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13 De-Internationalization and the Small Firm

Romeo V. Turcan

INTRODUCTION

The last decade of the twentieth century has contributed most to the body of knowledge about the internationalization of small firms. During that period, the focus was primarily on the growth – or positive development – of international business operations (Benito and Welch, 1997). The problem with the growth of the firm, however, is simply that most firms do not experience growth (Penrose, 1959). This is particularly true not so much at the initial internationalization stage, when firms start exporting, but at the next stage of real international commitment, for example making an international investment (Yip *et al.*, 2000). In such situations, trying to manage the firm's portfolio proactively (Douglas and Craig, 1996), managers may decide to reduce international engagement or leave the foreign market completely (Pauwels and Matthyssens, 1999). To date, the research on the withdrawal of small firms from cross-border activities (totally or partially) is relatively scarce (Benito and Welch, 1997; Pauwels and Matthyssens, 1999; Matthyssens and Pauwels, 2000; Crick, 2002). This chapter aims to further the understanding of cross-border activities of small firms by exploring the nature of the de-internationalization processes in small firms. To do this, literature from several disciplinary areas will be brought together and a conceptual framework of small firms' withdrawal processes will be developed.

A PERSPECTIVE ON INTERNATIONALIZATION

Processes of Internationalization

Two theoretical approaches dominate contemporary research on the internationalization of small firms (for a comprehensive review see Coviello and McAuley, 1999). They are (1) the stage approach initiated by Cavusgil (1980), Johanson and Vahlne (1977), Johanson and Wiedersheim-Paul (1975), and (2) the network approach initiated by Johanson and Mattsson (1988, 1992), Johanson and Vahlne (1977).

Known also as the Uppsala model, the stage approach suggests that each stage of internationalization involves an increased commitment to international activities

and that the process of internationalization is the consequence of the acquisition of experiential knowledge, in particular market-specific knowledge. Commitment increases as firms learn more and therefore become less uncertain about foreign markets (Johanson and Vahlne, 1977; Cavusgil, 1984). However, the stage approach was widely criticized (for a comprehensive review see Andersen, 1993, 1997), and widely challenged in the literature (for example Sullivan and Bauerschmidt, 1990; Bell, 1995; Bell *et al.*, 2001; Jones 2001; Knight *et al.*, 2001). The major limitation of the stage approach is in its use of linear models to try to explain complex, dynamic, interactive and frequently non-linear behaviour (Bell, 1995). Also, it does not include cooperative modes of entry and does not permit mode changes involving decreasing foreign commitment (Andersen, 1997). In this respect, internationalization can be viewed as a barrier to de-internationalization (Benito and Welch, 1997).

At the same time, the network approach has received a lot of attention and recognition in the process of explaining the internationalization of small firms (recent examples include Anderson *et al.*, 1994; Coviello and Munro, 1995, 1997; Coviello, 1996; Elg and Johansson, 1996; Tikkanen, 1998; Coviello and Martin, 1999; Dennis, 2000). The network approach is based on theories of social exchange and resource dependency, and focuses on firm behaviour in the context of a network of interorganizational and interpersonal relationships (Axelsson and Easton, 1992). It has been suggested that success in new foreign market development is rooted in a firm's relationships in current markets, whether these be domestic or foreign, rather than in the identification and analysis of foreign market characteristics and the development of tailored market strategies (Johanson and Mattsson, 1988). Also, the network approach provides for reciprocity between inward and outward activities (Crick and Jones, 2000), and recognizes the importance of the networking role on inward international activities as part of the growing research on networks and internationalization (Johanson and Mattsson, 1988; Johanson and Vahlne, 1990). The firms' propensities to influence their exchange conditions and form new linkages while terminating others (Elg and Johansson, 1996) might explain the process of reduction of international involvement.

