

**Exploring the Internationalisation of  
Chinese Privately-owned Enterprises (POEs)**

**By**

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# **ABSTRACT**

Internationalisation has long been a focus of research among international business scholars. However, there is little knowledge about Chinese firms' internationalisation processes. This study is based on the premise that Chinese firms may have different international behaviours, compared to Western firms, given China's distinctive institutional and cultural environments. To test this argument, this thesis examines Chinese firms' internationalisation rationales, approaches and influential factors. It focuses on small and medium-sized privately-owned enterprises (POEs) that are actively engaged in international operations. Interviews were conducted with decision makers of six POEs from four industries, including the telecommunications networks, electronics, meters, and textiles. These firms were located in Guangdong, Fujian and Zhejiang provinces. The data collected were analysed using within-case and cross-case analysis approaches. Findings were then compared to extant literature, including the Uppsala School's internationalisation process model (U-model) and the theory associated with international new ventures (INVs).

The findings presented here indicate that the Chinese POEs' internationalisation behaviours are not particularly different from their Western counterparts. Even though neither the U-model nor the INVs framework alone could fully capture the complexities of the Chinese POEs' internationalisation processes, both demonstrate their applicability in different ways. The study develops 15 propositions that should enable researchers to develop a better understanding of Chinese POEs' internationalisation processes. The thesis concludes with a discussion of the implications of these findings for theory

development and future research, as well as managerial implications. This case study contributes to a wider theoretical understanding of Chinese POEs' internationalisation behaviours.

***Key words:*** U-model, INVs, Chinese internationalisation process, Chinese internationalisation motives, privately-owned firms, SMEs' internationalisation.

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## **LIST OF ABBREVIATIONS**

China	The People's Republic of China
COE	Collectively-Owned Enterprise
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
INV	International New Venture
JV	Joint Venture
M&As	Mergers and Acquisitions
MNE	Multinational Enterprise
NBSC	The National Bureau of Statistics of China
NDRC	The National Development and Reform Commission
OECD	The Organisation for Economic Co-operation and Development
OEM	Original Equipment Manufacturer
POE	Privately-Owned Enterprise
R&D	Research and Development
SME	Small and Medium-sized Enterprise
SOE	State-Owned Enterprise
U-model	The Uppsala School's Internationalisation Process Model
UNCTAD	United Nations Conference on Trade and Development
WTO	The World Trade Organization

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# Chapter 1 Introduction

## ***Introduction***

*This chapter introduces the research background, research issues, and research problems, along with the major theoretical frameworks focused on in the study. The methodological approach, with justification of the study, is then presented. The chapter also briefly describes the expected research contributions.*

## **1.1 Background to Research**

Many firms perceive internationalisation as a strategy for survival and increasing profitability (Gerlinger, Beamish, & daCosta, 1989). This is because the marketplace is dynamic, product and technological life cycles are believed to be shorter with faster technological obsolescence (Coviello & Munro, 1995), and the cost of research and development (R&D) is increasing (Litvak, 1990). An expanded marketplace provides buffering against these factors and increases opportunities. Through internationalisation, firms have the chance to gain economies of scale and scope, obtain knowledge, prolong product life cycles, recover substantial R&D costs, enhance capabilities and innovation, and exploit entrepreneurial opportunities (Lu & Beamish, 2001; Vermeulen & Barkema, 2001).

Due to its importance, internationalisation has long been a focus of research among international business scholars, with systematic research in the field starting in the late

1960s. The nature of internationalisation behaviour is diverse. Different scholars take different directions to study the phenomenon, producing various models and theories to conceptualise it. Traditional research on internationalisation can be categorised into two main streams: the economic decision-based theories and the evolutionary behavioural theories (Benito & Welch, 1994). The economic decision-based approach concerns specific aspects of economics in internationalisation. According to this approach, decisions to internationalise are based on economic analysis. Prominent examples include internalisation theory, the transaction cost model, the eclectic paradigm and the resource-based approach. On the other hand, the evolutionary behaviour theories view internationalisation as an incremental process. Examples are the stage models and the network model. Since the 1990s, scholars found a large number of small and young firms from various countries internationalising rapidly. These firms are referred to as international new ventures (INVs). Their international behaviours contradict the traditional theories described above.

Among various theories, the Uppsala School's internationalisation process model (U-model) (Johanson & Vahlne, 1977, 1990, 2003; Johanson & Wiedersheim-Paul, 1975) and the international new ventures (INVs) framework (Jolly, Alahuhta, & Jeannet, 1992; Knight & Cavusgil, 1996; Lindqvist, 1991; Oviatt & McDougall, 1994, 1995; Preece, Miles, & Baetz, 1999) are widely discussed models internationally in recent years. The U-model, which emphasises internationalisation as a path-dependent process, has dominated the evolutionary behaviour perspective. In this framework, firms' internationalisation strategies are a function of their previous activities. The model has

received both praise and criticism regarding its utility. The emergence of INVs in the 1990s further challenged the U-model. An INV internationalises rapidly from inception, aiming to derive competitive advantages across nations early in its history (Oviatt & McDougall, 1994). These two established frameworks both explore firms' internationalisation processes, but arrive at different findings regarding internationalisation motivations, objectives, foreign market entry modes, foreign market selection and the influential factors that have impacts on firms' internationalisation decisions. They both have influenced internationalisation thought, research and practice since they were developed. Nevertheless, these models were developed and tested in Western countries and there is, as yet, little knowledge about their utility in developing countries. In light of the increasing involvement of business from developing countries in world trade, this represents an important research gap that is necessary to be filled through empirical study (UNCTAD, 2007).

This study seeks to investigate Chinese small and medium-sized privately-owned enterprises' (POEs) internationalisation rationales, approaches and determining factors. Since the People's Republic of China (China) opened its doors to embrace a more liberal trading system worldwide in 1978, it has increasingly become a major player in the global market. Its annual average gross domestic product (GDP) growth has been nearly 10% since then according to China's official statistics (Chinability, 2008). This remarkable growth rate is expected to remain for the upcoming few years (AFX International Focus, 2007). In terms of international trade, China has become the second largest exporter and the third largest importer of goods and services in the world for the

year 2006 (UNCTAD, 2007). Data also revealed that, in 2005, China was the third largest recipient of direct investment, just after the United Kingdom and the United States of America. In the meantime, China's overseas investment has grown rapidly. Many Chinese firms are globally diversified in various sectors. Contrary to China's increasing critical role in the world market, only very limited empirical work has been conducted on the outward internationalisation of Chinese firms - especially small and medium-sized enterprises (SMEs) (cf. Buckley et al., 2007). This is confirmed by conducting an extensive search on the most relevant international business journals such as *Journal of International Business Studies*, *International Business Review*, and *Journal of International Entrepreneurship* from the 1960s/1970s to the present time. Most existing studies were conducted in a descriptive manner, which indicates the need to investigate the phenomenon in an analytical manner.

In recent years, despite a huge and fast-growing domestic market, many Chinese companies have started making substantial forays abroad. Statistics revealed that there were more than 7,470 Chinese firms located in foreign markets, worldwide, at the end of 2003 (People's Daily Online, 2004). Many of those firms were small POEs. As the majority type of company in China, the development of POEs is vital to the country's stable economic growth and dynamic industrial expansion. In 2002, there were 2.4 million POEs in China, employing 34.1 million people (Lang & Hu, 2004). For the year 2005, POEs had created half the country's wealth (Zhao, 2006). Their contribution to the country's national prosperity is likely to further increase as a result of the privatisation policy in recent years. In contrast to their enormous contributions to the nation's stable

economic growth and dynamic industrial expansion, they face unfavourable institutional constraints compared to other types of enterprises in China. To date, the limited academic literature on Chinese enterprises' internationalisation has focused on multinational enterprises (MNEs) and state-owned enterprises (SOEs) (Buckley et al., 2007). In line with China's important international role, and the challenging situations that POEs face, it is critical to explore the internationalisation processes of Chinese POEs.

## **1.2 Research Issues and Contributions**

The above section has identified that there has been relatively little research into the internationalisation processes of firms from developing countries. In spite of China's important role in the international market, limited research has been conducted with the goal of understanding Chinese firms, especially with respect to the internationalisation behaviours of Chinese small and medium-sized POEs. With regard to these important research gaps in international business literature, this thesis has the objectives of identifying motives, approaches and influential factors that drive Chinese POEs toward internationalisation, hence, adding to the body of literature on internationalisation of firms. To fulfil its purpose, three main research questions are addressed in the thesis:

- *Why do Chinese POEs internationalise?*
- *What factors lead to internationalisation among Chinese POEs?*
- *How do Chinese POEs internationalise?*



Specific research objectives are:

- *To identify Chinese POEs' motives for internationalisation.*
- *To identify factors that lead to their internationalisation.*
- *To identify their objectives for internationalisation.*
- *To identify their approaches for realising international objectives.*
- *To identify their market selection criteria and evaluation.*
- *To identify their evaluation of international opportunities.*

To achieve these research objectives, a detailed evaluation of the U-model and INVs framework was conducted to provide a reference framework. Literature on motives and determining factors to internationalisation among firms from both developed and developing nations was also used. This serves as a theoretical foundation for the formulation of the key research questions. It also provides the theoretical background against which the research data were analysed. Throughout this study, the generalisability in the Chinese context was evaluated.

To comprehend fully the nature of Chinese POEs' internationalisation, flexible semi-structured interviews were conducted to obtain primary data. Six firms were selected from Guangdong, Fujian and Zhejiang provinces, across a range of industries. The findings were evaluated in relation to the above-mentioned literature. Ultimately, policy recommendations to decision makers are provided.

This project's contributions toward improving research, educational process and managerial practice are presented in Chapter 8. As an emerging market, the transitional nature of China's industrial and institutional environments is different from Western countries. Hence, it is anticipated that Chinese POEs will display rationales and behaviours of internationalisation that are partially consistent with extant literature and contain elements which are not explained in literature. The findings not only shed light on the way Chinese firms internationalise, but also add to our knowledge about international entrepreneurship and internationalisation in the context of small and medium-sized firms from a developing country. Moreover, the practical relevance of such findings can be assumed to serve the further development of internationalisation of Chinese SMEs, which is in the interest of, and important to, many constituencies such as local government, and domestic and foreign multinational enterprises.

### **1.3 Methodology**

Semi-structured interviews were chosen to obtain primary data. Secondary data was used to supplement information gathered from the primary research. It is well recognised that quantitative studies are critical for testing existing theory, while qualitative studies enable the researcher to generate rich insights into the research topic. Since the thesis has the objectives to gain knowledge of the complex and dynamic phenomenon of Chinese POEs' internationalisation, to make a theoretical contribution, it was decided to use a qualitative research approach. With an aim to produce more generalisable results, six firms across four industries were drawn from Guangdong, Fujian and Zhejiang provinces. The four industries were the telecommunications networks industry, the electronics

industry, the meter industry, and the textiles industry. To gain deeper insights, semi-structured interviews with managers/owners of internationally active SMEs were conducted.

## **1.4 Outline of the Thesis**

The thesis is divided into eight main chapters. Each chapter represents a specific stage of the research.

### *Chapter 1: Introduction*

This chapter introduces the research topic. It presents the research background, research issues, research problems and research methodology and defines the scope of the relevant literature for this study. It also briefly describes the expected research contributions and outlines the structure of this study.

### *Chapter 2: Research Background*

This chapter sets the basis from which the research has been undertaken. In order to give a better idea of the research issues, secondary data concerning SMEs' international performance, Chinese firms' international development, and the environmental conditions of the three provinces in which the interviewed firms are located is provided.

### *Chapter 3: Literature Review*

This chapter provides a comprehensive review of relevant literature in the research area. It examines SMEs' motives for and approaches to internationalisation as presented in the

literature. Factors that influence firms' internationalisation decisions and performance are reviewed. Literature on firms' internationalisation processes is discussed with the focus on the U-model and INVs framework.

#### *Chapter 4: Research Methodology*

This chapter discusses the selected research methodology based on the research objectives. It describes the procedures of collecting and analysing data. Techniques applied to address issues of research validity and reliability are discussed. Other issues, such as sources of data and ethical considerations, are also presented.

#### *Chapter 5: Company Profiles*

This chapter presents the data obtained from the interviews and archival records regarding the six studied Chinese POEs' internationalisation. The findings for each company are presented in the form of case reports.

#### *Chapter 6: Within-case Analysis*

This chapter takes an in-depth look at the collected data, as it compares to the literature. A within-case studies analysis approach is discussed and applied.

#### *Chapter 7: Cross-case Analysis*

This chapter further examines the findings of this study. A cross-case analysis approach is applied for analytical comparison. The main findings are evaluated in relation to the existing literature.

## *Chapter 8: Conclusion and Implications*

This chapter summarises the research. The contributions and managerial applications are then presented, followed by the discussion of research limitations and proposed future research areas.

# Chapter 2 Research Background

## ***Introduction***

*This chapter has three sections. The first section presents secondary data regarding SMEs' international development. The second section reports on China and Chinese firms' international performance, as well as the contributions of privately-owned enterprises to the country's growth. Background information concerning the development of the three provinces where the studied firms are located is also provided. The last section overviews this chapter.*

## **2.1 What are SMEs?**

Currently, SMEs account for about 95 to 99% of the business firms in the world (Cruz-Carreon, 2006). In Canada, the United States of America, and South Korea, the number reaches 99.7% (WTO, 2007b). In developing countries, SMEs play an equally important role, representing over 90% of firms outside the agricultural sector (WBCSD, 2007).

It is widely appreciated that SMEs make enormous contributions to the global economy. They are often credited as agents of innovation, employment generation, economic growth, wealth creation and social development (OECD, 2002; WBCSD, 2007). In the Organisation for Economic Co-operation and Development (OECD) countries, SMEs produce about one-sixth of manufacturing output, contributing 60 to 70% of manufacturing employment. In the United States of America, SMEs represent approximately 40% of the country's economic activities. During the 1990s, they created

90% of new businesses and generated about 75% of employment growth for the country. Regarding innovation, between 30 and 60% of SMEs in the OECD manufacturing sector are referred as innovative. In the United States of America, SMEs generate 50% of the country's innovations (OECD, 2002). In transition economies, SMEs' contributions are even more crucial. In addition to the above-mentioned contributions, they play a significant role in the process of industrial restructuring, privatisation and economic transformation (UNECE, 1997).

Despite the crucial contributions of SMEs to global economic development, there is no generally accepted definition of SMEs. Different countries define SMEs against various criteria. Generally, there are a number of defining measurements that have been applied: the number of employees, the value of company turnover, the amount of capital invested, the size of the balance sheet and the industry type (Ministry of Economic Development, 2005). According to the OECD (2005, p. 17), "*SMEs are non-subsidiary, independent firms which employ less than a given number of employees*". However, the number of employees used to define SMEs is not consistent. In Europe, according to the European Commission, SMEs are firms that have fewer than 250 employees with less than EUR50 million of turnover, and with balance sheets less than EUR43 million. In the United States of America, SMEs are considered as firms that have fewer than 500 employees (OECD, 2005). In New Zealand, enterprises with 19 or fewer employees are defined as SMEs (Ministry of Economic Development, 2005). In Japan, the criteria used to define SMEs vary by sector and are based on a combination of total amount of investment and the size of the workforce. Given this diversity, the OECD points out that "the

characteristics of a SME reflect not only the economic, but also the cultural and social dimensions of a country” (OECD, 2004, p. 10).

In China, the definition of SMEs is complex, since it varies by industry category, for regulatory purposes. Four criteria have been applied to define SMEs, including the number of employees, sales revenues, assets and industrial category. In 2003, the State Reform and Development Commission formally promulgated the SME division standards. Based on this, an SME in China may actually be a very large firm. According to the law, an industrial SME is defined as a firm that has up to 3,000 employees and has sales revenues of less than RMB300 million (approximately US\$40 million), with total assets up to RMB400 million (approximately US\$53 million). For the retail and restaurant sectors, SMEs are firms that have less than RMB150 million of turnover (approximately US\$20 million) and employ fewer than 800 employees (CBI Enterprise Institute, 2007).

### **2.1.1 Characteristic of SMEs**

SMEs face more obstacles in conducting business than do larger firms due to their inherent disadvantages. In comparison to MNEs, SMEs often have more limited financial resources, fewer capabilities and know-how, less formal business education, fewer economies of scale and scope, and less access to cutting-edge technology. They may also experience difficulties in obtaining access to investment and credit facilities (Bell, Murray, & Madden, 1991; Bonaccorsi, 1992; OECD, 2002; WBCSD, 2007). SMEs are marginalised by the institutional frameworks of most countries. Existing policies tend to cater to the big firm mindset (WBCSD, 2007). SMEs can also face survival threats such



as decline in customer base, shrinking of market size, sales and associated profits decrease, or performance downturn in their domestic markets (Chen & Martin, 2001, p. 559).

Meanwhile, SMEs' ownership, operational processes, organisational structures and management systems are also tend to be different from MNEs. In contrast to MNEs' formal organisational structures, SMEs' organisational structures tend to be simple. Their less complex and less sophisticated structures allow entrepreneurs to have more control and influence on the organisations, and also give SMEs flexibility to switch product lines, update technology, and change operational processes and organisational structures, hence allowing them to quickly response to changes in the environment (WTO, 2007b).

Even though SMEs generally lack resources, many of them still outperform their large counterparts, given that they possess advanced technology and products (Moen, 1999), and have creative advantages in generating new knowledge (Acs & Audretsch, 1990). Research has found that SMEs tend to spend far less on R&D than larger firms, but produce nearly twice as many innovations as large firms do on a per employee basis (Acs & Audretsch, 1990). Their strengths generally come from their rapid response to technological changes and customer needs. However, their difficulties in acquiring resources can limit their ability to respond to changes. For instance, a lack of skilled labour may constrain their transfer capabilities, limiting their ability to internationalise their innovations (Acs & Yeung, 1999). To overcome these weaknesses, many SMEs

utilise partnerships, networks and clusters to maximise their creativity, flexibility, and gain economies of scale and scope at the global level (OECD, 2002).

### **2.1.2 SMEs' International Performance**

The preceding section indicated that SMEs are often in a comparatively disadvantaged position as a result of their limited resources and experience. On the other hand, SMEs' flexibility and creativity are their competitive advantages. Evidence illustrates that there is a substantial number of SMEs involved in international business despite the persistent problems they face. The number has increased dramatically since the 1990s. According to a report by the OECD (1995), in the early 1990s approximately 10% of SMEs had foreign direct investment (FDI) worldwide. In terms of direct exports, it was reported that SMEs' export values accounted for 35% of the total value within Asian countries, approximately 26% of the total value across all the OECD member countries, and about 25 to 40% for manufactured exports worldwide. In the United States of America, there was a 107% growth rate among SMEs that had export activities over the period from 1992 to 1997. By 1999, nearly 97% of exporting firms were SMEs, exporting a third of the nation's total exports. In South Korea, there was a remarkable growth of SME participation rates in foreign investment in the manufacturing sector. Growth was 8% in 1998, climbing to 65% in 2000 (OECD, 1995, 2002).

### **2.1.3 Opportunities of Internationalisation for SMEs**

Traditionally, internationalisation is perceived as good for both firms and for national economic growth. From individual firms' points of view, foreign markets provide lucrative opportunities for growth (Mayer & Flynn, 1973). Through internationalisation, SMEs expand their business scope and business opportunities. Contractor (2007, p. 456-458) indicated seven benefits of international expansion besides associated costs. Through international expansion, firms are able to increase their financial performance since they can:

- gain knowledge that is not available in the domestic market
- get access to less costly inputs abroad
- exploit firm-specific assets
- accumulate global market power
- achieve international scale
- reduce risk of business cycle and foreign exchange volatility, and
- build up international experience

Similarly, Ghoshal (1987) contended that internationalisation is a means for firms to achieve their goals of maximising efficiency, diversifying risk and enhancing their learning capabilities. Through internationalisation, firms can exploit location advantages of different nations by locating each activity where they can achieve cost advantages. In the meantime, firms can also achieve economies of scale and scope through integrating activities across nations.

### **2.1.4 Challenges of Internationalisation for SMEs**

Internationalisation presents an important opportunity for growth and value creation. It also involves many challenges. The process occurs when the firm expands its business activities such as production, marketing, R&D, sales and service into foreign markets (Hollensen, 2007). Once the decision to go abroad has been made, firms need to make more decisions on the timing of investment, selecting foreign markets, entry modes, industries, locations, partners, recruitment and selection of qualified personnel, and other arrangements, against a range of considerations including level of perceived risk, level of resource commitment, degree of control over foreign operations, and market expectations. There are certainly challenges and costs associated with market identification and evaluation.

#### ***2.1.4.(1) Liability of Foreignness***

After having selected foreign markets and chosen entry modes, firms might find an array of new challenges confronting them. The most obvious challenge could be the liability of foreignness (Hymer, 1960; Zaheer, 1995, 2002), which refers to the costs (both financial and non-financial) of doing business abroad that are not experienced by local firms. By combining Hymer's (1960) and Zaheer's (1995) work, five types of disadvantages of doing business abroad can be identified. First, the spatial distance between the parent firms and their subsidiaries requires coordination across geographic distance. Hence, there are extra costs arising from travelling, transportation and coordination over distance. Second, compared to local firms, foreign firms have less information about the host country. To gain knowledge about the host market regarding economic, social, legal, and

cultural issues, to learn new ways of conducting business in the host market, and to establish local contacts, foreign firms need to bear considerable adaptation costs (Buckley & Casson, 1976; Hennart, 1982). Third, foreign firms can face discrimination hazards arising from stakeholders in the host countries including host governments, host consumers and host suppliers. This view is supported by Vernon (1977), who recognised that foreign firms experience another type of disadvantage, which is local bias. Host governments and indigenous firms often perceive foreign firms as threats to their technological and industrial developments, and hence against them. Fourth, firms' overseas performance is largely influenced by their home environments. Differential treatment from their home governments, such as sales restrictions, foreign exchange restrictions, complicated approval processes for international operations, and rapidly-changing regulations, create costs associated with organisational legitimacy, which have a significant negative impact on overseas operations. Economic factors such as foreign exchange risk and the cost associated with the managing of exchange rates could also put international firms into a cost-disadvantaged position.

The impact of the liability of foreignness is profound. Empirical work has confirmed that the liability of foreignness reduces foreign firms' performance through increased costs, reduced operating profitability and increased firm exit rates (DeYoung & Nolle, 1996; Miller & Parkhe, 2002; Miller & Richards, 2002; Zaheer, 1995; Zaheer & Mosakowski, 1997). Zaheer (2005, p. 343) concluded that the liability of foreignness will vary by firm, industry, home country and host country. Small firms would be expected to suffer more, compared to larger firms, as a result of their resource constraints and limited experience.

#### ***2.1.4.(2) Liability of Newness***

Besides the liability of foreignness, internationalisation is also associated with the liability of newness when new subsidiaries or overseas operations are established in foreign markets. There is a high failure rate associated with start-up organisations (Stinchcombe, 1965). As a start-up, new organisations may lack connections with stakeholders, and experience in business operations (Freeman, Carroll, & Hannan, 1983), may have inadequate foreign market information, and often have limited financial capacity and trained human resources (Erramilli & D'Souza, 1993). To survive, they generally need to establish new business relationships in the foreign market, recruit and train new employees, and spend time on building trusting relationships with these new employees, as well as develop other capabilities for overseas operations. Compared to MNEs, the liability of newness is generally more severe for SMEs. This is once again related to their financing and skilled labour constraints.

#### ***2.1.4.(3) Liability of Smallness***

While the liability of foreignness is applicable to all foreign firms with varying intensity, and the liability of newness occurs to firms when foreign subsidiaries are established, the liability of smallness is a potential challenge unique to all small firms. Size can have a significant effect on firms' international performance and is viewed as a proxy for international resource availability (Pedersen & Petersen, 1998). Internationalisation involves certain costs such as learning costs, transportation and communication, as well as fixed costs if any foreign production is to occur. Internationalisation is also more risky due to uncertainty in international markets. SMEs are widely recognised as being

handicapped by constrained resources (Bell, Murray, & Madden, 1991; Bonaccorsi, 1992). They may lack export market information, have limited financial capacity and trained human resources. Investing abroad may require SMEs to spread their resources too thinly over their foreign markets. As a result of the lack of trained human resources, SMEs might also have problems in coordinating international activities. Given the interaction between these factors, international challenges are viewed as more severe for SMEs compared to MNEs. Moreover, small firms have smaller economies of scale and scope, and may be in cost-disadvantaged positions compared to large firms.

Empirical study has revealed that small firms experience significantly more problems than large firms. The World Bank conducted a comprehensive survey to investigate business obstacles that different sized firms experience across business environments. It was based on a sample of over 10,000 companies from 80 countries in the private sector. The findings confirmed that, compared to their larger counterparts, small firms face more obstacles particular in the areas of financing, taxes, regulations, inflation, corruption and crime (Schiffer & Weder, 2001).

### **2.1.5 Synthesis**

SMEs are continuing to play an increasingly critical role in the development of global economics, which is a relatively new phenomenon. Traditionally, the majority of academic studies have focused on large MNEs (Dunning, 1988; Johanson & Wiedersheim-Paul, 1975). Due to the different characteristics between large and small firms, it is recognised that small firms may have different international behaviours

compared to their large counterparts. Reid (1981, p. 101) notes that the foreign entry expansion processes of small firms and large firms should be differentiated, and more empirical research in the area is required to understand the phenomenon thoroughly.

Many small-sized firms actively participate in the international market, even though the majority focus on their local markets. It is important to understand why SMEs internationalise, given their inherent disadvantages arising from small firm size and a lack of experience, what motivating factors influence their internationalisation, and what initial objectives they have for international operations. Internationalisation represents a double-edge sword to SMEs. On the one hand, it provides opportunities for them to expand, while, on the other hand, internationalisation involves various challenges confronting small firms. As SMEs' contributions to world economic growth are significant with expectations that they will continue increasing, it is worthwhile to investigate how SMEs overcome obstacles and stay competitive in their international journey, as well as how they utilise opportunities offered in the global marketplace.

Existing research concerning SMEs' internationalisation was generally conducted in developed countries (Johanson & Vahlne, 1977; McDougall & Oviatt, 1996). Little is known about the utility of such findings in explaining the international behaviours of firms from developing countries. The phenomenon of Chinese entrepreneurial firms' active internationalisation provides a favourable platform for examining existing theories and further developing new theories. As an emerging market, the transitional nature of China's industrial and institutional environments is largely different from developed



countries. Hence, Chinese firms might be expected to have different international behaviours compared to firms from developed countries. This thesis explores the internationalisation processes of small-sized Chinese POEs. It first seeks answers for the above questions regarding why such firms pursue foreign activities in more challenging and uncertain markets, given that their domestic market is full of business potential; what factors play a role in their internationalisation; and how they internationalise. This thesis also evaluates the theoretical and practical usefulness of current research in the Chinese context, which leads to the development of propositions to summarise the studied phenomenon.

## **2.2 China's Development**

Since China opened its doors to embrace a more liberal international trading system, in 1978, it has been through various economic restructuring, political reform and social changes. Increasingly, China has played an important role in the world market, with remarkable economic progress (see Table 2.1). Data from the International Monetary Fund (IMF), the World Bank and the CIA World Factbook reveal that China has become one the world's largest economies, accounting for around 6% of global GDP in 2007 (CIA The World Factbook, 2008a; The IMF, 2008; The World Bank, 2008). It is currently the world's second-largest economy in terms of purchasing power parity (PPP) (GDP Rankings, 2007).

<b>Table 2.1: China's development</b>	
<b>GDP</b>	<ul style="list-style-type: none"> <li>• About US\$50 billion in 1978</li> <li>• Over US\$3,000 billion in 2007</li> <li>• Represented 6% of global GDP in 2007</li> <li>• Nearly 10% annual growth rate over the past 30 years</li> </ul>
<b>Exports</b>	<ul style="list-style-type: none"> <li>• 11% annual growth rate since 1980</li> <li>• Export value reached US\$1056 billion, accounted for 40% of China's GDP in 2006</li> </ul>
<b>Imports</b>	<ul style="list-style-type: none"> <li>• 13% annual growth rate since 1980</li> <li>• Import value reached US\$890 billion, represented 34% of China's GDP in 2006</li> </ul>
<b>Inward FDI flow</b>	<ul style="list-style-type: none"> <li>• US\$0.08 million in 1979</li> <li>• US\$72 billion in 2005</li> </ul>
<b>Inward FDI stock</b>	<ul style="list-style-type: none"> <li>• US\$1.074 billion in 1980</li> <li>• US\$318 billion in 2005</li> </ul>
<b>Outward FDI flow</b>	<ul style="list-style-type: none"> <li>• US\$0.44 billion in 1982</li> <li>• US\$11.31 billion in 2005</li> <li>• US\$21.16 billion in 2006</li> </ul>
<b>Outward FDI stock</b>	<ul style="list-style-type: none"> <li>• US\$0.44 billion in 1982</li> <li>• US\$46.31 billion in 2005</li> </ul>

Source: CIA The World Factbook, 2008a; The IMF, 2008; The World Bank, 2008.

In 1978, China's GDP was only RMB362.4 billion (approximately US\$50 billion), which has risen to over US\$3,000 billion in 2007. This impressive economic growth is the result of a nearly 10% annual growth rate over the past 30 years (Chinability, 2008). The real GDP growth rate was 11.9% for 2007. Compared to this robust growth rate, China's economy has slowed slightly to 10.6% year-on-year in the first quarter of 2008. This situation is caused by wage and price inflation coupled with net export decline and a fall in the current account surplus. Even though the global market is experiencing weak growth and high inflation due to the combination of financial market turmoil, high oil and commodity prices and cooling housing markets, China is expected to remain vigorous at

a yearly average growth rate of 9 to 10% for 2008 and 2009, according to United Nations Conference on Trade and Development (UNCTAD) 2008 forecast (OECD, 2008).

