamptonshire, Local Economy, Vol. 13, No. 3, November, pp216-227**, organisations pointed to a range of resource constraints that impacted on their language training. These included: lack of financial resources, lack of time, lack of suitable courses, that staff once trained did not get enough foreign language practice and that the recruitment of staff with the appropriate language skills was not always possible. Furthermore organisations were often unaware that language training schemes were available. The result being that firms in Northampton were constrained over the long term by poor language training skills as evidenced in, **Cook, M. and Jones, J. (2002) Labour market information to support Wellingborough East masterplanning Matters of Fact Consultancy Report pp.1-90**.

The results from the empirical studies into foreign language ability and exporting are, therefore, unclear. Language skills may provide greater cultural sensitivity and enable some organisations to have a better grasp of market detail (Swift, 1991; Clarke, 1999). Furthermore, it may reduce the managers' perception of physical distance and aid the internationalisation process (Swift, 1991; Turnbull and Welham, 1985, Williams and Chaston, 2004). However, Knowles *et al.* (2006) argue that foreign language proficiency is only one of many factors that influence internationalisation. It should not be treated as a separate factor by itself but in combination with other factors that influence the level of internationalisation such as, decision-maker characteristics, intercultural competence and business experience. Nonetheless, successfully internationalised SMEs were more likely to have foreign language skills than less successful internationalised SMEs and at a higher level. Of greater interest is the fact that if SMEs had access to good levels of French it often meant that they were successfully internationalisers rather than just successful internationalisers in France. A single foreign language competence, therefore, can provide access to a wide variety of international markets.

7.4 Other management competencies and internationalisation

Managerial export competences within the literature have been referred to in a variety of ways such as: international competence (Belich and Duninsky, 1995), international marketing competences (Czinkota and

Ronkainen, 1994) and export skills and knowledge (Kedia and Chhokar, 1986). Empirical studies by Keng and Jiuan (1989), De Noble et al. (1989), and Cavusgil and Knight (1997) suggest that the most important competencies relate to business opportunities and market research, promotion of the business and products, selection of collaborators in international markets, pricing, sales force management, knowledge of business practices, awareness of competition, product R&D and adaptation. Lloyd-Reason and Mughan (2002) and Manolova and Manev (2004) argue that it is not only language skills but also values of the owner-manager in understanding culture as having positive effects on export performance. It is the acquired know-how formed by management from travelling abroad as well as emerging themselves in foreign cultures that exposes the entrepreneur to greater experiential knowledge of foreign markets and educates them about the level of competition (Moore, 1997; Doherty, 2000). Having access to individuals with experience of export markets was the third most important factor mentioned as to how Northamptonshire's organisations might achieve greater presence in overseas markets (**Cook, M., Coskeran, T. and Weatherston, J. (2004) *The Northamptonshire export survey* Northampton Business School (Northampton: University College Northampton Publications) pp.1-40**). The problem is that there is a lack of consensus as to which of the characteristics listed above makes the greatest impact on explaining the difference between successful and less-successful attempts to internationalise or even between international and non-international firms (Ibeh, 2000; Kamath *et al.* 1987; Aaby and Slater, 1989; Halikias and Panayotopoulou, 2003). Are the main entrepreneur competencies/characteristics the extent to which managers have been involved with foreign travel, the number of foreign languages spoken by management, the manager(s) amount and level of education abroad, whether they have lived there or worked abroad and hence these influences on access to wider networks, (Wiedershiem-Paul *et al.*, 1978; Bijmolt and Zwart, 1994; Reuber and Fischer, 1997; Leonidou *et al.*, 1998; White *et al.*, 1999; Obben and Magagula, 2003)? To this list Mathews and Zander (2007) have added the importance of international travel. They consider that the more internationally travelled and experienced the manager the greater the likelihood that they can shift away from the more traditionally “sticky” agglomerations of knowledge and economic activity to new ways of viewing markets. The balance of evidence, therefore, is that internationalised small firms were more likely to have had a decision maker who spent part of their life abroad (Aaby and Slater, 1989; Miesenbock, 1988; Reuber and Fisher, 1997). However, overseas market knowledge where it comes through having been born and educated overseas does not by itself provide the necessary conditions for the move into internationalisation, particularly for first generation immigrant entrepreneurs. The paper by **Cook, M., Ekwulugo, F. and Fallon, G (2003) *Start-up and Motivation Factors in UK African and Caribbean SMEs: An Exploratory Study*, paper presented at the 4th International Academy of African Business and Development Conference, Westminster Business School, London, pp 21-26**, suggested that overseas

knowledge and experience by themselves cannot overcome the greater finance, sector and other resource constraints faced by African and Caribbean businesses.

Although knowledge and experience of foreign markets may give advantages to the initial decision making and in the development of internationalisation once the initial foray is made (Aaby and Slater, 1989; Cavusgil and Zou, 1994; Madsen and Servias, 1997; Nakos *et al.*, 1998), international competence, that is cultural and country specific knowledge has been considered to be important also. Managerial experience, however, should not be confused with international outlook. It may well lead to the second, but that is not always the case (Bilkey, 1978; Da Rocha *et al.*, 1990; Reid, 1983; Welch and Wiedersham-Paul, 1980).

The managers' experience in exporting may also have an impact on whether the company becomes an exporter at all (Holzmuller and Kasper, 1991). Moini, (1995), Westhead, (1995), Ogbuehi and Longfellow, (1994), Da Rocha *et al.* (1990), Das, (1994) and Madsen, (1989) have argued that a positive relationship exists between the two, but in attempting to explain export intensity or export growth, international experience appears to have little effect (Cavusgil, 1984b). Therefore, as Williams and Chaston (2004) note, there appears to be some rank order in the manager's international knowledge/experience. International experience of living and working abroad are more important than foreign language knowledge, and these factors are more important than age, education and prior work experience on SME internationalisation (Leonidou *et al.*, 1998).

With regard to subjective characteristics such as the attitudes, perceptions and the personality of managers towards internationalisation, positive attitudes by managers or the management team have a positive influence on the internationalisation of the organisation. (Dicht *et al.*, 1983; Ali and Swiercz, 1991; Jaffe and Pasternak, 1994; Calof and Beamish, 1995; Leonidou *et al.*, 1998; Rundh, 2003). Personality also plays its part in decision to develop export activities (Halikias and Panayotopoulou, 2003). The managers willingness to take risks has also been positively linked to internationalisation (Williams, 1992; Vida *et al.*, 2000, Chetty and Campbell-Hunt, 2003). In fact Fillis (2001) goes as far as arguing that the drive and determination of the entrepreneur and their willingness to take risks can help overcome some of the resource deficiencies that can constrain international development.

However, Kamath *et al.*, (1987) and Aaby and Slater, (1989) suggest that much of the research into SME internationalisation shows that the findings have not been consistent as to which of the specific decision-maker characteristics that are important. Garnier (1982) also questions whether it is possible to ascertain statistical differences between managers of internationalised and non-internationalised firms particularly with respect to age and level of education. Furthermore separating out which factors have the greatest influence on internationalisation has proved difficult since the various dimensions of personal factors have often been combined or packaged with other internationalisation factors so that the impact of attitudes and

motivations (Birley and Westhead, 1992); international business competencies and skills (Chandler and Jansen, 1992); and demographic characteristics (Cooper, 1981) are somewhat cloudy.

Since either the owner manager or decision makers within an organisation may be key to the internationalisation decision this information gets stored with them. This suggests that when people move from one organisation to another or start-up another organisation then they carry this experience with them and this could explain the accelerated internationalisation of some SMEs where they leapfrog stages in the internationalisation process.