Patterns of Internationalization

However, the empirical literature on internationalization has tended to focus on the outward rather than inward patterns, while inward-outward patterns of internationalization have received limited coverage (Korhonen *et al.*, 1996). As a result a holistic approach towards internationalization of small (high-technology) firms has been called for (see for example Jones, 1999, 2001; Bell *et al.*, 2001; Fletcher, 2001), where both inward and outward patterns of internationalization are emphasized and described (recent examples include Welch and Luostarinen, 1993; Oviatt and McDougall, 1994; Bell, 1995; Korhonen *et al.*, 1996; Jones, 1999, 2001; Crick and Jones, 2000; Jones and Tagg, 2001).

The issue of inward–outward activities is crucial not only from an academic point of view, but also from a policy-making standpoint. As government organizations tend to encourage only outward operations (mainly exports that contribute positively to the balance of payments), and to some extent inward investment (which makes a positive contribution to the local economy and ultimately stimulates exports), many inward activities by foreign firms may be overlooked as internationalization opportunities for domestic enterprises. In their study, Korhonen *et al.* (1996) found that for a majority of Finnish SMEs the inward operations were their first internationalization stage, whereas the outward operations played a secondary role. Crick and Jones (2000) criticize the view of internationalization of small firms evident in the provision of trade assistance programmes and suggest that international expansion strategies other than pure exporting may better represent internationalization processes.

From the point of view of withdrawing from international activity, an understanding of inward–outward patterns of internationalization is pivotal as it allows the interrelation and integration of (such) decisions and (such) processes that identify a firm's individual pattern(s) of internationalization (Jones, 1999). In this context, the next section will bring together relevant strands of literature from several disciplinary areas in order to discuss and analyse the phenomenon of de-internationalization.

A PERSPECTIVE ON DE-INTERNATIONALIZATION

Why De-Internationalization?

To date, most of the literature on the internationalization of firms has focused on the growth – or positive development – of international business operations (Benito and Welch, 1997). The problem with the growth of the firm, however, is simply that most firms do not experience growth (Penrose, 1959). As argued earlier this is particularly true not only during initial internationalization, but also when there is real international commitment.

In an attempt to explain and understand how and why companies decrease their international involvement, it has been suggested that firms may experience 'epochs' of internationalization, followed by periods of consolidation or retrenchment, or they may be involved in particular 'episodes' that lead to rapid international expansion or de-internationalization (Kutschker *et al.*, 1997; Jones, 1999, 2001). Also the existence of different internationalization 'pathways', 'trajectories' and non linear 'patterns' and 'profiles' has been acknowledged and explored (Jones, 1999, 2001; Bell *et al.*, 2001; Jones and Tagg, 2001; Knight *et al.*, 2001). However, to date the research on the reduction of internationalization engagement is far less common (Benito and Welch, 1997; Pauwels and Matthyssens, 1999; Matthyssens and Pauwels, 2000; Crick, 2002), probably due to the seemingly negative and undesirable features associated with these

phenomena (Benito and Welch, 1997) – for example human nature having a tendency to suppress admission of failure (Clarke and Gall, 1987), or difficulty in getting longitudinal data (Benito, 1997). Also, the managers' decisions to either reduce the international engagement or leave the foreign market completely should not, *a priori*, be viewed as a failure (Pauwels and Matthyssens, 1999; Crick, 2002). For example, this issue becomes important when determining the trade support that might be required by managers (Crick, 2002), as trade support can be used to encourage withdrawal from foreign operations which may then allow the firm to maximize domestic market opportunities. Thus, investigating the underlying drivers of why and how small firms might reduce or even withdraw from their international engagement may lead to a better understanding of a more holistic internationalization process of the small firm (Pauwels and Matthyssens, 1999).