China's sustained economic growth rate is largely driven by its opening and rapid integration into the world trading and production systems. Based on China's national data from 1952 to 1997, Lin (2000) pointed out that the magnitude of export and import growth, investment growth, and labour force growth are the propelling factors of the country's overall growth. Data from UNCTAD (2007) demonstrated that China's export and import volumes have grown by 11 to 13% annually since 1980. Exporting is the most significant aspect of the country's international business so far, since it is based on low cost advantage (Child & Rodrigues, 2005). The export-to-GDP ratio has grown from 15% in 1990 to 30% in 2000, and reached 40% in 2006. For the year 2006, China's merchandise exports grew by 27%, reaching a value of US\$969 billion, which was over 8% of world merchandise exports. Its share of world services exports was 3.2%, with a value of US\$87 billion.

For imports, the value of goods and services imported was US\$890 billion in 2006, with a 20% annual growth rate. This value represented around 34% of China's GDP, accounted for 6% of the world total imports, up from 0.9% in 1982. As a result, China became the second largest exporter and the third largest importer of goods and services in the world (UNCTAD, 2007; WTO, 2007a).

Prior to the 1980s, inward FDI to China was virtually non-existent. Since then, increasingly, China has been well known for attracting FDI, as it has become the largest recipient of direct investment (IMD, 2004). Statistics from UNCTAD (2007) showed that, in 1979, the value of inward FDI flow was US\$0.08 million, while, in 2005, the value had rocketed to US\$72 billion, which represented 8% of global cross-border flows. Associated with this enormous inflow of FDI value, the stock of inward FDI had increased nearly 300 times from US\$1.074 billion in 1980 to around US\$318 billion in 2005, when it represented over 14% of China's GDP.

In the last decade, the Chinese government has started to encourage its indigenous firms to engage in international activities. To respond to the favourable investment policies, many Chinese companies have started making significant forays abroad. In 1982, both outward FDI flow and stock were worth US\$0.044 billion, which grew from virtually nil at the start of economic reforms in 1978. The value of net flows had surged to US\$11.31 billion, with stocks increasing to US\$46.31 billion, in 2005. The value of outward FDI flow further expanded, reaching US\$21.16 billion for the year 2006 (UNCTAD, 2007). Even though Chinese outward FDI is still relatively small compared to global flows, its growth rate is among the fastest. It is forecasted that China's outward FDI flows will overtake inward FDI flows by 2010, and that China will become the fifth largest global foreign investing nation after the United States of America, the United Kingdom, Germany and Japan (Forum, 2007). According to a study by Bain & Co. (2003), China's outbound FDI is expected to reach US\$86 billion by 2015.

China's outstanding growth in outward FDI is also manifested in the number of Chinese-invested enterprises in the world (see Table 2.2). Before 1985, foreign investors were exclusive to state-owned enterprises, and provincial and municipal international economic and technological cooperation enterprises. Under state guidance, there were only 185 Chinese international ventures worldwide, with an investment value of US\$0.154 billion by 1985. The scale of investment projects was small, and mainly in the form of joint ventures (JV) located in developing countries. In 1985, the Ministry of Foreign Economic Relations and Trade (MOFERT) issued a new directive, which allowed more enterprises, including private enterprises, to invest overseas, provided they had met criteria such as possessing sufficient resources. As a result, 616 enterprises went abroad between 1986 and 1990, involving US\$1.2 billion of capital. From 1990, the Chinese government actively encouraged Chinese businesses to invest in foreign countries. By 1996, the total number of Chinese overseas subsidiaries had climbed to 1,985, involving over US\$2 billion of investment capital (Tseng & Mak, 1996, p. 145-146). By the end of 2003, 3,439 Chinese enterprises had set up 7,470 foreign subsidiaries in 139 countries or regions worldwide with total overseas investment of US\$33.2 billion (People's Daily Online, 2004).

<b>Table 2.2: Chinese international ventures</b>		
<b>Year</b>	<b>Number of international ventures</b>	<b>Investment value</b>
By 1985	185	US\$0.154 billion
By 1990	801	US\$1.354 billion
By 1996	1,985	Over US\$2 billion
By 2003	7,470	US\$33.2 billion

Source: People's Daily Online, 2004; Tseng & Mak, 1996, p. 145-146.

### 2.2.1 Classification of Chinese Enterprises

There are four government defined types of enterprises in China (Poutziouris, Wang, & Chan, 2002) (see Table 2.3). The first category is the state-owned enterprise (SOE), which is under the governance of the state. The second one is the collectively-owned enterprise (COE). This type of firm is “owned by the population of a given locality” (Poutziouris, Wang, & Chan, 2002, p. 385), thus controlled by local governments (Chen & Huang, 2001). As a result of the central control system, some COEs are risk averse and have incompetent governance. Nevertheless, the privatisation of enterprises in the 1990s resulted in many of them being able to operate in a market-based environment, and to have autonomy in executing business activities (Zapalska & Edwards, 2001). The third kind of firm is the private and individually-owned enterprise (POE), which is defined as *“any entrepreneur who risks his/her own capital in the pursuit of economic wealth would belong to the private sector and to some extent, in the foreign funded sector of the PRC economy”* (Poutziouris, Wang, & Chan, 2002, p. 385). Firms that employ more than eight people are defined as “private enterprises”; otherwise, they are “individual enterprises” (Ping, 1997). The last category comprises other enterprises, including JVs, shareholding cooperatives and industrial enterprises.

<b>Table 2.3: Classification of Chinese enterprises</b>	
<b>Enterprises in China</b>	<b>Definition</b>
State-owned Enterprises (SOEs)	Under the governance of the State.
Collective-owned Enterprises (COEs)	Owned by the population of a given locality
Private and Individually-owned Enterprises (POEs)	Any entrepreneur who risks his/her own capital in the pursuit of economic wealth
Other enterprises	Includes joint ventures, shareholding cooperatives and industrial enterprises

Source: Poutziouris, Wang, & Chan, 2002.

Traditionally, SOEs have dominated most sectors, having the greatest scale and capital resources as a result of the central planning system. Prior to 1978, the Chinese government mobilised all of its resources to develop SOEs aiming to realise industrialisation. SOEs have the advantages with respect to gaining soft loans to fund their operations (Yang & Zhang, 2003). They receive financial support and gain access to important business information. This is the reason why the majority of Chinese enterprises involved in international operations are SOEs. According to UNCTAD's 2002 *World Investment Report*, most of the top 12 transnational corporations (TNCs) in China are SOEs. These firms controlled over US\$30 billion in foreign assets, with foreign sales of US\$30 billion as of 2001, and employed more than 20,000 foreign employees worldwide (UNCTAD, 2002). In 2003, SOEs accounted for 43% of the total outward investment stock, compared to 33% and 10% for public corporation and private companies, respectively (Asia Pacific Bulletin, 2004).

The development of POEs did not start until 1978, when the economic system reforms began. As a result of transformations, the government was forced to introduce market

competition, open up the market, liberalise trade policies, and encourage the development of private economy. In the 1990s, POEs experienced fast development under the market-based economy system (Yang & Zhang, 2003).

### **2.2.2 POEs' Contributions to China's Economic Development**

POEs' fast growth and development are a major driving force in China's economy. In the last decade of the 20<sup>th</sup> century, the private sector generated nearly 60 million jobs (Asiaweek, 2001). In 2002, there were 2.4 million POEs in China, employing 34.1 million people (Lang & Hu, 2004). In 2004, the Leading Group of First National Economic Census of the State Council and the National Bureau of Statistics of China (NBSC) jointly conducted a survey, finding that there were 1.98 million POEs in the country's secondary and tertiary industries. Compared to the data released in 2001, this was a 49% increase. Meanwhile, the increase in the number of POEs was accompanied by decreases in the numbers of SOEs and COEs. There were approximately 192,000 SOEs and 456,000 COEs in 2004. Each had a 48% and 46% decrease, respectively, compared to the data released in 2001 (GOV, 2005; The NBSC, 2005). By the end of September 2006, there were 4.869 million POEs, representing the majority of companies in China. These firms employed 63.95 million people, while their aggregate registered capital surged to US\$931 billion (Xinhua, 2006).

POEs' contribution to the nation is remarkable. Indigenous private enterprises have contributed one-third of China's GDP in recent years. In 2005, their contribution accounted for half of the country's wealth; if overseas-funded ventures are considered,



the proportion jumps to 65%. This proportion is expected to reach 75% in 2010, when over 70% of Chinese firms will be privately owned. In the meantime, POEs generate more tax revenues than all other types of firms. In many regions, the value even exceeds 80% of the local government revenues (Zhao, 2006).

China's increasing integration into global supply chains offers export opportunities, not only to large SOEs, but also to other types of firms. According to the Ministry of Commerce, POEs' export value exceeded US\$101 billion in 2004, with an annual growth rate of 68.6%. Compared to SOEs and other enterprises with foreign investment, this growth rate was 57.2% and 27.7% higher, respectively (People's Daily Online, 2005). Between January and September 2006, Chinese POEs exported a total of US\$173.1 billion, with an increase of 46% from the same period the year before (Xinhua, 2006). Table 2.4 summarises Chinese POEs' key performance from the 1990s to 2006.

<b>Table 2.4: Chinese POEs' performance</b>	
<b>Year</b>	<b>Performance</b>
1990s	Generated nearly 60 million jobs
2002	2.4 million POEs, employing 34.1 million people
2004	1.98 million POEs in the secondary and tertiary industries, exported over US\$101 billion with 68.6% annual growth rate
2005	Contributed half of the country's wealth
2006	4.0869 million POEs, employed 63.95 million people, with US\$931 billion total registered capital

Source: Asiaweek, 2001; GOV, 2005; Lang & Hu, 2004; The NBSC, 2005; Xinhua, 2006.

Despite their important contributions to the nation's prosperity and wealth, POEs are in a comparatively disadvantaged position. It is well known that SOEs receive enormous assistance from the central government, but less known is that COEs rely on local governments to secure resources, to access to credit capital and social networks, and to receive subsidies as well as political protection. In comparison to SOEs and COEs, POEs are relying on their own performance to survive and grow in the market (Nee, 1992). With the growing competition for factor resources and markets, they face difficulties in getting access to finance and critical resources. Schiffer and Weder (2001) reported that these small firms' most severe obstacle for doing business is financing, followed by taxes and regulations. Domestic private firms receive less than 10% of total bank lending, while SOEs borrowed more than 65% of banks' loans, producing just 25% of the country's output (Terrill, 2006; Zhao, 2006). In terms of taxes, POEs are experiencing discriminatory treatment. The maximum tax on POEs is as high as 84%, while the comparable number is 55% for SOEs and COEs. Foreign funded ventures can even enjoy tax-free status. This could be for a couple of years depending on the industry type and the location in China (China Business Information Network, 1997).

In the past few years, the Chinese government has reformed SOEs and repealed unfavourable policies, to create a competitive environment in which POEs can develop; this has included removing their financing, market-entry, legal and political constraints (Asiaweek, 2001). China's entry into the World Trade Organization (WTO) provides both challenges and opportunities for Chinese enterprises, including POEs. On the one hand, they will face fierce competition as a result of the opening market. On the other

hand, they will enjoy more development opportunities, from the rule of law and trading rights governed by the WTO regulations.

### **2.2.3 SMEs' Contributions to China's Economic Development**

In China, POEs are almost exclusively SMEs. The development of SMEs is vital to China's stable economic growth and dynamic industrial expansion. Compared to other Western countries, the development of Chinese SMEs has a relative short history, less than 30 years. In the 1970s, Deng Xiaoping reformed the economy. Since then, the number of SMEs has grown rapidly. However, there are inconsistent figures on the number of SMEs due to different definitions and collection methodologies (see Table 2.5). According to the National Development and Reform Commission (NDRC), there were 10,000 private sector SMEs in 1990, and the number grew to 3.65 million in 2004 (Hall, 2007, p. 30). Figures from the NBSC indicated that, by March 2002, the number of SMEs in China had exceeded 8 million, accounting for 99.4% of Chinese firms. About 60% of the national industrial output value and 40% of the national revenues came from these SMEs, which employed about 75% of the workforce in China's cities and towns (Xinhua, 2002, p. 30). Their Economic Census in 2006 revealed that there were 39 million private sector SMEs in 2004 (Hall, 2007). These figures are much higher than the data collected by NDRC. Currently, it is officially recognised that there are approximately 40 million SMEs (Hall, 2007). However, it is argued that this number has included individually-owned enterprises and self employed individuals. The precise number of SMEs with reasonable scale operations was 3.6 million in 2003, which increased to 4.3 million in 2006. It was reported that these SMEs generated 58% of the

nation's GDP, contributed 50% of the country's tax revenues, and created 75% of the country's jobs (CBI Enterprise Institute, 2007).

<b>Table 2.5: Number of SMEs in China</b>	
<b>NDRC</b>	<ul style="list-style-type: none"> <li>• 10,000 SMEs in 1990</li> <li>• 3.65 million in 2004</li> </ul>
<b>NBSC</b>	<ul style="list-style-type: none"> <li>• Over 8 million by March 2002</li> <li>• 39 million in 2004</li> </ul>
<b>CBI Enterprise Institute</b>	<ul style="list-style-type: none"> <li>• 3.6 million in 2003</li> <li>• 4.3 million in 2006</li> </ul>

Source: CBI Enterprise Institute, 2007; Hall, 2007, p. 30; Xinhua, 2002, p. 30.

## **2.2.4 Chinese Firms' Internationalisation Patterns**

In recent years, many Chinese firms have actively participated in the global marketplace. Nevertheless, they have been subject to limited research. Previous studies in the area are generally descriptive in nature and based on secondary data. By reviewing the existing academic research related to the internationalisation of Chinese firms, two features can be identified.

### ***2.2.4.(1) Active Governmental Involvement***

Similar to other developing and transition economies, which are typically characterised by active governmental involvement in business (Peng, 2000), China's increasing international involvement would not have been made possible without the government's participation. Before the mid-1980s, international trade was restricted and regulated. In the early 1990s, it was stated that "the Chinese authorities regard rapid economic growth

as critical for maintaining social stability, so helping firms pursue commercial opportunities overseas is seen as advancing national goals” (SMS, 2007, p. 9). Therefore, the Chinese government developed the *Go Out Policy* to encourage domestic enterprises to expand their investments abroad and to directly invest overseas (Wu, 2005). In 1999, the *Go Global Campaign* was launched, to actively encourage more enterprises to invest overseas in order to improve their international competitiveness. In addition to relaxing the approval process for outward FDI, other incentives have been employed, including export tax rebates, subsidies, foreign exchange assistance, national bank loans with preferential terms, and better access to the domestic market for goods produced by Chinese overseas affiliates (Child & Rodrigues, 2005). Even though many apparently similar policies had emerged in the 1980s and 1990s, many of them were minor adjustment of a political or administrative nature. It was not until 2005, when the Chinese government relaxed foreign exchange restrictions and the review of overseas investment, as well as creating government funds to support Chinese firms to invest overseas, that Chinese outward FDI started to increase substantially (Bomal, Faramin, Perez, & Zhao, 2007). However, state policies of stimulating international activities also created problems, such as internal price controls, exchange rate controls, constraints on domestic expansion as a result of regional protectionism, distortion of sector development and volatility in the macro-economic environment (Young, Huang, & McDermott, 1996).

Aside from the economic motivations behind international expansion, political and diplomatic motivations are also crucial (Qi, 1999). It is argued that China hopes to make use of overseas investment to develop interaction and collaboration with other countries,

thereby enhancing China's international economic and political influence (Wang, 2002). These motivations can be observed in the way in which the Chinese government developed its policies. In order to create a better environment for its enterprises to conduct business internationally, the Chinese government had signed "bilateral investment treaties with 103 countries and double taxation treaties with 68 countries" by early 2003 (Wang, 2002, p. 3). As a result, Chinese enterprises could be found in most countries on earth. In the meantime, "lists of target countries and sectors where investment is encouraged" were developed identifying countries that have resources and technology China lacks (Wang, 2002, p. 12). This led to clear geographical concentrations. Geographically close markets, mainly in South East Asia, and emerging markets represented the most popular destinations (Bomal et al., 2007; see also Exhibit 1 in Appendix A).

The three industrial sectors with the most investment in FDI are the resource, manufacturing and IT sectors (Bomal et al., 2007). Previously, the Chinese government encouraged enterprises to develop and utilise overseas natural resources and raw materials, and especially promoted the internationalisation of strategic sectors such as power generation, mining, automobiles, electronics, iron, steel, machinery, chemicals, construction, transport, aerospace and pharmaceuticals. Firms in these sectors have been given economic and political incentives. Special motivations were given to these enterprise-groups including high levels of protection and generous state financial support, as well as special rights in management autonomy, profit retention and investment decisions (Nolan, 2001). Later, the government encouraged firms to establish

manufacturing bases and marketing networks overseas. The policy was then shifted to encourage firms in service industries such as trading, banking, insurance, telecommunication services and logistics to participate in overseas markets. In recent years, the FDI policy has shifted direction by encouraging enterprises to establish R&D centres in developed countries, reflecting the desire of the Chinese government to create world class companies and brands (Bomal et al., 2007).

#### ***2.2.4.(2) Pushed and Pulled to Internationalise***

It is widely assumed that Western enterprises enjoy strengths in their domestic markets before they internationalise, and that they also have competitive advantages in the host markets, which allow them to overcome the liability of foreignness in foreign markets (Dunning, 1988). In contrast, Chinese enterprises are facing increased competition and declining profit margins in the home market, as foreign giants began flooding in to the Chinese market. Competition has been even more intensive after China entered the WTO in 2001. In the meantime, many of the firms in China are relatively young, so they are being hit with outside competition before they have become settled – especially with the rapidly-changing regulatory and policy environment. In the face of increasing domestic and foreign competition in the home market, going overseas to seek global cooperation may be a survival strategy for them. Similar strategies have been necessary for other industries facing intensive competition, for example, Japanese automotive firms faced with a saturated home market (Rose & Ito, 2008).

Internationally, Chinese firms are found investing in developed countries where they have no apparent competitive advantages over their Western competitors, due to administrative constraints from the home government over their operations, resource constraints, technology constraints, and knowledge constraints. They can utilise advantages such as low raw materials costs and low labour costs in China, however, these advantages tend to be limited to products that contain a high proportion of technologically lower or labour-intensive components. They are less critical for predominately highly technological products in more sophisticated markets (Child & Rodrigues, 2005). Therefore, many Chinese firms are going overseas not to exploit their competitive advantages but to gain knowledge, and to avoid the competitive disadvantages they are facing in the domestic market (Boisot, 2004).

Looking at the phenomenon of Chinese large firms' internationalisation, a study conducted by the Roland Berger Strategy Consultants found that there are both push and pull factors influencing the international activities of China's 50 "industry-leading" firms (Keller & Wei, 2003). Similar to firms from other countries, the studied Chinese MNEs were motivated to seek new markets, secure resources, obtain technology, and secure access to raw materials and natural resources; see Exhibit 2 in Appendix A. The fast growth of China requires enormous amounts of raw materials. Government authorities encourage large SOEs to undertake outward direct investment, in order to secure raw materials to meet the demand of the country's rapid economic growth. The Roland Berger survey showed that 20% of the participating enterprises go overseas for the purpose of securing resources such as iron ore, aluminium and oil; see Exhibit 3 in



Appendix A. This corresponds to the fact that, in 2003, approximately 25 to 30% of China's outward FDI went to resource-rich countries, namely Australia, Canada, Indonesia, Peru and Russia (Wu, 2005). Most Chinese firms are relative latecomers to internationalisation, with outdated technology, weakness in R&D, limited marketing capability, unsophisticated management skills, liability of foreignness, and a lack of internationally recognised brand names (Nolan, 2001). These are clearly their disadvantages. Internationalisation is a strategy for them to obtain access to advanced foreign technology, managerial know-how, R&D establishments, distribution networks, and even brand names in developed economies. To achieve these purposes, mergers and acquisitions (M&As) are increasingly becoming an important form of entering overseas markets. In addition, other motives that have been identified include diversification-seeking and strategic asset-seeking (Deng, 2004).

## **2.2.5 The Economic Performance of the Three Provinces Studied**

### ***2.2.5.(1) Guangdong Province***

Guangdong province is located on the southern coast of China. One of the country's most populous provinces, it exceeded 100 million residents in January 2005. As the biggest industrial zone in China, Guangdong province has experienced strong growth, and has become one of the richest provinces in the country, ranking first for GDP and sixth for per capita GDP in 2005. For 2007, its GDP was US\$422 billion, with an annual growth rate of 14.5%, contributing about 12.5% of the total national economic output. Guangdong's economy is based on manufacturing and exporting. It has the largest

international trade volume in China. In 2004, Guangdong's international trade volume was US\$357.13 billion, which increased 26% compared to 2003. The sizes of exports and imports were US\$191.56 billion and US\$165.58 billion with annual growth rates of 25.3% and 26.7%, respectively. In 2007, the province's foreign trade accounted for 29% of the country's total foreign trade, achieving a 20% annual growth rate (China Culture, 2008b; Guangdong statistical yearbook, 2007; National Bureau of Statistics of China, 2008).

Guangdong was economically backward before the economic reforms in 1978. Deng Xiaoping's *Open Door Policy* enabled the province to take advantage of its access to the ocean, proximity to Hong Kong and Macao, and historical links to overseas Chinese. It has marked advantages in utilising overseas capital and technology, and in carrying out foreign economic and technical cooperation. Meanwhile, to change the province's backward economic situation, the central government placed relatively low taxation rates on it until the 1990s, when the Chinese taxation system was reformed. This favourable policy led the province to an economic boom. Previously, most industries in Guangdong concentrated on producing labour-intensive products. In recent years, with fierce competition coming from other provinces, Guangdong was no longer the biggest production base in China. Its provincial government has gradually adjusted the province's industrial structure, aiming to maintain its economic development. Effort has been expended at establishing nine industries, including electronics and information, electronics and mechanics, food and beverages, petroleum, chemistry, construction materials, papermaking, medicine and automobiles. In 2004, these nine industries

accounted for 75.8% of the province's industrial output, while machinery and electronic products accounted for 67.7% of the province's total exports (China Knowledge, 2008b).

As one of the first provinces that were opened to the outside world, Guangdong has become the investment destination for many foreign firms. By 2004, it had drawn more than US\$150 billion of inward FDI (News Guangdong, 2008). Firms in Guangdong are also outward orientated. In 2005, its value of overseas direct investment was nearly US\$113 million, ranking fourth among China's provinces and cities (MOFCOM, 2006). The five largest export markets of Guangdong businesses are Hong Kong, the United States of America, Japan, the European Union, and ASEAN. About 86% of the province's exports went to these markets in 2004. Meanwhile, exports to Africa, South America and Russia have increased rapidly in recent years (China Knowledge, 2008b) (refer to Table 2.6).

<i><b>Table 2.6: Guangdong province</b></i>	
<b>Location</b>	On the southern coast of China
<b>Population</b>	Over 100 million residents in January 2005
<b>GDP</b>	US\$422 billion with an annual growth rate of 14.5% in 2007
<b>Foreign trade</b>	US\$357.13 billion in 2004
<b>Inward FDI</b>	Over US\$150 billion by 2004
<b>Outward FDI</b>	Nearly US\$113 million in 2005
<b>Main export markets</b>	<ul style="list-style-type: none"> <li>• Hong Kong</li> <li>• the United States of America</li> <li>• Japan</li> <li>• the European Union</li> <li>• ASEAN</li> </ul>

<b>Main industries</b>	<ul style="list-style-type: none"> <li>• Electronics and information</li> <li>• Electronics and mechanics</li> <li>• Food and beverages</li> <li>• Petroleum</li> <li>• Chemistry</li> <li>• Construction materials</li> <li>• Papermaking</li> <li>• Medicine</li> <li>• Automobiles</li> </ul>
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Source: China Culture, 2008b; China Knowledge, 2008b; Guangdong statistical yearbook, 2007; National Bureau of Statistics of China, 2008; News Guangdong, 2008; MOFCOM, 2006.

#### ***2.2.5.(2) Fujian Province***

Fujian province is located on the south-eastern coast of China, with a population of 34.66 million. Its economy has benefited from the geographic and cultural proximity to Taiwan. It is one of the wealthier provinces in China, ranking eleventh in 2003 for GDP and seventh for per capita GDP. Over the past decade, its GDP has grown by 12.5%, on average. In 2006, its nominal GDP was US\$94 billion, with a 13% annual growth rate (Invest in Fujian China, 2008; National Bureau of Statistics of China, 2008).

In 2000, the total value of imports and exports from Fujian province was US\$21.223 billion, which rapidly grew to US\$47.55 billion in 2004, with import value of US\$18.15 billion and export value of US\$29.4 billion. The province's major industries include building materials, forestry, light industry, electronics, chemicals, machinery and papermaking (China Culture, 2008a). In 2004, exports of machine and electronic products were US\$13.13 billion, which increased 43.1%, while exports of high-tech products increased by 46.9% to US\$6.84 billion (China Knowledge, 2008a).

Fujian province plays an important role in the country's international trade. It has established business relationships with more than 200 countries and regions in the world. In 2005, it had invested over US\$72 million in overseas, which made it the eighth largest regional investor in China (MOFCOM, 2006). For inward FDI, there were 1,723 foreign enterprises approved to invest in the province, with a total contracted foreign capital of US\$9,449 million in 2007 (East China Fair, 2008a) (see Table 2.7).

<b>Table 2.7: Fujian province</b>	
<b>Location</b>	On the south-eastern coast of China
<b>Population</b>	34.66 million
<b>GDP</b>	US\$94 billion with an annual growth rate of 13% in 2006
<b>Foreign trade</b>	US\$21.223 billion in 2000, US\$47.55 billion in 2004
<b>Inward FDI</b>	US\$9,449 million in 2007
<b>Outward FDI</b>	Over US\$72 million in 2005
<b>Main industries</b>	<ul style="list-style-type: none"> <li>• Building materials</li> <li>• Forestry</li> <li>• Light industry</li> <li>• Electronics</li> <li>• Chemicals</li> <li>• Machinery</li> <li>• Papermaking</li> </ul>

Source: China Culture, 2008a; China Knowledge, 2008a; East China Fair, 2008a; Invest in Fujian China, 2008; National Bureau of Statistics of China, 2008; MOFCOM, 2006.

### ***2.2.5.(3) Zhejiang Province***

Zhejiang is an eastern coastal province. It has a population of 47.2 million. Since the reform and opening up in 1978, Zhejiang has becoming one of the most dynamic provinces, with the fastest economic growth rate. From 1978 to 2002, its GDP and per

capita GDP grew with annual rates of 13% and 12.1%, respectively, placing it fourth among all provinces. Currently, it is one of the richest provinces in China, with its nominal GDP reaching US\$245.1 billion and a per capita GDP of US\$5,000 in 2007 (East China Fair, 2008b; Zhejiang China, 2008).

Zhejiang has long been a province mainly dependent on agriculture. It has transformed into a province of strong economy, with industry as the main sector over the past 20 more years. Its manufacturing is centred upon electromechanical industries, textiles, chemical industries, food, and construction materials. Zhejiang has attracted a host of foreign investors in a variety of sectors, including garments, chemicals, plastics, metals, and fibres. It also has become the second largest regional investor of outward FDI. China's official statistics showed that its value of foreign investment reached almost US\$184 million in 2005 (MOFCOM, 2006). The majority of Zhejiang's manufactured products are exported. In 2004, Zhejiang's exports reached US\$58.16 billion, while imports reached US\$27.07 billion, both with nearly 40% annual increases. In 2007, the volume of exports grew to US\$128.3 billion, and the volume of imports reached US\$48.5 billion. The export of electronic and mechanical products and high-tech products grew much faster than that of other export products, amounting to US\$21.71 billion and US\$3.87 billion in 2004, with 51.6% and 79.7% more than 2003, respectively. Zhejiang has established direct economic and trade relations with 221 countries or regions. The United States of America, Hong Kong, the European Union and Japan are Zhejiang's four main export markets (China Knowledge, 2008c, 2008d; East China Fair, 2008b).

The province's fast development has been driven by hard work, an entrepreneurial spirit, low labour costs, and an eye for the world market. In recent years, it has followed its own development model, called the "Zhejiang Model", which gives priority to the development of entrepreneurship, emphasises small businesses that are responsive to the market, invests heavily in infrastructure, and produces low cost goods in bulk for both domestic consumption and export. Compared to other provinces in China, Zhejiang's private sector is well developed. The sector contributed 55.1% to its GDP in 2004. Since 2003, many Zhejiang POEs started to undertake international business. In 2004, they already accounted for 41% of the province's exports, the volume grew to US\$61.9 billion in 2007 (China Knowledge, 2008d; Lu, 2007) (see Table 2.8).

<b>Table 2.8: Zhejiang province</b>	
<b>Location</b>	On the eastern coast of China
<b>Population</b>	47.2 million
<b>GDP</b>	US\$245.1 billion in 2007
<b>Exports</b>	<ul style="list-style-type: none"> <li>• US\$58.16 billion in 2004</li> <li>• US\$128.3 billion in 2007</li> </ul>
<b>Imports</b>	<ul style="list-style-type: none"> <li>• US\$27.07 billion in 2004</li> <li>• US\$48.5 billion in 2007</li> </ul>
<b>Outward FDI</b>	US\$184 million in 2005
<b>Private sector</b>	<ul style="list-style-type: none"> <li>• Contributed 55.1% to the province's GDP in 2004</li> <li>• Exported US\$61.9 billion in 2007</li> </ul>
<b>Main export markets</b>	<ul style="list-style-type: none"> <li>• the United States of America</li> <li>• Hong Kong</li> <li>• the European Union</li> <li>• Japan</li> </ul>
<b>Main inward FDI industries</b>	<ul style="list-style-type: none"> <li>• Garments</li> <li>• Chemicals</li> <li>• Plastics</li> <li>• Metals</li> </ul>

	<ul style="list-style-type: none"> <li>• Fibres</li> </ul>
<b>Main industries</b>	<ul style="list-style-type: none"> <li>• Electromechanical industries</li> <li>• Textiles</li> <li>• Chemicals</li> <li>• Food</li> <li>• Construction materials</li> </ul>

Source: China Knowledge, 2008c, 2008d; East China Fair, 2008b; Lu, 2007; MOFCOM, 2006; Zhejiang China, 2008.