Export competencies (export experience and expertise) are also important in explaining the SME's ability to make use of critical information and information sources (Seringshaus, 1993; Cavusgil and Zou, 1994). Even where individuals had no prior external market experience, their general level of knowledge arising from the industries in which they operated can lead to a high a level of international awareness. In fact Seringshaus argues that, the better the export competencies within the SME the better the organisation performs. Getting the right intermediaries and understanding the competition abroad is an important competence for management (Julian and Ramangalahy, 2003). It is lack of managerial competence to develop and manage export sales, to get market knowledge, to undertake product promotion, to price their products competitively and to find customers that are the problems. The extent to which price competitiveness is a good explanation of export activity, however, is difficult to confirm. It is supported by the work of Kirpalani and MacIntosh (1980) but Hirsch (1971) was unable to establish a significant link. In **Cook *et al.*, (2004a)**, over 40% of exporters had charged the same price for their products in both domestic and export markets. However, where prices varied it was the competitive conditions above others in the two markets that was the main driving factor between any price differential. This might suggest that a number of Northamptonshire's exporting firms did not have the competence to fully understand the whole range of factors that could, and should, have influenced their pricing decisions.

Finally, internationalisation may follow a strategy path within the SME, but the poor resource base and the high cost of both financial and non-financial resources may lead to more opportunistic behaviour and therefore intermittent or ad hoc internationalisation by SMEs (Westhead *et al.*, 2002). This may be the case particularly for smaller SMEs (Nassimbeni, 2001) and was a feature of confirmed in **Cook, M., Coskeran, T. and Weatherston, J. (2004a) The Northamptonshire Export Survey, Northampton Business School, Northampton, UCN Publications, pp. 1-40.**

7.5 The entrepreneurial manager or the entrepreneurial management group?

The link between the owner-manager and the international orientation of the SME has been established by Lloyd-Reason and Mughan (2002), Morgan (1997), Boatler (1994) and Wiedersheim-Paul (1972). Whether

this international orientation is due to the owner manager or to the group of decision makers in the small firm is open to argument (Miesenbock, 1988; Oviatt and McDougall, 1994; Reid, 1981). McDougall *et al.* (1994) argue that SMEs that are international from inception are often founded by a team of individuals with international experience. Reuber and Fischer (1997) and Crick *et al.* (2006) argue that internationally experienced management teams can be viewed as a resource that influences SMEs to undertake behaviours that lead to a greater degree of internationalisation. Thus the dominant coalition within the organisation, rather than the CEO or owner manager alone, determines the pattern and level of internationalisation. This result was supported by the work of Bloodgood *et al.* (1996), Reuber and Fischer (1997) and Gurau and Ranchhod (2006). Furthermore, Smith *et al.* (1995) and Reuber and Fischer (1997) argue that the influence of decision-makers on internationalisation should be modelled not directly but indirectly. For example, the experience of the founder or the management team is likely to influence the behaviours of the SME and it is these behaviours which will proceed to influence performance.

7.6 Resources approach to internationalisation

Internal determinants of SME internationalisation are also warranted by resource-based theory, though Bagchi-Sen, (1999) and the OECD (2002) argue that many SMEs lack the key resources to be active participants in international markets. The paper by **Cook, M., Coskeran, T. and Weatherston, J. (2004) The success and constraining factors behind the internationalisation of Northamptonshire's businesses: lessons from the Northamptonshire Business Survey 1998 (Northampton: University College Northampton Publications) pp.1-50**, confirms this perspective indicating that exporters faced more difficulties in obtaining the quality of the labour force they considered appropriate to their needs compared with non-exporters. In fact the work by **Cook *et al.* (2004)** goes further to show that these resource difficulties had significant impacts on the output, quality and growth of exporters.

Resource-based theory considers organisations as being made up of a unique bundle of tangible and non-tangible resources (assets, capabilities, processes, managerial attributes, information and knowledge) that are under the control of the organisation and enable it to undertake strategies whose goal is to improve organisational efficiency and effectiveness, (Barney, 1991; Wernerfelt, 1984). Failure to have the appropriate resources in terms of skilled workers may stifle the growth of organisations and prevent the shift to overseas markets. This is one of the issues raised in **Cook, M. and Jones, J. (2002) Labour market information to support Wellingborough East masterplanning *Matters of Fact Consultancy Report* pp.1-90**. However, the failure to consider appropriate training for exporting as indicated in **Cook, M., Coskeran, T. and Weatherston, J. (2004) *The Northamptonshire export survey* Northampton Business School**

(Northampton: University College Northampton Publications) pp.1-40 could also add to long term resource problems.

Many entrepreneurs may not wish to internationalise either because they do not have the internal resources or, if they do, they do not wish to commit them to the export market. As Holmlund and Koch (1998) note, there is a need to recognise the implications of the resource needs and endowments of small firms for internationalisation. Tallman and Fladmoe-Lindquist (1994) argue that is not only resource availability that is important behind the move into international markets but also interest in capability development. The individual's decision to act upon a discovered opportunity depends on prior personal skills and knowledge and perceived support from social networks (Kreuger, 2000; Kreuger *et al.*, 2000). It is also possible that firms gain resources/knowledge in their domestic markets and this acts a trigger to internationalise (Wiedersheim-Paul *et al.*, 1978). Firms with resource stocks or capabilities that are valuable, inimitable, rare and non-substitutable have a competitive advantage over their competitors both in domestic and overseas markets, Barney (1991). Barney (1991, p1) describes these resources as "...all assets, capabilities, organisational processes, firm attributes, information, knowledge etc. A new venture's ability to enter overseas markets may be directly related to the accumulation of these tangible and intangible assets (Bloodgood *et al.*, (1996); Autio *et al.*, 2000) as is their ability to gain and defend advantageous positions with regard to these relevant resources (Conner, 1991). Leonidou (1995b) considers the role of intangible resources (Capabilities and competencies) as particularly important for small firms enabling them to overcome international barriers due to the lack of financial and human capital resources. These intangible resources are argued to include factors relating to the founder and top management (Johnson, 2004; Oviatt and McDougal, 1994), learning capabilities (Autio *et al.*, 2000), knowledge (Knight and Cavusgil, 2004) and networks (Oviatt and McDougal, 1994; Zahra, *et al.*, 2003). But what are the characteristics of these resources? Barney (1991) suggests that they must be valuable, rare, imperfectly imitable and not substitutable. However, Grant (1991) suggests that they must embody durability, transparency, transferability and replicability. Therefore the attributes of the resources could be seen as relatively broad and with a blurring of boundaries between them (Andersen and Kheam, 1998). Ahokangas (1998) sees these intangible and tangible resources as lying in one of four categories

1. Internal firm-orientated resources. These are the critical resources needed for internationalisation that the firm alone owns or tries to develop
2. External firm-orientated resources. These consist of co-operative activity with other organisations, such as universities and research institutions to further develop the internal resources of the firm.

Categories 3 and 4 are associated with internal and external networks.

The Internal network orientated resource approach involves co-operation with other organisations through alliances where both firms seek to further develop resources which jointly are to the benefit of both organisations. A feature that was apparent in the analysis of African and Caribbean SMEs in Northamptonshire in the paper by **Cook, M., Ekwulugo, F. and Fallon, G (2003) Start-up and Motivation Factors in UK African and Caribbean SMEs: An Exploratory Study, paper presented at the 4th International Academy of African Business and Development Conference, Westminster Business School, London, pp 21-26**, where suppliers provided the link to wider contacts and were invaluable sources of support and information for one of the businesses at least. These networks were also considered to be important for other SMEs in Northamptonshire as discussed in the next section.

Category 4 considers external networks of the firm from the perspective of sharing resources to sharing control over the firm's resources, such as through a merger or joint venture. To overcome some of their resource-scarce factors some small firms may enter export markets in co-operation with other organisations (Boter and Holmquist, 1996). Through their networks entrepreneurs can acquire strategically important external information over time (Morgan and Katsikeas, 1997), some are pulled into internationalisation through their partner firm obtaining an international contract (Hellman, 1996) others internationalise through unsolicited orders (Moen, 1999), whilst still others are pushed into exporting through a range of factors including highly competitive domestic markets (Moen, 1999). See also my paper, **Cook, M (2006) Small Business and EU Policy, In International Business Economics: A European Perspective, 3rd edition, Edited by Piggott, J and Cook, M., Basingstoke, Palgrave MacMillan, pp. 346-371**, for a discussion of the various push and pull factors behind SME internationalisation.