How De-Internationalization is Defined

Welch and Luostarinen (1988, p. 37) introduced the term 'de-internationalization' arguing that 'once a firm has embarked on the process [of internationalization], there is no inevitability about its continuance'. Benito and Welch (1997) who made one of the first attempts to define de-internationalization, defined the concept as '. . . any voluntary or forced actions that *reduce* a company's *engagement in* or *exposure to* current cross-border activities' (emphasis added, p. 9). They also recognized the importance of differentiating between partial and full de-internationalization. The three constructs emphasized above require further investigation in order to improve the definition of de-internationalization. For example, when a company changes the foreign market servicing mode from investment to franchising (see Alexander and Quinn, 2002), partial de-internationalization, the company's *engagement in* and *exposure to* cross-border activities might still *increase* (see Hadjikhani, 1997). Thus, it might be argued (see also Kutschker *et al.*, 1997) that despite decreasing the level of internationalization, as represented by type of entry mode, the overall growth of the firm will be towards an increased level of cross-border activity.

However, the above definition of de-internationalization acknowledges that the cross-border activities of a firm can be (and must be) investigated holistically by understanding the hows and whys of both (inward–outward) internationalization and (inward–outward) de-internationalization decisions and processes. Thus, the process of cross-border activity of the firm can be defined as a cause – effect relationship between internationalization and de-internationalization, whereby a firm can not de-internationalize (the effect) without having internationalized (cause). If this statement is true, the cross-border activity paradigm (see Figure 13.1) evolves, whereby the firm de-internationalizes in the same way as it has internationalized by demonstrating the same but reverse behaviour.[1]

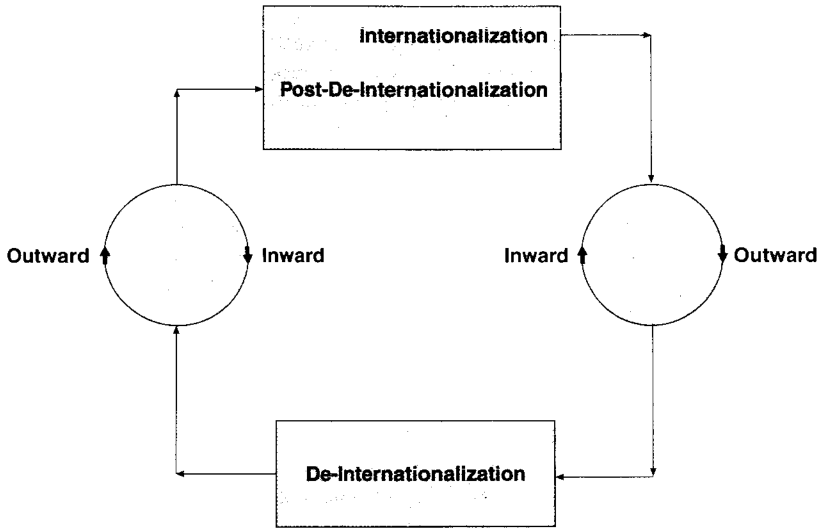

Figure 13.1 A model of cross-border activity

How De-Internationalization is Conceptualized

Despite the recent attempts to develop a holistic approach towards internationalization (for example Jones, 1999, 2001; Bell *et al.*, 2001; Fletcher, 2001), the concept of de-internationalization has not been fully developed and integrated within the cross-border literature. Benito and Welch (1997) undertook the first step towards developing a conceptual framework of the de-internationalization process and suggested that the probability of withdrawal from international operations declines as the commitment to these operations increases. They argued that de-internationalization, like advanced internationalization, should be seen as part of the broader perspective of the overall [cross-border] strategy of a firm. However, they also concluded that 'it takes us a limited distance in terms of providing an appropriate conceptual setting for de-internationalization moves and in seeking to explain them' (p. 19), and opted for further research that would follow de-internationalization moves by a number of firms through an extended period of time, and internationalization stages in order to clarify the circumstances and influences on decisions to withdraw.