## 2.2.6 Synthesis

In recent years, many Chinese firms actively participated in the global marketplace. However, there is relatively limited research into the area, due to the fact that Chinese firms' internationalisation is still a new phenomenon and Western academics lack access to Chinese firms. Earlier studies concerning Chinese firms' internationalisation have been mainly descriptive in nature, with their focus on MNEs and SOEs. What had not been recognised in the academic literature is the importance of the many small and medium-sized POEs engaged in international business. Given that China's further integration into global production networks and commitment toward economic reform, there is reason to believe that POE's internationalisation will greatly increase in the next few years. This would lead to their further contributions to the nation's wealth. In this sense, the internationalisation of POEs is a very important issue that is worth research attention. The preceding sections have provided evidence demonstrating that the Chinese market is huge, with fast growing potential. Despite the large and rapidly-developing market at home, many POEs opt to engage in international business, which raises interesting questions concerning the motives and the influential factors that lead to internationalisation, the objectives they have for participating in international operations, the approaches they



apply for realising international objectives, and the criteria they use to select foreign markets and evaluate international opportunities. This study seeks to answer these questions through qualitative research.

## **2.3 Summary**

SMEs have a critical role in the global marketplace. The number of SMEs engaged in international operations has increased dramatically, although many of them have inherent disadvantages arising from shortage of resources and experience. Despite their international performance, limited research has been conducted to conceptualise their international behaviours. This indicates that the internationalisation of SMEs is a very important issue that is worth research attention. This chapter has presented secondary data to emphasise the importance of understanding the internationalisation behaviours of Chinese firms, especially small and medium-sized POEs. In recent years, many Chinese POEs have actively participated in international operations, regardless of their large domestic market. This chapter provided evidence to show that this is a new phenomenon, given that China just opened its doors to the rest of world three decades ago. It also represents an important research area, as POEs are facing competitive disadvantages in the domestic market, and experiencing difficulties in achieving internationalisation, due to government restrictions. This research seeks to identify the initiatives behind the internationalisation of Chinese POEs, the factors that influence their internationalisation, and the approaches they use to achieve internationalisation.

Information provided in this chapter lays the foundation for the upcoming chapters. With this background information in mind, it is easier to appreciate Chinese POEs' internationalisation behaviours. The next chapter will review the literature concerning firms' internationalisation, with an emphasis on SMEs.

# Chapter 3 Literature Review

## ***Introduction***

*This chapter reviews literature relevant to the research focus presented in Chapter 1. It contains four sections. The first section briefly reviews theoretical frameworks used to understand firms' internationalisation. The second section examines SMEs' internationalisation, with an emphasis on specific internationalisation approaches and determining factors that drive SMEs toward internationalisation. The third section discusses literature on how small firms internationalise, focusing on the Uppsala School's process model (U-model) and the International New Ventures (INVs) framework. A comparison of these two frameworks is provided. The last section summarises the chapter in the context of the thesis.*

## **3.1 What is Internationalisation?**

Internationalisation has been a focus of research since the 18th century; systematic research in the field started in the late 1960s. Many scholars with different disciplinary backgrounds have studied firms' activities across national boundaries aiming to conceptualise the phenomenon. Existing models and theories drawing from multidisciplinary theoretical foundations offer valuable insights in explaining internationalisation from different perspectives. Due to its dynamic and complex nature, there is no one school of research can exclusively explain the phenomenon (Coviello & McAuley, 1999). This results in a vague definition of internationalisation. The most cited

definition is offered by Welch and Luostarinen (1988), who defined it as the process through which a firm increases its international involvement in overseas operations.

The different models and theories concerning internationalisation in the literature include the economic perspective, the behavioural school, the process-based perspective, and the holistic view (Coviello & McAuley, 1999). The economic perspective views internationalisation from an economic perspective, arguing that internationalisation decisions are based on economic analysis. Prominent examples include the internalisation theory, the transaction cost model, the eclectic paradigm and the resource-based approach. The internalisation theory has its foundations in the recognition of market imperfections (Hymer, 1960; Kindleberger, 1969). It argues that there are transaction costs associated with international business. To overcome issues such as governmental intervention and to minimise transaction costs, firms can internalise their value-adding activities across national borders (Buckley & Casson, 1976). This provides an explanation for why MNEs exist (Coase, 1937). Similarly, the transaction cost perspective argues that firms aim to minimise transaction costs associated with internationalisation (Hennart, 1982). The eclectic paradigm (Dunning, 1988) further explains factors that affect a company's decision with respect to going international through FDI. Three distinct sets of advantages that determine the involvement of firms in foreign production: ownership-specific advantages, location advantages and internalisation advantages. The eclectic paradigm proposes that companies are motivated to get involved in overseas investment and production by a mixture of these factors. Finally, the resource-based approach is

based on the view that firms make international decisions based on unique resources they possess (Barney, 1991; Wernerfelt, 1984).

The behavioural school perceives internationalisation as an evolutionary process (Melin, 1992). Representative models are the U-model and the network approach. The U-model explains internationalisation as a gradual development process. Firms enter foreign markets systematically and sequentially, with a varying number of stages; each stage involves an increased commitment to international involvement (Andersen, 1993; Johanson & Vahlne, 1977). The network approach (Johanson & Mattsson, 1988) draws on the theories of social exchange and resource dependency. It assumes that a firm's active networks are the main driving force of its internationalisation. The third view is the process-based perspective, which contends that internationalisation involves both inward and outward activities. Firms' foreign market selection and entry mode selection are related to their market offering, organisational capacity, personnel and structure (Welch & Luostarinen, 1988).

Finally, the holistic view incorporates all the other three views. This perspective defines internationalisation as "*the process by which firms both increase their awareness of the direct and indirect influence of international transactions on their future, and establish and conduct transactions with other countries*" (Beamish, 1990, p. 77, cf, Coviello & McAuley, 1999, p. 225). Some scholars also argued that internationalisation is not always about forward progression. Firms might withdraw their involvement in international

operations for strategic and financial purposes (Benito, 1997; Fletcher, 2001; Welch & Luostarinen, 1988).

In the 1990s, there was a new phenomenon, the emergence of international new ventures (INVs). This type of firm internationalises rapidly from inception, aiming to derive competitive advantages across nations very early in its history (Oviatt & McDougall, 1994). INVs' international behaviours have challenged traditional internationalisation theories. Various studies have been conducted to understand this phenomenon. Previous studies emphasise the role and influence of entrepreneurs in international business transactions.

### **3.1.1 Synthesis**

Within the international business domain, the various theoretical perspectives have attracted both support and criticism. That is partly because they were developed within specific contexts, to explain certain behaviours among internationalised firms. When the studied context and the focus of research are changed, the frameworks' utility is often controversial. In summary, the economic perspective emphasises the importance of internalising international activities. The behavioural school focuses on the processes by which firms change stages from domestic operations to FDI as a result of managerial learning. It recognises the need to externalise certain activities when firms lack international experience and knowledge. The emergence of INVs challenges these theoretical perspectives through rapid internationalisation and through selecting alternative governance structures. The economic perspective is formulated, in general,

with large firms in mind, while the behavioural school and the INVs framework are more able to explain small and medium-sized firms' internationalisation activities. Since the purpose of this study is to explore small POEs' internationalisation behaviours in China, the following sections will review literature that focuses on SMEs' internationalisation.

### **3.2 Literature on SMEs' Internationalisation**

Since the 1980s, research on the internationalisation of SMEs has increased, given that SMEs are playing a critical role in the international arena (Manolova, Brush, Edelman, & Greene, 2002). Although research on SMEs' internationalisation has a relatively short history, three schools of research can be identified: (a) internationalisation process, (b) export development, and (c) international entrepreneurship (Manolova, Brush, Edelman, & Greene, 2002, p. 11). The internationalisation process school has its focus on how SMEs progress in terms of foreign market selection and entry mode selection (Johanson & Vahlne, 1977; Melin, 1992). In addition, there is a large body of literature pertaining to exporting. The export development school examines factors that drive or hamper SMEs with respect to undertaking exporting, factors that affect their export behaviours, and how they expand their export activities (Cavusgil, 1984a; Cavusgil, 1984b; Crick & Chaudhry, 1997). Recently, many small firms have begun starting international activities while still young, which has drawn scholars to investigate their motives for rapid internationalisation. Previous studies have highlighted the role that individuals play in the process (Bloodgood, Sapienza, & Almeida, 1996; McDougall, Shane, & Oviatt, 1994).

In summary, the three schools are all seeking answers for the following questions:

- What motivates SMEs to undertake international operations?
- What factors impact on their internationalisation decisions? and
- How do they internationalise?

The following sections will review the literature on each of these areas.

### **3.2.1 SMEs' Internationalisation Motives and Approaches**

#### ***3.2.1.(1) Exporting***

Despite that many SMEs have international operations, many other SMEs focus strictly on their domestic markets. For firms that are involved in international business, internationalisation presents enormous challenges, along with opportunities for growth and wealth. These challenges create interest in discovering the motives behind SMEs' decisions regarding international engagement. Traditionally, it is regarded that the internationalisation of firms is most likely to start with exporting, as it involves lower resource commitment, less risk and offers more flexibility to withdraw from a market (Johanson & Wiedersheim-Paul, 1975; Kogut & Chang, 1996). Hollensen (2007, p. 42-48) classified firms' initial motives to start exporting, as proactive or reactive. Proactive motives occur when firms aim to exploit their unique competences through international operations. Examples include firms' managerial desire to engage in international operations; desire for profits and growth; and intentions to exploit unique technology and products, utilise foreign market opportunities, sustain economies of scale, and gain tax benefits. On the other hand, some firms might be pushed to internationalise, as they are



exposed to pressures or threats in the market. These decisions to internationalise may be based on reactions to competitive pressures, a small and saturated domestic market, overproduction, unsolicited foreign orders, extending sales of seasonal products, or proximity to international customers.

### ***3.2.1.(2) Foreign Direct Investment***

In contrast to exporting, FDI requires larger amounts of capital investment offshore and therefore involves more risk. However, many firms consider FDI as an attractive strategy. Through internalising foreign activities, firms can increase their control over foreign operations, receive higher rates of return, utilise location advantages from host countries, develop new knowledge, and reduce their transaction costs. The motives for firms to undertake FDI can be categorised as market-oriented, cost-oriented, and the acquisition of key inputs, according to Dunning's (1993) eclectic paradigm. Firms are mainly pulled to undertake FDI in order to gain access to high growth potential markets, to avoid trade barriers, to achieve cost advantages through cost reductions, and to acquire key inputs such as raw materials, brands, managerial know-how, technology and R&D.

Similarly, Makino, Lau and Yeh (2002) categorised the motives of FDI into strategic asset-seeking, resource-seeking and market-seeking, from the perspectives of asset-exploitation and asset-seeking FDI. The asset-exploitation perspective views that firms own distinct resources. Through FDI, they can transfer their existing advantages across borders at low levels of transaction costs. By doing so, they can maximise their current returns. On the hand, the asset-seeking perspective views FDI as a strategy that firms

apply to obtain assets that they lack, from foreign countries, for the purpose of survival, learning, growth and development. Makino et al (2002) found that different motives influence Taiwanese firms' location choices, with firms tending to invest in developed countries when they are seeking strategic assets and markets, and in less developed countries when their motives are to seek low-cost labour.

Zitta and Powers (2003) studied the motivations of various sizes of firm in different industries from around the globe to undertake FDI in the United States of America. They differentiated FDI into factor-seeking and market-seeking, based upon firms' internationalisation objectives, and grouped motivations for FDI into two groups: external and internal. Regardless of the type of FDI, Zitta and Powers (2003) noted that the decision to conduct FDI is motivated by a mixture of factors, such as market size, capital markets, human resources, political climate, and the need for growth, profits and technology.

### ***3.2.1.(3) Intermediate Entry Modes***

Even though exporting requires relatively lower resource commitment and involves lower risk, export firms have limited control over their foreign activities, little contact with their foreign markets, and there are not many opportunities for experiential learning. Through FDI, firms can have greater control over their overseas operations and access to local assets. However, FDI requires firms to commit large amounts of resources and it also involves substantial risk (Bartlett & Ghoshal, 1998). As a result, some firms select intermediate entry modes to achieve internationalisation. Intermediate entry modes, such

as licensing, franchising, management contracts, JVs, and coalition, allow firms to learn knowledge and skills while not engaging in full ownership. For the last two decades, it has been noted that many small-sized firms have been undertaking rapid internationalisation. Studies have found that these quickly-internationalising SMEs rely on hybrid structures to initiate global business. They utilise networks strategically to overcome constraints associated with resources and experience, thereby realising growth and value creation through international operations (Coviello & Munro, 1997; Oviatt & McDougall, 1994). Also, through networking, these small firms are able to share risk, reduce uncertainty, and gain important knowledge of their host countries and access to key assets, and therefore further build their competences.

#### ***3.2.1.(4) Synthesis***

There are various entry modes firms can apply to enter foreign markets. They can internationalise through exporting, FDI, or using other intermediate entry modes. These different entry modes are associated with different degree of risk, control level, resource commitment, and return from investment. As a result, the selection of an internationalisation approach requires the evaluation of these factors, along with others that have been found to be related to firms' internationalisation activities. The following sections will review these factors individually.

### **3.2.2 Factors Influencing SMEs' Internationalisation**

In spite of SME's small characteristics, many of them are actively engaged in the international arena. A large body of empirical research has been conducted to identify factors that facilitate or hamper these small firms with respect to internationalisation.

These factors can be differentiated as:

- Global environmental conditions
- Home country variables
- Host country factors
- Industry attributes
- Firm characteristics and
- Individual characteristics

In reality, these factors are interrelated, in terms of influencing firms' internationalisation performance.

#### ***3.2.2.(1) Global Environmental Factors***

Various changes in the global environment have driven SMEs toward internationalisation. Firstly, market factors such as the fall of trade barriers, accompanied with harmonisation in business practices, make markets link between countries more efficiently, which allow firms to gain easier access to foreign markets and reduce both the costs and the risk of international business (Reynolds, 1997; Whitelock & Munday, 1993). Human capital is more internationally mobile, which allows firms to quickly gain foreign market knowledge through recruitment (Autio, 2005). Nevertheless, globalisation is a challenge

for SMEs as it forces them to compete with firms from everywhere in the world regardless of size, both at home and abroad (Etemad, 2004). Secondly, fast development of technology has led to lower communication and transportation costs. This enhances firms' ability to coordinate cross-border activities, which in turn enables them to compete with MNEs in the global market (Holstein, 1992; Madsen & Servais, 1997). Thirdly, the rapid changes in technology, the highly technological complexity and the high cost of R&D lead to a trend to form global networks, which also facilitate the involvement of SMEs in the global arena (OECD, 2002). Establishing partnerships with suppliers, distributors, trading companies and so forth help small firms to reduce market uncertainty. Through networks, SMEs can supply their goods and services in the global level, and so take advantages of scale and scope to increase their return on investment. Fourthly, there is an increasing role for niche markets (Knight, 2000; Oviatt & McDougall, 1995). SMEs exploit their unique competencies and target these niche markets to avoid direct competition with larger firms. Moreover, the increase in cultural convergence has also made it easier for SMEs to target these niche markets internationally (Hedlund & Adne, 1985).

### ***3.2.2.(2) Home Country Factors***

The size of the home market is associated with the firm's decisions in its international operations. Insufficient local market opportunities and home market saturation act as pushing motives for a firm to seek overseas market opportunities. Through foreign market expansion, the firm would be able to gain economies of scale and scope, and thereby sustain economic growth (Hollensen, 2007; Kuo & Li, 2003). On the other hand,

the firm might decide not to go abroad when the domestic market generates sufficient business for it to grow (Fillis, 2002), or when it receives significant competitive protection from the government (OECD, 1997).

Studies also demonstrated that public policy initiatives and labour costs affect firms' international activities. Shaw and Darroch (2004) studied 516 New Zealand entrepreneurial new ventures' perceptions of barriers to internationalisation. Findings revealed that the lack of government assistance is one of the top barriers that impede New Zealand firms' to go abroad. Liu and Shu (2003) used secondary data to examine the impact of industry factors on export performance across industries in China. They concluded that low labour costs are a significant advantage that Chinese firms utilise to compete in international markets. Buckley et al. (2007) also found an impact of changes in China's policy on Chinese outward FDI location choices.

### ***3.2.2.(3) Host Country Factors***

Host country characteristics are related to the choice of location for foreign activities. Conventional studies revealed that factors such as production costs, market potential, exchange rates and political factors of the host country determine the size and the structure of foreign investment flows. Kinoshita (1998) reported that the policy environment is the most critical determinant of Japanese FDI location decisions in Asia, while cheap labour cost is not influential. In contrast, other studies of Taiwanese SMEs' FDI determinants found that the motives to utilise abundant host country labour resources

and low production costs increased the probability that they would conduct FDI (Kuo & Li, 2003; Wei & Christodoulou, 1997).

Buckley et al. (2007) used secondary data to examine factors that influence Chinese outward FDI location choices for the period of 1984 to 2001. Their results indicated that Chinese firms' outward FDI location choices are related to foreign market size, geographic proximity, trade volume between China and the host country, exchange rate, inflation rate, level of political risk, natural resources endowments, and market openness in the host country.

#### ***3.2.2.(4) Industry Factors***

Industry attributes are found to influence firms' international behaviours. Among those attributes, the nature of industrial competition is found to play a critical role. According to the oligopolistic reaction theory, firms' international activities are largely influenced by their competitors' movement (Knickerbocker, 1973). Mascarenhas (1986) pointed out that non-dominant firms in a variety of industries in the United States of America pursue international strategy to avoid domestic competition with market leaders. Ito and Rose (2002) investigated large MNEs' competition behaviours in the global tire industry. The study provided evidence of oligopolistic reaction behaviour. It revealed that FDI decisions were related to the industry's competition intensiveness in terms of competitor numbers and the relative strength of the incumbents' market positions.

Meanwhile, firms from different industrial sectors might have different international behaviours. Traditionally, due to the distinctive characteristics of service, service firms are assumed to have different international entry modes compared to manufacturing firms. For manufacturing firms, internationalisation process is assumed to start with exporting, which gradually progresses to FDI (Johanson & Wiedersheim-Paul, 1975), while many service firms start their international process with partnerships and JVs (Coviello & Munro, 1997). What is more, industry conditions also have an impact on location selection. Chadee, Qiu and Rose (2003) studied the location choice of 6,430 foreign equity JVs in China between 1984 and 1996. Their findings showed the impact of industry attributes on the choice of locations, with service firms tend to invest in large cities with favourable economic environment.

### ***3.2.2.(5) Firm Factors***

Firms' internal resources have become the subject of research with the aim to discover their impacts on the firms' international performance. A substantial number of studies have found that firms' possession of unique assets have largely influenced their internationalisation speed (Rialp, Rialp, & Knight, 2005; Oviatt & McDougall, 1994) and decisions on foreign development (Dunning, 1988; Hymer, 1960). Bloodgood, Sapienza and Almeida (1996) noted firms that possess unique resources have a greater tendency toward internationalisation. Wernerfelt (1989) indicated that firms' resource constraints such as a shortage of labour or physical inputs, shortage of finance, lack of suitable investment opportunities, or lack of managerial capacity, limit their market selection and profit expectation.



Size of a firm is related to the available resources that the firm possesses. In FDI literature, firm size is emphasised as a determinant of FDI (Chen, 1992; Horst, 1972; Kuo & Li, 2003; Lall, 1986). Kinoshita (1998) investigated factors that determine Japanese manufacturing firms' FDI decisions in Asia. Results demonstrated that firm size is related to FDI location choices. Small firms tend to go to countries where labour cost is low and infrastructure is sufficient, while large firms are influenced by host country market size and strategic considerations when selecting locations. In export literature, firm size is also widely recognised as having an impact on firms' internationalisation decisions and performance. However, the relationship between the two variables is mixed. Westhead (1995) found that number of employees and sales revenue size are positively related to the propensity for a firm to be an exporter. Bilkey and Tesar (1977) however used the number of employees as a measure of size, and found a negative relationship between the two variables, as smaller firms are more likely to export. Cooper and Kleinschmidt (1985) also noted a negative relationship between organisational size and export growth. Nevertheless, other studies indicated that there is no significant relationship between firm size and degree of internationalisation (Bonaccorsi, 1992; Cavusgil, 1984). This evidence suggests that more empirical investigations on the effect of firm characteristics are worthwhile.

International performance is also influenced by a firm's previous foreign operation experience. Empirical studies demonstrated that previous overseas experience is positively associated with export volume (Denis & Depelteau, 1985), degree of aggressiveness toward exporting (da Rocha, Christensen, & da Cunha, 1990), and the

possibility of conducting FDI (Wei & Christodoulou, 1997). Similarly, Zhou (2007) examined newly founded Chinese privately-owned SMEs' early internationalisation. It was reported that the possession of foreign market knowledge is a mechanism that results in early and rapid internationalisation.

It is also noted that a firm's R&D intensity is tied to its international performance. Research revealed that there is a positive relationship between R&D intensity and export motives (Kalleberg & Leicht, 1991), export intensity (Cavusgil & Nevin, 1981), export performance (Simon, 1992), export growth (Cooper & Kleinschmidt, 1985), and FDI decisions (Kuo & Li, 2003). However, technology was found to have a negative impact on export intensity (Sriram, Neelankavil, & Moore, 1989). Learning is another influential factor. When a firm values the knowledge it could learn from international activities, it is more likely to increase its foreign participation (Burpitt & Rondinelli, 2000). Other studies have emphasised that a firm's organisational structure and its position in the domestic market affect its export activities (Cavusgil, 1984b; Crick, 1995), while network linkages direct its location choice for FDI (Chen & Chen, 1998).

### ***3.2.2.(6) Individual Factors***

Many studies have been conducted to detect how human capital influences a firm's competitive strategies and its international performance. Many studies have found that a firm's international behaviour is a function of managerial characteristics (Bloodgood, Sapienza, & Almeida, 1996; Cavusgil, 1984b; Perlmutter, 1969; Reid, 1981). Entrepreneurs' experience, skills and competencies have a significant impact on firms'

development (Cooper, 1981; Cooper, Gimeno-Gascon, & Woo, 1994; Storey, 1994). Their background and degree of foreign language experience are also related to the firms' international involvement (Barrett & Wilkinson, 1985; Simpson & Kujawa, 1974; Wei & Christodoulou, 1997). Firms with diverse management know-how may be able to identify more opportunities in foreign markets, and undertake more competitive strategies (Carter, Williams, & Reynolds, 1997).

Moreover, it is widely recognised that management attitudes and preferences toward internationalisation are highly correlated to firms' export activities. These include decision-makers' perceptions of risk and costs, their expectations of firm growth, market development, opportunities and profits. Their positive expectations toward internationalisation facilitate international activities (Bilkey & Tesar, 1977; Cavusgil, 1984b), while negative concerns act as barriers (Bauerschmidt, Sullivan, & Gillespie, 1985; Wei & Christodoulou, 1997).

### **3.2.2.(7) *Synthesis***

Many small firms take advantages of globalisation, and actively participate in foreign countries aiming to reap international opportunities. The existing literature provides some understanding of motives and influential factors toward internationalisation. However, of the studies on the motives for internationalisation, the majority is focused on the determinants of a particular international activity and limited to a particular industry. The research in this area can be enhanced by investigating the motives for various international activities across industries. Meanwhile, the research stream lacks a study of

why SMEs from developing countries participate in international operations. This study extends this stream of literature by investigating motives that influence Chinese POEs' attitudes toward various international activities across a range of industries.

Internationalisation is a dynamic and complex process. It involves a change of state and discontinuity. Numerous antecedent variables are found to play a role in a firm's internationalisation process, whose internationalisation outcomes are sensitive to the conditions of those variables. Anything changing in the global environment, home country, host country, industry, within the firm and management team may facilitate or impede a firm's international operations. These factors are also dependent on each other in influencing a firm's international performance. Nevertheless, conventional research has only investigated certain factors that were deemed to be influential, providing incomplete information on the issue. Moreover, conventional research examined influential factors of various international activities in an isolated manner. There is a need to incorporate all these factors when investigating their determinants on a firm's internationalisation decision in order to address the issue comprehensively.

To address these issues, this study explores influential factors of internationalisation through personal interviews. This approach allows one to explore potential influential variables arising from the macro global environment, national conditions, industry attributes, the dynamism of the firm base, and quality of entrepreneurship, as well as the relationships between these variables and a firm's international activities.

### **3.3 How do SMEs Internationalise?**

Among various schools of internationalisation, the U-model and the INVs perspective are the most influential frameworks internationally in recent years. These two frameworks explain how firms internationalise from different perspectives, which provide useful ideas and foundations toward our understanding of Chinese POEs' internationalisation. This section reviews previous work in the development of the two perspectives, which acts as a reference framework for analysing Chinese POEs' internationalisation processes in the upcoming chapters.

#### **3.3.1 The Uppsala School's Internationalisation Process Model**

According to Welch and Luostarinen (1988), internationalisation is the process through which a firm increases its international involvement in overseas operations. Different schools of thought have emerged in the literature to explain this process. Traditionally, all stage models explain the process as a gradual development process. Firms enter foreign markets systematically and sequentially through a varying number of stages, each stage involves an increased commitment to international involvement (Andersen, 1993; Johanson & Vahlne, 1977). The U-model was developed by researchers from the Uppsala University (Johanson & Vahlne, 1977; Johanson & Wiedersheim-Paul, 1975). It is also known as the "stage model", or "process theory of internationalisation" (Autio, 2005). It has become the most influential stage model.

Based on a study of four Swedish firms, Johanson and Wiedersheim-Paul (1975) asserted that a firm's involvement in a specific foreign market follows an establishment chain as following:

1. *No regular export activities*
2. *Export via independent representatives*
3. *Establishment of sales subsidiary*
4. *Full commitment of overseas production*

They argued that the internationalisation process is an evolutionary approach starting from the stage of ad hoc exports to more committed and riskier foreign market entry modes. Each stage represents a firm's increased commitment to its international transactions. Due to the lack of foreign market knowledge, high risk aversion and high perceived uncertainty, a firm internationalises in a slow and gradual manner. Meanwhile, in this model, the emphasis is on psychic distance (Grady & Land, 1996), which is defined as how differences in language, culture, education level and legislation are perceived to inhibit the flow of information between a firm and its foreign market. It suggests that a firm generally commences foreign activities in countries that are geographically and socio-culturally closest due to psychic distance. That is because the firm has little experiential knowledge about foreign operations, thus countries that have closer psychic distance to its home country are perceived less risky. In this vein, the firm can recognise more opportunities in the host countries and it has low uncertainty regarding doing business in those countries. In summary, the U-model describes the internationalisation process as evolving through geographical expansion, product and operational development.

Based on the behavioural theory (Aharoni, 1966) and the theory of firm growth (Penrose, 1959), Johanson and Vahlne (1977) further developed the U-model. They described the internationalisation process as a function of increased knowledge development and market commitment, while knowledge development and market commitment are interdependent. Market decisions and market knowledge affect a firm's current activities and its commitment to its foreign markets, while current activities and commitment decisions in turn influence the amount of knowledge that the firm gains and also its market commitment. The authors identified two kinds of knowledge regarding international operations: objective knowledge and experiential knowledge. Objective knowledge is transferable from one country to another and it is able to be taught as well; while experiential knowledge is firm specific and is acquired only through experiencing the market (Johanson & Vahlne, 1977, 1990).

The model is described as a learning model of the internationalisation process (Forsgren, 2002). It is assumed that a firm develops in the domestic market first, and starts foreign activities with low risk, low commitment and indirect exporting approach to psychically close markets. Over time, the firm learns about its foreign markets, the behaviours of its customers, suppliers, competitors and other stakeholders. It also gains knowledge about how to organise and develop its activities in the host market. The effect of this learning is that experience in the host market will increase the firm's stock of international management know-how, which can be used as a reference in other international markets. Furthermore, through experiencing foreign markets and foreign operations, the firm can easily discover and evaluate foreign business opportunities, learn what factors lead to

success, which lead to the reduction of uncertainty about foreign commitments (Chang, 1995).

As a firm gradually accumulates objective and experiential knowledge, integrates and uses the knowledge through its international involvement, reduces its perceived risk and uncertainty about foreign operations, it progressively increases its foreign market commitments. This is manifested in the markets entered and in the mechanisms used for market entry. The firm starts to enter more psychically distant countries. With the need to control operations in each specific country, it also starts to select riskier market entry modes, for instance, sales subsidiaries (Johanson & Vahlne, 1977). Its increase in foreign market commitments is also reflected in the firm's market offerings, organisational capacity, personnel and structure (Welch & Luostarinen, 1988), which further enhances its market knowledge, leading to commitment of more resources into the market and being more active in the market.

Internationalisation can be viewed as a dynamic cycle by repeating this process over and over again. It is a slow and incremental process as it takes time for the firm to learn about foreign markets and develop foreign operation skills. Compared to earlier studies, the role of psychic distance is reduced, while the concepts of commitment and knowledge are the foundation of the model. According to the model, additional market commitments are either made in small steps unless the firm has large resources, or market conditions are stable and homogeneous, so relevant market knowledge can be gained through means



other than experience, or the firm has considerable experience from markets with similar conditions (Johanson & Vahlne, 1977).