A more recent approach is to connect the resource based view and that of international entrepreneurship (Alvarez and Busenitz, 2001; Rangone, 1999). Entrepreneurs are seen as a source of sustained competitive advantage so that the resource shifts more towards the entrepreneur and away from the firm, (Foss *et al.* 1995). Schumpeter, (1950), Penrose, (1959), Alvarez and Busenitz, (2001), Barney *et al.* (2001) and Langlois (1995) argue that entrepreneurial knowledge, relationships, experience, training, skills, judgement and the coordination of resources are resources themselves and add value to the firm particularly if they are not easy to imitate. Thus entrepreneurs are aware of the chance to combine resources from different national markets because of their own competencies (knowledge, background and networks). The role of the entrepreneur is to assemble the competencies within the organisation to develop an international presence. Ruzzier *et al.* (2006) have further developed the model of Antonic and Hisrich (2000) to integrate the theory of SME's internationalisation process with international entrepreneurship. In doing so they have modified Antonic's and Hisrich's work by separating the founder's/manager's characteristics from the organisation's characteristics. They further divide the founder's/manager's characteristics into two parts: human and social

capital reflecting the importance and role of the founder's/manager's characteristics in the internationalisation process. The human capital characteristics include such things as:

International Business Skills;

International orientation;

Environmental perception;

Management know-how

Johanson and Mattsson (1993) in their characterisation of the internationalisation process also add to the network and incremental, gradualist models by including a third aspect of the internationalisation process, that of the business strategy-based theory of internationalisation. The firm is assumed to have some form of competitive advantage in its domestic markets and if this cannot be efficiently exploited without high levels of transaction costs, then firm seeks to internationalise as a way of exploiting this advantage.

Where sectoral clustering occurs in a regional locality, SMEs can also gain advantages by leveraging resources from the locality to overcome barriers to internationalisation (Taymaz and Kilicaslan, 2005). In other words SMEs may borrow resources such as marketing capabilities, technology and the like. There are therefore, ways in which the resource deficient SME can obtain their "missing" resources if they so wish. One approach that offers up an alternative explanation of how the leverage of resources can be used to help organisations gain access to external markets is through their use and development of networks.

Chapter 8 Network and firm based approaches to internationalisation

8.1 Network theory

An unsolicited order from an overseas customer (Bilkey and Tesar, 1977; Welch and Wiedersheim-Paul, 1980), or an invitation from a domestic customer to join in a venture overseas, will both involve less uncertainty, and indeed lower marketing costs, than cold-calling potential overseas customers and it is not at all surprising that the role networks play are often included in the studies of internationalisation of SMEs, Coviello and McAuley, (1999). In fact Carson *et al.*, (1995) and Dana and Wright (2003) suggests that an entrepreneur whose contact networks are internationally spread is more likely to be involved in international markets. Networks formed by the decision-maker can also be the catalyst for internationalisation (Merrilees *et al.*, 1998, Coviello and McAuley, 1999) but Johanson and Mattsson, (1988); Mckieran, (1992), Vatne, (1995); O'Farrell and Wood, (1998), Rundh, (2001); and Fillis, (2001) have argued that they can also provide a source of sustained competitive advantage in further developing an international presence. This idea has received support from Jackson (1981), Crick and Chaudhry (1995) and Zararullah *et al.*, (1998). In fact, Coviello and Munro (1995), Carson *et al.* (1995), and Shaw and Conway (2000) argue that network theory offers an important alternative explanation of SME internationalisation. The failure to take into account networks is one of the major weaknesses of stage theory, Westhead *et al.*, (2004). O'Farrell and Wood, (1998) go further and argue that external network resources are generally ignored in internationalisation. They argue that for smaller SMEs whose international development may suffer from resource constraints then internationalisation may depend upon the quality and the quantity of relationships they develop with others. Less experienced exporters also face the same problems as indicated in my paper, **Cook, M. (2002) Supporting the internationalisation of manufacturers: the need for a more tailored approach *Proceedings of the 5th SMESME International Conference 'Stimulating manufacturing excellence in small and medium enterprises, Ashcroft Business School, University of East Anglia, UK, May pp.270-277.*** The paper, **Cook, M., Ekwulugo, F. and Fallon, G (2003) Start-up and Motivation Factors in UK African and Caribbean SMEs: An Exploratory Study, paper presented at the 4th International Academy of African Business and Development Conference, Westminster Business School, London, pp 21-26** also provides evidence of the importance of networks both with suppliers and with support agencies for the African and Caribbean community within the Northamptonshire economy. Better links with organisations in foreign markets were also an important factor that would ease entry into, and reduce the barriers to, foreign markets, for Northamptonshire's SMEs in **Cook, M., Coskeran, T. and Weatherston, J. (2004) *The Northamptonshire export survey* Northampton Business School**

(Northampton: University College Northampton Publications) pp.1-40. In fact the survival, growth and international expansion of SMEs are strongly linked to the ability of the entrepreneur to use their personal and social networks (Coviello and Munro, 1997; Coviello and MacAuley, 1999; Ibeh, 2000). My paper, **Cook, M., Coskeran, T. and Weatherston, J. (2004) *The Northamptonshire export survey Northampton Business School (Northampton: University College Northampton Publications) pp.1-40***, also indicates that firms in Northamptonshire realised that networks were important and that some firms at least were eager to develop these. See also my paper, **Cook, M. (2006) *Small business and EU policy*, In: J. Piggott and M. Cook (Eds.) *International business economics: a European perspective 3rd edition (Basingstoke: Palgrave MacMillan) pp.346-371*** for a discussion of the importance of alliances.

These networks and alliances lead to small firms expanding and developing their social capital and this can provide resources to the individual SME, resources that could not have obtained independently. Further Coviello and Munroe (1995) argue that SMEs internationalise more quickly by linking themselves with established networks and in this way firms internationalise because other firms in their (inter)national network have done so. Networks also provide the smaller firm with the ability to tap into resources from larger organisations. They may appear to be borrowing size (Phelps *et al.*, 2001).

Network theory should not be considered in isolation from other theories. Johanson and Mattsson (1993) have developed a network approach somewhat similar to that of the stages approach to internationalisation with an emphasis on gradual learning and the development of market knowledge through the interaction within the network. Johanson and Mattsson (1993) identified four stages of internationalisation: the early starter, the late starter, the lonely international and the international amongst others. The emphasis of their model is that the firm that internationalises develops positions in relation to their contemporaries within a foreign network. SMEs begin by using the network to develop domestic markets, then internationalising, further market penetration is the third stage and then connecting with markets in a wide range of different countries in the final stage.

Within the network approach the management of international relationships is considered important (Blankenburg *et al.*, 1996). The management and knowledge of the network relationship, however, may be embedded in one person and this can have a substantial impact on internationalisation (Davidson and Honig, 2003; Hoang and Antoncic, 2003). Furthermore the inter-firm and interpersonal relationships can also influence foreign market selection (Andersen and Buvik, 2002); the time of internationalisation (Oviatt and McDougal, 1994); propensity to export (Westhead *et al.*, 2001) and the degree of internationalisation (Brush *et al.*, 2002). Ibeh (2000) argues that these can influence the strategic action behind internationalisation.