Another area of research that has been concerned with withdrawal from foreign operations is the literature on divestment, and, to a lesser extent, on export withdrawal. The conceptual framework that emerged from the divestment research (for a review see Chow and Hamilton, 1993) has been based primarily on two streams of literature, one from economics (Buckley and Casson, 1976; Dunning, 1980; Williamson, 1985) that focuses on asset specificity (see Porter, 1976) as a barrier to exit (Nargundkar *et al.*, 1996; Karakaya, 2000), and the second from strategic management that approaches divestment from the product life-cycle perspective (Harrigan, 1980; Harrigan and Porter, 1983) and the product portfolio perspective (Porter, 1987) with the main theme being strategic change and strategic fit (Kelly and Amburgey, 1991; Zajac *et al.*, 2000). In an attempt to understand the determinants of de-investment (for example Haynes *et al.*, 2000), it was found that divestment was systematically related to leverage, corporate governance, strategy and – to a limited extent – market structure characteristics.

However, despite the fact that de-investment has been viewed as the end result of strategic decisions regarding: (1) reallocation or concentration of productive resources at a national, regional or global level; (2) change of foreign market servicing mode, for example from local production to export; or (3) complete withdrawal from a host country (Benito, 1997), and that there is a large amount of empirical research on de-investment (for example Hoskisson *et al.*, 1994; Chang and Singh, 1999; Haynes *et al.*, 2000; Mata and Portugal, 2000; Shin, 2000; Tegarden *et al.*, 2000), the focus of the research has been on product and business exits rather than on exits from international markets (Matthyssens and Pauwels, 2000). This makes it difficult, or impossible, to make any inferences about how and why a (small) firm might change its foreign market serving mode.

Recent exploratory studies (Wheeler *et al.*, 1996; Pauwels and Matthyssens, 1999; Matthyssens and Pauwels, 2000; Alexander and Quinn, 2002) try to minimize this problem by employing inductive qualitative research. For example, in a cross-case analysis, Alexander and Quinn (2002) focused on decisions, processes, effects and response phases of the divestment process in the retail industry. They found that divestment had an impact on subsequent market-entry mode; that is, initially the firms established subsidiaries through a high-control mode of entry, then they switched to partnerships, concessions and franchising as the favoured entry mode. Wheeler *et al.* (1996) studied the structural dynamics in the distribution of foreign-produced machine tools in the UK, and suggested, *inter alia*, cyclical influences on intermediary choice in importing whereby a firm may switch, say, from sales subsidiary to independent agent/distributor. Although Matthyssens and Pauwels (2000) and Pauwels and Matthyssens (1999) did not focus on switching between entry modes, they performed a retrospective strategy process study of export withdrawals, focusing primarily on cognitive and behavioural processes in the decision-making and implementation processes. In their attempt to build middle-range theories, three processes were uncovered: (a) escalation of commitment; (b) creation of strategic flexibility; and (c) confrontation between processes (a) and (b). To the above, Crick (2002), in his research on the withdrawal of small firms from exporting, indirectly proposed a comprehensive list of reasons for discontinuing export activities.

As can be seen from the above review, a theoretical understanding of the process of de-internationalization, especially within small firms, is in its infancy. The question arises how to apply the existing research to the study of the de-internationalization process in small firms. The next section discusses this issue and presents a conceptual model of de-internationalization in small firms.

DE-INTERNATIONALIZATION OF THE SMALL FIRM: A CONCEPTUAL MODEL

De-Internationalization: Emerging Themes

While the research to date on de-internationalization has focused on large corporations, some issues might form the core constructs of research on de-internationalization of the small firm. These constructs are (1) commitment, (2) strategic change, and (3) time (see Figure 13.2).