Johanson and Vahlne (1990, 2003) recognised that a firm is a system involving different types of actors. Changing and building relationships with its stakeholders will have played a critical role in its internationalisation process. They believed that a firm's set of network relationships facilitates its entry to new markets, and determines its international expansion nature. Entering new markets in turn provides it with opportunities to develop new relationships, which opens up new possibilities for further international expansion. Even though the process model of internationalisation has been extended to business relationship learning and commitment, it is still the result of the interaction between experiential knowledge development and commitment but with the concerns of relationship partners. Learning about each other, learning from each other, learning how to coordinate with each other, as well as learning how to build business networks are the foci of this model. The gradual increase in trust between firms is sustained by the coordination and commitments among actors. Commitments are made toward defending and developing existing relationships and network structures. In this model, the focus of learning and commitment-building shifted from previous uncertainty reduction to opportunity development (Johanson & Vahlne, 1990, 2003).

The conventional U-model of internationalisation has drawn a lot of debates over its utility in the last decade. On the one hand, it has gained considerable support. Many companies were found to follow this pattern of evolution, for example, Finnish industrial

companies and Japanese foreign investment in South-East Asia (Welch & Luostarinen, 1988). On the other hand, the model has attracted significant criticism as a great number of empirical studies had found that firms have not followed this approach to internationalise (Buckley, 1982; Chang & Grub, 1992). It has been criticised as too deterministic, and unable to capture the realities of firms' international activities, since some firms choose other expansion modes rather than exporting as their first step in their internationalisation processes (Nordstrom, 1991). Turnbull (1987) concluded there are also other factors that determine a firm's internationalisation decision, for instance, a firm's market knowledge and market commitment, the operating environment, the industry structure and its strategy. He also criticised the model by claiming that the choice of entry modes is independent of a firm's previous experience in export markets. Firms in different industries may choose different entry modes and different internationalisation patterns in different countries. More criticism emerged with the observation of the new type of firm: INVs (Oviatt & McDougall, 1994). Andersson and Wictor (2003) claimed that the U-model is not adequate to explain the internationalisation of INVs since these firms internationalise faster than the U-model predicts. Bell et al. (2001) found that older firms internationalise like INVs once they start their international journey. They named this type of firm "Born again global". Meon and Servais (2002) conducted a study to compare the utility of the U-model and INVs framework in describing SMEs' internationalisation processes. They found no relationship between the age of the studied firms and their export intensity, global orientation, distribution, psychic distance, or the number of the markets served.

### 3.3.2 The International New Ventures Framework

INVs are also known as “Born Globals” (Knight & Cavusgil, 1996), “Global Start-Up” (Oviatt & McDougall, 1995), “Instant Internationals” (Preece et al., 1999), “Infant Multinationals” (Lindqvist, 1991) and “Committed Internationalists” (Jolly et al., 1992). According to Oviatt and McDougall (1994, p. 49), the definition for an INV is “*a business organization that, from inception, seeks to derive significant competitive advantage from the use of resources and the sale of outputs in multiple countries.*” Obviously, these firms do not follow the traditional stages pattern in their internationalisation processes. Their rapid internationalisation strategy questions the slow and incremental nature of the U-model. Moreover, the U-model fails to explain why these firms start their international operations not long after their inception, how they start and enter international markets simultaneously, with some actually starting their international operations before establishing their domestic bases (Bell, 1995; Boter & Holmquist, 1994; Buckley, Newbould, & Thurwell, 1979; Coviello & Munro, 1995).

Research interest in INVs started in the 1990s, even though since the late 1970s, the INV phenomenon has been found in different countries across various industries (Buckley et al., 1979; Knight & Cavusgil, 1996). Garnier (1982) provided evidence for the phenomenon of INVs in Canada. He indicated that INVs might be formed by proactive entrepreneurs. Foreign markets were not an addition to the domestic market. A study of small manufactures in the United States of America by Brush (1992) found that 13% of the sample began international activities during the first year of existence. In an Australian study, Rennie (1993) identified several firms whose management was globally

oriented, who viewed the world as their marketplace right from the establishment of the company. They tended to be small in size, and applied state-of-the-art technology to develop distinctive products targeting the niche markets. Also they began overseas activities within two years after their creation. What is more, exports generated a large proportion of their revenues, as at least a quarter of their total production was sold in overseas markets.

### ***3.3.2.(1) Factors Giving Rise to INVs***

Oviatt and McDougall (1994, p. 48) proposed a theoretical framework for greater understanding of INVs based on transaction cost analysis, market imperfections and the international internalisation of essential transactions. The framework presented is “how INVs fit within the theory of the MNE”. Four basic criteria are required for all sustainable INVs. They are as follows (Oviatt & McDougall, 1994, p. 33-37):

*Element 1: Internalization of Some Transactions*

*Element 2: Alternative Governance Structures*

*Element 3: Foreign Location Advantage*

*Element 4: Unique Resources*

It is recognised that SMEs are generally handicapped by constrained resources (Bell et al., 1991; Bonaccorsi, 1992). As start-up firms, SMEs can face the liability of newness (Stinchcombe, 1965). They can lack export market information, have limited financial capacity and trained human resources. Knight and Cavusgil (2004) reported that in order to achieve foreign market success early in their evolution, INVs rely on hybrid structures

to leverage innovation, knowledge, and capabilities in a way not matched by competitors. Outsourcing is the most common way for INVs to gain access to assets and knowledge that they do not own. Due to the existence of market imperfections, it is rational for them to own certain vital assets according to the framework. By doing so, they would have valuable resources to exchange in an economic transaction. Therefore, they need to decide what valuable resources they are going to own and what resources they are going to externalise, which leads to the selection of alternative governance structures.

Oviatt and McDougall (1994) suggested that alternative governance structures enable INVs to initiate global business, which explains the importance of networks in INVs' internationalisation processes. By selecting appropriate partners, INVs can gain access to financial, marketing, and managerial resources and leverage these resources from multiple countries to achieve goals without needing to own all the international capabilities themselves. Networks also facilitate founders of INVs to identify international business opportunities, establish credibility, gain access to critical resources, and form cooperative strategies (McDougall & Oviatt, 2003). Indigenous firms have location advantages over INVs as they have better knowledge regarding the local environment. Through alternative governance structures, INVs are also allowed to utilise their partners' foreign market knowledge, skills and experience that they lack. What is more, INVs will be able to control their vital assets and markets, as well as to spread capital and other risk. This is confirmed by Bell (1995), who claimed that these firms use different market entry combinations for risk minimisation purpose. The impact of

networks on INVs' opportunity identification, foreign market selection and expansion strategies is also recognised by other studies (Coviello & Munro, 1995).

The theory of MNEs, for example the eclectic paradigm (Dunning, 1988), suggests firms that are involved in foreign operation possess some ownership advantages compared to local competitors in the host country. This can be even true in this modern era of rapid transportation, contemporary communication infrastructures and low trade barriers. High technology allows valuable knowledge to travel across national borders with speed at low marginal costs. INVs can take this advantage to transfer their valuable resources to countries where indigenous firms are less competitive than themselves. They can also be more competitive through offering differentiated or low cost goods and services to target a particular buyer group in foreign markets (Knight & Cavusgil, 2005). Autio (2005, p. 15) reviewed Oviatt and McDougall's work and other's research, suggesting three potential "internationalisation competitive advantage" sources. The first one may arise from international resource base asymmetries. Through accessing and leveraging valuable resources across nations, INVs will be able to gain competitive advantages. The second potential arises from INVs' ability to generate new knowledge, resources and technology. The last one is the dynamic capability effect of early internationalisation. It is argued that "early internationalisation may help root a more innovative and dynamic strategic posture on the new venture" as young firms may have "learning advantages of newness" (Autio, 2005, p. 12).

To successfully internationalise, INVs also need to own unique resources, which will enable them to achieve sustainable competitive advantages. Barney (1991) argued that organisational resources that are valuable, rare, difficult to imitate and non-substitutable can yield sustained competitive advantages in domestic and overseas markets. These unique resources could be assets, capabilities, organisational processes, information, knowledge and technology. Owning these resources grants INVs differential advantages in foreign markets (Knight & Cavusgil, 2005). However, as the context is dynamic and complex, INVs need to continually form and reform their unique resources (Autio, 2005).

### ***3.3.2.(2) Types of INV***

Considering the above criteria, four types of INVs are identified based on the number of countries involved and the level of co-ordination of value chain activities: (a) export/import start-ups, (b) multinational traders, (c) geographically-focused start-ups, and (d) global start-ups. Successful global start-ups are identified by possession of seven characteristics (Oviatt & McDougall, 1995, p. 34-37):

- (1). A global vision exists from inception
- (2). Managers are internationally experienced
- (3). Global entrepreneurs have strong international business networks
- (4). Preemptive technology or marketing is exploited
- (5). A unique intangible asset is presented
- (6). Product or service extensions are closely linked
- (7). The organisation is closely coordinated worldwide.

Oviatt and McDougall (1999) later presented a conceptual framework for explaining accelerated internationalisation. The framework proposes that rapid changes in technology are the foundation of the accelerated internationalisation. To explain the speed, the breath and the modes of internationalisation as well as the role of emerging businesses in the internationalisation process, four key building blocks of the theory are identified, which include political economy, industry conditions, firm effects and the role played by management teams.

There are two streams of research that have emerged in relation to innovative technology of INVs. One asserts that INVs are generally found in the leading-edge technology industries. They produce state-of-the-art goods and services for significant international niche markets (Rennie, 1993). In order to survive, they have to commercialise worldwide to generate sufficient revenues (Jolly et al., 1992). McDougall et al. (1994) suggested that early internationalisation is a condition for INVs to survive as opportunity windows are short in dynamic sectors. This explains how and why INVs quickly become multinational in their early stages. Other research concludes that INVs could be found in traditional manufacturing sectors as well (Knight & Cavusgil, 1996). Nevertheless, our understanding of the accelerated internationalisation phenomenon is still limited (Oviatt & McDougall, 1999).

### **3.3.3 Differences between the U-model and the INVs Framework**

The first and foremost difference between the two models is the level of aggregation in analysing internationalisation process. The U-model focuses more on the firm level and



extends to the environment level, but largely ignores the role individuals play within firms. The firm level activities are the main factors to explain a firm's international behaviour according to the original U-model. "Foreign market commitment decisions are made, not by individual managers, but through a decision process into which the various power coalitions of the organisation participate" (Autio, 2005, p. 12). Moreover, through experience, a firm incrementally learns and gains knowledge about its foreign markets, which acts as the foundation for its subsequent increasing market commitment and expansion to more psychically distant countries (Johanson & Vahlne, 1977). The model was extended to include the environment through involving the firm's network relationships with customers and suppliers (Johanson & Vahlne, 1990). Nevertheless, the network concept is mainly used at the organisational level.

In contrast to the U-model, the INVs perspective examines the individual level behaviours, the firm level factors as well as the external involvement. The framework highlights the role that entrepreneurs plays in firms' internationalisation process. It is argued that the founding entrepreneurs' international experience, competencies, vision, and awareness of growth opportunities residing outside national borders drive the INVs to pursue their international growth opportunities (Autio, 2005). Entrepreneurs are regarded as critical for firms' internationalisation strategies as they can change the firms' operations and structures, which in turn shape the firms' internationalisation behaviours and performance (Jones & Coviello, 2005, p. 298). What is more, entrepreneurs use their personal networks to get access to resources from other entrepreneurs, which is an important facilitating condition for early internationalisation. They also have the ability to

change and develop networks that they belong to (Oviatt & McDougall, 1994). The INVs perspective also examines firms' environment. As firms and entrepreneurs do not exist in a vacuum, entrepreneurs influence their environment through their entrepreneurial actions, while in turn the environment influences their activities (Bygrave & Hofer, 1991).

Looking at the two models' internationalisation strategic postures, the U-model tends to suggest that the internationalisation process is passive, as it is a result of a reaction to unsolicited export orders. Firms following the U-model may be weakly internationally orientated. In contrast to this model, INVs are strongly internationally orientated, which is manifested in their commitment of a fair amount of resources to foreign markets in their early stages (Knight & Cavusgil, 1996, 2004); their founders and managers' international vision with proactive international strategies (Covin & Slevin, 1989; Lumpkin & Dess, 1996); and their internationalisation as a result of opportunity-seeking.

We can also find that the two models are different in terms of the speed, scope and extent of internationalisation. Internationalisation speed measures the rate at which a firm enters new markets, while internationalisation scope is manifested in the number of foreign markets a firm has conducted business in, and internationalisation extent looks at the proportion of revenues that a firm generates from its overseas activities (Jose & Alejandro, 2005). The U-model assumes that internationalisation is a slow and incremental process due to the fact that relevant information from foreign markets is difficult to obtain. Firms follow a linear pattern to internationalise as a result of acquiring relevant information through first-hand experience. On the other hand, the INVs

perspective suggests that internationalisation is a speedy process. It is found that INVs skip some stages of international development that have been suggested by the U-model. Due to the fact that INVs can mobilise their unique resources to combine with fixed resources in the target markets, they can rapidly internationalise to achieve competitive advantages.

In terms of internationalisation scope, the U-model indicates that firms start their international activities in markets that have smaller psychic distance from their own markets. Their international expansion is the result of learning. The INVs perspective argues that psychic distance is not an issue, as firms could build strong networks in foreign markets. These networks also provide them with resources and knowledge to start business in other foreign markets simultaneously. What is more, these networks provide them with local knowledge about the environment, which reduces the perceived psychic distance. In the meantime, human capital is more internationally mobile, in line with the fall of trade barriers. This implies that INVs can easily employ internationally experienced personnel of many different nationalities. Therefore, psychic distance is not considered important any more.

For the extension of internationalisation, according to the U-model, firms start their business in their domestic markets first, foreign activities follow the logic of the establishment chain beginning with no regular export activities. For INVs, foreign operations are viewed as being as important as their domestic business. They generate a great proportion of revenues from their overseas activities (Rennie, 1993). Hence, it is

fair to assume that at the early stage of their international operation, firms following the U-model have a relative smaller internationalisation extent compared to INVs.

The two models also differ in terms of their foreign market entry modes. The U-model argues that firms going overseas start with ad hoc export activities. They then follow the logic of the establishment chain to select modes that yield more control and more rewards, which are also more risky. The shifting of market entry modes is the function of the firm gaining knowledge about foreign operations. In contrast to this argument, the model of INVs asserts that firms do not necessary enter a foreign market with exporting, and that there are a variety of entry modes to select from. Through their networks, INVs can have a presence in a host country without 100% ownership of the enterprise.

Last but not least, the two models also differ in the resource base that a firm can draw on to create value. The U-model assumes that “all of the firm’s technology-creating resources are concentrated in its home base. The firm then uses these resources to generate the value-added outputs that can be exported and eventually, manufactured in foreign locations” (Autio, 2005, p. 14). The firm is more home-country orientated as its value creation is produced in the domestic country and then diffused to its foreign markets. In this vein, internationalisation is a result of growth and a means for the firm to disseminate its goods and services. In contrast, INVs are more world orientated as their valuable resources are generated internationally. Internationalisation is necessary for them to grow as it is a means for them to generate important resources and create value. Through cross-border resource combinations, INVs achieve competitive advantages.

Meanwhile, their competitive advantages are sustained by either protecting their valuable resources or by regenerating valuable resources associated with internationalisation (Autio, 2005).

From the above discussion, Table 3.1 is derived, which summarises the differences between the two frameworks.

<b>Table 3.1: Differences between the U-model and the INVs framework</b>		
	<b>The U-model</b>	<b>The INVs framework</b>
<b>Level of analysis</b>	Firm level	Individual level
<b>Internationalisation strategic posture</b>	Weak international orientation, reactive	Strong international orientation, proactive, opportunity-seeking
<b>Internationalisation speed</b>	Slow	Rapid
<b>Internationalisation scope</b>	Small	Large
<b>Internationalisation extent</b>	Small	Large
<b>Mode of entry</b>	Following the establishment chain logic	No predetermined sequence
<b>Market selection</b>	Compliance with the psychic distance concept	Irrespective of the psychic distance concept
<b>Resource base orientation</b>	Home resource base	Internationally dispersed resource base

### 3.3.4 Similarities between the U-model and the INVs Framework

The proceeding evidence shows that the U-model and the INVs framework are different in terms of explaining a firm's international orientation, internationalisation speed, scope

and extent, as well as foreign market entry modes and selection. They also have common characteristics, as Table 3.2 shows.

<b>Table 3.2: Similarities between the U-model and the INVs framework</b>	
<b>Knowledge</b>	Both frameworks emphasise the importance of knowledge for firms to grow, but each uses different sources to gain knowledge
<b>Uncertainty reduction mechanisms</b>	Both frameworks deal directly with the issue of uncertainty but with different mechanisms
<b>Control mechanisms</b>	Both frameworks identify that there is a need to control their operations but with different control mechanisms
<b>Networks</b>	Both frameworks recognise the importance of networks for internationalisation

First of all, both models emphasise the importance of knowledge for firms to grow. They both agree that experience is influential in firms' internationalisation processes as their development is path-dependent. According to the U-model, experiential knowledge is a prominent factor and an independent variable of uncertainty reduction, which leads to firms' market commitment and finally international expansion. Knowledge could be acquired only from operating abroad. While the U-model emphasises managerial knowledge, market knowledge and network knowledge, the INVs perspective tends to focus on entrepreneurial knowledge and knowledge intensity (Prshanthan, 2005). For INVs, managers' previous international experience has enormous impacts on the firm's rapid internationalisation strategy (Autio, Sapienza, & Almeida, 2000). Stuart and Abetti (1990) showed that entrepreneurs' international experience and their managerial competencies are the most significant factors influencing early performance of INVs, because entrepreneurs with more international experience are more likely to perceive

opportunities in international markets. This in itself influences the firms' international activities. Argyrous (1993, 2000) argued that INVs are much sophisticated in terms of the length and variety of experience of their owners and/or managers. Madsen and Servais (1997) also suggested that INVs' internationalisation process can be understood as an evolutionary process with a strong element of learning. Another study of INVs by McNaughton (2003) also concluded that the number of geographic markets served is positively related to the age of the firm. That can be explained by the accumulation of knowledge.

Secondly, both models deal directly with the issue of uncertainty but each with a different focus. In the U-model, uncertainty is reduced through management learning. Firms' perceived uncertainty is decreased in association with the accumulation of knowledge about international transactions, and learning starts only after the inception of the firm. This is not the case for INVs because many industries are globalised, which allows new entrants to gain foreign knowledge before business operations. What is more, entrepreneurs obtained international knowledge, experience and skills before the birth of their businesses through their personal networks, international contacts, prior overseas working experience, overseas travelling and education as well as the prevalence of global media. This in itself reduces uncertainty.

Thirdly, both models identify that there is a need to control their operations but with different control mechanisms. Control is significant for firms to ensure the achievement of their purposes. It is also the factor that determines risk, return and the performance of

their foreign activities (Barkema & Vermeulen, 1998). The U-model asserts that a firm's internationalisation process starts with low commitment activities, and that valuable resources are generated in the home country to be distributed to its target foreign markets. This implies that a firm controls its foreign operations through gradual internationalisation. Control is gained through their full ownership of assets. By internalising the external market, a firm can compete better as it can protect its unique advantages. Hence transaction costs are reduced. For INVs, it is infeasible to own all the resources that are required for their operations as they are new entrants with a weak capital position. They often seek partners who complement their own competencies to fulfil their goals (Madsen & Servais, 1997; Oviatt & McDougall, 1994). In this vein, INVs need to maintain protection of proprietary knowledge in order to become sustainable (Knight & Cavusgil, 2004). For them, control is achieved through controlling their valuable resources, for example, using trademarks, brand names, and patents to protect their proprietary assets. Control is also realised through governance structures. Developing suitable administrative routines and organisational processes, selecting the most appropriate structure are the strategies that INVs employ to protect their valuable assets, as well as to utilise their partners' resources. Lastly, control is realised through developing social processes such as trust, commitment and dependence in their networks.

Another similarity is that both models recognise the importance of networks. Networks enable firms to develop opportunities according to the U-model (Johanson & Vahlne, 2003), and also help INVs to rapidly internationalise. Etemad (2004) declared that the victories of INVs are the results of their coalition strategies, which enable them to gain



globe market share collectively at the cost of others. However, the U-model uses the network concept only at the organisational level. In this model, firms are part of a large network; they have limited control over strategy planning and implementation, thus top management plays a minor role in the firm's international strategy (Johanson & Mattsson, 1988). INVs use networks at both organisational and personal level, which emphasises that entrepreneurs have ability to choose and manage networks that they belong to (Oviatt & McDougall, 1994).

### **3.3.5 Synthesis**

The U-model and INVs frameworks are the two most discussed models in the literature of international business. These models explain different phenomena of internationalisation with different foci. However, these models were developed and tested in developed countries. Their generalisability in the developing country context is less known. This thesis applies these models to understand Chinese POEs' internationalisation behaviours. By using the two models as a reference framework, their utility in the Chinese context can be examined.

## **3.4 Summary**

This chapter provides a reference framework by reviewing relevant literature on firms' internationalisation. It places its emphasis on motives that drive SMEs toward internationalisation, factors that facilitate or hamper their internationalisation decisions, approaches that they apply to internationalise, and the processes that they internationalise.

The two internationalisation approaches: the U-model and the INVs framework are comparatively reviewed with the aim to find out their differences and similarities in explaining firms' internationalisation processes.

This chapter contributes to the overall study by reviewing diverse and relevant literature, which provides a theoretical reference framework. It illuminates theoretical perspectives and gaps in the existing literature. This reference framework will serve to help the researcher form key research questions for interviews. It will also provide the theoretical background against which the research data will be analysed. The next chapter will discuss the selected research methodology in line with the data collection procedures, the sources of the data, the analysis procedures, as well as ethical considerations.

# Chapter 4 Research Methodology

## ***Introduction***

*This chapter describes the research methodology adopted for this study. It discusses on the methodological considerations and the choices made, along with the research design, the criteria for selecting sample firms, and the procedures for collecting data, consistent with the research aims and objectives of this thesis. This chapter consists of six sections. The first section justifies the use of qualitative methods and case studies based on semi-structured interviews. Section 4.2 details the procedures used to collect data, focussing on the issues of validity and reliability. Section 4.3 discusses the sources of the data. It explains the criteria used to select sample firms and interviewees, and the size of the sample. Section 4.4 handles issues regarding the research procedures. It describes the interview outline and the procedures used for data analysis. Section 4.5 deals with ethical considerations. The last section summarises this chapter.*

## **4.1 Justification for the Methodology**

Chapter 2 discussed the research gap in the literature related to Chinese POEs' internationalisation. The goals of this thesis are to gain deeper understanding toward Chinese POEs' internationalisation, and hence to provide a rich knowledge base for future empirical studies. In the service of these goals, this study relies on qualitative methods. Semi-structured interviews with managers/owners of internationally active small and medium-sized POEs have been conducted.

### **4.1.1 The Qualitative Methodology**

Both quantitative and qualitative research methodologies have their strengths and weaknesses. This study adopts a qualitative research approach to collect evidence on the internationalisation of POEs in China. The reasons for choosing this research technique are as follows.

Firstly, the selection of a research design needs to fit the research questions, since it connects research questions to the procedures for data collection. Quantitative studies are useful for rigorously testing existing theory. They are employed to measure and analyse relationships between variables; thus, findings are more reliable with large samples (Bogdan & Biklen, 1998). However, empirical studies are criticised for not being able to capture people's attitudes or feelings. As such, a quantitative study may not be appropriate for exploring the complex side of humanity (Wright & Crimp, 2000). As discussed in Chapter 1, the objectives of this research are to comprehend fully the phenomenon of Chinese POEs' internationalisation and to add knowledge to the literature of international business, rather than to test existing theory. This research design requires a qualitative approach, with the aim of identifying variables and observing patterns, which would contribute to theory development. Thus, a qualitative approach is more appropriate than a quantitative one for this study.

Secondly, as an emerging market, the transitional nature of China's industrial and institutional environments is quite different from that of Western countries. Chinese firms might then be expected to have different international behaviours, compared to Western

firms. As a result, existing theory, for example, the U-model and the INVs approach, may not be directly applicable to Chinese POEs' internationalisation. Because Chinese POEs' internationalisation is not well understood, the relationships among various attributes are not clear, and theory development is still in the early stage. It is noted that qualitative studies provide rich insights into the complex and dynamic relationships among relevant factors. They are important to holistically understand phenomena in context-specific settings (Patton, 2002). Moreover, qualitative studies are intended to discover, construct and build theory, rather than testing it (Bonoma, 1985; Tsoukas, 1989). Given the insufficient state of our theoretical knowledge about Chinese firms' internationalisation, and the complexity of the phenomenon, it is viewed as more appropriate to use qualitative methods (Bonoma, 1985).

Lastly, the selection of a qualitative methodology is in response to the call for qualitative works by Carson and Coviello (1996) and Fillis (2001). These authors claimed that quantitative methodologies have dominated internationalisation literature, while qualitative research and case study approaches are largely lacking. They advocated the use of a variety of research methodologies to better understand the dynamic nature of internationalisation. Fillis (2001) argued that the quantitative method hampers the development of new theories. To understand the behaviours of smaller firms' internationalisation, alternative research methods are required. Echoing these authors' calls, this thesis applies qualitative methodologies, aiming to gain context specific knowledge of Chinese POEs' internationalisation, which, in turn, will facilitate further development of new theories.

#### **4.1.2 Case Study Research**

The case study is “*a way of organizing...social data so as to preserve the unitary character of the social object being studied*” (Goode & Hatt, 1952, p. 331). This thesis adopts the case study as the research strategy, due to the following reasons. Firstly, Yin (1989, p. 16) suggested three conditions for selecting this research strategy, including the type of research question, the control an investigator has over actual behavioural events, and the focus on contemporary as opposed to historical phenomena. The researched phenomenon is contemporary, involving various “why”, “how” and “what” questions regarding Chinese POEs’ internationalisation issues, as well as the respondents’ perceptions of internationalisation. Existing knowledge about the phenomenon is shallow and incomplete, the boundaries between the phenomenon and context are not clearly evident, and the investigator has little control over actual behavioural events. An exploratory case study offering an in-depth insight into the real dynamics of the situation was selected, as it will allow appreciation of the complexity of organisational behaviour more clearly (Eisenhardt, 1989).

Meanwhile, the objectives of this research are to identify the rationales, influential factors, approaches and processes of Chinese POEs’ internationalisation, to evaluate the findings in relation to the existing literature, and, therefore, to provide a knowledge base for further studies. Case studies, which aim to provide description, test theory or generate theory, will allow this study to achieve its objectives (Eisenhardt, 1989, p. 535).

### **4.1.3 Semi-structured Interviews**

Interviewing was the major research method for this study; this approach is recognised as one of the most powerful tools for gathering data regarding complex occurrences. Compared to other methods of data collection, the approach allows for greater depth, since participants are able to discuss their interpretations and meanings of internationalisation from their own points of view, explain the underlying reasons for undertaking business activities in unfamiliar environments, describe the criteria they apply to evaluate international opportunities and the approach they use for realising their international objectives (Jones, 1985; Laing, 1967). Semi-structured interviews with open-ended questions were undertaken to probe in-depth insights. By asking open-ended questions, the researcher allows respondents to answer questions on their own words and own ways. Thus, unique and meaningful information, as well as unanticipated answers, can be gained. Another benefit of using semi-structured interviews is the high degree of flexibility. It allows the participants to ask questions when uncertainty arises, and enables the researcher to probe for more details (Lincoln & Guba, 1985, p. 269).

## **4.2 Instruments Used to Collect Data**

According to Eisner (1991, p. 58), good quality data is critical for qualitative study, which can help one to “understand a situation that would otherwise be enigmatic or confusing”. Regardless of the research design, there are four relevant considerations to assess the quality of research: construct validity, internal validity, external validity and

reliability (Kidder, 1981, p. 7-8; Yin, 1989, p. 40-46). This study has taken actions to deal with these considerations, in order to assure the quality of the research.

#### **4.2.1 Construct Validity**

Construct validity means establishing appropriate operational measures for the concepts being studied (Yin, 1989, p. 41). To increase construct validity, this study has used multiple sources of evidence for data collection, as suggested by Yin (1989). Semi-structured interviews were the major source for collecting data. Open-ended questions were used, to gain information regarding the facts of the firm's internationalisation decision and the interviewee's opinions about these events. In evaluating managerial interview data, one has to be wary of associated problems including "bias, poor recall and poor or inaccurate articulation" (Yin, 1989, p. 91) and measurement error issues resulting from the informant's position bias and other characteristics (Phillips, 1981). Because internationalisation in China has been relatively recent, few problems with respect to institutional memory regarding the internationalisation decisions would be anticipated when the respondents in the target organisations were asked to recall the decisions of interest. To further ensure this research is free from these issues, archival records were collected in conjunction with interviews. Various types of information, such as news clippings and media publications about each company, along with company web pages and documents, were examined and compared with the interview data, to mitigate against potential bias in the information. This between methods triangulation approach provides confidence that the obtained data is truthful, therefore counteracting potential bias associated with any one approach (Cohen, Manion, & Morrison, 2004).



Another strategy that has applied to increase the validity is combining levels of triangulation. Three levels of analysis - the organisation, the industry and the institution - were used in this study (Denzin, 1970). Each individual firm is the primary unit of analysis, in the attempt to explain organisational behaviour in the internationalisation process. Firms in the same industry were grouped, to study their behaviour patterns. Meanwhile, each firm's and each group's relationships with different institutions of the society were analysed, to identify the impact of the society on them.