International networks are also more than the developing export relationships. Networks can be built up during the inward phase of internationalisation and some of these may be used subsequently to develop

outward activity, (Welch and Luostarinen, 1988). The work by Korhonen *et al.*, (1996) appears to confirm this, though Holmund and Kock (1996) failed to find any connection between outward and inward activity amongst Finnish SMEs. For one of the African and Caribbean SMEs in Northamptonshire their relationship with suppliers in the UK allowed the organisation to access important suppliers from overseas, (Cook, M., Ekwulugo, F. and Fallon, G (2003) **Start-up and Motivation Factors in UK African and Caribbean SMEs: An Exploratory Study**, paper presented at the 4th International Academy of African Business and Development Conference, Westminster Business School, London, pp 21-26). My paper Cook, M. (2006) **Small business and EU policy**, In: J. Piggott and M. Cook (Eds.) *International business economics: a European perspective* 3rd edition (Basingstoke: Palgrave MacMillan) pp.346-371, further confirms this relationship between importing and exporting.

Resources also play another part in the SME network arrangements. Firms that lack experience of internationalisation may not have the quality and quantity of resources that enable them to recognise potential partners and therefore their networks are smaller and weaker (Le Gales *et al.*, 2004). If they recognise this resource deficiency some SMEs may seek to appoint managerial talent which has that experience or develop links with external providers which can fill this gap (Holmund and Kock, 1998; Mughan *et al.*, 2004).

As well as having relevance for traditional firms, networks can be seen to be important for born-global firms as these firms seek to use their networks to gain quickly competitive advantage (Bell *et al.* 2003). However, Bell *et al.* 2003; Coviello and Martin, 1999) argue that although networks may be useful in setting-up international contacts and shaping an organisation's internationalisation, they may constrain the firm in its scope and the nature of the market opportunities available. Furthermore, some SMEs may want to remain independent and this fear of loss of control may lead to some reluctance by SMEs to enter into networks.

8.2 The sectoral approach to internationalisation

Much of the initial work into SME internationalisation focussed on engineering and manufacturing firms (Hunt *et al.* 1967), and my paper, Cook, M. (2002) **Supporting the internationalisation of manufacturers: the need for a more tailored approach** *Proceedings of the 5th SMESME International Conference* 'Stimulating manufacturing excellence in small and medium enterprises, Ashcroft Business School, University of East Anglia, UK, May pp.270-277, also takes this approach. However, there has been increasing evidence of interest in other sectors such as retailing (Burt, 1991; Muniz-Martinez, 1998), the service sector (Vandermerwe and Chadwick, 1989) and craft firms (Fillis, 2004). The method, rate and pace of internationalisation has been found to vary by sector (Crick *et al.*, 2006) and this work confirms the results established in my paper, Cook, M. (2000) **Training and Skill Needs for Successful Exporting: An**

Econometric Approach, Journal of European Business Education, Vol. 10. No. 1, December, pp. 33-47

where manufacturing SMEs were more likely to be export active and felt they had the greater capacity to export in the future compared with those firms in the service sector in Northamptonshire. Part of the sectoral differences in SME internationalisation can be ascribed, however, to the different characteristics of the management teams rather than the sector (Anderson, 1993; Oviatt and McDougal, 1994 1995, Coviello and McAuley, 1999,; Jones, 1999, Crick, 2004). Sector differences may also partly explain the particular approach that some SMEs take in entering international markets. Bell *et al.*'s (2004) study indicated that traditional manufacturing firms were more likely to follow a stages approach to internationalisation whilst technology based SMEs could be more associated with internationalising from inception.

8.3 Firm specific factors and exporting

Aaby and Slater (1989) have identified firm characteristics and competencies as providing an important part of SME internationalisation. They argue further that firm competencies are more important than firm characteristics. These would include technology, level of R&D, systematic market research (Cavusgil and Nevin, 1981), product attributes, delivery and networking. Furthermore, Caloghirou *et al.* (2004) has argued that it is firm specific factors that are more important than industry variables in explaining SME internationalisation. Firm size is one of these. It might be expected that firm size and exporting are positively related since the fixed costs of search, marketing and negotiation confer economies of scale. This positive relationship has been confirmed in a number of studies (Tookey, 1964; Hirsch, 1971; Cavusgil, 1976; Daniels and Goyburo, 1976; Bilkey and Tesar, 1977; Cavusgil *et al.*, 1979; McConnell, 1979; Kirpalani and MacIntosh, 1980; McGuinness and Little, 1981; Piercy, 1981; Schwarting and Wittstock, 1981; Reid, 1982; Ganier, 1982; Reid, 1983; Czinkota and Johnston, 1983; Cavusgil, 1984a and 1984b; Kaynak, 1985; Köglmayr and Müller, 1986; Seringhaus, 1986; Cavusgil and Naor, 1987; Keng and Juan, 1989; Westhead, 1994; Tyebjee, 1994; Caughey and Chetty, 1994; Reuber and Fischer, 1997; Moen, 1999, Hall and Tu, 2004). The positive relationship between exporting and size of SME was also confirmed in a number of studies of SMEs in Northamptonshire; see **Cook, M. (2000) Training and Skill Needs for Successful Exporting: An Econometric Approach, Journal of European Business Education, Vol. 10. No. 1, December, pp. 33-47, Cook *et al.*, (2003) and Cook *et al.*, (2004)**. However, categorising firms into the standard size groups that define an SME might hide more heterogeneous differences. It may be important to consider the size of the groups within each SME category in a more disaggregated fashion. Moen (1999) argues the case that larger small firms are more highly motivated to report export success than micro firms. He sees that as an indication of the greater amount of resources that are available to larger small firms. Bilkey and Tesar (1977), Bonacorsi (1992) and Katsikeas *et al.* (1997), however, found either no relationship

between firm size and exporting or only evidence of a weak link. Bilkey, (1978) also argues that although there may be evidence of a link between firm size and exporting, beyond some point, exporting would not appear to be correlated with size – a view which is supported by Withey (1980), Bonaccorsi, (1992) and Calof, (1994) amongst others. Though what this size factor is varies, depending upon the sector that is being investigated (Bell and Young, 1998) and the strategies involved in facing up to international challenges. It is also likely that the growth of the internet may reduce the impact of size on internationalisation (Ibeh, 2000), a feature that was more important for manufacturers with smaller export-to-sales ratios in Northamptonshire, as included in my paper, **(Cook, M. (2002) Supporting the internationalisation of manufacturers: the need for a more tailored approach *Proceedings of the 5th SMESME International Conference 'Stimulating manufacturing excellence in small and medium enterprises, Ashcroft Business School, University of East Anglia, UK, May pp.270-277***). This paper also distinguishes between manufactures with larger export-to-sales ratios from those with smaller export-to-sales ratios. The former face a significantly different range of problems in export markets from the latter. This raises issues of the type of public policy and support that is appropriate for the different organisations.

The age of the company has also been linked to the move to internationalise. This may be a proxy for firm size, but age played a significant part in the move to internationalisation for the SMEs in Northamptonshire as noted in the paper **Cook, M., Coskeran, T. and Weatherston, J. (2004) *The Northamptonshire export survey Northampton Business School (Northampton: University College Northampton Publications) pp1-40***.

Apart from the controversial issue of firm size and its influence on internationalisation, resource allocations (Cunningham and Spigel, 1971), the management of export operations (Pavord and Bogart, 1975; Cavusgil and Nevin, 1981, Ogram, 1982; Kaynak and Kothari, 1984), excess production capacity (Weidersheim-Paul *et al.*, 1978, Johnston and Czinkota, 1982; Kaynak and Kothari, 1984; Diamanthopoulos *et al.*, 1990), the firm's country of origin (Sernighaus, 1993), the industrial sector and export destination (Evirgen, Modur and Cavusgil, 1993) and diversity of export markets (Hart *et al.*, 1994) have all been posited as explanations of SME internationalisation. A further factor which has been argued as influencing outward internationalisation is the firm's history. This would include previous export experience (Garnier, 1982) and importing experience (Welch and Luostarinen, 1993).

Many of the factors listed above could have a two-way causality effect on internationalisation. For example, if the factor firm size is considered; firm size could be positively related to the decision to internationalisation, whilst at the same time internationalisation could influence firm size.