Commitment
When conditions deteriorate, decision-makers may be faced with a dilemma over whether to risk continuing or withdraw (Drummond, 1995). In such circumstances, decision-makers may compound the problem by continuing to act irrationally (Staw and Ross, 1987; Brockner, 1992). Brockner (1992) defined the tendency for decision-makers to persist with the failing courses of action as escalating commitment, where a decision to persevere might only escalate the risks. It is argued that several factors encourage decision-makers to become locked into failing courses of action (Staw and Ross, 1987). These are psychological, social, structural and project-related (for a review see Brockner, 1992; Drummond,

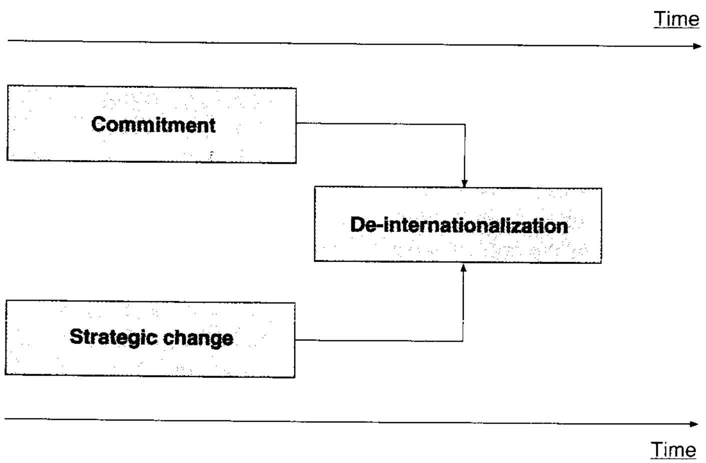

Figure 13.2 Small firms' context of de-internationalization

1994). Based on these factors, Bowen (1987) developed a model that suggests that withdrawal is more likely to occur in conditions opposite to those believed to favour persistence, that is low commitment and low equivocal information. Drummond (1995) corroborated Bowen's model and extended it by arguing that the escalation is a function of commitment and power with information as an important component of power.

From the perspective of the small firm, it is the founding entrepreneur that makes a unique contribution to the firm's development (Hill and Wright, 2001), and it is entrepreneurial commitment, determination, vision, energy, tolerance of risk and ambition that makes the entrepreneurial process happen in these firms (Hill and McGowan, 1999). Hence, according to Drummond's model (1995), the entrepreneur would be viewed as being highly committed and having high perceived power, thus making the withdrawal less possible. Therefore, there will be a challenge for researchers to study both tacit and explicit entrepreneurs' decisions to de-internationalize in order to identify and estimate the salience of the factors which finally prompt withdrawal (Drummond, 1995). The most difficult task, however, is how to operationalize and measure the commitment in a dynamic way – a task that remains a challenge (Pauwels and Matthyssens, 1999). In addition, there will be a need to define and operationalize the perceived failing course of action[2] and to account for cognitive bias in investigating the de-internationalization decision process (Watson and Everett, 1993, 1999; Das and Teng, 1999).

Strategic Change
Planning for adversity is well worth the effort (Porter, 1976), so decision-making processes not only need to allow for the possibility of failure, but also need to facilitate withdrawal where appropriate (for example Drummond, 1995; Crick, 2002). However, strategic changes like divestiture, diversification and replacement of the manager available to large corporations (Porter, 1976; Harrigan and Porter, 1983; Staw and Ross, 1987; Brockner, 1992; Hoskisson *et al.*, 1994; Nargundkar *et al.*, 1996; Benito, 1997; Benito and Welch, 1997; Pauwels and Matthyssens, 1999; Haynes *et al.*, 2000; Mata and Portugal, 2000) are not generally available to small firms.

Alternatively, decisions to de-internationalize might be viewed in the context of change in the business networks, especially in the dyadic networks (for example Anderson *et al.*, 1994; Halinen *et al.*, 1999). For example, Halinen *et al.* (1999) emphasized the central role of business-relationship dyads for understanding the mechanism of network change and for the purpose of understanding dyadic network dynamics, introduced the term 'critical event' as an incident that triggers radical change in a business dyad and/or network. According to them, the start of a radical change depends on the actions and intentions of dyadic partners. Thus there will be a need to develop a longitudinal approach in order to understand fully and anticipate the change in the dyadic network (see for example Welch and Welch, 1996) – that is, actions and intentions that will help understand the de-internationalization process of small firms.

