Understanding SME entry into emerging markets using institutional and resource-based theory

Introduction
Entry strategies of foreign firms into India and China are rapidly growing topics in the marketing and international business literatures (Johnson & Tellis, 2008; Luo, 2004; Luo & Park, 2001) and most research on foreign firms doing business in emerging markets concludes that firms find these markets to be quite different to those of the developed Western world (Neilsen, 2005). For example, the institutional environment choice of market entry strategy, market segmentation and the role of intermediaries reflect some of the challenges that firms face in entering and doing business in emerging markets (Freeman & Sandwell, 2008). However, as Johnson and Tellis (2008) note, how firms succeed in these markets has gone largely unexamined in the academic literature.

In this study, we explore the drivers for successful market entry and development by small and medium-sized enterprise (SMEs) into one of the large emerging markets – India. In doing so, we make several contributions. First, our study exclusively addresses SMEs, and does not include larger firms following FDI strategies. Recent research on international entrepreneurship has examined entry and performance with respect to emerging markets, but to date, there has been little, if any, research on foreign SME entry and development in the large emerging economies. Given that many developed economies rely largely on SME activity for their GDP growth (Ayyagari, Beck, & Demirguc-Kunt, 2007), focusing on the internationalisation of this subgroup of firms is critical. Second, by incorporating a range of country level variables, we consider the role of institutions (both host and home country) on SME entry and development. This augments the increasing attention paid to the role of institutions in foreign firms’ engagement with emerging markets (Meyer, Estrin, Bhaumik, & Peng, 2009; Peng, Wang, & Jiang, 2008). Third, following Benito, Petersen, & Welch (2009), we broaden our investigation to include post-entry factors that influence the longer term involvement of SMEs in India. It is important to consider market entry as a dynamic process that includes how firms develop after entry (Gao, Murray, Kotabe, & Lu, 2010; O’Farrell, Wood, & Zheng, 1998). Fourth, where the literature does address emerging markets and SME internationalisation, the emphasis has been on SMEs from emerging markets (Amal & Filho, 2010; Zhu, Hitt & Tihanyi, 2006) as opposed to SMEs entering emerging markets. In particular, the entry of SMEs from developed countries into large emerging markets is an under-researched area. Finally, we offer a theoretical context for SME internationalisation into emerging markets. This extends existing research, which has focused on identifying key influencing variables and antecedents of success (Johnson & Tellis, 2008). The link between resource availability and the effects of institutions has recently led researchers to argue that more insights can be gained by combining an institution-based view with resource-based views of international business in emerging markets (Meyer et al., 2009; Wright, Westhead and Ucbasaran., 2005). In responding to what the top international marketing and management journals seek to publish (Lepine & Wilcox King, 2010) and ‘combining lenses’ (Okhuysen & Bonardi, 2011), we develop a new theoretical position for SME internationalisation to emerging markets that extends theoretical insights from studies of MNE market entry behaviour (Meyer et al., 2009).

The paper is structured as follows. First, a succinct review of the relevant literature is presented. An overview of the research methodology then follows. Next, the results are presented and a conceptual framework is illustrated using these findings and insights generated from institutional and resource-based theory. Finally, implications for future research are identified.
Literature Review
SME Internationalisation and Market Entry
In addition to firm level factors affecting market entry and entry mode (Delios & Beamish, 1999), country level factors, such as political risk, national institutions and culture, geographical distance, and market size also have an effect (Ojala & Tyrväinen, 2008). However, the majority of studies of internationalisation and foreign market entry (even recently) have emphasised the MNE as the unit of analysis, rather than the SME (Petersen, Welch and Benito, 2010). Many theories of foreign market entry that were developed to explain the activities of MNEs have also been applied to SMEs, but it is now well-established that SMEs have different characteristics and drivers for internationalisation and entry mode choice (Brouthers & Nakos, 2004). It is well known that SMEs face a number of liabilities when entering foreign markets that are less impactful for MNEs. These include liabilities of smallness (Aldrich and Auster, 1986), foreignness (Zaheer, 1995) and outsidership (Johanson and Vahlne, 2009). Further, SMEs suffer resource constraints compared with MNEs (Coviello and Munro, 1997). In the context of emerging market entry from a developed country perspective, these liabilities and resource constraints would be especially challenging, given the institutional, cultural and psychic barriers that the firm is required to overcome. Research on this combination of influences and how SMEs respond in the context of market entry is underdeveloped, and, given the importance of SMEs to economic development, warrants further research.