Even allowing for firm specific and entrepreneurial factors, some SMEs will still find it difficult to enter international markets because of barriers to internationalisation. These barriers might relate to the internal

features of the firm or the entrepreneur such as the lack of resources/competencies, but they can also be external to the organisation.

Chapter 9 Barriers to internationalisation

Failure to have the appropriate resources or competencies, both human and physical, can provide barriers to internationalisation and Leonidou (1995) has argued further that these export barriers should include those structural, operational, attitudinal and other constraints that prevent the organisation's initiation, sustainability and development into internationalisation. Morgan and Katsikeas (1997) have categorised these barriers to internationalisation as lying in one of four areas. Firstly an insufficient pool of resources can lead to strategic obstacles - a feature fairly prominent in the survey by **Cook, M. and Jones, J. (2002) Labour market information to support Wellingborough East Masterplanning, Matters of Fact Consultancy Report pp.1-90**, where the poor skills base and level of training not only constrained firms in this local market but also deflected other firms and more highly trained people to other regions/areas. Furthermore, the paper indicated that many low skilled people did not wish to take up any training and did not see the value of it, thereby continuing resource rationing in the region.

Secondly, an organisation's costs and lack of profit can lead to operational (and logistical) obstacles. Thirdly, there may be information obstacles through a limited range of international market knowledge (also see Miesenbock, 1988). Finally, the organisation may not be able to sustain the necessary interactions with key parties (process-based obstacles). Ramaswami and Yang (1990) suggest similar types of barriers to exporting: export knowledge; internal resource constraints; procedural barriers; and exogenous barriers. These external barriers were not considered to be as important as internal constraints as noted in my paper, **Cook (2004b)**. Though where they did exist, the level of demand in current markets, strength of competition and the difficulty in attracting highly skilled labour were seen to be the main external barriers. **Cook (2006)** also notes that the costs of internationalisation are a barrier; these include external market analysis, the translation of documents and the adaptation of products for external markets. Barriers also varied between whether the SME was importer only, an exporter only, or undertook both types of activity, as shown in my paper, **Cook, M. (2006) Small business and EU policy, In: J. Piggott and M. Cook (Eds.) International business economics: a European perspective 3rd edition (Basingstoke: Palgrave MacMillan) pp.346-371**. Suarez-Ortega (2003) argues that there is no common consensus as to the set of barriers to internationalisation and that export knowledge relates to the lack of information about export markets whilst internal resource constraints are the failure to possess particular resources that help to initiate and expand internationalisation. The internal barriers might include financial resources (Keng and Juan, 1989) the lack of personnel devoted to export activities (Rabino, 1980), and the lack of production capacity (Bauerschmidt *et al.*, 1985). It was the combination of internal labour constraints and financial constraints that were the

main factors holding back both exporters and non-exporters in Northamptonshire as shown in my paper, **Cook, M. (2000) Training and Skill Needs for Successful Exporting: An Econometric Approach, Journal of European Business Education, Vol. 10. No. 1, December, pp. 33-47.** In fact the paper argues further that for exporters in particular, the main barrier was with the lack of management capability. Resource constraints, such as the access to finance and suitably qualified staff were also concerns raised by the African and Caribbean firms in **Cook, M., Ekwulugo, F. and Fallon, G (2003) Start-up and Motivation Factors in UK African and Caribbean SMEs: An Exploratory Study, paper presented at the 4th International Academy of African Business and Development Conference, Westminster Business School, London, pp 21-26.** Even where financial constraints are not a major barrier before exporting commences they may well become increasingly important once exporting is underway (CEDEFOP, 2002)

The report by **Cook, M., Coskeran, T. and Weatherston, J. (2004) The Northamptonshire export survey Northampton Business School (Northampton: University College Northampton Publications) pp.1-40** also suggested that capacity constraints, fear of the unknown and greater need for personal business contacts were important barriers to exporting. Although not the most important constraint on the organisation, the need for language skills was a more important skills gap for exporters rather than non-exporters in the study by **Cook, M., Coskeran, T. and Weatherston, J. (2004) The success and constraining factors behind the internationalisation of Northamptonshire's businesses: lessons from the Northamptonshire Business Survey 1998 (Northampton: University College Northampton Publications) pp.1-50,** Of more concern in the same study was the greater management skills gap for exporters. This is not to say that SMEs in Northamptonshire had not responding to their training gaps. In fact a greater proportion of exporters in the study by **Cook et al. (2004b)** had used external training providers to fill their training needs than had non-exporters.

Barriers to internationalisation may also be external to the SME. These procedural barriers to internationalisation can have their origins in either the domestic or overseas market and according to Ramaswami and Yang (1990) can be divided into two types: controllable barriers that can be overcome with the correct experience and non-controllable barriers such as non-tariff barriers. Exogenous barriers are uncertainties that arise as a result of other players in the market, such as the behaviour of competitors, overseas governments, and political instability. In my paper, **Cook, M. (2002) Supporting the internationalisation of manufacturers: the need for a more tailored approach Proceedings of the 5th SMESME International Conference 'Stimulating manufacturing excellence in small and medium enterprises, Ashcroft Business School, University of East Anglia, UK, May pp.270-277,** evidence is provided to support this view and it adds further to the importance of external barriers by noting the

difficulty of trading in highly competitive markets both at home and overseas and the strength of the domestic currency as a deterrent to trade. In fact in their study of Northamptonshire's SMEs, **Cook, M., Coskeran, T. and Weatherston, J. (2004) *The Northamptonshire export survey* Northampton Business School (Northampton: University College Northampton Publications) pp.1-40** provide evidence that the strengthening of the exchange rate could result in active exporters leaving export markets completely.

Because internationalisation is often associated with increased risk this can impact on the behaviour of the SME owner who may be more averse to risk and uncertainty (Calof, 1994). The small firm's resources may be more limited and if a problem occurs they may not have the ability to cope. The fixed costs of internationalisation may also be higher for smaller firms. Failure of the foray into international markets may therefore, be more costly for the small firm (Buckley, 1989). If small firms follow a strategy of survival and independent ownership (Westhead, 1997) rather than risky strategies of higher potential growth in external markets, then they may undertake most, if not all, of their business activity in the domestic economy. If this is coupled with their lack of expertise and lack of resources, then domestic market sales take a priority. Not only are small firms resource constrained and micro firms even more so, but for micro firms their resource scarcity may not be able to be overcome so easily through investing and hiring people with the appropriate international experience (Westhead, *et al.* 2002). The paper by **Cook and Jones (2002)** argues further that internationally experienced personnel might not even exist in the local labour market and if they do they prefer to work in other more prosperous regions. Barriers faced by SMEs may also vary with the firm's level of export commitment, Suarez-Ortega (2003). SMEs, and in particular smaller firms, may again have their chances of success in international markets blighted quite significantly by government-imposed barriers such as tariffs (Bilkey and Tesar, 1977; Rabino, 1980).

For some entrepreneurs the barriers to exporting may only be discovered once internationalisation is underway (EIM, 2005), leading to an early exit from the activity or constraints on their general performance. A feature confirmed in my paper, **Cook, M. (2002) *Supporting the internationalisation of manufacturers: the need for a more tailored approach* Proceedings of the 5th SMESME International Conference 'Stimulating manufacturing excellence in small and medium enterprises, Ashcroft Business School, University of East Anglia, UK, May pp.270-277.** Some may re-enter export markets at a later date, others may not (Crick 2004). The paper by **Cook, M., Coskeran, T. and Weatherston, J. (2004a) *The Northamptonshire Export Survey*, Northampton Business School, Northampton, UCN Publications pp. 1-40,** indicates that only 10per cent of Northamptonshire non-exporting SMEs in the sample had been exporters before and they were unlikely to re-enter export markets in the short term. O'Farrell *et al.*, (1998) also suggests that international activity goes in stages rather than being continuous, as

some firms complete an international project then await a new one. In the interim they return to activity in the domestic market.