#### **4.2.2 Internal Validity**

Internal validity concerns the accuracy of findings (Cohen et al., 2004). It refers to the extent to which the findings truly describe the studied phenomenon. To increase internal validity, this study has used various approaches through the research process. Firstly, interview protocols were developed in line with the purpose of the study. Secondly, pilot case studies were conducted, with the aim of assessing the clarity of the questions, as well as increasing the consistency and the soundness of the research design. Thirdly, since the research was conducted in Mandarin, peer examination was used to proofread the Chinese version of the research proposal, the information sheet and the interview schedule, with the aim of eliminating any inaccurate use of terminology. Fourthly, each interview was transcribed on the same day of the interview, to facilitate accurate recording of the conversation. Fifthly, respondent validation was carried out, to obtain more valid data. Upon the completion of summarising each case, data was sent to the respondent for checks on the researcher's interpretation. Lastly, triangulation of sources was applied to address the issue of credibility.

### 4.2.3 External Validity

External validity relates to the generalisability of a study's findings beyond the immediate research; generalisability is interpreted as comparability and transferability in the context of qualitative research (Eisenhart & Howe, 1992; Lincoln & Guba, 1985). In this vein, some authors (Lincoln & Guba, 1985; Schofield, 1993) argued that rich description of the research should be supplied, to enable others to determine the study's comparability and transferability. Yin (1989, p. 21) argued that the goal of the case study is to expand and generalise theories. He advocated the use of replication logic in multiple-case studies, which allows the researcher to compare the studied phenomenon across cases and therefore identify similarities and differences with regard to the key issues. This approach increases case diversity, and also reduces case selection bias, which in return enhances the findings' validity. Eisenhardt (1991) echoed that multiple cases enable researchers to find out common patterns across cases and avoid identifying chance associations. She (1989, p. 545) also argued that there is no *a priori* reason for choosing a particular number of cases for research, and that it is feasible to have between four and 10 cases, depending on the assessment theoretical saturation (when incremental learning becomes minimal with additional cases), as well as resource constraint considerations. In light of these issues, six firms across a range of industries were systematically selected for this study. This number of cases is deemed sufficient to provide the necessary information and to increase the degree of confidence in the findings.

Moreover, this study aims to increase its analytic generalisability by developing propositions, whose transferability to other situations can be tested in further research.

Firestone (1993) categorised generalisation into three levels: generalisation from sample to population, analytic generalisation, and case-to-case transfer. “In analytic generalisation, the investigator is striving to generalise a particular set of results to a broader theory” (Yin, 1989, p. 44), which can be achieved through conceptualising and developing propositions (Punch, 2005a). On the basis of analysed data, propositions were generated to link common factors among the cases. Through empirically testing of these propositions in future, the findings can be applied to other cases.

#### **4.2.4 Reliability**

Reliability consists of a demonstration that a result is replicable. For qualitative studies, the emphasis is on conducting the same case study over again, following the same procedure within the same context, and expecting the same results (Yin, 1989). Bogdan and Biklen (1998, p. 48) regard reliability as a degree of accuracy and comprehensiveness. In other words, reliability reflects the fit between the recorded data and the studied reality. There are several ways to enhance a study’s reliability, including developing an interview schedule and conducting pilot case studies; this study has done both, to ensure that the research has high quality.

##### ***4.2.4.(1) Interview Schedule***

In order to keep the subject in mind and to increase efficiency of interview, given time constraints, a detailed interview schedule was developed. It served as a guideline for each interview, while allowing flexibility such that the researcher can modify the sequence of

interview questions, explain them when necessary, and clarify the meanings of both questions and answers. Each interview was roughly divided into three sections focusing on collecting information about the participant firm's background information, its rationales behind internationalisation decision, and the respondent's comments about the company's international activities. The first section sought information about the company's age, size, market situation, products, and internationalisation history and operations. After gaining this background information, more specific questions emerged as the interview unfolded, including the motivations and the objectives for internationalisation, the strategies applied for internationalisation, the information needs, and the factors that influenced the internationalisation decision. These are the key issues of interest regarding Chinese POEs' internationalisation. The last section requested the interviewee's perceptions about the firm's international performance, and the firm's future strategies. These questions were formulated in a way that would help to answer the research questions. After development, they were translated into Mandarin. Peer examination was used to ensure that the meaning in Chinese was valid, clear and free from academic jargon.

#### ***4.2.4.(2) Pilot Studies***

Silverman (1993) suggested that careful piloting of interview schedules and training of interviewers are ways to enhance the reliability of interview research. Before conducting interviews with the sample companies, two pilot studies were conducted with small and medium-sized POEs in China. The criteria for selecting the pilot cases were based on convenience and accessibility using personal contacts. One pilot case was a firm in the

construction material industry, located in Shenzhen. The other one was in a high tech industry, and located in Nanjing. These pilot interviews were critical for providing valuable insights into the research issues and also helping the researcher to refine the interview plans. Moreover, since the interviews were conducted in Mandarin, these pilot studies were extremely useful for the researcher to ensure that correct terminologies were used. Therefore, any ambiguity of instructions and terms was avoided for the ‘actual’ interviews. Lastly, these pilot studies also served to improve the researcher’s interview skills, such as being able to ask good questions, being a good listener, being flexible, being focused within the studied subject and being unbiased during the interview process (Yin, 1989, p. 62-63). These were the crucial steps to increasing the reliability of the study.

### **4.3 Data Sources**

Similar to quantitative research, qualitative research also confronts with the issue of sampling. However, qualitative sampling focuses on identifying cases, setting the boundaries and constructing a sampling frame (Punch, 2005b). For this research, a purposive sampling strategy was adapted to select samples and interviewees, according to the research objectives, the selected research methodology, and resource availability and constraints.

As one of the largest counties in the world, China has a population of over 1.3 billion people. Within the 23 provinces, there are 56 ethnic groups (CIA The World Factbook, 2008b). Each province and each ethnic group has its own culture. Hence, it would be

reasonable to expect that firms from different parts of China will have different international behaviours. Due to the limited amount of time available for this thesis and constraints with respect to financial resources and accessibility, indigenous POEs located in the south-eastern part of China were the subject of this research. Compared to other regions in China, this region has better economic performance, more sophisticated infrastructure, more open policies toward international trade, and better development of entrepreneurship. Data obtained from studying firms located in the south-eastern part of China are expected to yield particularly comprehensive knowledge of the population of interest for this study.

Since the unit of analysis is Chinese POEs and the primary phenomenon of interest is the why, how and what of their internationalisation, independent POEs that are engaged in international activities using a wide range of market entry modes, such as exporting, international JVs and FDI constitute the focal group. Because SMEs are the central of this research, this study is limited to firms that have fewer than 3,000 employees, according to the official definition of SMEs in the Chinese context. Lastly, this study is only interested in firms that were established after the 1980s, when China's *Open Door Policy* was implemented. This criterion allows a full understanding of the impact of policies on the studied firms' internationalisation. Following these selection criteria, similar examples from various industries were selected, which permits a systematic study of the phenomenon. As a result of the greater case variety, the findings should be more analytically generalisable. In addition to these criteria, other considerations, such as the willingness of the company to participate in this study and the availability of the firm's

archival data, were also included when selecting the firms for the study. The interviews with managers/owners who are principally responsible for international operations have been made possible through referral by two Chinese officers. The interviewed firms that were located in Zhejiang province were contacted through an officer from the Yuhang Municipal People's Government (Yuhang.gov.cn, 2008), and other studied firms located in Guangdong and Fujian provinces were contacted through another officer who works for the Guangdong Technology Venture Capital Group Co., Ltd (GVCGC, 2008).

Information regarding each firm's internationalisation behaviour was collected through open-ended interviews with top management and persons directly involved in the internationalisation decisions. Hence, two more criteria were applied to selecting interviewees for the study. Firstly, interviewees must be decision-makers in the participating firms, such as CEOs, executives, owners, or owner-managers. These people were selected, as they have access to critical information about the subject matter of interest. Also, as decision-makers, they represent their company's attitudes and approaches toward internationalisation. Moreover, interviewees must have been involved during the time when the decision to internationalise was taken. This ensures that the interviewees would be able to provide relevant, accurate and comprehensive information to inform our research questions.

#### **4.4 Administration of Procedures**

A shortlist of firms was selected after examining the recommended firms against the criteria listed above. Managers/owners of these firms were first contacted by telephone,

to invite participation in the research. The nature of the study, including the research objectives, the research issues, the research method, required information and its importance, was explained to potential participants during the telephone conversations.

Confidentiality of responses was assured for the individuals and the companies. Firms that indicated a willingness to participate were further contacted by telephone, to make interview appointments with key informants. A few days before the interview, each firm was once again contacted, by sending them the Mandarin version of the research proposal, the participant information sheet and the interview schedule, which covered the broad topics with a list of questions that would be asked during the interview. This was done to further inform the participants of the nature of the study, and to assure them of the study's confidential nature. This step was also aimed at ensuring that participants truly understood the project, and to make sure that they were willing to participate in the study. As a prerequisite to participation, the informants were asked to complete a participant consent form, which provided the information necessary to complete the interviews with the assurance of informed consent. Copies of the research proposal, the participant information sheet, the participant consent form and the interview schedule have been included in the Appendices; see Appendix B, C, D and E.

#### **4.4.1 Data Analysis**

Personal interviews were conducted during the early part of 2008. In all cases, the interviews were conducted at the company sites. The informants were the executive



/owner principally responsible for international business within each firm. The interviews lasted from one to two hours.

Upon completion of the interview, collected data was transcribed immediately, in order to increase accuracy, and to make sure the analysis could take place smoothly. A thematic analysis was conducted manually, following the approach suggested in the literature (Miles & Huberman, 1994). Firstly, each case was treated as a stand-alone entity. Information gathered from the interview, combined with data collected from archival records, was written up as a whole case report. The case report was then sent to the respondent for review and validation. Revision was conducted, if necessary. This was in an effort to capture the true essence of the interview and reduce interpretation bias from the researcher, to achieve the construct validity. After confirmation, each case report was then translated from Mandarin to English. This was followed by a thorough study of each individual case. Findings were coded for each firm along a number of dimensions, including the motives for internationalisation, the factors that influence international activities, the nature of international activities, international presence, and the process of internationalisation. This part is essential. It enables the researcher to manage a large volume of data in a way that allows patterns across cases to emerge, which lays the foundation for cross-case comparisons to take place at a later stage (Eisenhardt, 1989; Yin, 1989). Secondly, to conduct cross-case analysis, summarised data was segmented and edited to identify common themes across diverse cases, and individual variations. To undertake qualitative analysis, the data was organised and displayed in different ways. This approach is valuable, in that it allows the researcher to draw common themes that

emerge from many of the cases. It also enables the researcher to identify causality and complex relationships between variables. This serves as the foundation for developing new theory (Eisenhardt, 1989). Finally, the findings from the cross-case analysis were also compared with the literature presented in Chapter 3.

According to Eisenhardt (1989), there are two situations where theories built from cases are invalid. One is when the researcher tries to include every detail in building theory. This results in the lack of simplicity in the theory. Another is when the built theory lacks generalisability, as it is based on an idiosyncratic phenomenon. To maximise validity at this stage, several strategies have been applied, such as focusing on the research questions, using respondent validation as described above, presenting the data correctly and objectively, and making inference objectively based on the presented data. To address the issue of generalisability, this study has developed testable propositions regarding Chinese POEs' internationalisation behaviours. Future studies can replicate this study, and empirically test the developed propositions in other situations.

## **4.5 Ethical Considerations**

This research has attended to ethical issues before, during and after the interviews. As discussed above, prior to the interviews being undertaken, the participants were fully informed about their involvement in the study, by sending them copies of the research proposal, the participant information sheet and the interview schedule. At the beginning of each interview, subjects were well informed about their rights with respect to taking part in the research; signed consent forms were obtained from all participants. During the

interviews, issues such as confidentiality of subjects and minimising biased results were addressed by following the procedures suggested by the Human Ethics Committee of Victoria University of Wellington, for which this study attained formal approval. Also, the study was conducted carefully and correctly under the supervision of both supervisors for this thesis.

## **4.6 Summary**

This chapter has justified the use of a qualitative research methodology to gain a rich understanding of situational and contextual knowledge of Chinese POEs' internationalisation. Multiple sources of evidence and multiple case studies were applied to increase the validity of the study. An interview schedule was developed and pilot case studies were conducted to deal with the issue of reliability. The samples and the interviewees were selected from the south-eastern part of China against a number of criteria. The administration of procedures for data collection was described. The procedures of data analysis were discussed. Ethical issues about the study were covered. The next chapter will present the collected data.

# Chapter 5 Company Profiles

## ***Introduction***

*Chapter 4 justified the methodological framework and data collection techniques utilised for conducting the current research. This chapter provides general sketches for each of the six case studies. Detailed information about internationalisation patterns for the companies will be provided in Chapter 6.*

## **5.1 Summary of the Data**

Based on the criteria given in Chapter 3, data from six privately-owned firms were collected. Those firms are referred to in the thesis as *Company A*, *Company B*, *Company C*, *Company D*, *Company E*, and *Company F*, to preserve confidentiality. The sample companies were selected from within the manufacturing sector, including the telecommunications networks industry, the electronics industry, the meter industry, and the textiles industry. Table 5.1 shows the industry distribution of the sample firms. All six companies have met the definition of manufacturing SMEs in China, having fewer than 3,000 employees, and annual sales revenues of less than RMB300 million (approximately US\$40 million) with total assets of less than RMB400 million (approximately US\$53 million). The firms were each founded in the 1980s or 1990s, and started international activities in the 1990s. The size of the companies ranged from about 300 employees to around 3,000 employees. The number of countries in which these firms undertake business ranged from a few to more than 100 countries. The approaches that the firms employ to achieve internationalisation are diversified, including exporting, JVs,

alliances, and wholly-owned subsidiaries. There were both push and pull motives behind these firms' internationalisation decisions. Various factors, including global environmental factors, home country factors, host country factors, industry factors, firm factors, and individual factors, contribute to these organisations' decisions on internationalisation and location selection.

<b>Table 5.1: Distribution of the firms by industry</b>	
<b>Industries</b>	<b>Number of firms</b>
Telecommunications networks industry	1
Electronics industry	2
Meter industry	1
Textiles industry	2

## **5.2 Company Background Information**

### **5.2.1 Company A**

*Company A* was established in the late 1980s, with fewer than 30 employees, in the telecommunications networks industry located in Fujian province. The company started the business by selling foreign telecommunication products in the domestic market. It was not until the early 1990s that the company started to develop and produce its own products. With the mission to provide excellent communications network solutions and services to their customers, the company has produced a wide range of products and solutions, including wireless products, network products, software and terminals. Currently, it has around 3,000 employees, including over 1,000 employees in overseas

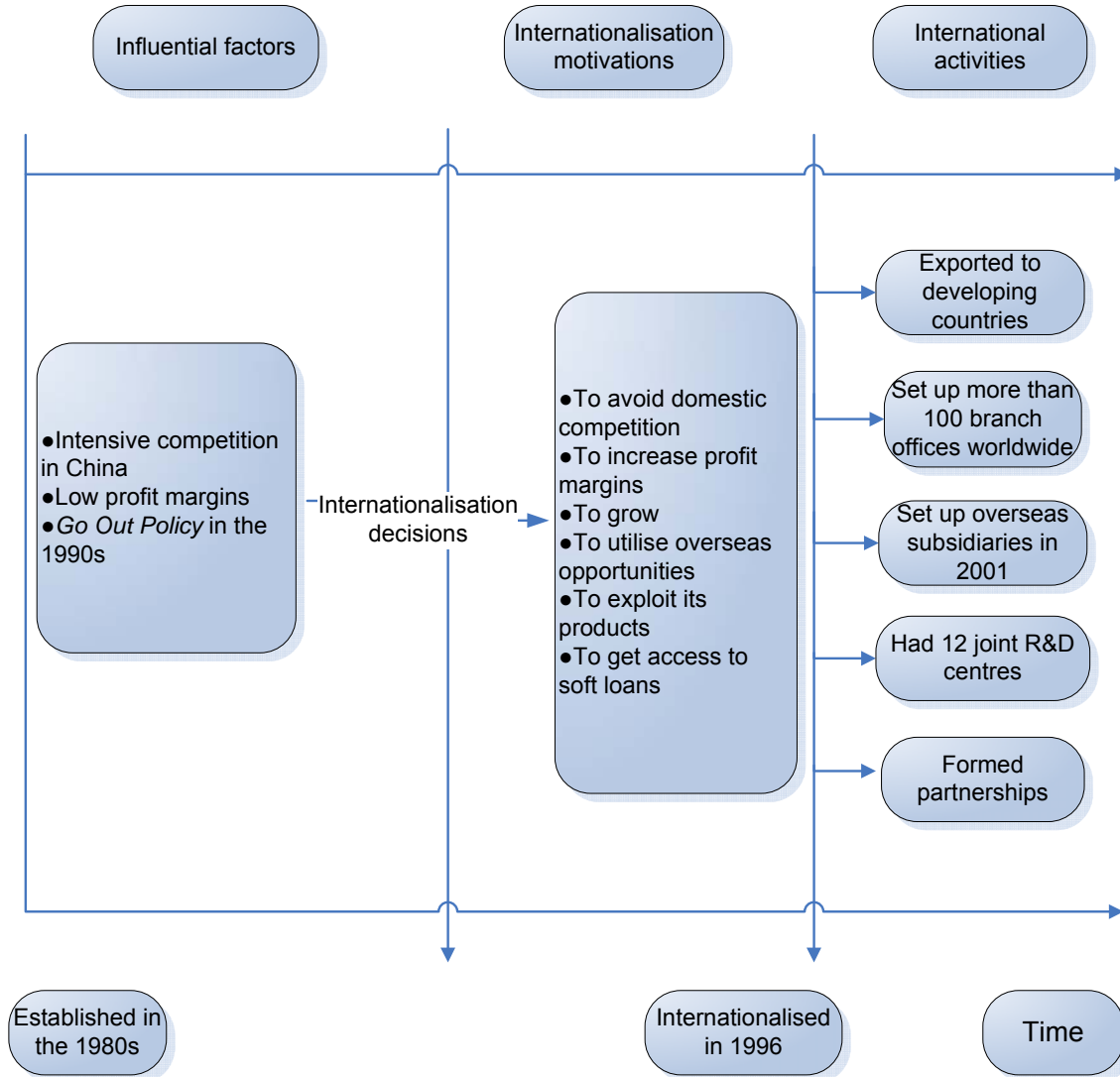
markets. Its products and services are available in over 100 countries. To achieve its international ambitions, the company had more than 100 branch offices and 12 R&D centres around the world by 2007. In 2005, sales revenues from overseas markets surpassed domestic sales revenues, counting for 58%; this figure grew to 65% in 2006, and over 70% in 2007.

This company expanded its business into foreign markets in 1996 through exporting. At that time, the firm had developed rapidly to have around 300 employees. The motives for it to internationalise were both push and pull. In the 1990s, the competition in the domestic telecommunications networks market was getting intensive. The management team analysed both the domestic market and the international market. They found that the domestic market had entered an era of vicious competition, according to the executive interviewed for this study. Firms in the industry cut their prices in order to gain market share, and profit margins were dropping. Different from the Chinese market, the international market focused more on product quality and technology, but less on price. Given that the management team believed the company's market offerings could meet the quality and technology thresholds in the international marketplace, they realised that it might be more profitable to operate in overseas markets, compared to the Chinese domestic market. As a result, they expected that internationalisation would expand the firm's market space to exploit its market offerings, increase its profit margins and hence lead the firm to achieve sustainable growth. In addition, the Chinese government and institutional environment also played a critical role in accelerating *Company A's* internationalisation process. In the 1990s, the government's *Go Out Policy* allowed the

company to have access to low interest rate loans, which enabled it to internationalise rapidly.

Based on its own strengths and weaknesses, the company started its internationalisation journey with exporting. Countries that were weak in their telecommunications industry were its primary targets. In order to provide quick service to its customers, the company later set up branch offices in its foreign markets. In 2001, it established its first overseas subsidiary. To keep abreast with advanced technology, managerial know-how, R&D establishments, distributional networks, *Company A* formed joint R&D laboratories with other leading players in the industry, worldwide, and worked closely with international leading consultancies in fields such as production operation, marketing, management processes and brand development. It also formed various partnerships with its customers and suppliers. By working closely with them, the firm would be able to provide their customers with high quality, excellent service and low operating cost products. This, in turn, is expected to enhance its competitiveness and profitability. Figure 1 depicts certain critical events in the company's international development process.

**Figure 1: Company A's internationalisation timeline**



### 5.2.2 Company B

*Company B* operates in the electronics industry. It was found in 1981 in Guangdong province. The company identifies itself as an international electronics corporation. In 2006, its sales turnover reached RMB213 million (approximately US\$30 million), with total assets of RMB305 million (approximately US\$40 million). At present, its number of



employees has reached over 2000 in China, with 50 permanent representatives and 200 expatriates in its foreign markets.

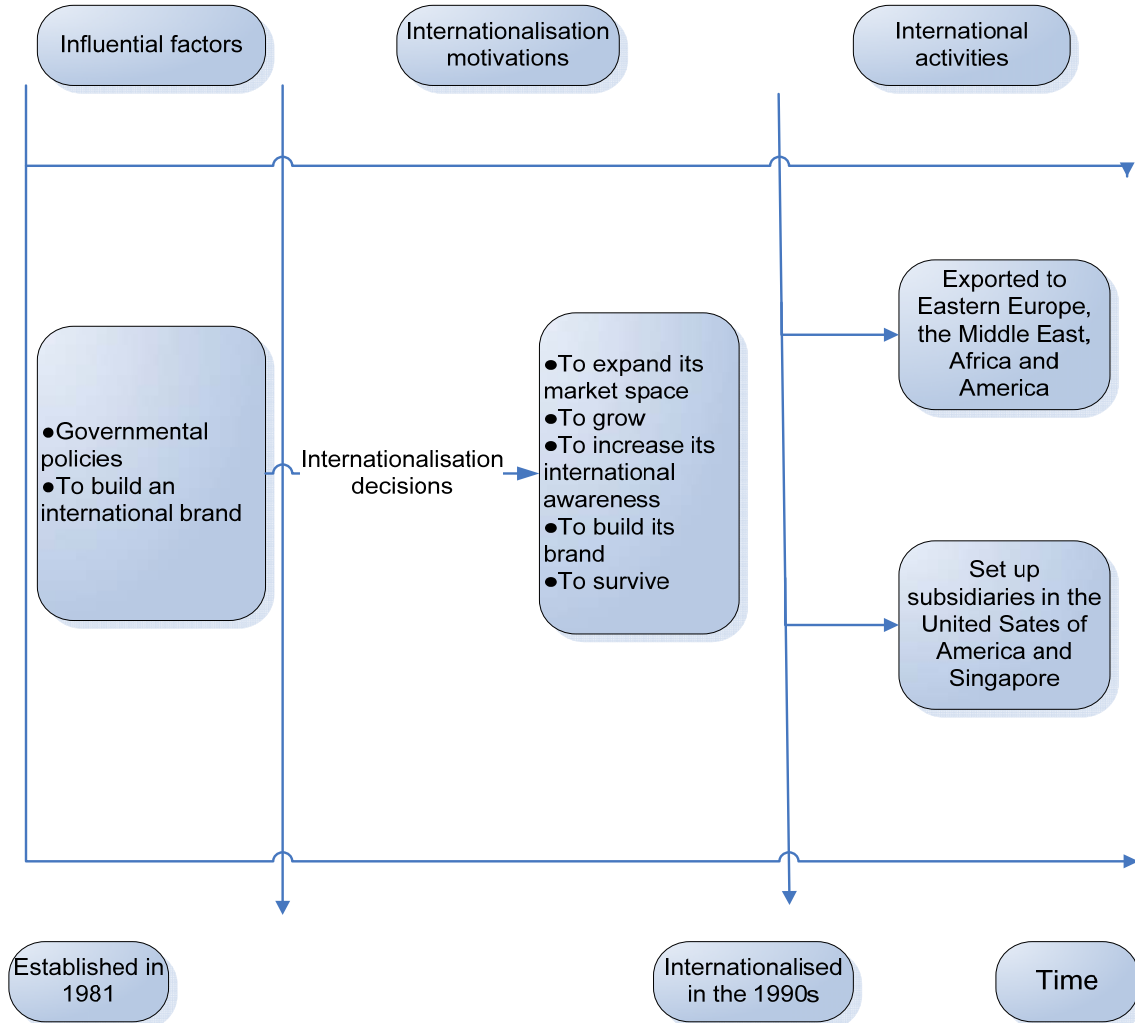
In the 1980s, the company was mainly producing video compact disc (VCD) players. In the 1990s, the VCD player industry died out. By then the management team believed that there were two strategies to sustain the firm's development: diversification and internationalisation. To achieve diversification, the company created six business divisions, to produce an extensive range of products. These divisions are the mobile communication division, the consumer audio and video system divisions, the portable system division, the IT division and the electronic equipment division. To achieve internationalisation, the company has been aggressively exploiting new markets in Eastern Europe, the Middle East, Africa and America since the 1990s. In the United States of America and Singapore, it has set up wholly-owned subsidiaries. In the meantime, it has also formed partnerships with local telecommunication carriers and agents worldwide. Since 2005, its sales turnover generated from overseas markets accounted for over 30% of its total sales turnover, with a continuous positive growth rate.

When *Company B* decided to go abroad, it clearly understood its weaknesses and strengths. Compared to other international leading firms in the industry, it did not have a well-known brand. In addition, it only had a small enterprise scale with underdeveloped marketing networks, and its technology was not as sophisticated as its competitors'. However, it had the strength of low production costs, which was deemed to be its trump card in order to succeed in the cutthroat global marketplace. The company considered

that building an international brand would become its core competitive advantage in both the domestic and the international markets. This goal pushed it to go international. In addition, the company was also pushed to export. For instance, roll-out of the third generation (3G) networks was slow in China. Partly hoping to have its own 3G standards, the Chinese government delayed awarding the 3G licenses to telecom carriers. Due to this delay, the company had to sell its 3G phones to other telecommunication operation businesses overseas. This had impacts on its foreign market selection. Countries in which 3G networks were launched were the firm's selected locations.

The manager interviewed for this study commented that, after so many years of international operations, the company had accumulated some international experience. Internationalisation is deemed to be successful for this firm; it provides opportunities for it to compete with other leading players in the international arena, and to increase its international awareness of international operations, as well as the world's awareness of the company. In the future, the company would like to change its management processes, and standardise its products, aiming to serve more international customers. Meanwhile, it is equally important for the firm to focus on both the domestic market and the international market, and to learn from larger players in the industry. Figure 2 describes the motives behind *Company B*'s internationalisation decision, the events that led it toward internationalisation, as well as its international activities.

**Figure 2: Company B's internationalisation timeline**



### 5.2.3 Company C

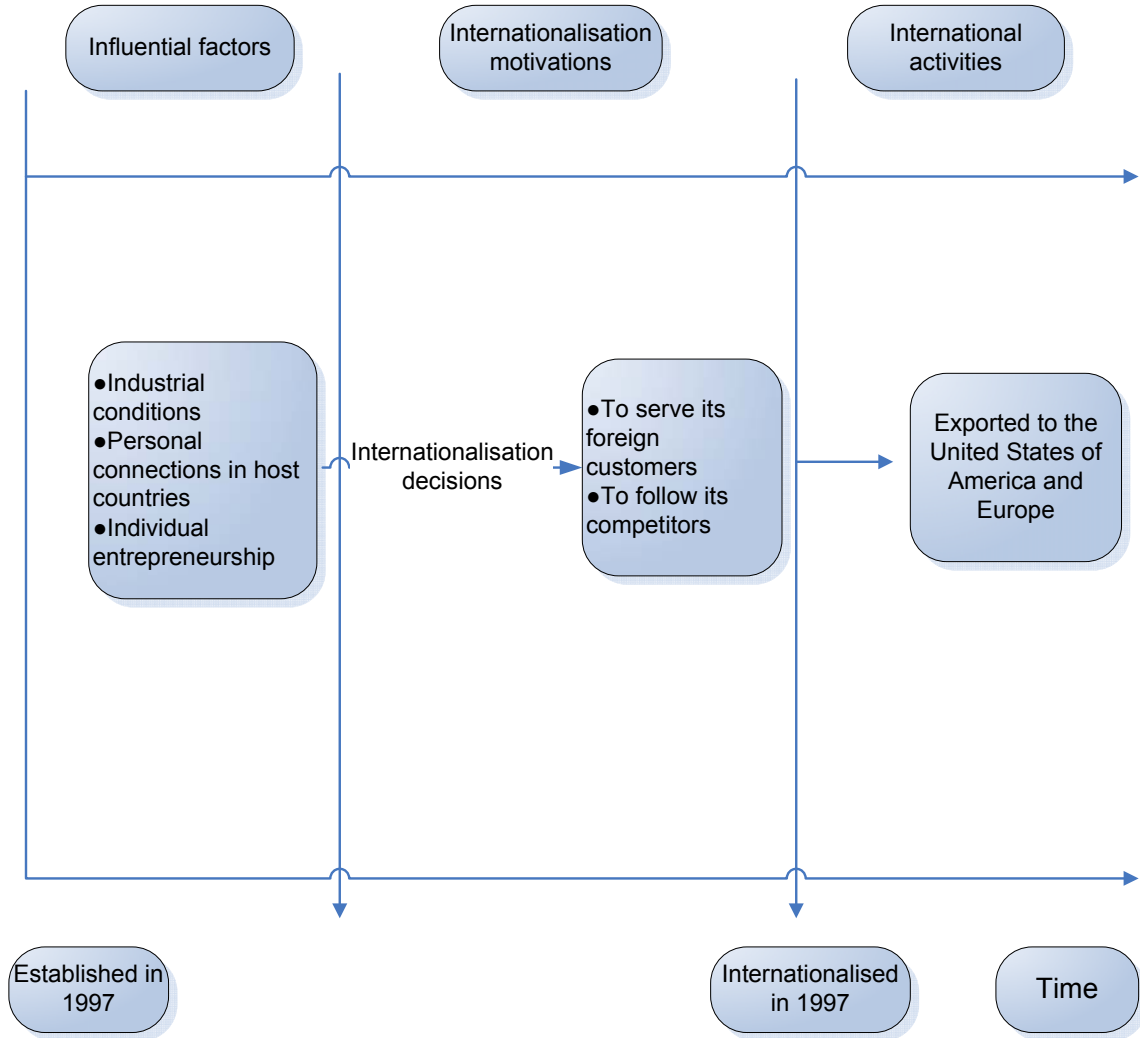
*Company C* was selected from the electronics industry, and is located in Zhejiang province. It was established in 1997, with 50 employees. Currently, it has 320 employees and 50 engineers in the domestic market as well as six expatriates in overseas markets. It has more than 1,000 product items under its six product lines, including car amplifiers, pro-sound amplifiers, crossovers, noise filters and hi-low converters, inverters and

modulators. With this extensive product mix, the company has had its annual sales reach RMB50 million (over US\$6 million).