Resources and the Resource-Based View (RBV) of the Firm
In the context of market entry, resources have generally been considered from the perspective of MNEs transferring resources to the host country (Meyer, Wright & Pruthi, 2009b). In this situation, the focus is on the associated benefits accruing to the host country. However, by considering the resource needs of the foreign firm, rather than resources that it can transfer to the market (Hennart, 2009), the RBV can help to explain mode choice, both at entry and during development of the firm in the market. The choice of mode thus depends largely on the resources needed by the foreign firm, in order for it to engage effectively in the host market (Meyer et al., 2009b). As noted by Meyer et al. (2009a), firms entering emerging markets are more likely to need ‘context specific’ resources in order to perform effectively. Context-specific resources include networks and relationships with agents, distributors and government agencies, which can all provide information and local knowledge, enabling access to skills relevant to the firm’s business. This might include access to channel partners and advice on intellectual property rights or legal requirements (Peng & Heath, 1996). Context-specific resources thus represent a number of important tangible and intangible assets and capabilities (Brouthers & Hennart, 2007; Peng & Heath, 1996).

Institutions and Institutional Theory
Of the different theoretical perspectives used for explaining firm strategies for entering and engaging with emerging economies, institutional theory is considered to be the most relevant in an emerging economy context (Peng et al., 2008; Meyer et al., 2009a). Institutions constitute those external factors and influences that impact on the functioning of the market mechanism, and are classified as formal or informal (North, 1990). They have an important role in ensuring that firms can engage in market transactions, without “incuring undue costs or risks.” (North, 1990, c.f. Meyer et al., 2009a: p.63). The impact of institutions on SMEs has been the focus of a small stream of research, notably within the fields of entrepreneurship and international entrepreneurship (Wright et al., 2007; Lu et al., 2010). In general, it is concluded that SMEs have more difficulty in managing the negative effects of weak formal institutions, characteristic of emerging markets, largely because they lack resources (Lu et al.,
While informal institutions in emerging markets tend to be stronger, compensating for weak formal institutions (Peng et al, 2008), SMEs often face challenges relating to cultural and psychic distances (Coviello & Munro, 1997) when entering these markets.

Research Methodology
Method, Sample and Data Collection
Research was conducted using an exploratory qualitative approach, which is considered appropriate for studying phenomena in depth (Eisenhardt, 1989). The unit of analysis was the firm, with relevant senior managers in the firms being interviewed. Sixty two New Zealand firms were purposively selected for the study, based on the following criteria. They were characterised as small to medium sized (< 10 - 250 employees) according to the OECD categorisation of firm size (OECD 2005), and were involved in a range of both manufacturing and service industries; all had internationalised into India. A semi-structured questionnaire was prepared, guided by key constructs identified from the literature. These included external and internal factors, capturing both institutional and firm-level resource-based influences. Open-ended questions were included in order to gain deeper insights into the phenomena being investigated (Crouch & McKenzie, 2006). Data were collected using face-to-face interviews with the CEO/Managing Director, and/or International Marketing Manager of each firm. Two interviewers were present during each 1-2 hour interview; these were audiotaped and later transcribed.

Data Analysis
Analysis of the transcribed data was carried out using the computer assisted qualitative analysis software programme, NVivo 8. For the purposes of analysis, each interview was treated as a ‘case’ (Miles & Huberman, 1994). Interview data were initially coded using open coding, and then grouped into within-case themes and patterns using an axial coding process, which helps to identify the key factors and their patterns of interaction within and between the case (Strauss & Corbin, 1998). Further iteration and sub-coding took place using selective coding, where the case data revealed specific aspects relating to the core theme involved. Pattern-matching (Miles & Huberman, 1994) was used to compare patterns and themes across cases.