Export-related assistance may help small organisations overcome some of the barriers to internationalisation, since the owner managers of small firm may not have the resources, business skills or personnel to assemble and interpret appropriate international information (Culpan, 1989 and Westhead *et al.*, 2002). Crick and Czinkota (1995) have shown that exporting small firms are largely unaware of government programmes that had been developed to assist small firms in their export activity. Even where they know these programmes exist they may not take them up particularly if they have doubts as to whether the public sector agencies can make any real difference. This was a concern of Northamptonshire's SMEs indicated in my paper, **Cook, M. (2000) Training and Skill Needs for Successful Exporting: An Econometric Approach, Journal of European Business Education, Vol. 10. No. 1, December, pp. 33-47**, and further espoused in the contrasting means and level of support that was provided by UK Business Link when compared with its American contemporaries in **MacDonald, S. and Cook, M. (1997) Research Note: Letters from America: a lesson for Business Link *International Small Business Journal* 16(1) pp.74-79**. The failure to engage with government support agencies was also a feature for the African and Caribbean SMEs in Northamptonshire, **Cook, M., Ekwulugo, F. and Fallon, G (2003) Start-up and Motivation Factors in UK African and Caribbean SMEs: An Exploratory Study, paper presented at the 4th International Academy of African Business and Development Conference, Westminster Business School, London, pp 21-26**. This issue further received tentative support in **Cook, M., Coskeran, T. and Weatherston, J. (2004) *The Northamptonshire export survey* Northampton Business School (Northampton: University College Northampton Publications) pp.1-40** and in **Cook, M., Coskeran, T. and Weatherston, J. (2004) *The success and constraining factors behind the internationalisation of Northamptonshire's businesses: lessons from the Northamptonshire Business Survey 1998* (Northampton: University College Northampton Publications) pp.1-50**.

Cook *et al.*, (2004) also have shown that it is exporters that are likely to require a greater level of assistance if they are to remain export active. But to whom do exporters and non-exporters turn to for advice about external markets? In both the papers by **Cook *et al.* (2003, 2004)** knowledge of export advice providers was high but the take-up of information from them relatively low. Some of Northamptonshire's SMEs seemed wedded to using sources of advice that were appropriate for their domestic market activity but which could be deemed as less appropriate for overseas markets. In fact at the time the two surveys (**Cook *et al.*, 2003, 2004**) were undertaken there was the view that even where international information was available local public support agencies lagged behind in their knowledge of new and emerging markets.

Culpan, (1989) and Westhead *et al* , (2002) have also argued that small firms (irrespective of their size) with larger resource endowments, greater diversity in both management and industry know-how, better human resources practices and wider networks may be better positioned to deal with export barriers. Barriers may also be physical or perceived. If the latter, companies that perceive fewer risks and barriers associated with exporting usually have a positive attitude to internationalisation and this reflects in their export performance (Bilkey and Tesar, 1977; Czinkota and Tesar, 1982; and Donthu and Kim, 1993; Vida *et al.*, 2000; Williams, 1992). Where barriers exist and resources are limited, SMEs may be able to surmount these by operating in niche markets where they can concentrate their limited resources (Fillis, 2001).

The impact of technology and the internet may also have contributed to the reduction in export barriers that SMEs face, Hamill and Gregory (1997). Conversely it might be the lack of resource investment in technology that can constrain SME internationalisation, a feature noted in my paper **Cook, M. (2000) Training and Skill Needs for Successful Exporting: An Econometric Approach, Journal of European Business Education, Vol. 10. No. 1, December, pp. 33-47**

9.1 External conditions and internationalisation

External factors can provide the motivator for SME internationalisation, the so called push into internationalisation. SME involvement in international markets may come from impromptu business opportunities, or because the growth in domestic inventories may lead to sales in foreign markets. Both of these may be considered as "one-off" effects. Where the domestic market is in longer term decline or local demand sluggish, the owner-manager may become increasingly orientated to overseas markets. Toni and Nassimbeni (2001) note that for smaller firms at least, the move to internationalisation may rely more on serendipity than on strategic behaviour.

Industry instability (measured in terms of the rate of technology) has been seen to have a positive impact on internationalisation, (Zou and Stan, 1998). However, the link between export market attractiveness, the search for better business opportunities, the desire to share entrepreneurial risk through increasing the geographical spread of sales, the desire to leave a highly competitive domestic market, the decision to copy what other companies are doing and the firm's objective to gain economies of scale, have all received less support behind the move to internationalisation (Kaynak and Kuan, 1993; Moini, 1992; Madsen, 1989; Johnson and Czinkota, 1982). Even though many SME complain about the problems of domestic government red-tape in constraining their performance, it may be that foreign government regulations are as important in the constraining international activity (Pavord and Bogart, 1978; Bilkey and Tesar, 1977; Kaynak and Kothari, 1984). Such barriers did appear to act as a constraint on Europe's SMEs and one aspect of the Single European Act was to reduce these. My paper, **Cook, M. (2006) Small business and EU**

policy, In: J. Piggott and M. Cook (Eds.) *International business economics: a European perspective* 3rd edition (Basingstoke: Palgrave MacMillan) pp.346-371, suggests in some instances at least one set of government barriers had been reduced by the SEM, but these had been replaced by a new set of barriers.

Chapter 10 Contribution to Knowledge

10.1 Achievement of Research Aims

The five research aims that were set out in Chapter 1, Section 1.2, are discussed in terms of the research findings and the contribution these have made.

1. Gain a better understanding of the drivers of regional and national competitiveness and their underpinning by both FDI and the level of small firm activity.

The thesis makes use of a number of different methodological approaches to investigate the regional and firm level determinants of international competitiveness. Chapter 3 developed the concepts of regional and national competitiveness in relation to both entrepreneurial activity and Foreign Direct Investment (FDI). The opening three papers in this thesis have provided a better understanding of the drivers of FDI at the regional level, indicating the multi-faceted range of determinants. Moreover the papers included on FDI provide evidence that regional determinants of FDI differ between the regions and therefore there is a requirement for varying the regional policies to attract FDI. The remaining papers in this thesis consider SME activity and in particular the resource factors and competencies that lead to SMEs to internationalise. The papers provide a range of factors, at the firm, entrepreneur and external level that influence whether firms seek to internationalise This includes the papers, **Cook (2000)**, **Cook (2002)**, **Cook, Coskeran and Weatherston (2004a and 2004b)** and **Cook and MacDonald (1999)**. The papers **MacDonald and Cook (1997)**, **Cook and Jones (2002)** and **Cook, Ekwulugo and Fallon (2003)** approach entrepreneurship more so from a constraint perspective to the growth of the SME in the Northamptonshire economy concentrating specifically on the lack of resources faced by SMEs. These resources could be specific to the organisation such as a lack of appropriately skilled labour, **Cook and Jones (2002)**, to issues with external support, **MacDonald and Cook (1997)**, to financial and on to other resource constraints, **Cook, Ekwulugo and Fallon (2003)**.

2. Engage with, and develop, theories of foreign direct investment.

Chapter 4 has drawn together the major theories of FDI using the works of Dunning (1993b, 1998 and 2002), Cantwell and Mudambi (2005) and Manea and Pearce (2004) amongst others. The main drivers of can be isolated to market-seeking factors, efficiency-seeking factors, strategic asset-seeking factors and government influences on FDI.

Although Chapter 4 has analysed the theoretical determinants of FDI, the three papers, **Fallon, Cook and Billimoria (2003)**, **Fallon and Cook (2004)** and **Fallon, Jones and Cook (2004)**, starting from the theoretical perspective, develop a much better understanding of FDI at the regional level by developing a range of measures of the explanatory variables that can affect FDI at the regional level.

