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International market establishment among small and medium sized Swedish furniture producers

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Abstract
Small and medium sized enterprises (SMEs) are vital for a country's economy considering export growth, creation of job opportunities, and general economic development (Mtigwe, 2005). Thus, acknowledging the societal importance of SMEs in general and internationalization of SMEs in particular, it is puzzling how little research attention this area attracts. One reason why few internationalization studies focus on SMEs is that international involvement is a resource-demanding activity, and most SMEs operate under tight resource constraints resulting in low freedom of action. Among SMEs that are involved in international business, export is often the preferred entry mode. In this research, export is included as the entry strategy component of the international establishment model called the modified PSE model. Since the original PSE model was developed for large corporations entering emerging markets, it has been altered to fit SMEs entering foreign markets through export. The modified PSE model is based on four components: perception of internationalization barriers; strategy competence; entry strategy; and performance. All empirical material for this study will come from small and medium sized furniture producers in Sweden. Along with a theoretical discussion, this conference paper includes a presentation of the research model, sample frame, and research design.

Keywords: SME, furniture producer, perception of internationalization barriers, strategy competence, export, and performance.

Introduction
Regardless of company size, international involvement has become more and more essential for survival and growth (Axinn and MatthysSENS, 2002; Chetty and Campbell-Hunt, 2003; Coviello and McAuley, 1999; Minifie and West, 1998). Thus, from the perspective of small and medium sized enterprises (SMEs)\(^3\), international involvement is highly important as it

\(^3\) For a firm to be considered a small and medium sized enterprise the following requirements must be met (European Commission, Enterprise and Industry Publications):
enables, at the lowest level, meeting the tough international competition. Further, as the globalization effects on any firm are becoming more and more evident and unavoidable, even the non-exporter can feel the pressure from international competitors.

"During the last decades, the global business scene and the European one in particular have enhanced international competition affecting both enterprises with an export profile and enterprises focusing on the domestic market." (European Commission, 2003, pp. 9)

Being internationally active is not only important on the individual business level, but also on a national level. Existing research have found that SMEs are key to develop export growth, employment opportunities, and therefore positively contributes to the general economic development of the country (Mtigwe, 2005). For example in EU, 99 percent of all firms are SMEs, providing 75 million job opportunities and accounting for two thirds of the jobs in the private sector (European Commission, 2006). Further, between 2005 and 2006 these European SMEs increased their export by 12 percent (European Commission, 2007).

Considering how critical international business is on both firm and country levels, little research has, until recently, been focused on internationalization among SMEs. The small size of these firms and their limited access to resources are mentioned as the main reasons for the neglect (Holmlund and Kock, 1998; Zacharakis, 1997). Moreover, existing research on SMEs is often based on older theories (Axinn and Matthyssens, 2002) developed for larger firms (Coviello and McAuley, 1999, Chetty and Campbell-Hunt, 2003). In conclusion, more and updated research on international establishment among SMEs is necessary.

This research on internationalization among SMEs is conducted within the framework of an international establishment model called the PSE model. The PSE model comprises the three interrelated components of perception of entry barriers; strategy competence; and entry strategy.

First presented in 2001 (Pehrsson, 2001) the model was developed as a reaction to existing international market entry research that was being too tied to either the school of industrial organization (IO) or the resource based view (RBV) (Pehrsson, 2002). Considering the simultaneous importance of external and internal factors for a firm's international approach, one strength of the PSE model lies in its inclusion of both these elements. Another benefit of the model is the compact and well-defined

Have fewer than 249 employees, an annual turnover not exceeding 50 million EURO, and not be owned to 25 percent or more by a partner.
structure that frames the research without forcing set rules onto the empirical setting to be studied.

However, the PSE model was developed for large telecommunication operators active in internationally emerging markets\(^6\), and as a result should not be used in its original design while studying small and medium sized companies international establishment. Resting on the foundation of the original PSE model, the modified PSE model is introduced to particularly benefit studies of international market establishment among SMEs.