Results and Conceptual Framework Development
Factors influencing the entry mode of the NZ SMEs into India and their subsequent business development broadly fell into firm-level factors and country-level factors, in accordance with the findings of others (e.g. Johnson & Tellis, 2008). Firm-level factors included firm resources and firm characteristics, and country level factors revealed separate, as well as related, influences of host and home countries (see Appendix 1 and 2). We use the institutional and resource-based theoretical perspectives to interpret our findings, as these provide appropriate lenses through which to view and interpret these results (Peng et al, 2008).

The SMEs relied almost entirely on external agents (primarily their business partners) when dealing with host country formal institutions, such as government agencies and regulatory authorities. Not only were the partners important for connecting the SME to key institutional bodies, but also for advising the SME manager on how to interpret and implement the formal rules, which tended to be loosely and inconsistently applied and monitored – characteristic of a weak formal institutional environment. The SME managers built strong relationships with their Indian partners, who were able to bridge the formal institutional distance faced by the SME. With respect to the informal institutional environment, SME managers stressed the need to gain credibility or legitimacy with their business partners and
to understand the cultural and social norms that govern the relationship-building process. Having a strong relationship with a business partner who was respected and well connected in the local business environment, as well as society more broadly, tended to transfer legitimacy to the NZ firm, as the relationship was seen as an endorsement of the latter’s trustworthiness and acceptance. Our study also revealed some interesting findings regarding the importance and interaction between home and host country institutions. Home country institutions (e.g. the government trade development organisation, NZTE) provided support for the SMEs in New Zealand prior to entry, including training and market research support. Through their offices in India, home institutions, also played a critical role, establishing connections for New Zealand SMEs with potential customers, as well as with host country institutional bodies. Further, at a diplomatic level, there was significant interaction between the home and host country institutions in terms of trade negotiations and diplomacy – all building awareness and legitimacy for New Zealand as a trading country, and for the NZ firms involved in trading relationships in India.

Regarding resources, we found that the SMEs were very dependent on the market in India for accessing critical resources, especially in the early stages of entry. Resource scarcity of SMEs internationalising has been well documented (Coviello and Munro, 1997). The types of resources required by the SMEs reflected aspects of cultural, psychic and institutional distance, as well as market size. Specifically, the resource needs centred on intangible resources, such as connections and relationships, and market knowledge; tangible resource needs reflected the firms’ deficiencies in scale, finance and access to distribution channels. The Indian partner, again, played a critical role in providing these resources, or brokering access to them. Given the extent and nature of these resource deficiencies, it is somewhat surprising that these SMEs are able to successfully enter and develop in this market. Further examination of the findings revealed the importance of resource-matching (Hennart, 2009), where the SMEs were able to offer specific resources that were valuable to the local partner. These included intellectual property, high levels of commitment and relational capability, and niche products and services that were scalable. To facilitate both resource and partner access, most SME managers chose to invest in a representative office in the market. Over time, as the SMEs gained knowledge, experience and market position, they were able to internalise some of the resources they formerly accessed externally, a process of ‘gradual internalisation’ (Petersen et al., 2010); but they retained a hybrid governance mode, either an informal partnership, or a formal equity joint venture. None of the managers anticipated moving to a wholly-owned subsidiary, signalling an expectation that their business partner would remain an essential element of their business model. Finally, we found that the characteristics of the firm, such as size, age, nature of product or service, and prior international experience, tended to influence the extent to which the firm was impacted by host country institutions and resource requirements as they entered and developed their business in India.

On the basis of these findings, we see that institutional factors that influence SME entry and development into emerging markets arise from both the host and home country, and from their interaction. Firms access resources, both internally and externally, the latter providing for the firm’s resource deficiencies associated with market entry. These institutional and resource-based factors and their interactions, as well as the potential moderating role of firm characteristics, in the context of SMEs entering and developing business in emerging markets are illustrated in a conceptual framework presented in Figure 1. The framework provides a theoretical basis for understanding the process of internationalisation of SMEs into emerging markets. Our findings suggest some important aspects that may be specific to SMEs entering emerging markets, considering the established literature on MNE market entry.