3. Examine the drivers of FDI in the UK regions.

Research aim 2 was concerned with the development of the theories of FDI, however, research aim 3 placed emphasis on examining and developing the regional drivers of FDI. The two papers, **Fallon, Cook and Billimoria (2003)**, and **Fallon and Cook (2004)**, using the theoretic models that have been developed by Dunning (1993b, 1998 and 2002), Cantwell and Mudambi (2005) and Manea and Pearce (2004) amongst others, provided a better understanding of the range of actual variables that can be used within the four broad categories of market-seeking, strategic asset-seeking, efficiency-seeking and government variables that underlie the attractiveness of regions. The two papers indicate the many and varied ways in which a single variable, say regional skills can be measured. The paper by **Fallon, Jones and Cook (2004)** widens the understanding of "regional variables" by examining the determinants of FDI to countries within a region (Eastern Europe)

4. Develop the main theories that determine SME internationalisation.

There are many and varied definitions of SME internationalisation. Chapter 6 discusses these in detail and the approach adopted in the papers included in this thesis is one of exporting as measure of internationalisation. The thesis, in Chapters 7 and 9, also explores and develops the main theories promulgated to explain SME internationalisation, such as stage theory, the theory of born-globals and born-again globals, network theory and sectoral and firm specific factors. In particular the papers **Cook, M (2002)** and **Cook, Ekwulugo and Fallon (2003)** show the importance of networking to internalisation, as do the two papers by **Cook, Coskeran and Weatherston (2004a and 2004b)**. The paper by **Cook (2002)** show important differences between manufacturing SMEs and non-manufacturing organisations, whilst that by **Cook (2000)** appears to confirm that size plays its part in successful SME internationalisation supporting the majority of studies which have used size as a determinant of SME export behaviour. The papers by **Cook (2002)** and **Cook, Coskeran and Weatherston (2004a and 2004b)**, also suggest SMEs with bigger export-to-sales ratios face different problems in export markets than do their small export-to-sales contemporaries and that the age of the firm may influence exporting behaviour.

5. Examine in detail both entrepreneurial and firm level competencies behind internationalisation and the barriers to internationalisation.

Chapters 7 focused on the entrepreneurial and firm level competencies behind internationalisation whilst Chapter 9 considers the lack of competencies as providing a barrier to internationalisation.

One specific entrepreneurial characteristic is examined in detail - that of language competence in the papers by **MacDonald and Cook (1998) and Cook and Macdonald (1999)**. Whilst there is a view that language training is important to internationalisation, muddling through was often a strategy utilised. The second paper **Cook and MacDonald (1999)** widens the discussion to the ways in which SMEs have responded to their language deficiencies and highlights the ways in which language training can be enhanced. The importance of foreign language was also evident in two further studies of SME internationalisation, **Cook and Jones (2002) and Cook, Coskeran and Weatherston (2004)**. A number of the papers in this thesis also recognise the impact of other management competencies on internationalisation such as export experience, (**Cook, Coskeran and Weatherston (2004a and 2004b)**), and this result contrasts with that provided in **Cook, Ekwulugo and Fallon (2003)**. Language competence and foreign market experience as just two of a number of entrepreneurial factors (both at an individual and management team level) that inhibit internationalisation as explored in **Cook, Coskeran and Weatherston (2004a and 2004b)**, **Cook and Jones (2002) and Cook, Ekwulugo and Fallon (2003)**.

The lack of skills in general, not just internationalisation skills, may also act as a barrier to attracting potential exporting SMEs into a region but also for existing SMEs to develop overseas. This is evidenced in **Cook and Jones (2002)**. Finance constraints also act as a barrier to internationalisation - see **Cook (2000) and Cook, Ekwulugo and Fallon (2003)**. However, external barriers are also important constraints on SME overseas activity as shown in **Cook (2002)** and the true level of these may only be discovered once export activity is underway. Barriers to exporting may be overcome through the collective activity of public and private support agencies, however, the papers by **Cook (2000), MacDonald and Cook (1997) and Cook, Coskeran and Weatherston (2004a and 2004b)** suggest that the take-up of advice and information can be very patchy.

10.2 Contribution to Knowledge

A number of taxonomies of FDI location have been developed such as those by Cantwell and Mudambi (2005), Dunning (1993b, 1998 and 2002) and Manea and Pearce (2004). However, although there has been a range of studies into the determinants of inbound Foreign Direct Investment (FDI) both at a developed and

developing country level there has been less research conducted into the determinants of regional FDI. In particular, there have been a limited number of studies that have examined the regional determinants of FDI in the UK. The papers, **Fallon, Cook and Billimoria (2003)**, and **Fallon and Cook (2004)** provide a much richer analysis and better understanding of the regional determinants of FDI. Moreover, **Fallon and Cook (2004)** develop the notion of regional determinants further by being one of the few papers that includes national as well as supranational variables as determinants of FDI.

The work on FDI has contributed to developing a better understanding of the regional determinants of FDI. In particular, the papers provide an insight in the varying importance of regional, national and supranational factors in determining FDI and the important differences between the mix of factors within regional FDI. Even though the same factor might influence FDI in different regions, the research within **Fallon, Cook and Billimoria (2003)**, and **Fallon and Cook (2004)** suggests that the actual variable used to measure this factor may differ. For example, if the level of education of the workforce was a significant explanatory variable in a number of regions, then its significance might be measured in a number of ways, such as, the number of individuals with 5 A-C GCSE's, the proportion of the regional population with NVQ level three or above, the number of graduates within the region. The two papers also provide a better understanding of the factors that can be varied at a regional level by the regional authorities. The outcomes that can be derived from these papers are that the drivers of FDI into the UK regions differ between regions. Regional policy-makers, therefore, cannot just follow the policies adopted by other regions to attract FDI but should adapt to their own need. Furthermore the papers argue that the extent to which the regional authorities can influence the factors that affect regional FDI may be limited. This may be due to their limited regional budgets, but mainly through the factors being more under the control of the national authorities.

The paper by Fallon, **Jones and Cook (2004)** takes a wider perspective to regional FDI analysis. The region is defined in a broader sense - Eastern Europe - and the flows of FDI into countries within this region are analysed. The results confirm, again, but now at the wider regional level, the differing factors that affect FDI into a number of Eastern European countries. Once again this suggests that the various Eastern European countries need to adopt different approaches to attracting FDI. Moreover, the results from this paper suggest that the Bevin and Estrin (2000) model may only be appropriate for countries that are in the first stage of marketisation. More advanced economies in Eastern Europe may need to possess attractiveness factors for FDI far closer to those of the Western European economies.

10.3 Contribution to SMEs knowledge

The papers on SMEs included in this thesis are grounded in the local market. There is the use of existing theories being tested within the context of a sub-regional economy - Northamptonshire. The papers provide for the first time, an-depth analysis of SME activity at the county level considering language competence, other skill competencies and resources both at the entrepreneurial and firm level. The research on SMEs at the county level has informed a number of developments by Northamptonshire Chamber and the Export Bureau of Business Link

This more localized approach to internationalization, resources and competencies is important as not knowing whether SMEs in Northamptonshire are the same or different to SMEs elsewhere in the UK has important consequences for local and regional policy.

The papers on foreign languages knowledge and use by Northamptonshire's SMEs, **MacDonald and Cook (1998) and Cook and Macdonald (1999)** add to the understanding of the importance of languages, language training, and language delivery to SMEs at a time when the internationalization of SMEs has taken more centre stage. The single paper on ethnic/Black SMEs (**Cook, Ekwulugo and Fallon, 2003**) also was important in highlighting this community's differences to other SMEs in the county. Furthermore, it raises a series of questions for these communities in a region which does not have a large ethnic population and suggests more local policy initiatives should be employed rather than relying on the larger or national ethnic initiatives that would be appropriate for areas with a greater proportion of ethnic communities such as London, Bradford or Leicester.