Time

Although all phenomena exist in and through time, researchers often ignore, treat implicitly, or treat explicitly but in an inadequate manner the duration and rates of time (George and Jones, 2000). Further, George and Jones (2000) argue that time can and should play a much more important and significant role in theory and theory-building because time directly impacts the what, how and why elements of a theory (see also Welge and Holtbrugge, 1999; Hurmerinta-Peltomaki, 2001; Jones and Coviello, 2002). Thus, it is time that makes it possible to consider four phenomena which are of crucial importance to internationalization and de-internationalization strategies: timing, duration, chronological sequence and velocity of different cross-border moves (Kutschker and Baurle, 1997).

Hence, fundamental to the entrepreneurs' experience of time in the present is the knowledge he/she has of the past and how he/she uses this knowledge to envision the future (Butler, 1995); that is, how the present is determined depends roughly on entrepreneurs' subjective perceptions and experiences, even if there is objectivity[3] behind it (for example Chapman, 1982), paying special attention to decision-makers' personal and social idiosyncrasies (Macharzina and Engelhard, 1991) in order to get insights into how and why small firms (see Scott and Rosa, 1996) might de-internationalize. Accordingly, attention must be paid to the way a phenomenon is created subjectively out of a person's ongoing experience, and constructs must be defined so as to reflect the dimension of time (George and Jones, 2000) – that is, (1) codes and memories; (2) congruence and horizons; and (3) present experience (Butler, 1995).

De-Internationalization: A Conceptual Framework

As the above discussion suggests, the conceptual framework of de-internationalization process research (see Figure 13.3) is based on three constructs (1) the commitment of *entrepreneurs* which is influenced by project, psychological, social and structural factors; (2) change in dyadic networks, that is triggered by a critical event, and depends on the actions and intentions of dyadic partners (*entrepreneurs*); and (3) time, that is experienced in the present by *entrepreneurs* by relating

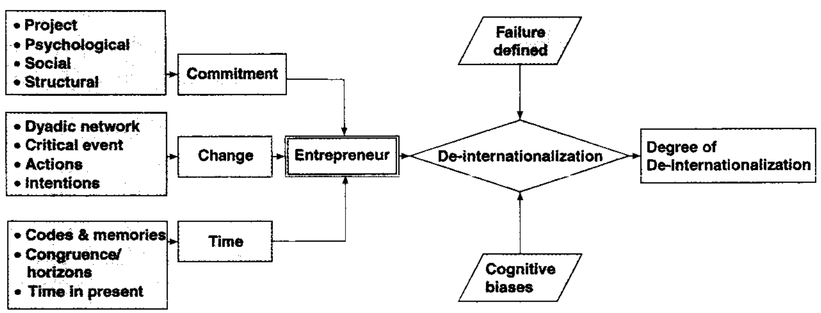

Figure 13.3 A conceptual framework of de-internationalization

themselves to codes and memories (past), and congruence and horizons (future). As control variables, failures have to be defined and cognitive biases accounted for.

Building De-Internationalization Theory

The previous discussion clearly suggests that in order to develop an understanding of the process of de-internationalization of small firms, there is a need for a paradigm shift from positivism towards realism (Guba and Lincoln; 1994), the ontology of which assumes that there is a 'real' world out there to discover even if it is only imperfectly and probabilistically apprehensible (Godfrey and Hill, 1995), and that the research deals with complex social phenomena involving reflective people (Healy and Perry, 2000) particularly when studying networks relationships (Hill *et al.*, 1999). By employing the realism paradigm in de-internationalization process research, the researcher understands the need to minimize the distance between the researcher and the entrepreneur (Hill and Wright, 2001). This epistemology suggests that the research methodology must be inductive in nature based on case studies (Eisenhardt, 1989; Yin, 1994), longitudinal (Pettigrew, 1995), and should use mainly in-depth interviews and observations in order to clarify the circumstances and influences on decisions which are made (Benito and Welch, 1997).