Thus, the research presented here is restricted to international establishment among SMEs. All empirical material will come from small and medium sized furniture producers in Sweden, a group of companies often described as conservative, operating within a mature industry. As the empirical data is collected from an industry resistant to change, but where competition is fierce, the theoretical applicability will be put to a tough test. Within the furniture industry only twelve percent of the firms have more than 30 employees, and the average firm has only four employees (Trä & Möbel Forum, 2008). Hence, the vast majority of the furniture producers in Sweden are small and medium sized.

Based on the above discussion and acknowledging that knowledge is missing on the complex issue of why some firms become internationally involved and why others continue serving only the domestic market, the research purpose is presented.

**Purpose**
The purpose of this research is to describe what differentiates small and medium sized Swedish furniture producers from each other considering their perceptions of internationalization barriers, entry strategies, strategy competences, and performance.

**Theoretical Framework**
The theoretical framework for this research rests on the PSE model, briefly described below. Thereafter the modified PSE model is introduced and presented in more detail, with particular emphasis on what is different compared to the preceding version.

**The original PSE model**
The structure of the PSE model is in the shape of a tripod, allowing examination of the relationship to be found between how entry barriers are perceived (P), level of strategy competence (S) available within the firm,\(^6\) A firm entering an emerging market is faced with essentially the same obstacles and uncertainties as a firm entering a foreign market (Pehrsson, 2001). Therefore, entry into a foreign market and entry into an emerging market is here treated without distinction.
and what entry strategy (E) the firm selects for establishment into emergent markets. See *Figure 1* below for the original PSE model.

![Figure Y](image)

**Perception of entry barriers**  
**Entry strategy**

**Strategy competence**

*Figure Y*: The original PSE model is an international market entry model consisting of three components as shown above (Pehrsson, 2001).

**The modified PSE model**

The modified PSE model is based exclusively on the original PSE model. However, because the original model was developed and applied around multinational corporations entering (emerging) markets, the need to questioning its relevance when used on exporting SMEs is apparent. For example, compared to large companies and corporations, smaller individual businesses operate with restricted access to financial, physical, human, technological, and organizational resources (Ekeledo and Sivakumar, 2004). Operating under strict resource constraints results in small margin of error (Wolff and Pett, 2006), which limit the firm's freedom of action with regards to, for example, market entry.

Below, each of the four components of the modified model is presented. Note that no attempts will be made to use the modified PSE model to study the internationalization *process* of the firms by capturing time effects.

**Perception of internationalization barriers**

A firm’s internationalization is simultaneously influenced by, and therefore depends on, the following three factors: the firm's key decision maker; the internal organization; and the firm’s external environment (Axinn and MatthysSENS, 2002; FillIS, 2002; Leonidou, 1995). In the original PSE model, perception of entry barriers includes only factors external to the firm as defined by Porter. This is despite the fact that Pehrson (2001) states that people within an organization influence how the firm perceives opportunities, and barriers. The modified model acknowledges that barriers to internationalization can stem from different sources. For clarity, the barrier component is therefore renamed from perception of entry barriers to *perception of internationalization barriers*. 

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Further, within the literature on entry barriers facing SMEs in their internationalization process, different authors group barriers differently. Leonidou (2000) discusses attitudinal; structural; procedural; and operational barriers, while Westhead et al (2004) use the following groupings: strategic; informational; process-based; and operational. In this research, barriers will be grouped into psychological; operational; product/market related; and organizational (Hamill, 1997).

Psychological barriers include perceptions of internationalization as being too expensive; too risky; not appropriate for the particular type of business; and not considered as a result of the domestic market being of satisfactory size. According to Hamill, operational barriers refer to hindrances related to the handling of export paperwork and documentation; lack of language skills; and delays in receiving payments. Organizational barriers include lack of resources to devote to export and lack of export experience. Finally, product/market barriers are factors caused by a misfit between what the firm has to offer and what the market demand. One example of a product/market barrier is the need for product adaptation.