*Company C* started its international activities in the same year in which the business was established. Before the business was established, the founder was working in the R&D department of another electronics firm, as an expatriate. During his international assignment, he managed to establish some personal networks with foreign firms. When he returned to China, he founded the company. The start-up capital was from his own and family's savings. From the first day the business was established, it has had its focus on the international market. At present, 90% of its products are exported, mainly to the United States of America and some European countries. Original equipment manufacturing and exporting are the firm's major international strategies.

The company was motivated to go international by several factors. Firstly, at that time the electronics industry was highly industrialised. As a result of this, the firm saw its future in the international market coming through mass production strategy. Secondly, there were many players in the domestic market, and high investment levels had caused overcapacity in the industry. Many of the players in the domestic industry were original equipment manufacturer (OEM). To survive, the company saw the need to go abroad. Thirdly, the founder's previous international experience, overseas networks and international connections helped him to get orders from foreign markets. This also affected the company's selection of foreign markets. Figure 3 illustrates the firm's internationalisation development.

**Figure 3: Company C's internationalisation timeline**



Over the past few years, the firm's international performance was satisfying, according to the owner. In the future, the company plans to change its international strategies in the following areas. First, it would like to speed up the process of upgrading and updating its products. Second, it would like to change its operating strategy from manufacturing periphery products to producing entire products with its own production chain.

### 5.2.4 Company D

*Computer D* is company that manufactures meters. It was established as a traditional meter manufacturer in 1982, in Guangdong province. It now has transformed into a high-tech company, becoming one of the largest meter manufacturers in China. It engages in R&D, manufacturing, and sales of energy meters, water meters and power automation systems. In the domestic market, it has production bases in Hangzhou, Chongqing and Shenzhen, with 27 wholly-owned subsidiaries around the country. Internationally, the company's products can be found in over 40 countries covering the five continents. *Company D* started its international activities in 1999. At that time, it had approximately 300 employees. Over the last nine years, the company has grown to have around 500 employees, including 50 expatriates. In 2005, its sales revenues achieved RMB176 million (more than US\$20 million).

Earlier financial reports demonstrated that the company was operating profitably before internationalisation; its sales revenues increased about 30% annually, with positive cash flows and relatively high profit margins. Even though the company was doing well, it still chose to go offshore. The rationales behind this were, first, the industry was expecting to experience severe price competition at home. As a result of this pressure, the firm expected that profit margins would fall. Second, meters were highly standardised in the domestic market. According to the CEO, internationalisation was viewed not only as a means for the firm to keep its position in the industry and to achieve further development, but also for it to sustain its technological edge by learning from other leading international companies. Moreover, internationalisation was deemed as a proactive

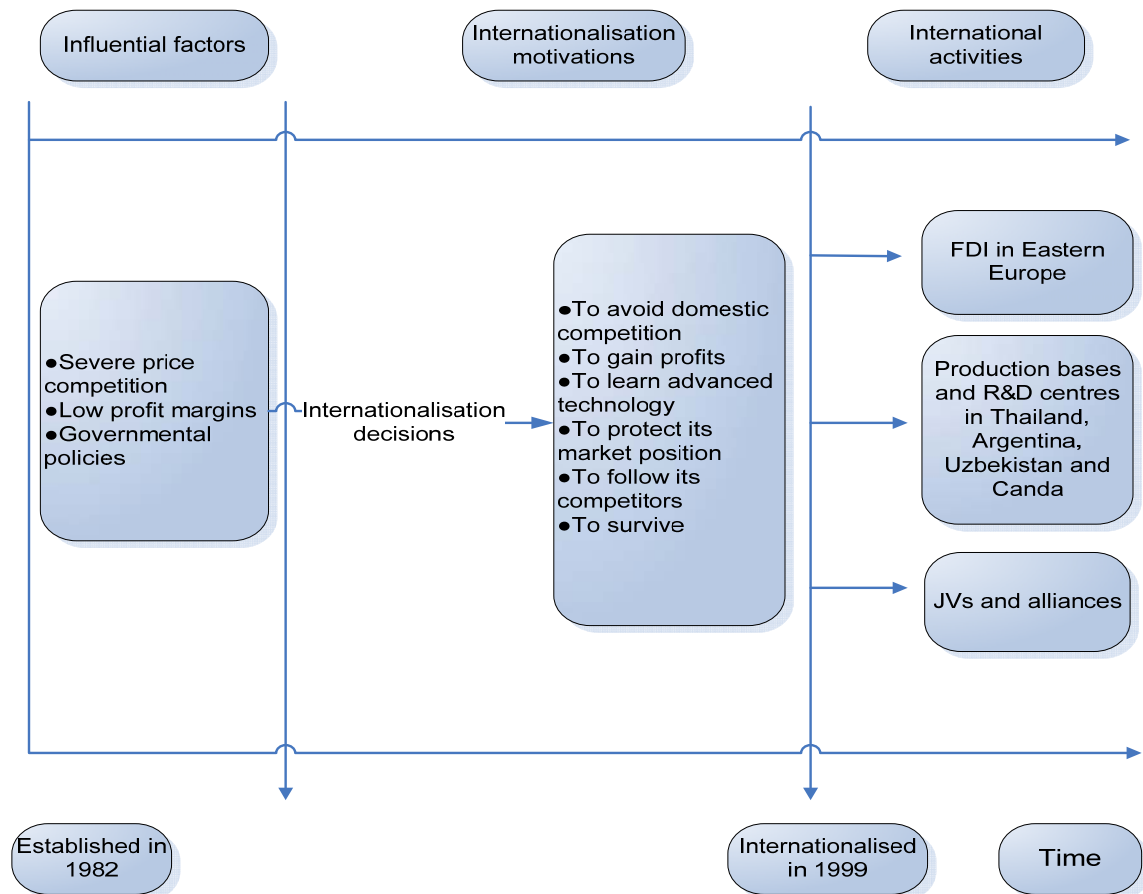
strategy for the firm to survive in a highly globalised world. As more and more foreign firms have businesses in China, *Company D* saw the need to go international as well. In addition, the Chinese government's policy of encouraging Chinese companies to go out had an impact on the firm's internationalisation decision.

FDI was the initial strategy that the firm adopted in its early internationalisation stages. By having a strong presence in a foreign country, *Company D* would be able to learn more quickly about the local market, and gain experience. This was also achieved through localisation. The firm tends to recruit local personnel. In terms of market selection, countries that have high degrees of market openness, large consumption capabilities, reasonably high living standards, low political risk, low economic risk, and relatively low costs for conducting businesses were the firm's top priority. Under these criteria, the company made its first move into some Eastern European countries. At present, it has production bases and R&D centres in Thailand, Argentina, Uzbekistan and Canada. In the future, *Company D* would prefer JVs and alliances over other entry modes. The rationale behind this is that, through cooperating with local firms, *Company D* would be able to quickly enter markets, and absorb advanced technology that is crucial for it to upgrade itself.

Internationalisation has profound impacts on *Company D*'s financial performance. On the one hand, internationalisation is profitable, in that it increases the company's sales revenues and profit margins. On the other hand, internationalisation is expensive, as the company has spent large amount of money in recruiting skilled staff, selecting markets,

monitoring its overseas investment risk, and building and developing relationships with international partners. Looking back at its international performance, the CEO remarked that internationalisation is a “must have” strategy for the company. Even though the company has been doing well, there are some issues that might affect its later development, such as the lack of technology innovation and marketing development. In the near future, the company has its focus on the development of its brand and its business culture. It plans to invest more in technology innovation and marketing management. The company’s internationalisation development is shown in Figure 4.

**Figure 4: Company D’s internationalisation timeline**



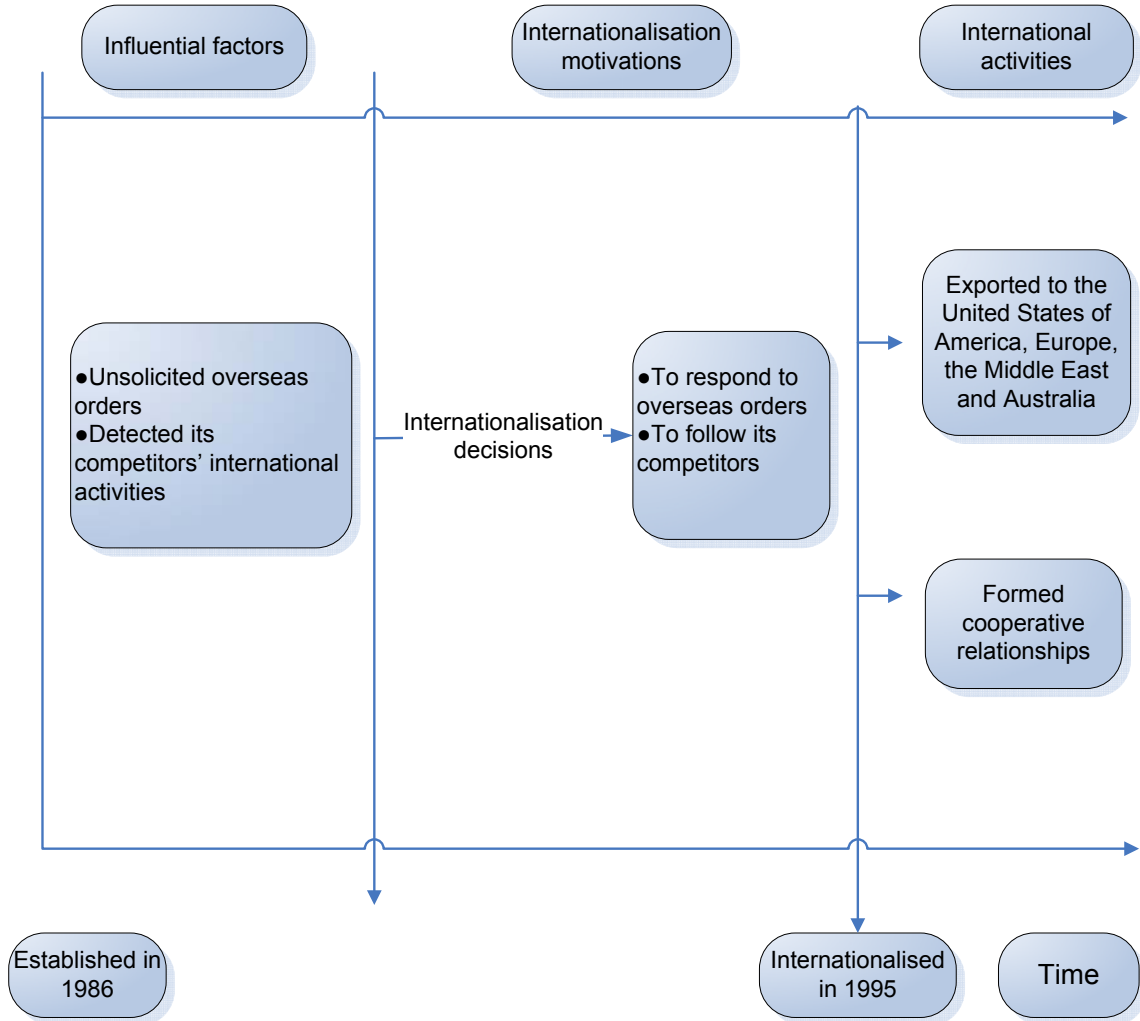


### **5.2.5 Company E**

*Company E* operates in the textiles industry, and is located in Zhejiang province. It specialises in manufacturing upholstery fabrics and finished products, and was set up in 1986. Over the past 22 years, the company has developed into a leader of the domestic Chinese textiles industry. At present, its annual production capability is 10 million meters of fabrics. Each year, it develops thousands of new patterns to meet customers' demand. The goods are mainly sold to the United States of America, Europe, the Middle East and Australia.

The company started its international activities in 1995, when it received an order from overseas. Besides this, the company had observed that its competitors had international activities, which also motivated it to internationalise. At that time, it had around 300 employees, and sales revenues of RMB50 million (around US\$7 million), with relatively high profit margins. Since then, the company has not grown in terms of the number of employees. However, it has imported more advanced equipment from Europe, adopted scientific management systems, and enhanced its innovation abilities, which has led it to further improve its production process, and increase its productivity, resulting in the growth of sales revenues. In recent years, the company has moved away from exporting toward forming cooperative relationships with non-Chinese firms in foreign markets. It also has striven to build its brand. Figure 5 demonstrates the timeline of the firm's internationalisation development.

**Figure 5: Company E's internationalisation timeline**



Over the past 10 or more years, the company has done well internationally. However, its performance has been largely affected by the international market conditions. Since August 2007, its export volume has decreased slowly. This was influenced by political factors and economic factors, such as international trade barriers, the fluctuation of exchange rates, the export tax rebate policy in China and the crisis of the economy in the United States of America.

In the future, the firm plans to work closely with industrial associations, and increase its integration with them. Meanwhile, in order to achieve further development and enhance its competition capabilities, the firm has invested heavily to develop larger production scale and to further improve its management systems. It also has strategies with respect to diversifying its market offerings. In recent years, it has diversified into the catering, and the hotel, software development and information services industries.

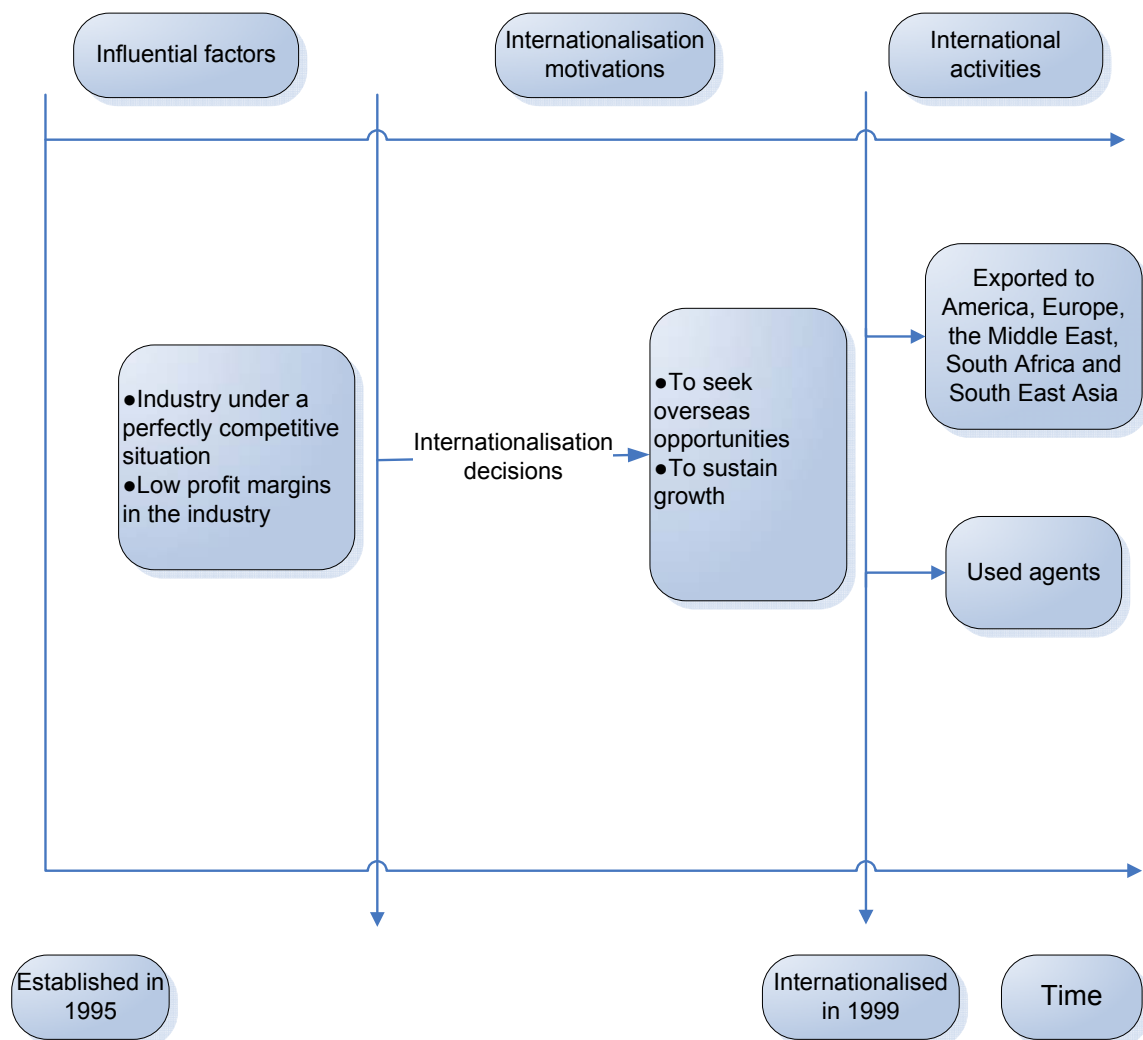
### **5.2.6 Company F**

*Company F* was founded in 1995, and operates in the textiles industry in Zhejiang province. It positions itself in the high end of the market. Each year, the company produces a variety of ornamental fabrics and finished products, as well as developing thousands of kinds of new assortments. Its annual production capability is eight million meters of fabrics. Four years after its inception, *Company F* started to export its goods. At that time, it already had 300 employees. The number had grown to around 550 employees, including 50 in overseas, by 2008. Its products are mainly sold to Europe, America, the Middle East, South Africa, and South East Asia. In recent years, the company's output value has exceeded RMB100 million (over US\$12 million).

In the late 1990s, the domestic textiles industry was already operating under effectively a perfectly competitive situation, with many suppliers. *Company F* was faced with limited demand and declining profit margins, due to the dramatic expansion of production capacity in the domestic market. To stay competitive and sustain growth, the company positioned itself in the high end market, by paying more attention to the processes of

weaving, piece dyeing, and designing of high quality products. As a result of this strategy, *Company F* saw its markets in countries that had high consumption power. As a newly developed firm, it did not have its own distribution channels, so internationalisation was initiated with exporting. A couple of years later, the company had gained some useful international experience. Having mastered how to position and price its products in foreign countries, the firm changed its market entry mode to using agents. Figure 6 presents the timeline of the firm's internationalisation development.

**Figure 6: Company F's internationalisation timeline**



Reviewing the company's previous international performance, the manager remarked that the company could do even better if it could receive more support from industry associations. He also wished that the company could learn more from other enterprises in the industry. His advices to other Chinese firms that are planning to internationalise were to reap benefits of their industry associations, and to learn more about the foreign market before entering the market. In the near future, the company is aiming to have a better understanding of its foreign markets, and therefore provide products that can maximise its customers' satisfaction.

<b>Table 5.2: Company background information</b>						
	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>E</b>	<b>F</b>
<b>Year established</b>	Late 1980s	1981	1997	1982	1986	1995
<b>Year of initial overseas involvement</b>	1996	1990s	1997	1999	1995	1999
<b>Industry</b>	Telecommunications networks	Electronics	Electronics	Meters	Textiles	Textiles
<b>Current company size</b>	Around 3000 employees	Over 2250 employees, with turnover of RMB 213 million, total asset of RMB 305 million	Nearly 400 employees	About 500 employees, sales revenues of RMB176 million	Approximately 300 employees, annual production capability of 10 million meters of fabric, sales revenues of RMB50 million	Around 550 employees, annual production capability of eight million meters of fabric
<b>Overseas markets</b>	Over 100 countries, Asia, Africa, the Middle East, Europe, and America	Eastern Europe, the Middle East, Africa and America	The United States of America and Europe	Products are sold to 40 countries	The United States of America, Europe, the Middle East and Australia	Europe, America, the Middle East, South Africa and South East Asia
<b>Revenues generated from overseas</b>	Over 70%	Over 30%	90%	--	--	--

## 5.3 Summary

This chapter has briefly described the collected data. It also has provided key information on each firm's internationalisation process. Table 5.2 summarises the initial data collected. The next chapter will take an in-depth look at the data. The within-case analysis approach will be applied to further study each case.

# Chapter 6 Within-case Analysis

## ***Introduction***

*Chapter 5 presented the collected data for each of the selected six case studies. This chapter presents in-depth discussions of the findings. A within-case analysis approach is applied, which studies each individual firm in the context of the research issues. Specific motivations for, and characteristics of, the international operations of the Chinese POEs are identified.*

## **6.1 Within-case Analysis**

Based on the findings summarised in the previous chapter, the current chapter further investigates the selected firms individually using within-case analysis. By comparing the findings against the literature reviewed in Chapter 3, this chapter discusses each firm's internationalisation patterns. More specifically, it examines:

- their motives for internationalisation
- factors that have impacts on their internationalisation decisions
- their approaches for realising their internationalisation objectives
- their internationalisation intensity
- their international resource base orientation, and
- their mechanisms for reducing uncertainty.

### 6.1.1 Company A

*Company A*'s internationalisation was initiated by both push and pull motives. It was pushed to internationalise, as there was heavy competition in the domestic market. *Company A* was extremely enthusiastic about growing, which forced it to seek markets overseas. At the same time, the decision to internationalise was also based on proactive reasons. First of all, the firm's motivations to grow and to make profits were very strong. Going overseas would allow it to increase its production volume, decrease per unit costs, gain efficiency and boost profit margins, and thereby develop a sustainable business. Secondly, their research indicated that there was enormous potential in the global marketplace, with higher profit margins and less competition. Going overseas would allow the firm to exploit foreign market opportunities. Thirdly, internationalisation would also offer an opportunity for the firm to exploit its products and technology. Different from the Chinese market, foreign markets placed more emphasis on product quality and technology. The company scrutinised its strengths and weaknesses, and decided that it could provide goods that would meet the quality and technology thresholds of the global market. Lastly, *Company A* had access to soft loans at that time, which allowed it to expand to a number of countries simultaneously. Therefore, there was a combination of home country institution factors, host market factors, industry attributes and firm factors that facilitated the firm's internationalisation decision.

Compared to other international leading firms, *Company A* had relative disadvantages in product quality and technology, but had substantial price advantages. To exploit its price advantages, it started its international activities in countries where the



telecommunications industry was underdeveloped. These countries tend to have less foreign competition, and consumers who are more price sensitive. Relying on its low price advantage, *Company A* initially entered markets in Asia, Africa and the Middle East, and then further extended to Europe and America, after gaining sufficient international knowledge and experience.

Applying the U-model and the INVs framework to analyse *Company A*'s internationalisation process, the result shows that it is a gradual development process, which is consistent with the U-model. It first expanded its business through exporting. After gaining market knowledge and experience, it made further commitment to overseas markets, which was manifested in changing its market entry modes. In order to quickly respond to its customers, *Company A* has set up more than 100 branch offices in foreign markets. It has established R&D centres, formed JVs with global players, and founded subsidiaries around the world, with the aims of acquiring know-how and advanced technology, and to build its brand. It first expanded to developing countries and then to developed countries, which fits well with the notion of psychic distance; as a developing country, it can be posited that China is socio-culturally closer to other developing countries than to developed countries.

However, the U-model can not fully account for *Company A*'s internationalisation process. First of all, the model argues that internationalisation is a reactive posture. In fact, there were both reactive and proactive motivations for *Company A* to go offshore. Second, the model also argues that internationalisation is a slow process. This is

inconsistent with *Company A*'s internationalisation speed, as it has expanded to more than 100 countries within 20 years. As far as internationalisation speed is concerned, *Company A* conforms more to the INVs model. By internationalising quickly, the company has been able to grow rapidly and gain important competitive advantages. Third, the U-model assumes that overseas activities generate a small proportion of a firm's revenues. In contrast, a large proportion of *Company A*'s revenues has been generated from overseas markets since 2005, which is consistent with the INV criterion of at least a quarter of total production being sold to foreign markets (Rennie, 1993). Fourth, the U-model contends that a firm is more home-country orientated. It creates its value in the domestic country and then diffuses to its foreign markets. This is not the case for *Company A*. To generate new resources and keep abreast with the most advanced technology in the global market, the firm established 12 R&D centres around the world to derive value and resources, which is consistent with INVs. Fifth, according to the U-model, a firm controls its foreign operations through full ownership of assets. In contrast, to achieve its goals in foreign countries, *Company A* uses the control mechanisms that are advocated by the theoretical perspectives associated with INVs such as it achieved control over its international activities through managing its valuable resources, and through developing suitable governance structures and social processes. For instance, it had been approved for more than 400 patents and trademarks to protect its proprietary assets by 2008. It also works with international consultancies to develop appropriate organisational structures, administrative processes and strategies to protect its valuable assets. Last, the company has established various cooperative relationships with its

customers, suppliers, and leading industrial players. This strategy is well supported by both the U-model and the INVs framework.

The above discussion demonstrates that neither the U-model nor the INVs perspective alone, sufficiently captures the complexities involved in *Company A*'s internationalisation process, even though each explains some aspects of the process. Applying the U-model to *Company A*'s example, it explains issues regarding the firm's foreign market entry modes and foreign market selection. However, the company's internationalisation speed, scope, extent, and control mechanisms are better explained by the INVs perspective. In addition, the company's rapid internationalisation process would not be achieved without the influence of the government and the state authorities. Neither model has attended to the involvement of the government in the firm's international activities.

### **6.1.2 Company B**

*Company B*'s motivations toward internationalisation tended to be reactive. Its failure in the VCD player industry forced it to seek new ways to sustain the company. Internationalisation was one of the strategies. Through internationalisation, the company could expand its market space, gain wealth, access to sophisticated technology, and achieve its goal of building a well-known brand. Meanwhile, the Chinese institutional environment also played a critical role in pushing the company to sell its 3G mobile phones in foreign countries. Therefore collectively, *Company B*'s decision to go international was influenced by home country, host country, industry and firm factors.

*Company B*'s internationalisation process illustrates a pattern of evolution. It expanded to foreign markets by providing customised network solutions for telecom carriers. After obtaining sufficient international knowledge, experience and skills, the company reduced its perceived uncertainty about conducting business internationally, and committed more resources in its overseas markets. It now has wholly-owned subsidiaries in Singapore and the United States of America, with the Singapore operation engaged in the production of mobile phones, liquid crystal display (LCD) televisions (TV) and notebook computers. Still, the resource base that the firm can draw on to create value is definitely home-country orientated. At present, it has three R&D centres, all located in China. New technology is created and manufactured in the domestic market before being distributed to its foreign markets. In terms of control mechanisms, the firm has tended to internalise its external market operations. Both of its subsidiaries in the United States of America and Singapore are wholly-owned. This strategy allows it to exercise maximum levels of control over its foreign operations.

In terms of market selection, *Company B* obviously does not follow a path predicted by psychic distance theory. Due to the fact that its product offerings tend to be aimed more toward the luxury market, the company targets mainly developed countries in Eastern Europe, the Middle East, Africa and America. Those countries are generally not geographically and socio-culturally close to China. Market potential for LCD TVs and notebook computers in developing countries tends to be limited, while 3G mobile phones can only be used in countries that have launched 3G networks. These issues obviously constrain this company's market selection.

Thus, the U-model has some utility in explaining *Company B*'s internationalisation regarding internationalisation posture, market entry modes, international orientation, control mechanisms and uncertainty reduction mechanisms, however, psychic distance theory is not applicable to the company's market selection decision. Its characteristics of rapid internationalisation speed and large internationalisation scope are similar to INVs.

### **6.1.3 Company C**

*Company C* has many aspects of being an INV. It started its international activities in a number of countries simultaneously with its inception. With 50 employees, the firm was small in size. Foreign markets are its main focus, as 90% of its products are exported; this meets the INV characteristic of having more than a quarter of a firm's products exported (Rennie, 1993). The founder has played a critical role in the firm's internationalisation decision. Before the company was established, he had developed rich personal networks with foreign companies, and had a strong international orientation. He set up the enterprise with the purpose of serving those companies. As a result, products were customised according to those clients' needs. In addition, the decision to internationalise was also influenced by a bandwagon-type effect. Through internationalisation, the firm could keep abreast with its competitors in the industry.

However, in contrast to INVs, *Company C* tends to internalise its foreign activities. Ten years after its inception, it is still at the stage of exporting and acting as an OEM supplier. It is also home-country orientated, with all of its activities in the value chain generated in

the domestic market. The firm has full ownership over its assets. This is due to the fact that the domestic market has abundant resources and low production costs.

Thus, *Company C* has demonstrated some characteristics of INVs. The entrepreneur was the main reason that the company started its international activities. His previous international experience, overseas networks and international connections propelled the firm to engage in international operations. His positive expectations toward internationalisation influenced the firm's internationalisation speed, scope and extent. However, while the company had sales outputs in multiple countries, it did not derive any valuable resources from overseas, which is different from traditional INVs.