The framework considers the interaction between internal and external resources, suggesting that firms can switch their emphasis between these in response to changes in
institutional strength. For example, as our findings suggest, SMEs would be expected to draw
more fully on external resources to overcome difficulties associated with a weak institutional
environment, as they enter an emerging market. As they gain experience, the SMEs would
likely accumulate necessary internal resources, and use external resources to a lesser extent.
The framework also shows firm characteristics and home country institutions as moderating
these interactions, also indicated in our findings.

![Figure 1: Conceptual Framework for SME Foreign Market Entry and Development](image)

**Figure 1: Conceptual Framework for SME Foreign Market Entry and Development**

**Conclusion**

This study explored the experiences of SMEs from a small developed nation, New
Zealand, in entering and engaging in business in India. We have attempted to interpret our
findings through two mutually reinforcing theoretical lenses – institutional theory and the
resource-based view (RBV). This is a key contribution of this research, as there are few
theoretical or conceptual frameworks depicting developed-country SME internationalisation
into emerging markets offered in the extant literature; this is despite calls for more research in
this area, particularly empirically- and theoretically-grounded research (Peng et al., 2008).

A key question underpinning our study is: do SMEs differ from MNEs in market entry
into emerging markets? In addressing this question, we highlight a number of key findings,
which provide a platform for further research and implementation in practice. First, it appears
that there are a number of established influences on firms’ foreign market entry and
development identified from research on traditional markets that play out differently with
respect to SMEs entering and developing business in India. This relates, in particular, to the
nature of the interaction between institutions and resources, as well as between home and
host country institutions. Further, the study highlights the importance of intangible external
resources for SMEs entering India, and the gradual internalisation of these resources as firms
develop in the market. Our findings also suggest that SMEs rely heavily on a business
partner in India, suggesting the need for hybrid governance modes, such as joint ventures. We
highlight the role of both the local partner and home country institutions in bridging across
institutional distance and in brokering access to the market and external resources.

The findings lead to a range of opportunities for further research. Drawing on the lenses
of the resource-based view of the firm and institutional theory, the conceptual framework
should be further developed and tested empirically. Further, the study suggests some key
points of departure from existing MNE-based research for SMEs entering and developing
business in emerging markets, which warrant further research.
REFERENCES


Appendix 1

Firm-level Resources and Country-level Institutional Factors affecting Market Entry and Development of SMEs into India

<table>
<thead>
<tr>
<th>Resources (Firm Level Factors)</th>
<th>Institutional Environment (Country-Level Factors)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Pre-entry preparation and market entry processes</strong></td>
<td><strong>Host Country Factors</strong></td>
</tr>
<tr>
<td>Pre-entry Planning</td>
<td>Government Involvement in Business</td>
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<tr>
<td>Market Entry Process</td>
<td>Bureaucracy and Corruption</td>
</tr>
<tr>
<td>Credibility and Reputation</td>
<td>Infrastructure</td>
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<tr>
<td><strong>Entry Mode Choice</strong></td>
<td><strong>Home Country Factors</strong></td>
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<tr>
<td>Mode selection</td>
<td>Local Labour</td>
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<tr>
<td>Local Intermediaries</td>
<td>Government Assistance</td>
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<tr>
<td><strong>Post-Entry Market Development</strong></td>
<td><strong>Home-host Market Factors</strong></td>
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<tr>
<td>Relationships</td>
<td>New Zealand Image in India</td>
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<tr>
<td>Marketing Strategy</td>
<td>Cultural / Psychic Distance</td>
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<td>Long-term Commitment</td>
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<tr>
<td><strong>Firm Characteristics</strong></td>
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<td>Firm and Management Experience</td>
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### Pre-entry Preparation and Market Entry Processes

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<tr>
<th>Resources</th>
<th>Pre-entry Planning</th>
<th>Market Entry Process</th>
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<tbody>
<tr>
<td>Pre-entry Planning</td>
<td>&quot;Successful market entry needs to be well planned and requires investment in learning about the institutional environments.&quot; (Engineering Consulting Company)</td>
<td>&quot;The first successful bid took about four years to be realised and required development with local consultants, and an intensive phase of learning about the institutional environments in India. In addition, finding a suitable county representative with the support of the New Zealand High Commission was a decisive factor for a positive market entry into India.&quot; (Engineering Consulting Company)</td>
</tr>
<tr>
<td>Credibility and Reputation</td>
<td>&quot;You need to prove your value if you’re new in the market – you need to establish credibility…. Building credibility at the top level before getting sales is very important.&quot; (Electronics Company)</td>
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### Entry Mode Choice