Strategy competence
The strategy competence of a firm's management team is made up by the two sub-concepts of relatedness and market experience. The relatedness concept is not frequently used when discussing international establishment among SMEs. The main reason might be that relatedness commonly is used to discuss to what degree a firm's different business units align with the firm's core competence (Pehrsson, 2000). By definition, SMEs are restricted size-wise suggesting that they might not operate multiple business units. Thus, the relatedness aspect of SMEs' strategy competence cannot necessarily be determined based on a business unit's relatedness to the core competence of the firm. Instead it might be more appropriate to think of relatedness as how different firm functions or departments utilize resources and conduct activities that are similar to each other. This is in line with Farjoun's (1998) definition of relatedness as referred to relationships between activities or resources.

This research proposes that relatedness, as similarity between domestic and foreign activities and utilization of resources, is measured along the lines of pricing; general management skills; administrative skills; after-sales services; and brand recognition.

The market experience concept used in the PSE model will be adopted without any major changes. Thus, a firm's market experience will be subjectively measured by the firms' stated knowledge of or confidence with local competitors and local customers. The question is how much does a firm know about its competitors' product offers; customers; degrees of customization; pricing; and levels of research and development (R&D)?
How much a firm knows about its local customers will be evaluated in terms of customer types and locations. Higher confidence level will imply more market experience.

**Entry mode**

Market entry strategy decisions include entry mode selection for a particular target country and establishment of a marketing plan for the target market (Albaum et al. 2005). In accordance with existing research (Pehrsson, 2001), the inclusive term *entry strategy* will be substituted in the research model by the more specific term *entry mode*.7 Because SMEs are known to have restricted access to resources, they typically enter foreign markets using a low resource demanding entry mode such as export (Lages and Montgomery, 2004). Benefits associated with export, as compared to other more advanced entry modes, include: low risks; low resource commitment; and high flexibility (Leonidou and Katsikeas, 1996). As a result, export is commonly considered an easy and attractive entry mode, particularly among SMEs (Morgan and Katsikeas, 1997). Considering these findings in light of the contextual setting of this study, the decision was made to restrict entry mode options for this study to different kinds of export. Export is here defined in terms of how products made in Sweden are sold in foreign countries through different direct and indirect sales channels.

Firms are believed to select entry modes, in a path-dependent fashion, in accordance with the stage theory. In a review of current empirical work of the export development process completed by Leonidou and Katsikeas (1996) resulted in the three-category classification of pre-engagement, initial, and advanced involvement.

In the *pre-engagement* category, firms are not involved in international business for one of three reasons. First, some SMEs, or rather their founders, may simply not have the ambition to grow beyond a certain size or market (European Commission, 2003). The key decision maker or management team might have reached the conclusion that internationalization does not fit the firm's type of business, and that the domestic market provides adequate demand now as well as in the future.

"exporting may not always be the best growth strategy, especially if the firm can achieve positional competitive advantage in the domestic market" (Leonidou and Katsikeas, 1996)

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7 Sarkar and Cavusgil (1996) define international entry mode as "the institutional arrangement" (Sarkar and Cavusgil, 1996, pp. 826) that make it possible for a company to enter a market with its products and resources.
Second, some companies are interested in export even though they are not presently involved. One reason for why these firms are not involved includes the perception of internal and external entry barriers as being too high to bridge (European Commission, 2003). Third are the de-internationalized firms. These are companies that have been involved in international businesses but for some reason regressed to the pre-engagement phase.

In the initial export category, export is sporadic and is either increasing or decreasing. Firms answering unsolicited orders, thus reactive export behaviour (Riddle and Gillespie, 2003), belong for example to this first export phase (Leonidou, 2003). However, indirect export is the preferred entry mode for firms in this developmental phase. Indirect export is when a firm supplies a foreign market through an intermediary domestic partner (European Commission, 2003). For this study the indirect export modes included are export agents and piggyback\(^8\). General advantages associated with indirect export include: low costs; access to export professionals; speed of export volume accumulation; and low risk. The main disadvantages include lack of (end) customer contact; product goodwill is not ascribed the producer; and potential conflicts of interest between producer and intermediary (Albaum et al. 2005).