#### **6.1.4 Company D**

The motivations for *Company D* to expand its market presence into overseas countries were a mix of both push and pull. Its decision to internationalise was driven by its exposure to pressures in the domestic market. Severe price competition in the meter industry forced it to react. Expanding into foreign markets was expected to allow it to gain more profits. Meanwhile, the domestic market was becoming saturated, which was manifested in the way that meters were highly standardised. The company aimed to learn from international leading firms; this was one of the reasons it opted to internationalise. By competing with successful firms in the global market, *Company D* would be able to learn the most advanced technology from them, which would allow it to develop distinctive products and gain competitive advantages in the local market. In addition to these industry and firm factors that acted as push motives, the company's decision to go

abroad was influenced by global environmental factors and home country factors. The fall of trade barriers resulted in many foreign firms coming to conduct business in China. The contacts that *Company D* had with other foreign firms in China drove the management team to believe that international business was feasible. This reduced the uncertainty that it had in terms of international operations. What is more, the Chinese policy of encouraging firms to exploit foreign markets played a catalytic role in facilitating the company's involvement in the global arena. All these factors together influenced *Company D*'s internationalisation decision.

By looking at *Company D*'s internationalisation process, it is clear that neither the U-model nor the INVs perspective can explain the company's internationalisation behaviour alone. Firstly, the company did not follow the logic of the establishment chain from the U-model, as its international activities were initiated with FDI and then shifted to JVs and alliances. According to the U-model, firms that lack international experience and international knowledge are expected to start their international business with exporting, which is less risky compared to other market entry modes. For *Company D*, one of the purposes for internationalisation was to acquire new technology. FDI would facilitate this by accelerating the learning process, while JVs and alliances would allow it to quickly learn the foreign market.

Secondly, the psychic distance theory of the U-model predicts that firms will first expand to countries that have closer psychic distance to their home countries. By looking at the markets that *Company D* selected, this was obviously not the case. The company clearly

had its own market selection criteria, rather than being constrained by geographical and socio-cultural distances. The selection of foreign markets was influenced by foreign markets' political and economic environments. Thus, the U-model has limited usefulness in explaining *Company D*'s market selection behaviour.

Thirdly, *Company D*'s resource base orientation tended to follow the INVs framework, which contends that firms' valuable resources are internationally dispersed. Consistent with this perspective, internationalisation allows *Company D* to draw vital resources from different locations and generate distinct outputs. At present, it has production bases and R&D centres in Asia, South America and North America. By combining resources obtained from different countries, the company was able to position itself as a high-tech company and became one of the largest meter manufacturers in China.

Fourthly, both the U-model and the INVs framework note that knowledge is influential for firms' growth. However, the U-model suggests that knowledge is acquired primarily from foreign operations. In contrast, the INVs perspective argues that knowledge can be gained through various resources, such as through firms' networks, and entrepreneurs' previous international experiences. Reviewing the mechanisms that *Company D* applied to acquire international knowledge suggests that it has been accomplished by forming cooperative relationships with local firms, recruiting local people, and by having presences in the foreign markets. Therefore, the INVs perspective can be applied to explain the mechanisms that *Company D* adopted to gain knowledge.



Lastly, with respect to controlling its foreign operations, the firm initially adopted the strategy of internalisation. Through FDI, it had full ownership over its assets. While this is deemed to be more risky, it generally has lower associated transaction costs. Recently, the company changed its entry mode, establishing partnerships with local firms in foreign markets. This indicates that for *Company D*, control is not achieved through full ownership of assets but through developing appropriate administrative structures to protect their resources.

### **6.1.5 Company E**

*Company E* did not actively seek to internationalise. Its international market selection and entry initiatives resulted from opportunities created through an external approach to the firm, rather than an internal decision to seek export opportunities. Another trigger was a bandwagon-type effect. The company noted that its competitors had international operations. It decided to jump on the bandwagon through exporting. These triggers hint that the firm originally did not have a strong international orientation. However, the company has successfully entered new markets in Europe, the United States of America, the Middle East and Australia over the past 13 years, which demonstrates that it has moderate internationalisation speed and large internationalisation scope. Meanwhile, the firm remains home-country orientated. Most of its activities are carried out in China, including resource procurement, product design, manufacturing, and sales. That is mainly because the costs of labour and raw materials in China are low. For this firm, it is more profitable to generate outputs in the domestic market than anywhere else in the world. As a result, *Company E* controls its international operations through full ownership of assets.

It reduces its perceived uncertainty about international operations mainly through management learning along with replicating other firms' behaviours.

Therefore, the U-model has utility for explaining *Company E*'s internationalisation process, in terms of its internationalisation strategic posture, modes of entry, resource base and control mechanisms. However, the company's criteria for selecting foreign markets clearly do not match the psychic distance theory. It has mainly entered countries that have high consumption power. These countries are not necessary culturally close to China. Consistent with the INVs perspective, the company has relatively rapid internationalisation speed and large internationalisation scope.

#### **6.1.6 Company F**

Insufficient domestic market opportunities in the late 1990s encouraged *Company F* to seek overseas market opportunities. Consistent with the U-model, *Company F*'s internationalisation process was passive, a reaction to market pressures. Initially, the company used the export mode. After gaining international knowledge and experience, it slowly shifted to using agents, which allowed it to have more control over its foreign operations. Similar to *Company E*, *Company F* is also home-country orientated, with all its value created in the domestic market, and eventually exported to overseas markets. This is associated with the fact that the production of textiles does not require extensive technological expertise, and the costs of production and labour in China are low. Similarly, it also can be viewed as having relatively rapid internationalisation speed and large internationalisation scope. Within less than a decade, the company's products can

be found in America, Europe, the Middle East, South Africa and South East Asia. In terms of market selection, as its strategy is to position itself in high-end markets, developed countries with high consumption power are its target markets.

The company acquired international knowledge slowly through its overseas operations. Consistent with the U-model's prediction, the company emphasises managerial and market knowledge. The manager stated that, after 9 years of international operations, the company finally understood how to position itself in foreign markets. The firm's accumulated market knowledge reduced its perception of uncertainty and risk in foreign markets. In this vein, uncertainty regarding international operations is reduced through managerial learning. Meanwhile, with respect to controlling its foreign operations, the company tends to internalise all its assets. This is related to the industry characteristic of low technological requirements, and the home country characteristic of inexpensive production costs. It is interesting to note that the firm views its networks within industry associations as allowing it to learn more quickly about international operations.

## **6.2 Summary**

This chapter has examined each of the six Chinese POEs' internationalisation processes with focus on their internationalisation intentions, factors that influence their internationalisation decisions, approaches that they undertake to fulfil their internationalisation objectives, and their foreign market selection criteria. More specifically, this chapter evaluates the utility of the U-model and the INVs framework in

explaining the Chinese POEs' internationalisation processes. Table 6.1 summarises the within-case results.

<b>Table 6.1: Results of within-case analysis</b>						
	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>E</b>	<b>F</b>
<b>Internationalisation strategic posture</b>	Proactive and reactive	Reactive	Proactive	Proactive and reactive	Reactive	Reactive
<b>Internationalisation motives</b>	To avoid domestic competition, to increase profit margins, to grow, to utilise foreign market opportunities, to exploit its products, and to get access to soft loans	To expand its market space, to grow, to increase its international awareness, to build its brand, to survive	To serve its foreign customers, to follow its competitors	To avoid domestic competition, to gain profits, to learn advanced technology, to protect its market position, to follow its competitors, to survive	To respond to overseas orders, to follow its competitors	To seek overseas market opportunities, and to sustain growth
<b>Determining factors</b>	Home country policies, host countries' conditions, industry attributes and firm characteristics	Industry attributes, firm factors, home country policies and host country policies	Connections in host countries, industry conditions and individual entrepreneurship	Global environment factors, home country and host countries' conditions, industry attributes and firm factors	Global environment factors, industry conditions, home country policies and host country conditions	Host market characteristics, and industry attributes
<b>Foreign market selection criteria</b>	Started with developing countries, then moved to developed countries	Developed countries	Countries where the entrepreneur has connections	Countries that have stable economies and policies, high living standard and low business operating costs	Countries that have high consumption power	Developed countries with high consumption power
<b>Compliance with the psychic distance concept</b>	Yes	No	No	No	No	No
<b>International activities</b>	Exporting, branch offices, R&D centres, partnerships, and subsidiaries	Exporting, partnerships, wholly-owned subsidiaries	Exporting and OEM	FDI, JVs and alliances	Exporting	Exporting
<b>Compliance with the establishment chain concept</b>	Yes	Yes	No	No	Yes	Yes

<b>Internationalisation speed</b>	Rapid	Rapid	Rapid	Rapid	Moderate	Moderate
<b>Internationalisation scope</b>	Large	Large	Small	Large	Large	Large
<b>Internationalisation extent</b>	Large	Moderate	Large	--	--	--
<b>Resource base orientation</b>	Internationally dispersed resource base	Home resource base	Home resource base	Internationally dispersed resource base	Home resource base	Home resource base
<b>Control mechanisms</b>	Controlling valuable resources, developing suitable governance structures and social processes	Internalising valuable assets	Internalising valuable assets	Full ownership of assets and developing suitable governance structures	Full ownership of assets	Full ownership of assets
<b>Uncertainty reduction mechanisms</b>	Various means	Mainly through management learning	Personal networks, international connections, and overseas experience	Observing other firms	Observing other firms and management learning	Through international exposure and management learning

# Chapter 7 Cross-case Analysis

## ***Introduction***

*This chapter further examines the findings by using a cross-case analysis approach. It aims to analyse the collected data in such a way as to address the research objectives, as well as to identify common behaviours across the cases. The U-model and INVs framework are employed as reference frameworks for the analysis. Based on the results, 15 propositions are developed to capture the Chinese POEs' internationalisation experience.*

## **7.1 Cross-Case Analysis**

Chapter 5 provided key background information regarding each company's internationalisation process. In order to understand more about the firms' internationalisation behaviours, Chapter 6 used the within-case analysis approach to analyse each case individually, focusing on the research questions. The current chapter employs cross-case analysis to identify and summarise the similarities and differences among the cases, with regard to the research issues of the study.

### **7.1.1 Motives for Internationalisation**

According to the U-model, internationalisation generally is a result of firm growth. Firms tend to be passive toward internationalisation, and unsolicited export orders cause a firm to initiate its international activities. In contrast, INVs tend to actively seek opportunities

in overseas markets from inception. Aiming to create distinct value and achieve sustainable competitive advantages by combining resources that are generated in different markets, INVs seek international opportunities aggressively. Hence, internationalisation is a means to achieve growth (Autio, 2005). Looking at the rationales behind the sample Chinese POEs' internationalisation decisions, it is clear that some of them are pushed to internationalise, consistent with the U-model (*Companies B, E and F*), some are pulled to utilise foreign market opportunities as the INVs framework suggests (*Company C*), and some are influenced by both push and pull forces (*Companies A and D*). This is manifested in their different reasons toward internationalisation as discussed below.

Similar to their Western counterparts (Hollensen, 2007), the rationales behind these Chinese POEs' internationalisation decisions include their strong desires to explore and open up new markets (*Company B*), to maximise profits (*Companies A, B and D*), to grow (*Companies A and D*), to utilise foreign market opportunities (*Companies A, C and F*), to exploit their market offerings (*Companies A, B and D*), and to sustain economies of scale (*Company A*). Chinese firms are recognised as latecomers with strong liability of foreignness in the international arena. Most of them have outdated technology, weakness in R&D, limited marketing capabilities, unsophisticated management skills, and a lack of internationally recognised brands (Nolan, 2001). In line with previous literature, this study finds that internationalisation is a strategy for the Chinese POEs to improve their capability and assimilate advanced technology (*Companies B and D*), and to build international brands (*Company B*). Moreover, the Chinese POEs pursue internationalisation as a means to achieving diversification, in order to improve their

competitiveness (*Companies B and E*) (Deng, 2004). From these perspectives, the firms in the sample appear to deem internationalisation as necessary for growth, which supports the suggestion made by the INVs framework. In addition, the study also provides evidence of managerial urge to have international operations stimulates these companies to engage in international operations (*Company C*). This is also consistent with the INVs perspective, which notes the critical role that entrepreneurs play in driving international decisions. What is more, part of the rationale for going international is to exploit the Chinese government's favourable policies toward internationalisation (*Companies A and D*). Once again, this reveals that some Chinese POEs' internationalisation postures are proactive.

Conversely the decisions to internationalise are passive for some Chinese POEs. The results suggest that the Chinese POEs may decide to internationalise as a response to unsolicited foreign orders (*Company E*). A bandwagon effect is another trigger that prompts the Chinese POEs to engage in international operations (*Companies C, D and E*), as firms feel the need to internationalise when they discover that their competitors have overseas operations. Meanwhile, the Chinese POEs' internationalisation decisions are also associated with the goals to avoid the ruthless competition present in the home market as a result of market saturation (*Companies A and D*), and to avoid unfavourable policies in the domestic market (*Company B*). Interestingly, internationalisation is even viewed as a strategy to survive for some Chinese POEs (e.g., *Companies B and D*). Part of the reason that these firms opt to go international is to protect their profit margins (*Companies A and F*) and market positions (*Companies D and F*). For these firms,



internationalisation is either viewed as a way to sustain their growth or to catch up with other firms. Table 7.1 illustrates different motives that these six Chinese POEs have toward internationalisation.

<b>Table 7.1: Chinese POEs' motives toward internationalisation</b>						
	<b>POE A</b>	<b>POE B</b>	<b>POE C</b>	<b>POE D</b>	<b>POE E</b>	<b>POE F</b>
<b>To expand market space</b>		•				
<b>To gain profits</b>	•	•		•		
<b>To achieve growth</b>	•					•
<b>To utilise foreign market opportunities</b>	•		•			•
<b>To exploit market offerings</b>	•	•		•		
<b>To sustain economies of scale</b>	•					
<b>To respond to unsolicited foreign orders</b>					•	
<b>Managerial urge</b>			•			
<b>To avoid competition</b>	•			•		
<b>To protect profit margins</b>	•					•
<b>To protect market position</b>				•		•
<b>To survive</b>		•		•		
<b>To improve capability</b>		•		•		
<b>To build an international brand</b>		•				
<b>To achieve diversification</b>		•		•		
<b>Institutional influence</b>	•	•		•		
<b>A bandwagon-type effect</b>			•	•	•	

### 7.1.2 Factors that Lead to Internationalisation

A variety of factors that determine firms' internationalisation decisions have been identified in the literature, including the macro global environment, home country conditions, host country conditions, industry attributes, firm characteristics, and individual entrepreneurship. Consistent with the previous literature, the interviews reveal that the fall of trade barriers in the global arena has facilitated internationalisation (*Companies D and E*). As more and more foreign firms have businesses in China, Chinese enterprises are forced to compete with them in the domestic market. The experience of competing with foreign companies in the domestic market motivates these firms to compete internationally. This experience also reduces the firms' perceived uncertainty and assessments of the risk of conducting business abroad.

In terms of home country factors, the research demonstrates that public policy initiatives and production costs are influential. In the 1990s, the Chinese government developed the *Go Out Policy* and launched the *Go Global Campaign*, to encourage domestic enterprises to expand their operations abroad (Child & Rodrigues, 2005; Wu, 2005). The Chinese POEs are stimulated to go offshore and exploit the advantages of benefits such as tax incentives, subsidies and soft bank loans (Child & Rodrigues, 2005) (*Companies A and D*). On the other hand, China's unfavourable domestic policies also force indigenous firms to seek market space outside of the country. State policies related to internal market controls, exchange rate controls, and constraints on domestic expansion influence the Chinese enterprises' international decisions and performance (Young, Huang, & McDermott, 1996). To avoid the impact of these unfavourable policies, some firms

choose to go overseas (*Companies B and E*). In addition to the impact of public policies, the Chinese POEs' internationalisation decisions are also related to the country's resource endowments. The inexpensive labour resources and low production costs grant Chinese enterprises substantial cost advantages for competing in the global market.

The extant literature has found relationships between host country characteristics and firms' foreign market selection. In line with previous studies, this research finds that the Chinese POEs' investment decisions are related to the location attractiveness of host markets including market potential, political environment, economy environment, and business operating costs.

The empirical results from this study demonstrate that industry attributes also play a crucial role in determining the Chinese POEs' international activities. The firms' international activities are influenced by the intensive competition and the low profit margins in their industries (*Companies A, D, and F*). A bandwagon effect is another influential factor that was also acknowledged by *Companies C, D and E*. These firms noticed that their competitors have international operations, and felt the need to follow their rivals' movements to protect their own positions in the industry. This supports earlier findings by Knickerbocker (1973) and Ito and Rose (2002).

The impact of firms' characteristics on their internationalisation has been widely recognised. Previous literature has found that firms' possession of unique assets influences their internationalisation tendency, speed and development (Bloodgood et al.,

1996; Dunning, 1988; Hymer, 1960; Oviatt & McDougall, 1994; Rialp, Rialp, & Knight, 2005). The interviews support these findings, by demonstrating that the Chinese POEs' internationalisation behaviours are related to their market offerings. In particular, their market offerings appear to influence their foreign market selections. For example, *Company A*'s market offerings have relatively unsophisticated technology, but have cost advantages. This imposed some initial constraints on its foreign market selection. In contrast, *Company B*'s sophisticated 3G mobile phones are limited to countries that have launched the necessary networks. In addition to market offerings, this research also proves that learning is related to the Chinese POEs' internationalisation activities. *Company D*'s enthusiasm to learn advanced technology facilitated its engagement in the global market. This motive also led it to make a large resource commitment in its first foreign country, by selecting FDI as initial entry mode, recruiting local personnel to accelerate the learning speed, and selecting countries that have favourable political and economic environments.

The INVs framework has emphasised the impact of entrepreneurs on firms' international development. Consistent with this, the example of *Company C* highlights how the entrepreneur influenced the firm's international involvement. His international experience, his skills and competencies in the electronics industry, and his rich connections with foreign companies largely reduced his perceived uncertainty and risk about international operations. In the meantime, his high expectations of firm growth in the international arena also led the firm to early and rapid internationalisation.

Overall, this study provides evidence that the Chinese POEs' international operations are influenced by numerous variables, which supports previous findings in the literature. The global environment, home country conditions, host country conditions, industry attributes, firm factors, and entrepreneur characteristics all play critical roles in the Chinese POEs' internationalisation processes. These factors are interrelated, with respect to their influence on firms' international performance. Of these factors, location attractiveness of host countries and industry attributes, including competition intensity, level of profit margins, and behaviours of the firm's competitors, seem to be particularly important to the Chinese POEs' internationalisation decisions. In addition, the Chinese government's policies toward internationalisation and the resource endowments in China also play important roles in influencing the sample Chinese POEs in the international arena. Table 7.2 summarises the factors that lead each interviewed firm to internationalise.

<b>Table 7.2: Decisive factors that lead Chinese POEs to internationalise</b>							
	<b>POE A</b>	<b>POE B</b>	<b>POE C</b>	<b>POE D</b>	<b>POE E</b>	<b>POE F</b>	<b>Decisive factors</b>
<b>Global environmental factors</b>				•	•		The fall of trade barriers in the global arena
<b>Home country conditions</b>	•	•		•	•		Public policy initiatives, production costs, home country's resource endowments
<b>Host country factors</b>	•	•	•	•	•	•	Location attractiveness
<b>Industry attributes</b>	•	•	•	•	•	•	Industry competition, profit margins, following other competitors
<b>Firm characteristics</b>	•	•		•			Market offerings, learning motives
<b>Individual entrepreneurship</b>			•				International experience, skills, competencies, international connections, expectations for firm growth

### 7.1.3 Approaches for Realising Internationalisation Objectives

Internationalisation comprises a variety of market entry mode options, including exporting, licensing, contract manufacturing, strategic alliances, franchising, equity JVs, and wholly-owned subsidiaries. Different options have different combinations of risk, control, costs, resource commitments and expected returns. According to the U-model, exporting would be an initial entry mode for firms when they start their international operations. As they lack foreign market knowledge, it would be rational for them to select an entry mode that involves low risk and requires the least amount of resource commitment. After gaining sufficient market knowledge and experience, firms have the option to increase their degree of internationalisation through committing more resources to their foreign markets. This study finds that the Chinese POEs employ various market entry modes to achieve their internationalisation objectives, as shown in Table 7.3.

<b>Table 7.3: Chinese POEs' internationalisation approaches</b>						
	<b>POE A</b>	<b>POE B</b>	<b>POE C</b>	<b>POE D</b>	<b>POE E</b>	<b>POE F</b>
<b>Exporting</b>	•	•	•		•	•
<b>JVs and alliances</b>				•		
<b>Branch offices</b>	•					
<b>Subsidiaries</b>	•	•		•		

Table 7.3 demonstrates that exporting as the most common practice among the studied Chinese POEs. Out of the six interviewed enterprises, five selected exporting as their initial international entry mode. Only *Company D* started its international activity with FDI. Meanwhile, establishing wholly-owned subsidiaries in overseas markets is the

preferred later investment mode among the firms in this study (*Companies A and B*). This strategy involves more risk and requires much more resource commitment. In exchange, it allows firms to have more control over their foreign operations. The Asia Pacific Foundation of Canada and the China Council for the Promotion of International Trade (2006) jointly conducted an online survey to understand Chinese companies' outward investment intentions in 2006. Their findings concluded that outward direct investment is a long-term development strategy for Chinese firms to learn advanced management methods and to seek new markets. Similarly, this study also identified that the Chinese POEs are pulled to directly invest abroad, with the aim to acquire key inputs (Buckley et al., 2006). Through FDI, they are able to achieve long term growth by keeping abreast with advanced technology, learning new management skills from other international firms and building well-known brands (*Companies A, B and D*).

The results of the 2006 Canadian survey also showed that establishing sales offices and setting up equity JVs with local firms are the most common practices by Chinese companies. In contrast to those findings, this research indicates that these two entry modes are not preferred among the participating Chinese POEs.

#### **7.1.4 Internationalisation Intensity**

There are three dimensions that can be applied to measure a firm's internationalisation intensity: speed, scope and extent. A firm's internationalisation intensity is positively related to its internationalisation speed, scope and extent. Internationalisation speed measures how fast a firm enters new markets, internationalisation scope refers to

geographic diversification, and internationalisation extent looks at the importance of foreign activities for the firm (Jose & Alejandro, 2005).

Applying these three dimensions to measure the interviewed Chinese POEs' internationalisation intensities, the results are mixed. *Company A's* internationalisation intensity is rather high. Within 12 years of beginning internationalisation, it was doing business in over 100 countries through various international activities as well as a large proportion of revenues being generated from overseas markets. *Company B* can also be defined as having a high degree of internationalisation intensity. Over the last decade, it has been aggressively exploiting foreign markets. It internationalises rapidly by skipping stages in the establishment chain. Given that less than a quarter of its sales turnover was from overseas markets, *Company B's* internationalisation extent is relatively small. For *Company C*, its internationalisation can unquestionably be described as early and rapid. It started its international operations from the inception of the business. At present, 90% of its revenues are generated from overseas. Despite having rapid internationalisation speed and large internationalisation extent, the company has limited internationalisation scope. As for *Company D*, it has expanded to over 40 countries in its nine years of international experience. It has also set up production bases and R&D centres in a number of countries. It skipped stages by selecting FDI as its initial internationalisation entry mode. As such, the company has high internationalisation speed and scope. Compared to these companies, *Companies E* and *F* seem to have moderate internationalisation speed. In terms of the number of countries in which these two companies have business, they are both geographically diversified.



Table 7.4 is derived based on the above discussion, and shows that the studied Chinese POEs have tended to internationalise at a rapid speed. They also have tended to be geographically diversified in selecting foreign markets.

<b>Table 7.4: Chinese POEs' internationalisation patterns</b>						
	<b>POE A</b>	<b>POE B</b>	<b>POE C</b>	<b>POE D</b>	<b>POE E</b>	<b>POE F</b>
<b>Rapid internationalisation speed</b>	●	●	●	●		
<b>Geographically diversified</b>	●	●		●	●	●
<b>Large internationalisation extent</b>	●		●			

### 7.1.5 Resource Base Orientation

According to the U-model, firms tend to be home base orientated, with the bulk of its valuable resources concentrated in the domestic market. In contrast, the INVs perspective states that firms tend to mobilise their unique resources from different countries to create sustainable competitive advantages (Autio, 2005). Looking at the sample Chinese POEs' resource base orientations, the results show that some of them are home base orientated, with their products and new technology generated in the home market before being distributed to foreign markets (*Companies B, C, E and F*), while others are more internationally orientated, as they have R&D centres around the world to create new technology and have wholly-owned subsidiaries overseas, to learn new knowledge (*Companies A and D*). Table 7.5 shows each interviewed firm's resource base orientation.

<b>Table 7.5: Chinese POEs' resource base orientation</b>						
	<b>POE A</b>	<b>POE B</b>	<b>POE C</b>	<b>POE D</b>	<b>POE E</b>	<b>POE F</b>
<b>Home resource base</b>		•	•		•	•
<b>Internationally dispersed resource base</b>	•			•		

However, when interpreting these findings, the industry attributes, the firm's international objectives and the home country factor endowments should be included. Those companies that are located in high-tech industries tend to be international orientated, as the distinctive resources required are internationally dispersed (*Company A*). Firms that have an aim to learn new knowledge through internationalisation are also more internationally orientated (*Company D*). In contrast, those firms that are in traditional industries, such as textiles, have products that are more labour or capital intensive, which involve less technology. It is more profitable for these firms to have key activities conducted in China, in order to take advantage of low production costs.

#### **7.1.6 Uncertainty Reduction Mechanism**

There are various approaches that the interviewed Chinese POEs have applied to reduce perceived uncertainty regarding international operations. Table 7.6 demonstrates that the Chinese POEs in this study reduce their uncertainty mainly through management learning (*Companies A, B and F*), which supports the U-model idea (Johanson & Vahlne, 1977). Meanwhile, the Chinese POEs also reduce their uncertainty through networks, entrepreneurs' international connections and overseas experience (*Companies A and C*), which is consistent with the INVs perspective. Another approach that the studied Chinese

POEs use to reduce their uncertainty is through observing their competitors' international behaviours (*Company E*), or through observing other foreign companies' behaviours in the local market (*Company D*). Once again, the studied firms' approaches to reducing uncertainty regarding international business can not be fully captured by either the U-model or the INVs framework. Each model has some explanatory power on explaining certain firms' approaches, but not for others'.

<b>Table 7.6: Mechanisms that Chinese POEs apply to reduce uncertainty</b>						
	<b>POE A</b>	<b>POE B</b>	<b>POE C</b>	<b>POE D</b>	<b>POE E</b>	<b>POE F</b>
<b>Management learning</b>	•	•				•
<b>Networks</b>	•		•			
<b>International connections</b>			•			
<b>Previous overseas experience</b>			•			
<b>Observing other firms</b>				•	•	

## 7.2 Propositions

Section 7.1 uses a cross-case comparison approach to reveal common international behaviours across the sample of Chinese POEs regarding their motives for internationalisation, factors that influence internationalisation decisions, approaches for achieving internationalisation objectives, internationalisation intensity, resource base orientation, and mechanisms used for reducing uncertainty. Key elements in the investigated phenomenon have been identified across the sample. The present section recontextualises the observed key elements into 15 propositions, aimed at increasing the

study's analytic generalisability. It is anticipated that future research will extend this study through empirically testing the following propositions:

*P1: Chinese POEs' internationalisation is influenced (i.e., pushed or pulled) by changes in trade barriers.*

*P2: Chinese POEs' internationalisation is grounded in domestic factor endowments and triggered by institutional changes.*

*P3: Chinese POEs' internationalisation is influenced by the attractiveness of host country factors.*

*P4: Chinese POEs' internationalisation is influenced by the dynamics of domestic competition.*

*P5: Chinese POEs' internationalisation is influenced by firms' needs to acquire new knowledge.*

*P6: Chinese POEs' internationalisation is influenced by the founder's previous international experience and international orientation.*

*P7: Chinese POEs tend to start out with exporting before moving to more complex entry modes.*

*P8: Chinese POEs that envision emerging global competition for their products prefer direct investment entry modes that provide them with faster internationalisation, higher levels of control and deeper knowledge about their host countries.*

*P9: Chinese POEs tend to opt for rapid internationalisation.*

*P10: Chinese POEs tend to be geographically diversified, aiming to leverage location-specific advantages.*

*P11: Chinese POEs' internationalisation patterns are not well explained by psychic distance.*

*P12: Chinese POEs that are interested in obtaining new knowledge tend to be internationally orientated.*

*P13: Chinese POEs that are in high-tech industries tend to be internationally orientated.*

*P14: Chinese POEs that are in traditional industries tend to be domestically orientated.*

*P15: Chinese POEs work to reduce uncertainty through experiential learning.*

### **7.3 Summary**

This chapter further analyses the six studied cases with a cross-case study approach to understand Chinese POEs' internationalisation processes and to comprehend theory through searching for patterns across diverse case contexts. From the discussion, 15 testable propositions have been developed. In the following chapter, the thesis points out limitations and suggests a future research agenda.

# Chapter 8 Conclusion

## ***Introduction***

*This chapter presents the findings and relates them to the existing literature. The conclusions from the analysis are discussed first, followed by the contributions of the research. The chapter then discusses the limitations of the study and proposes future research areas. The chapter concludes by exploring managerial implications of this study.*

## **8.1 Introduction**

Internationalisation has long been drawing research attention. Due to its dynamic and complex nature, there are various views concerning internationalisation in the literature. Frequently, previous research has its emphasis on MNEs from Western countries. Since the 1980s, many small firms have been actively engaging in international business, despite constraints with respect on resources and knowledge. This phenomenon has drawn attention from international business researchers. The U-model and INVs framework are two influential theoretical perspectives for explaining how firms internationalise in the Western context. However, limited studies have been conducted to test these frameworks' applicability in explaining how firms from developing countries internationalise.

Since China opened its doors to the rest of the world in the late 1970s, it has not only attracted many outsiders to conduct business in China, but it has also encouraged a substantial number of Chinese firms to expand their markets outside of China. Despite

the rapid growth in the number of Chinese firms that have international operations, there is very little research specifically investigating their internationalisation approaches.