The paper by **Cook and Jones (2002)** provides evidence of the need to further disaggregate SME activity even further down from the county level to that of the borough or even ward level. Different counties and different sub-county areas often face different issues and therefore, county policy initiatives may not provide a one-size-fits-all policy for all areas of a county.

The paper by **Cook (2002)** also indicates the importance of disaggregating SME by sector. Manufacturing and non-manufacturing SMEs face different problems and difficulties in their search and utilisation of international markets

Although the paper by **Cook (2006)** develops the context and extent of internationalization, pulling together the main theories of SME internationalization, the main thrust of the arguments running through the papers on SMEs is that of resources and competencies. The papers by **MacDonald and Cook (1998) and Cook and Macdonald (1999)** highlight the lack of language competence by Northamptonshire's SMEs and provide ways by which this can be overcome. The papers by **Cook, Coskeran and Weatherston (2004a**

and 2004b) indicate the importance of resource factors in internationalisation, the critical issue of “size” behind exporting and the lack of support some SMEs perceived in developing their international presence. The paper by **Cook (2000)** concentrated more on the skill issues for successful exporting and highlighted the importance of support to overcome the barriers to internationalisation. The issue of resources constraints was evident in the paper by **Cook and Jones (2002)** in particular it indicated that the problems with skills and competencies were more acute in some areas of the county and this may lead to their failure to diversify into higher value-added activities.

Central to the papers in this second part of this thesis is an investigation of UK county level SMEs in Northamptonshire a hitherto under-research area. The different methodological approaches provide therefore, a rich picture of the intricacies of resources and competencies at both the firm level and county level.

Collectively the research work on FDI and SMEs has provided a fertile picture of the level of competencies and capabilities of regions and firms. It has identified the need to have local policies for local regions and also suggests that FDI might be driven by some factors that are different to those espoused by the development agencies. With regard to internationalising SMEs, the results of the work suggest a number of competencies that local firms are lacking in their attempt to internationalise or that they need to improve if they wish to increase their international presence.

The papers therefore, contribute to developing a greater understanding of the importance of firm and regional competencies in both sustaining and developing SME activity, developing the conditions for attracting FDI to a region and then contributing to regional and national competitiveness. They have also developed a better understanding of the factors that underlie FDI and SMEs (entrepreneurial) activity.

10.4 Implications for Policy makers

The research has raised as many questions as it has answered. The exact nature of what makes both nations and regions more competitive is not clear-cut. At a national level, competitiveness is often linked to productivity and therefore what improves productivity can be seen as improving competitiveness. FDI is one of the factors that can improve international, national and regional competitiveness, yet the results of the work developed here indicate that there is not "one size fits all" policy that can enhance all regions chances of attracting FDI. Regions are different as to their current competencies and resources and government and local agencies need, therefore, to stress different policies for different regions.

As for the resources and competencies of Northamptonshire's SMEs for internationalisation the results point to some underlying worries for the county, in that there are various forms of skill deficiencies both at managerial level and throughout the workforce of SMEs. These may well have been reduced since the time of the studies, and may not be generalised to other areas, nonetheless they paint a picture of a county which might struggle to leverage itself further up the competitiveness ladder. Perhaps this is a further indication of the parochialness of the county, but this needs to change if levels of competitiveness and higher value added external FDI is not to pass the county by.

10.5 Limitations of the research

By its very nature can context specific research be readily generalisable? To the extent to which findings relate to, and develop existing theory then clearly the work here has a more significant context. So in the case of the papers on FDI these seek to add to the existing theoretical literature. However, starting from the bigger picture, in Chapter 3 the drivers of UK and regional competitiveness were examined. This thesis has concentrated on only two, FDI and entrepreneurial activity, and for the latter the emphasis has been on the internationalisation of SMEs. Therefore, although the papers have developed a range of proposals as to how FDI and SMEs can be developed at the regional level, the other factors that can affect UK and regional competitiveness are outside the scope of this thesis. In examining the regional determinants of FDI and the factors that affect regional entrepreneurial activity a number of issues arise. In the case of the econometric models used to examine FDI, one potential weakness may lie in the dependent variable. FDI is measured here in terms of the number of project successes. This does not take into account the value of the project, the jobs created through FDI, or the jobs safe guarded by FDI. Furthermore neither is the type of FDI nor the skill levels of those employed through FDI examined. Leaving aside the issue of the period over which the data has been collected, the actual measurement of the variables included in the models is not all encompassing and a wider variety of national and supranational variables needs to be used. The papers on FDI make use of multi-variate least squares models, alternative econometric models need also be used and developed to test for the determining factors behind FDI. The FDI papers also make use of data on regional variables in the regional econometric models, it may be that the regional is still too large an entity and FDI could be better explained by looking at FDI at the county level. For example, in the West Midlands the rural counties of Shropshire and Hereford and Worcester may have different attractiveness factors for different types of FDI than those of Staffordshire, the West Midlands and Birmingham.

Although the papers presented here on FDI make use of up-to-date quantitative data, the papers analysing SMEs cover a wider number of years and to that extent the policies at a local and regional level may well have shifted.

In the papers discussing SME internationalisation the econometric studies in papers have the dependent variable measured by whether the SME is an exporter or not. Internationalisation of SMEs can be considered to be wider than this definition. The papers also take a rather positive perspective to SME internationalisation and an alternative approach might have been to consider firms that were once export active, or those that have never been exporters. Although sample sizes are adequate for much of the analysis of the econometric studies into SME internationalisation, moving from the county level to generalise to the region or national level may not be straight forward. This may be the case particularly for the study of African and Caribbean SMEs in Northamptonshire where sample sizes make generalisations more difficult. Finally, a number of the papers, such as **Cook, Coskeran and Weatherston (2004a and 2004b) and Cook and Jones (2002)** arose from specific commissioned work. The commissioning bodies drove the direction of the initial research and as such the research may not have been able to explore all the theoretical and practical issues facing SMEs in enough detail.

10.6 Future research progression

The two papers included in this thesis which considered the determinants of regional FDI began with an analysis of two regions **Fallon, Cook and Billimoria (2003)** before widening out the study to consider four regions **Fallon and Cook (2004)**. One starting point for future research is to increase the number of regions incorporating an increased number of inner-core, outer-core and peripheral regions. Increasing the number of explanatory variables would also provide much richer understanding of the regional drivers of FDI. In particular a greater use of national and supra-national variables should be made. It has already been noted in the previous section that different ways of measuring regional FDI activity (the dependent variable) should be included, such as, jobs created, value of FDI projects and jobs safeguarded. These changes should be undertaken alongside further developments in the statistical models used. To some extent the research is a one-sided dealing with the regional, national and supra-national factors that influence FDI inflows into regions. A more balanced approach could be to examine recent FDI that has come into a region from the MNE's perspective seeking information from the MNE itself as to what were the factors that initially attracted the MNE to the region. A further strand of research would also be to consider whether the attractiveness factors that caused MNE's to move to region are still there or whether other attractiveness factors now dominate the MNEs decision to stay in the region.

One of the reasons why regions/countries seek FDI is for the employment it brings. To what extent were the expected jobs actually created and how did they match the skill desirability levels of the region? The papers on FDI considered total FDI into a region or country, another area of research needs to consider the factors driving manufacturing and non-manufacturing FDI. To what extent are they different and to this extent are the factors that drive FDI from a regional perspective affected by the source country of the FDI? With regard to clustering are the factors that drive FDI in specific clusters the same as those that drive more "general" FDI? Finally, a longitudinal study of regional FDI needs to be undertaken to show how the impact of regional FDI links to actual changes in regional and national competitiveness.

As for the area of SMEs, further research is required to analyse SME resources and competencies - particularly in the area of local rather than regional or national markets, with the emphasis on whether it is possible to drive forward the "entrepreneurial region/area". Even if increased numbers of jobs or more small businesses are achieved, the linking of the types of jobs and output from the SME needs to be connected more closely with ways of improving regional competitiveness.

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