At the advanced export level we find the more experienced exporters involved in regular export activities. Firms conducting direct export are often found in this advanced state of development. When a company sells directly to a foreign importer or buyer, it is called direct export. Different sorts of direct export included in this study of exporting SMEs are: foreign sales branches (Leonidou and Katsikeas, 1996) including foreign resident salespeople; and traveling salespeople\(^9\). The benefits of these direct export modes include no profit sharing; full control; direct communication with foreign customers; permanent structure; product goodwill is granted the producer; and the possibility of attaining economy of scale. Further, foreign-based agents or distributors (Albaum et al. 2005) are also to be included as direct entry mode channels. Among all the different approaches to direct export, using exclusive agents or distributors is the easiest and less costly way (Ibid.). In general, direct export is believed to entail higher degree of management commitment; risks; and costs, than

\(^8\) Piggyback is sometimes considered a mix between indirect and direct export (Albaum, 2005). However, for this study piggyback is considered indirect due to the domestic nature of the transactions.

\(^9\) A travelling salesperson is based out of the producer's domestic market (Albaum et al. 2005). Holmlund and Kock (1998) found that one the most important entry modes among Finnish SMEs were to have their own salesmen. One advantage with sending their own salesman around to visit foreign customers included the direct contact established with customers and end-users.
indirect export. But while risks and costs are up, the direct exporter might be rewarded with higher return on investment.

Thus, this study will allow for separation between non-international firms, direct and indirect exporters. Consequently, it will be possible to comment on how firms' choices of entry modes influence perception of barriers; strategy competence; and performance. However, working within the framework of the static PSE model, no attempts will be made to comment on whether different firms pursue different strategic approaches or if they have reached different levels of internationalization as part of an ongoing process.

**Performance**

Attempting to increase our knowledge about what factors influence firms' performance positively and negatively is logically of great interest to researchers, politicians, and not least practitioners. As a result, such research has received a great deal of research attention.

Also, the individual components of the PSE model have been used in performance-searching research efforts. Perception of entry barriers and strategy competence have shown particular appropriateness (Pehrsson, 2004a; 2004b; 2006a; 2006b). But using performance as a dependent variable in simple research models is likely to fail as:

"Performance feeds back upon itself through numerous mechanisms." (March and Sutton, 1997, pp. 701)

Therefore, the interest here is to determine the possibility of treating performance as more than just a dependent variable along with the other three interrelated components. What has been done within existing literature when it comes to using performance as an independent variable?

During a literature review of journals in strategy and organizational behavior, March and Sutton (1997) found that almost a third of all articles included performance as a variable. They also discovered that in 71% of these articles performance appeared as a dependent variable. In only 12% of the cases, performance was included as an independent variable, and in the remaining 11% of the reviewed articles, performance was treated as both an independent and dependent variable. From these findings, it is clear that while performance has been used both as an independent and reciprocal variable, the frequency of this research approach is scant.

Further, in an empirical study of Portuguese SMEs, performance was included as an independent variable (Lages and Montgomery, 2004). The results from their study show that export performance is an antecedent
of the firm's commitment to export and that export performance influence the firm's export strategy\textsuperscript{10}.

In line with most models of organizational learning, Lant et al. (1992) include firms' past performance as an explanatory variable of strategic change. Their findings show that a firm's past performance (poor or successful) has both a strong direct and indirect influence on the organization's strategic orientation. More precisely, successful past performance indirectly influence strategic change by having a positive significant effect on environmental awareness. This is supported by Wiersema and Bantel (1992) who conclude that a firm's part performance positively influences its strategic change in terms of diversification. In other words, a firm that demonstrates strong performance can assign resources for environmental scanning and analysis. Correspondingly, poor performance leads to reduced external information seeking.

