# Internationalization - theoretical introduction.

Work Package 2

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**INTERNATIONALIZATION – theoretical framework**

Process of internationalization has been widely recognized in the last decade, as more and more companies decide to go abroad and expand their business. In literature, the term "internationalization" refers to continuous process of choice between policies which differ from the status quo of the company, and constitute a certain stimuli for shifting to higher export phases and revenues. Internationalization also implies modification of company's insight into its prospects and increases in capacity to compete on global markets. From different point of view, internationalization can be perceived as a kind of entrepreneurial act, which leads to go far beyond domestic market and go internationally.

The process itself is recognized as highly demanding, while it requires lots of efforts and recourses (financial and managerial ones) to be effective and self-sustaining. Getting sufficient financing resources to internationalize, on one hand creates huge opportunities for companies to gain new markets, but – on the other hand it constitutes a risk of failure. Another thing is, that going abroad requires not only financial resources, but also non-material ones. The last one can be identified as skills and knowledge, managerial experience and many others. Non-financial resources are often even more valuable and contributing to general company`s performance than pure financial capital.

If a company does not meet basic requirements to keep the process going, sometimes is occurs that it has o be stopped as resources are too limited. One of the possible reasons for that is lack of professional knowledge, skills and information, but also it can be interrupted by environmental turmoil which exposes the company for high risk.

To tackle the internationalization process and make it effective, there emerges a need of holistic approach to the issue. Occasional activities on external markets should not be treated as internationalization, as they do not really influence company` long-term growth. From very classical (traditional) perspective, the internationalization is seen through the lens of economies of scale, which is a characteristic domain of big companies. Small and medium sized enterprises are at far greater risk when stating activities on foreign markets. Small and medium sized companies are more like to operate on home markets [Coviello & Munro 1997; Holmlund & Kock 1998,Lindmark 1998]. However, due to fast and broad globalization, small and medium sized enterprises start going abroad, and gradually become important players on world markets. Globalization requires global exposure, creates needs for becoming a part of global business chains. These can is highly demanding for companies, creating new opportunities for gains creation. Companies which do not incorporate themselves into global systems, take huge risk of being left behind and perceived as peripherical entities.

In general, "internationalization" can be explained as "*the process of increasing involvement in international operations*..." [Aharoni 1966], which encompasses wide array of activities. Knight and Cavusgil [1996], define internationalization as process when company becomes more and more involved in international business, entering new external – often distant – markets. However passively perceived, they [Knight and Cavusgil, 1996] state that the process can be slow due to significant adaptations needed to get fully assimilated into foreign market and gain ability to adjust to changing environmental conditions.

Today, as the globalization process is broad and inevitable, "*there is no place for companies to hide from foreign competitors - all companies need to plan for growth and survival in a world of global competition"* [Root, 1994]. More and more companies chose "less" traditional pattern of internationalization and grow internationally fast, investing little resources. These novel ways of internationalization encompass for example internet trading, and using new information and communication technologies to become more effective, gain new markets and clients. Despite potential weakness these companies usually succeed in global market.

**WHY TO INTERNATIONALIZE**

Process of internationalization can be justified differently. According to Reiner [2008] and Ferdows [1997], companies tend to internationalize their activities, by hoping to get access to low-cost production, access new highly-skilled labor. They also state that companies determine their internationalization paths due to proximity of the external market. Dunning [1998] also underlines that companies tend to fulfill the "market seeking", "resource seeking" or "efficiency seeking', which is supposed to lead to better outcomes and benefits. Following empirical evidence provided by Van Dierdonck [2002], it is right to state that combination of the above elements persuades companies to internationalize. He [Van Dierdonck, 2002] also adds two motivations more: taking advantage of reallocation and better socio-economic environmental conditions in external markets.

However, if we are to define some common reasons for entering external market and starting co-operation with foreign partners. It is widely acknowledged that firms seek for internationalization due to:

☐ access to low-cost production, achievable through ease for getting low-cost labour force and/or recourses;
☐ access to skill, which is desirable if company need highly qualified workers – not accessible at domestic market – that would enable productivity growths;
☐ availability of more labour;
☐ inter-country and global competition which forces companies to strengthen their relative position;
☐ proximity of markets and suppliers – which makes the business easier and enables cost reduction;
☐ social and political advantages;
☐ sound macroeconomic policies in other countries which enhance foreign companies to invest.