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<th>Entry Mode Choice</th>
<th>Mode selection</th>
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<tr>
<td>Mode selection</td>
<td>&quot;Now that we have found the appropriate operational mode (own representative and staff, and a warehouse in the market), the company is, after a number of years, experiencing rapid growth in India. Our business there is becoming significant.&quot; (Specialised Manufacturing Company)</td>
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<tr>
<td>Local Intermediaries</td>
<td>&quot;The appointment of a good on-the-spot agent is crucial, and this process must be given detailed attention by each and every exporter.&quot; (Solid Energy Ltd)</td>
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### Post-Entry Market Development

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<tr>
<th>Post-Entry Market Development</th>
<th>Relationships</th>
<th>Marketing Strategy</th>
<th>Long-term Commitment</th>
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<tbody>
<tr>
<td>Relationships</td>
<td>&quot;We can only be successful in winning projects in India because of having agents who are very well connected politically and who can introduce us to the right officials.&quot; (Engineering Consulting Company)</td>
<td>&quot;Generally, we get good brand loyalty, as our products are of high quality.&quot; &quot;Know your customers well, help them make money, and they’ll be pretty loyal.&quot; (Industrial Manufacturing Company)</td>
<td>&quot;Another success factor... is to take a long-term commitment early because of the importance of relationships and personal networks.&quot; (Engineering Consulting Company)</td>
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### Firm Characteristics

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<th>Firm Characteristics</th>
<th>Firm and Management Experience</th>
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<tr>
<td>Firm and Management Experience</td>
<td>&quot;I have experience at working in both places (India and New Zealand). My experience with the general business practices there and dealing with the people there and, you know, the process that is followed in terms of entering and the various intricacies of that... assessing the time it will take for decision-making, particularly with the public sector and government sector, yes that does help a lot.&quot; (Security Company)</td>
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### Institutions

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<th>Institutions</th>
<th>Host Country Factors</th>
<th>Bureaucracy and Corruption</th>
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<tr>
<td>Host Country Factors</td>
<td>&quot;One of the entry barriers to the Indian market is the biased public procurement procedure and the process of short-listing companies. &quot; (Engineering Consulting Company)</td>
<td>&quot;We could not have bridged the huge gulf of understanding with respect to the intricacies of the market, cultural sensitivities, the numerous regulatory hurdles, or been able to deal with the red tape. The agent company has worked hard in lobbying the Federal and state authorities on relevant matters. There would have been major cost issues in trying to deal with such matters with&quot;</td>
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<td><strong>Infrastructure</strong></td>
<td>“We cannot build the market until the infrastructure is present. We need to invest in order to integrate our systems into the financial systems in most places. We have spent approximately $1M on software development and marketing in India to get the market ready.” (Software Company)</td>
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<td><strong>Local Labour</strong></td>
<td>“We weren’t prepared for the skill level and the productivity level. We expected too much out of what was available locally. We didn’t have the right project management on site to get the best out of resources that we had locally.” (Security Company)</td>
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<tr>
<td><strong>Home Country Factors</strong></td>
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<tr>
<td><strong>Government Assistance</strong></td>
<td>“We got a lot of assistance from NZTE before we went to India. They gave us some very useful market information and some ideas on what we needed to do to be ready for the market” (Software Company)</td>
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<tr>
<td><strong>New Zealand Image in India</strong></td>
<td>“New Zealand image – very positive.” (Telecommunications Company)</td>
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<tr>
<td><strong>Home-host Market Factors</strong></td>
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<tr>
<td><strong>Host Market assistance</strong></td>
<td>“We used NZTE services in India, and got a very, very, valuable market research report. NZTE did a really good job – they understood our business and our potential customers – an outstanding report.” (Specialised Manufacturing Company)</td>
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