This study is designed to build on and extend existing studies by empirically examining Chinese POEs' internationalisation processes. More specify, it aims to understand more about the motives of Chinese POEs with respect to internationalisation and the factors that influence their internationalisation decisions, the approaches that they apply to achieve their internationalisation objectives, and how they evaluate potential foreign markets and behave in the global market. This study applies the U-model and INVs perspective as reference frameworks for the analysis.

Primary data was colleted through six semi-structured interviews with managers/owners of internationally active firms in the south-eastern part of China. These firms are all privately-owned, and they fit the Chinese definition of SMEs. Within-case and cross-case analyses have been conducted, in order to develop an understanding of these firms' internationalisation processes. Based on the data, it is possible to make some concluding remarks about the extent to which the existing literature can explain the internationalisation processes of Chinese POEs, and to present research implications and indicate areas for future research.

## **8.2 Research Findings**

In Chapters 6 and 7, the within-case and cross-case analyses demonstrated that the Chinese POEs' internationalisation processes are dynamic and complex. Firstly, their

decisions to internationalise are determined by both pull and push forces. On the one hand, some of the Chinese POEs view internationalisation as a means to growth. On the other hand, others are passive toward internationalisation, such that the internationalisation decision is a reaction to threats that they are exposed to in the domestic market. This thesis argues that neither the U-model nor the INVs perspective can fully capture Chinese POEs' internationalisation posture.

Secondly, these Chinese POEs' internationalisation decisions are influenced by various factors. The global environment, home country conditions, host country factors, industry attributes, firm characteristics, and the quality of individual entrepreneurship all influence the Chinese POEs' internationalisation decisions and performance. The interaction of different factors influences the process in different ways. From this observation, six propositions have been developed, pertaining to each factor. Looking at how the global environment influences the interviewed firms' internationalisation, Proposition 1 suggests that *Chinese POEs' internationalisation is influenced (i.e., pushed or pulled) by changes in trade barriers*. China's business policies and its low production costs directly influence some POEs in their international decisions and performance. Hence, Proposition 2 suggests that *Chinese POEs' internationalisation is grounded in domestic factor endowments and triggered by institutional changes*. The findings also show that the Chinese POEs' internationalisation decisions are influenced by the location attractiveness of host countries. This leads to Proposition 3, that *Chinese POEs' internationalisation is influenced by the attractiveness of host country factors*. In terms of industry impacts, the findings reveal that the interviewed firms' internationalisation decisions have been strongly affected by competition intensity in their domestic



industries. As a result, Proposition 4 is developed, which proposes that *Chinese POEs' internationalisation is influenced by the dynamics of domestic competition*. In line with previous findings, this study also finds that the Chinese POEs' internationalisation decisions are associated with their desire to obtain new knowledge. Therefore, Proposition 5 suggests that *Chinese POEs' internationalisation is influenced by firms' needs to acquire new knowledge*. The impact of the founders on these young Chinese POEs' internationalisation processes is observed in this study, leading to Proposition 6, which suggests that *Chinese POEs' internationalisation is influenced by the founder's previous international experience and international orientation*.

Thirdly, this study suggests that exporting is a popular approach for the Chinese POEs to internationalise, consistent with the U-model. Five of six firms studied selected exporting as their initial approach to operating in foreign markets. After gaining sufficient knowledge, *Companies A and B* invested more resources in their foreign markets, and changed their entry modes to more risky ones. This is consistent with the establishment chain concept from the U-model. Also consistent with previous findings in the literature, the Chinese POEs set up subsidiaries in foreign markets with the aims to acquire critical inputs and achieve long-term growth. Based on these findings, Propositions 7 and 8 are derived. Proposition 7 proposes that *Chinese POEs tend to start out with exporting before moving to more complex entry modes*, and Proposition 8 suggests that *Chinese POEs that envision emerging global competition for their products prefer direct investment entry modes that provide them with faster internationalisation, higher levels of control and deeper knowledge about their host countries*.

Fourthly, results from the interviews reveal that some of the Chinese POEs tend to have high internationalisation intensity. These firms have internationalised rapidly. In terms of selecting foreign markets, they are geographically diversified, and their market selection criteria are inconsistent with the psychic distance perspective. These firms are pulled to foreign markets that offer strong market opportunities, rather than to markets that are geographically and socio-culturally proximate to the Chinese market. These all seem to support the INVs perspective. By looking at these POEs' internationalisation processes, three propositions are developed. Proposition 9 indicates that *Chinese POEs tend to opt for rapid internationalisation*. Proposition 10 is that *Chinese POEs tend to be geographically diversified, aiming to leverage location-specific advantages*. In terms of foreign market selection, Proposition 11 proposes that *Chinese POEs' internationalisation patterns are not well explained by psychic distance*.

Fifthly, the interpretation of Chinese POEs' resource base orientation needs to take firm characteristics, industry attributes and China's inexpensive production costs feature into consideration. The firms that value learning new knowledge and that operate in high-tech industries tend to be internationally orientated, while those that can utilise the low production costs in the domestic market are more home base orientated. Three propositions are derived based on these observations. Proposition 12 is that *Chinese POEs that are interested in obtaining new knowledge tend to be internationally orientated*, Proposition 13 proposes that *Chinese POEs that are in high-tech industries tend to be internationally orientated*, and Proposition 14 is that *Chinese POEs that are in traditional industries tend to be domestically orientated*.

Lastly, the Chinese POEs in the study reduce their uncertainty regarding international operations through various means. Management learning is a popular method. By experiencing the foreign market, firms gain first-hand knowledge. This reduces their perceived uncertainty, which, in turn, may lead them to commit more resources to the market. This is entirely consistent with the U-model's suggestion of experiential learning and incremental internationalisation. In addition, networks and observing other firms' international operations also facilitate the reduction of uncertainty. Accordingly, Proposition 15 is formed, which suggests that *Chinese POEs work to reduce uncertainty through experiential learning.*

In summary, this thesis evaluates the theoretical and practical utility of some widely-cited streams of current research, in the context of POEs in China. It finds that neither the U-model nor the INVs framework is sufficient to explain Chinese POEs' internationalisation behaviours. While neither framework can explain the Chinese POEs' internationalisation phenomenon on its own, they provide considerable value in analysing the internationalisation actions of the Chinese POEs when they are combined. Similar to INVs in other countries, Chinese POEs have internationalised at a rapid pace, they are not constrained by psychic distance, and they rely heavily on networks to facilitate their fast internationalisation. Compared to the traditional U-model, they are more flexible. However, management learning is their main means of reducing uncertainty as the U-model suggests. Based on these findings, 15 testable propositions have been developed regarding different aspects of Chinese POEs' internationalisation.

### 8.3 Research Limitations and Future Research Areas

While the results of this study contribute knowledge to the international business literature, there are certain limitations that should be recognised and overcome in future research. Firstly, due to the qualitative nature of this research, it should be acknowledged that the results cannot be statistically, but only theoretically, generalised to other similar empirical contexts. Future research could build on this study by using a quantitative research methodology. Empirically testing the 15 developed propositions would shed further light on Chinese POEs' internationalisation processes.

Secondly, this study is conducted in a single-country context: China. This raises the concern that the findings might be country-specific. Studies with comparative samples of firms from other countries should be used to test and extend the generalisability of the findings.

Thirdly, samples were drawn from a cross-section of industries, including telecommunications networks, electronics, metres and textiles, located in the provinces of Guangdong, Fujian and Zhejiang in south-eastern China. Even though there is no *a priori* reason to believe that Chinese POEs from these industries, located in these provinces, would behave differently from general Chinese POEs, this sample may not be fully representative of the entire country. The results from this study should be interpreted in light of these limitations. Future research would be warranted to investigate Chinese firms from different industries and located in other parts of China, which would give further insights into how Chinese enterprises internationalise.

Fourthly, all the studied firms have a relatively short history of internationalisation, having started their international activities in the 1990s. Similar to their Western counterparts, the Chinese POEs' internationalisation is dynamic, and there are various factors influencing the process. Meanwhile, the environment that surrounds the firms continues to change. These factors suggest that longitudinal studies, based on companies' internationalisation processes over time, would provide very useful knowledge from an evolutionary perspective.

Fifthly, the analysis is based on foreign activities of small and medium-sized privately-owned firms. Since there are four kinds of enterprises in China (Poutziouris, Wang, & Chan, 2002), caution should be exercised when generalising the findings beyond this type of firm. It would be fruitful for future research to investigate other types of firm's internationalisation processes, as well as make comparisons.

Lastly, the interviewed firms were selected from the manufacturing sector. Since the tertiary industry is increasingly important to the economy, further research could investigate Chinese POEs' international behaviours in the services sector.

These limitations offer opportunities for researchers to build on the findings from this study. Besides those already noted, there are other research areas that are worth research attention. Previous studies have found that many Chinese firms start foreign operations with equity-based entry modes, such as cross-border M&As, JVs, and greenfield investment, to shorten their learning processes (Cooke, 2006; Hong & Sun, 2004; Wu,

2005). In contrast to those findings, this study finds that the Chinese POEs seem to choose exporting for their initial internationalisation before moving to more complex entry modes. This difference may be due to this study's focus on small and medium-sized POEs, also the small sample size may well be another explanation. Future research could empirically examine various types of Chinese firms' initial market entry modes for the full range of firm sizes and with a larger sample size.

## **8.4 Implications of This Study for Chinese Firms**

Based on the analyses of rich and detailed data, this study offers implications for Chinese firms that have international operations or are planning to go international. Firstly, despite the fact that internationalisation involves enormous challenges, all the interviewed firms indicated that their decisions to internationalise were rational. Most assessed their international operations as being successful. Other Chinese enterprises that are planning to go overseas may be encouraged by the fact that the interviewed POEs all noted that internationalisation represents some real opportunities of which Chinese firms should not be afraid. To capture benefits from internationalisation, a thorough business plan is a valuable asset, and having some knowledge about the foreign market beforehand is also a necessity.

Secondly, Chinese enterprises are latecomers in the current global marketplace. As such they have disadvantages when competing in sophisticated markets; these include lacking managerial know-how, understanding of global strategy and international brand recognition. In contrast, Chinese firms have cost advantages compared to their Western

counterparts, given that China has an abundance of labour and raw materials. However, this advantage is diminishing since China entered the WTO in 2001. More and more foreign firms are able to utilise China's low material costs and low labour costs to enhance their own competitive advantages, as a result of the reduction in trade barriers. In order to become competitive, Chinese firms may want to focus on utilising factor endowments in their home country to achieve cost advantages. Simultaneously, they could diversify geographically, to leverage location-based advantages. Through integrating production from the low-cost home base with acquired competencies developed overseas, they should be more able to achieve sustainable competitive advantages.

Thirdly, internationalisation presents an important opportunity for growth and value creation. It also involves many challenges. Since there are political, economic, legal and cultural differences between host and home markets (e.g., McDougall & Oviatt, 1996), a firm needs to have different ways of doing business in different markets. In order to compete successfully with foreign firms in the global marketplace, Chinese POEs need to understand the local environments and adjust their business behaviours. As *Company B* remarked, Chinese firms need to have an open attitude and a cultural sensitivity to foreign markets. They need to adjust their market offerings to meet their foreign customers' needs rather than just transferring the domestic market needs to their foreign markets.

Lastly, Chinese POEs should utilise various networks. They could seek advice from governmental agencies for different issues, from generic market intelligence to market entry regulations or even to specific customised research. For those that are planning to start doing international business, they also could utilise industry associations to obtain internationalisation knowledge from other firms that already have international operations.

## **8.5 Implications of This Study for Chinese Policy Makers**

Chinese firms are vulnerable to the challenges of international business, as many lack experience and human resources, and have outdated technology. A survey of businesses in China suggested that about 55% of China's overseas investment enterprises were making profits, 17% were making losses, and the remaining 28% were breaking even in the 1990s (Shi, 1998). Accordingly, supportive public policies will be especially useful to firms.

Firstly, it is recommended that programs be tailored to the particular needs of those firms most in need of assistance. Training programs that help to upgrade managerial competencies would be particularly useful. In the meantime, to help domestic POEs to accelerate their internationalisation speed, the government could provide POEs with information about potential investment destinations, including the regulations and the investment environment.



Secondly, policy makers need to understand what impacts their policies have on Chinese firms' international performance; this should enable them to devise better policies for helping Chinese firms to become more competitive in the global market.

Thirdly, the government would also be advised to consider reducing the constraints that it exercises over indigenous firms. Bureaucracy and government interference in corporate affairs pose difficulties for companies trying to compete in the hyper-competitive global market. Thus, the state authorities might consider giving firms more autonomy over their international operations. Moreover, the government should also simplify application procedures and improve its information services pertaining to international operations.

Lastly, despite the fact that the private sector is the major driver of China's economy, indigenous POEs are experiencing discriminatory treatment, such as paying higher tax rates and having difficulties in receiving bank loans. To achieve a more sustainable national growth, China needs to use its resources in a more efficient way. In other words, POEs should enjoy equal treatment in taxation and financing as other types of firm.

## **8.6 Conclusion**

This research aims to understand Chinese POEs' international practices. The main research objectives are to understand why Chinese POEs internationalise, what factors drive them toward internationalisation and how they internationalise. By applying the U-model and INVs perspective as reference frameworks for the analysis, this study assesses

the explanatory power of each of the approaches in explaining the internationalisation behaviours of small and medium-sized Chinese POEs.

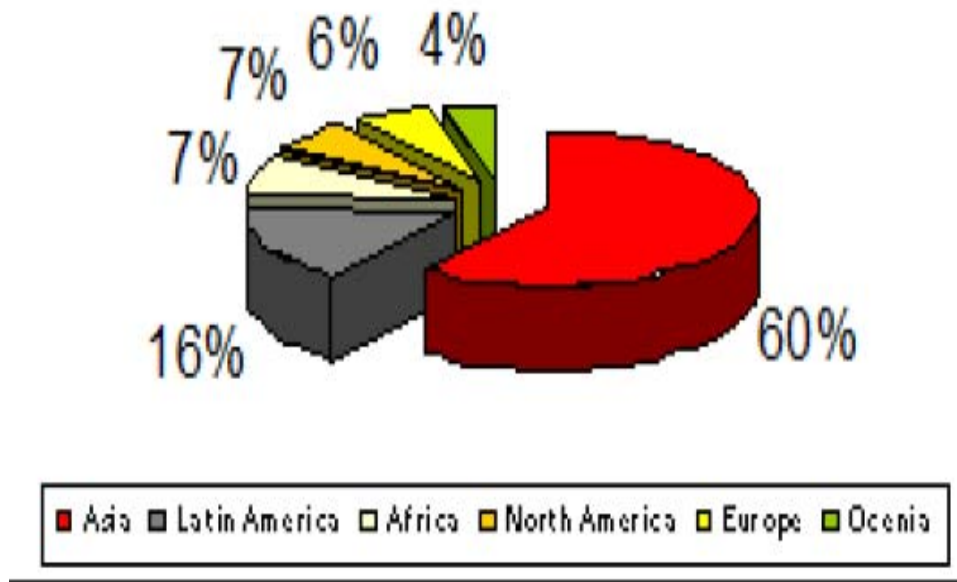
The thesis has addressed the research objectives through conducting semi-structured interviews with decision makers of six internationalised POEs in China. The findings show that Chinese POEs in the sample are pulled and pushed to internationalise, and that there are various reasons behind the firms' internationalisation decisions. This study also identifies a collection of factors, including the global environment, home country conditions, host country factors, industrial attributes, firm characteristics, and the quality of individual entrepreneurship, that have impacts on the firms' internationalisation processes. Looking at how the Chinese POEs internationalise, the results show that many of the Chinese POEs select exporting as their initial entry mode. Nevertheless, some of the firms have internationalised rapidly. These firms are also geographically diversified. The findings suggest that the concept of psychic distance does not provide strong explanatory power for these Chinese firms, since they are attracted by foreign markets that offer strong opportunities, rather than markets that have closer psychic distance to their home country. In terms of resource base orientation, some of the firms tend to be very internationally orientated. These firms have strong desires to acquire new knowledge through international operations. By merging knowledge gained in host countries with advantages found at home, these firms are able to improve their positions both domestically and internationally. The technology level of their industry also appears to affect the firms' international orientations, as the firms that operate in traditional industries seem to be more home base orientated; it may be that, for these firms, China's

inexpensive labour and low production costs better serve their needs. Meanwhile, Chinese POEs work to reduce their perceived uncertainty about international operations through various means, with management learning as a preferred means.

In conclusion, Chinese POE internationalisation behaviours do not appear to be particularly different to those of their Western counterparts. Neither the U-model nor the INVs framework can fully explain Chinese POE internationalisation processes on its own. However, each of the approaches has demonstrated its applicability to different aspects of the internationalisation of POEs in the rapidly developing Chinese environment.

## **APPENDIX A: EXHIBITS**

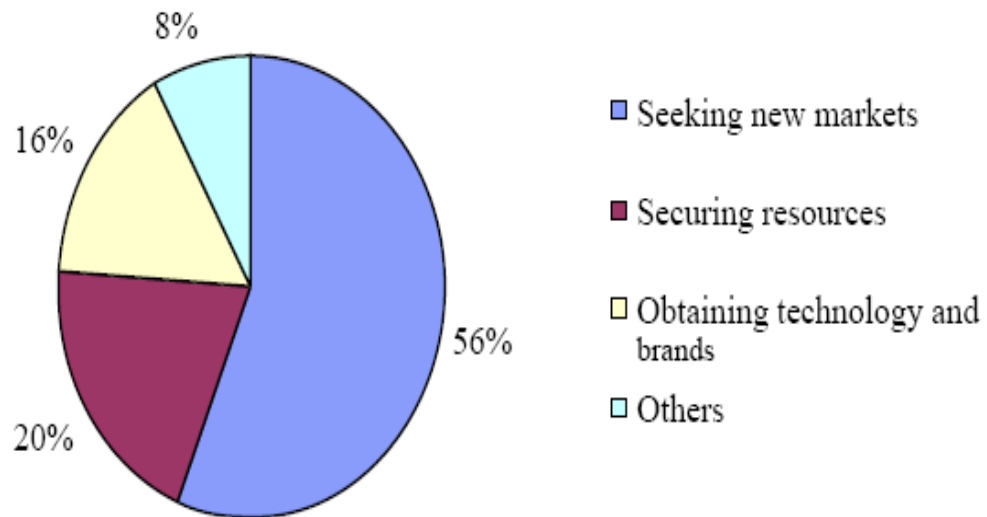
**Exhibit 1: Geographical allocation of Chinese outward FDI in 2005**



Source: MOFCOM

(Source: Bomal, C., Faramin, A., Perez, R., & Zhao, M. (2007, P. 8.). A new leap forward for China: Chinese outward direct investment (ODI) [Electronic Version]. Retrieved December 16, 2007, from [http://www.globalfinance.org/portal/data/publications/students/Chinese\\_ODI.pdf](http://www.globalfinance.org/portal/data/publications/students/Chinese_ODI.pdf))

**Exhibit 2: Motivations of Outward FDI from Survey of China's "Top 50 Industry-Leading Firms"**



Source: Roland Berger Strategy Consultants, 2003

(Source: Wu, F. (2005, P. 8.). *Corporate China goes global*. Singapore: Nanyang Technological University)

**Exhibit 3: China's Consumption of World Commodities as Shares of World Total**

<b>China's Consumption of World Commodities as Shares of World Total</b>		
	<b>1995</b>	<b>2003</b>
Iron Ore	30	35
Aluminium	9	19
Steel	12	27
Copper (refined)	10	20
Zinc (refined)	12	20
Cement	33	37
Oil	5	8 (2004)

Source: UBS Investment Research;  
International Energy Agency

(Source: Wu, F. (2005, P. 25.). *Corporate China goes global*. Singapore: Nanyang Technological University)

## **APPENDIX B: RESEARCH PROPOSAL**



## **Section 1. Nature and Aims of the study**

People's Republic of China (China) is one of the largest countries in the world. Since China opened its doors to embrace a more liberal trading system worldwide in 1978, it has increasingly played an important role in the world market, with fast growth rate. Meanwhile, there are an increasing number of Chinese companies that have been active in the international arena despite a huge and fast growing domestic market. Many of these firms are privately-owned enterprises. Nevertheless, limited empirical research has been conducted to understand Chinese firms' especially Chinese privately-owned enterprises' internationalisation. This study seeks to address the existing research gap by investigating the rationales, influential factors and approaches driving Chinese privately-owned enterprises' internationalisation.

### ***1.1 Research Questions***

- *Why do Chinese privately-owned enterprises internationalise?*
- *What factors lead to internationalisation among Chinese privately-owned enterprises?*
- *How do Chinese privately-owned enterprises internationalise?*

### ***1.2 Specific Research Objectives***

- *To identify Chinese privately-owned enterprises' motives for internationalisation.*

- *To identify factors that lead to their internationalisation.*
- *To identify their objectives for internationalisation.*
- *To identify their approaches for realising international objectives.*
- *To identify their market selection criteria and evaluation.*
- *To identify their evaluation of international opportunities.*

## **Section 2. Research Methodology**

The research adopts semi-structured interview approach to obtain primary data. Target respondents will be CEOs, executives, owners, and owner-managers who were involved in the firm during the time when the decision to internationalise was taken. Each interview seeks to collect information about the participant firm's background information, rationales behind internationalisation decision, and the respondent's comments about the company's international activities. Each interview is expected to last around two hours. This research is strictly confidential. The information from this study will be reported in aggregated manner such that no individual participant or participate company name will be identifiable. Ethical approval has been obtained under the Victoria University of Wellington research guidelines.

## **Section 3. Benefits and Contributions of the Research**

### ***3.1 To Your Organisation***

Internationalisation presents an important opportunity for growth and value creation. It also involves many challenges. By understanding the nature of internationalisation, firms can gain maximum from their internationalisation. Meanwhile, by understanding factors

that influence on Chinese privately-owned enterprises' internationalisation decisions, more and more privately-owned enterprises might opt to engage in international activities. This would further contribute to the country's economic growth as well as strength its global position.

### ***3.2 To the Research Field***

This research would add knowledge to our current understanding of Chinese firms' internationalisation. Findings not only would shed light on the way Chinese firms internationalise, but also add to knowledge about international entrepreneurship and internationalisation in the context of small and medium-sized firms from developing countries. Moreover, the practical relevance of such findings can be assumed to serve the further development of internationalisation of Chinese small and medium-sized firms, which should be of the interest and importance to many constituencies such as local government, domestic and foreign multinational enterprises.

## **APPENDIX C: PARTICIPANT INFORMATION SHEET**



**Title of the research Project:**

**Exploring Chinese Privately-owned Enterprises' (POEs') Internationalisation**

A research study to fulfil the requirements of the Master of Commerce and Administration (MCA) in International Business at Victoria University of Wellington in New Zealand

Dear Sir or Madam,

My name is Churu Lin. I am a Masters student in International Business at Victoria University of Wellington in New Zealand, undertaking research into Chinese privately-owned enterprises' internationalisation processes. As part of my Masters degree, I am here in China to conduct empirical research, which will eventually lead to writing a thesis. Internationalisation is a strategy that firms apply for different reasons with different approaches. This research seeks to learn about internationalisation of Chinese privately-owned enterprises. In this study I seek to conduct semi-structured interviews with decision-makers (i.e. CEOs, executives, owners, owner-managers involved in the firm during the time when the decision to internationalise was taken) of internationally active POEs. During interviews, open-ended questions will be asked. This study aims to improve our knowledge of Chinese privately-owned firms' internationalisation and entrepreneurship. The aggregated results may be used for presentation in professional and academic conferences and journals, but no individual company will be identifiable in any published or presented material.

The University requires that ethics approval be obtained for this research. This is to ensure your interests are protected and that you knowingly consent to helping me with my research. This approval has been granted by the Pipitea Human Ethics Committee. Participation in this research is completely voluntary. Participants' responses will form the basis of this study, which will be kept strictly confidential to myself and my

supervisors. The interviews will be taped, if you give consent. The data will be removed from our files three years after the end of the research. The information from this study will be reported in an aggregated manner such that no individual participant or participating company name will be identifiable. This thesis will be submitted to my school for marking, and a copy will be kept in the University library after it has been marked. The interview will last for around two hours. You may refuse to provide any information that you deem too sensitive. You can withdraw at any time during the interview, or up to two weeks after the interview, without having to provide any reason for your decision. After the interview, you will receive a transcript for your review and validation. If the researcher does not hear back from you within two weeks' time, it is assumed that the transcript is acceptable. If you desire, you will receive a summary of the research report upon completion of this project. In return for your generous time, you will receive a gift from New Zealand.

Your participation would be much appreciated. Should you have any questions regarding this research, please do not hesitate to contact me or my supervisors. I thank you in advance for your participation, and wish that your career and business are thriving and prosperous all the time.

Yours sincerely,

Churu Lin

Email: [linchur@student.vuw.ac.nz](mailto:linchur@student.vuw.ac.nz)

Signed:

Date:

**Supervisors:**

Dr. Elizabeth Rose

Email: [elizabeth.rose@vuw.ac.nz](mailto:elizabeth.rose@vuw.ac.nz)

Dr. Peter Zettinig

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School of Marketing and International Business  
Rutherford House, 23 Lambton Quay, Pipitea Campus  
Wellington, New Zealand

## **APPENDIX D: PARTICIPANT CONCENT FORM**

**Confirmation and Signatures:**

I, -----, give consent to my participation in the research project entitled:

**Exploring Chinese Privately-owned Enterprises' (POEs') Internationalisation**

In giving my consent I acknowledge that (please tick the appropriate boxes):

- ☐ I have been given enough information and have understood clearly the purpose of this research project.
- ☐ I have had an opportunity to ask questions and have them answered to my satisfaction.
- ☐ I have read the Participant Information Sheet, and I understand that my participation in this research is totally voluntary and that I may withdraw myself from this project at any time during the interview, or up to two weeks after the interview, without having to give reasons.
- ☐ I understand that any information or opinions I provide will be kept confidential to the researcher and the supervisors, and the information from this study will be reported in non-attributable manner, such that neither my identity nor my company name will be identifiable.
- ☐ I also understand that the data collected from the interview will be destroyed three years after the end of the research.



☐ I understand that the information I give will not be used for any purpose other than that stated in the Participant Information Sheet accompanying this form.

☐ I agree to take part in this research.

☐ I agree to have conversation taped.

Signed: \_\_\_\_\_

Date: \_\_\_\_\_

I would like to receive a project summary when it is completed.

Tick box ☐

E-mail or Postal Address:

\_\_\_\_\_  
\_\_\_\_\_

## **APPENDIX E: INTERVIEW SCHEDULE**



## **I. Opening**

- **Introduction**

Thank you for your willingness to be interviewed. The study aims to understand Chinese privately-owned enterprises' internationalisation phenomenon. Your participation will provide valuable information for this research topic. I am grateful for your help in this study.

- **Purpose**

During the interview, I would like to ask you some questions about your company's background, motivations for internationalisation, factors that lead to internationalisation, objectives for internationalisation, approaches for realising international objectives, market selection criteria and approaches to evaluating international opportunities.

- **Benefits to participating**

Your participation in this study will contribute knowledge to our understanding of how and why Chinese small and medium-sized firms pursue internationalisation. In return for your generous time, you will receive a small gift from New Zealand. In addition, I will provide you with a summary of the results after I have finished the research project, if you desire.

- **Time Line**

This interview will last around two hours, though we can talk longer if you like.

- **Confidentiality**

I want to remind you that your participation in this study is entirely voluntary, and you may always refuse to provide any information that you deem too sensitive. You may also stop at any time and ask me any questions you may have. You can withdraw at any time during the interview without having to give any reason. At any time up to two weeks after the interview, you will also have the right to withdraw from the project or have your answers erased. To withdraw, simply contact me or my supervisors via the contact information provided on the previous page. Information that would make it possible to identify you or your company will never be included in any sort of report. I would also like to ask your permission to record this interview. The data will be accessible to myself and my supervisors. The information will be removed from our data files three years after the end of the research. Do you have any questions? Are you ready to start?

## **II. Interview Structure and Process**

*Each interview will be organised into three parts. The first part aims to find out general information about the participating firms. The second part seeks to find out each firm's internationalisation experience. The last part will seek comments from interviewees regarding their firms' international operations.*

- **Business background information**

1. When was your business established?
2. When did the company start international operations?
3. How was your firm's performance, in terms of revenues, before internationalisation?  
How did internationalisation affect your revenues?
4. How many employees did you have when you started international operations?  
How many employees do you have currently in China? How many employees do you currently have abroad?
5. At the time when you started internationalisation, what kind of competition did you face in China? How has it changed since then?

- **Rationales behind internationalisation decisions**

1. Which factors were most critical when your firm first considered international operations?
2. What were your initial objectives for your international operations?
3. How did you know which foreign markets to enter? What were your criteria?
4. How did you initially/subsequently enter markets (i.e. exporting, sales offices) and what were the rationales for these approaches?
5. If you think about the conditions at the time when you took the decision to internationalise, what factors had the greatest impact on your decision?

- **Personal factors**

- **Factors within your company (for instance, an overcapacity)**

- **Industry factors (such as competition or shortage of supply)**

- Threats or opportunities in the institutional environment at home
  - Changes abroad you perceived to affect you (positively or negatively)
- **Comments**
    1. How do you feel about your firm's international operations so far?
    2. What was the most beneficial decision you have taken with respect to internationalisation?
    3. What would you do differently if you started internationalising again?
    4. How do you see your international business in the future?
    5. What is your advice for other companies that are considering international operations, in your region and for firms in your industry?

### **III. Closing**

- **Summarising**

*Summarising the main issues discussed during the interview.*

Is there anything else you want to add or anything you want to ask me about?

- **Thank the respondent for participating**

Thank you for the time you took for this interview, and thank you for sharing your experience. I should have all the information I need. Would it be alright to call you if I have any more questions? Should you have anything you want to discuss further, please do not hesitate to contact me.

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