To show the above in slightly different perspective, we can conclude that companies tend to internationalize due to 4 different motives. These are: "resource seeking", "market seeking", "efficiency seeking" and "strategic asset seeking" [see Dunning 1998].

Companies which enter foreign markets, can act in different ways, which – in effect – leads to acquiring certain goals. The simplest way to go abroad is to start exporting products and services. It is relatively easy, however requires certain financial resources for i.e. marketing actions. An alternative ways to internationalize is to develop a joint venture, in order to sell the products and services through a company operating in similar business, or – just sell license to company abroad and collect royalties. Similar way of internationalization is to create a contract with foreign company to do the business for a certain [%] of sales. This rather simply, however requires deep research to find an appropriate partner. The last possible way to start operating abroad is just open an overseas office or subsidiary company.

However, before starting to internationalize, it is highly recommended to think over few issues, which might be prerequisites for such changes. In effect, the company owners and/or managers shall think over the following:
☐ place/country of setting up new business and/or seeking a business partners;
☐ ask themselves "is it a good time" for my company to internationalize?;
☐ consider all pros and cons, putting special emphasis of risk taking;
☐ clarify all financial settings and agreements;
☐ assess the necessary resources that would be engaged in internationalization process;

☐ do deep and detailed market research identifying all potential barriers for doing business.

All the issues listed above, constitute a bundle of "questions" that should be answer, if we are to reduce the risk of failure. One also shall have in mind, that in certain markets/countries there can be met different constrains which disable our business to be a "success story". It is highly recommended to think about the all aspects associated with cultural and language barriers, religion, general economic performance, average level of disposable income, political stability/instability, legal conditions and government regulations.

Generally, the process of internationalization is perceived as something positive, which brings high benefits. We try to summarize the main advantages of entering new, external markets. They can listed as: expansion to foreign markets; new demand creation, increasing consumer base; financial profits generation; access to new technologies and innovation, risk sharing with external partner(s), new brands/products/services creation, growth in competitive power, offset in seasonal market fluctuation.

**STEPS TO INTERNATIONALIZE**

For a company that intends to internationalize, we can distinguish the following steps of entering external markets:

**Step 1**: Decide whether your company is "ready" to go abroad. Think if you have sufficient financial and human resources, do you have excellent knowledge on the market/country you wish to start to operate in?

**Step 2**: Do deep and extensive market research; analyze trends, economic and legal conditions, cultural/language/religious constrains.

**Step 3**: Prepare a detailed plan of future actions, allocating specific roles for certain people; share role and responsibilities;

**Step 4**: Find a business partner that you can trust (!);

**Step 5**: Think how and for you are going to be paid, try to prepare a kind of forecast for the next few years including optimistic and pessimistic scenarios;

**Step 6**: Try to identify all the risks, and think how you can avoid them;

**Step 7**: Write a "co-operation proposal" and then final legal agreements;

**Step 8**: Define "step-by-step" action plan of how to gain foreign market to minimize the risk of failure;

**Step 9**: Develop efficient monitoring system;

**Step 10**: GOOD LUCK!. 4

**TO SUM UP**

Nowadays, most companies tend to go international. The first big advantage of this time-consuming and often costly process is getting into foreign markets and gaining benefits of this. To be more general, we can distinguish several different "pros" explaining why companies should go abroad. The first advantage is creation of solid basis for further growth. When acting on domestic market, a company finally reaches the "limits" of market saturation of their products – this is a good sign to step further and start selling abroad. The next thing is getting more customers as your home market appears to be too small to extend your activities. This is strictly linked with growth potential, as global expansion allows for external market penetration and attracting more buyers. The last thing – in a general classification – is ability to discourage local competitors, and being first in getting to new markets.

Benefiting from more customers, growth potential and larger market, constitutes the three main "pros" why companies should try to go international. It is a massive attraction for firms and it is worth to put lots of efforts for this.

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