CONCLUSIONS

While the extant literature has emphasized the role of domestic and foreign country factors on the initial choice of foreign market entry modes, less is documented on the effect of changes in the external environment, or indeed internal changes within the firm on the continuance of internationalization beyond selected decisions. Perhaps the questions that most need to be addressed by firms, policy-makers and researchers are, 'To what extent is this mode of operation continuing to deliver returns and positive performance and, if less than optimal, what change would better effect attainment of projected targets?'

Thus, the importance of the proposed conceptual framework for the study of the process of de-internationalization is twofold. First, it may help to develop a better theoretical understanding of small-firm internationalization. Second, if there is a better understanding of the factors that are likely to influence de-internationalization and post-de-internationalization decisions, this will help policy-makers develop trade-support strategies.

Notes

1. It has been argued elsewhere (for example Boddewyn, 1985; Casson, 1986) that it is possible to see divestment of international operations as the reverse of the investment process. Or, as Benito and Welch (1997) question whether these forces (that move a firm forward internationally over time) operate in reverse, perpetuating a withdrawal process.

2. For example, in the USA the buy-out of a small firm by a large corporation is viewed as an exit strategy (Westphal, 1999), whereas in Germany a merger with another company is perceived as failure (Achtenhagen, 2002).
3. As Halinen *et al.* (1999) argue, they (environmental forces) are always transmitted within the network through individual relationships; or as Macharzina and Engelhard (1991) point out, internationalizing firms adjust to their environments through their decision-makers.

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14 Satisfaction with Paying for Government Export Assistance

John Knight, Jim Bell and Rod McNaughton

INTRODUCTION

How should governments assist exporters most effectively? This question has vexed export researchers over two decades, and a definitive answer remains elusive. Most governments have trade-promotion programmes in recognition of the need to assist small firms in various areas. The motives of such programmes include a desire to stimulate export-led economic growth, increase the international competitiveness of firms, and reduce the trade deficits affecting many nations in recent decades (Leonidou and Katsikeas, 1996; Czinkota and Ronkainen, 1998; Moini, 1998). A continuing problem is that the effectiveness of government assistance programmes is difficult to measure (Seringhaus, 1986; Seringhaus and Rosson, 1990; Diamantopoulos *et al.*, 1993), and there is doubt as to whether governments deliver what firms require. A further problem is that such government assistance programmes fly in the face of emerging attitudes towards free trade and the removal of subsidies and tariffs. A response of some governments is to introduce commercial charges for services. It becomes important to know whether firms consider they receive value for money, and whether providing such commercial consultancy services is the business that governments should be in.

New Zealand has, since the mid-1980s, conducted one of the most radical economic reforms seen in any modern economy. Prior to 1984, import-substitution policies maintained 'Fortress NZ' as one of the most highly protected economies in the OECD (Winkelman and Winkelman, 1998). Subsidies were rife and non-tariff barriers were widespread. In fact the proportion of New Zealand imports subject to non-tariff barriers far exceeded that of any other OECD country (Laird and Yates, 1990). An extreme example was that in the 1970s margarine was only available on a doctor's prescription, a measure to protect the highly important dairy industry. Since 1984 successive governments have instituted a programme of radical unilateral reforms of New Zealand's trade policy in a manner that is unique in the developed world. The removal of import licensing and reductions in tariff levels have 'turned the economy into one of the most open, market-oriented and lightly regulated in the OECD' (OECD, 1999). In line with its free-market philosophy, the New Zealand government has instituted 'user pays' principles into virtually every aspect of export services. Until 1997, government grants

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