Thus, existing research demonstrates that, while it is not the practice within the field of international strategy, treating performance as an independent variable can be worthwhile. Therefore, the idea is to incorporate performance into the frame of the model together with the other three interrelated components. The result would be a modified PSE model made up by four (possibly) reciprocal components, relating to each other depending on the contextual settings.

Finally, performance can be assessed by financial and non-financial measures and can be either objective or subjective (Pehrsson, 2004a; 2004b, 2002). Thirkell and Dau (1998) advocate that export performance should be measured using a multi-item performance scale including both objective and subjective measures. Here overall firm performance will be measured using the objective financial measurement of ROA, and the subjective financial measurement of satisfaction with overall performances as related to industry average.

**Research model**

Based on the preceding theoretical discussions, the research model is established. This model is an outgrowth of the original PSE model to particularly benefit research of SMEs. For the model see *Figure 2* below. Evident in *Figure 2* and consistent with the original PSE model, no directional relationships of dependence are specified between the factors included in the model. Instead the strength and direction of existing relationships are likely to vary depending on firm specific attributes and is therefore a possible result of this study.

\textsuperscript{10} Export performance was found to have significant indirect effect on product strategy adaptation; significant direct effect on pricing strategy adaptation; and significant direct and indirect effect on distribution strategy adaptation (Lages and Montgomery, 2004)
Perception of Internationalization Barriers

Entry Strategy

Strategy Competence

Performance

Figure 2: The modified international market entry model.

Further, based on the theoretical discussions of the original and modified PSE model, it is at this point possible to add more detail to the modified model. In Figure 3 sub-components and other elements have been added, offering a research model with increased structural clarity.

Perception of internationalization barriers
Psychological
Operational
Product/ market
Organizational

Entry mode
Non-exporter
Sporadic export
Indirect export
Direct export
Other

Strategy competence:
Relatedness
International market experience

Performance
Objective financial measure
Subjective financial measure

Figure 3: The detailed modified international market entry model includes sub-components and elements.

Research design
In line with the purpose of the research, the relationships between the different components of the model are to be investigated. Therefore a number of hypotheses are constructed. Due to the fact that the hypotheses are not yet satisfactorily constructed, they are not included in this paper. The empirical data to be used for hypotheses testing will be collected using a quantitative survey addressed to the key decision makers or owners of the firms. All firms included in this study will initially be contacted by phone, whereby they are asked to participate in the study. The respondents will have the option to complete the survey over the phone, electronically using E-mail, or in written form (paper copy).
Sample
To be considered of interest for this research, all firms must be a SME and a furniture producer. The definition of SME used in this study is as defined by the European Commission, see footnote 1. In accordance with existing studies (European Commission, 2007), firms without employees will be excluded. Further, to control for sample heterogeneity, only furniture producers will be included in this study. Thus neither suppliers of parts and components nor retailers will be included. Approximately 420 companies in Sweden comply with the above definitions.

Discussion
Theoretical contributions originating from this research are along the dimensions of perception of internationalization barriers (including barriers regardless of origin), different degrees of export involvement (ranging from non-exporters to highly involved direct exporters), definition of relatedness (define relatedness as degree of similarity between domestic and foreign business with regards to certain attributes), and adding performance as a forth component of the model. Each one of these theoretical contributions refers to the specifics that this research is focused on SMEs, and the existing PSE model had to be modified accordingly.

Further, being promising but still relatively new, the PSE model should benefit from being tested in a different contextual situation. It will be interesting to learn to what degree the PSE model can be used to explain behaviors among small and medium sized firms within one industry.

On a practical level, the aspiration is that this research should contribute to the furniture industry to some degree. At the lowest level, the study should provide a foundation for discussion among the industry members and a platform for insight among politicians and other interested parties. From a government perspective the study provides profiles of companies at varying degree of export engagement that can be used for designing export promotion programs. To ensure that the results of the study is efficiently communicated back to the practitioners and other interested parties, a brochure consisting of the main results will be distributed once the results are available.

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