



Master's thesis

INTERNATIONALIZATION PROCESS OF FAMILY FIRMS: REASONS, NETWORKS AND OB-  
STACLES

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## ABSTRACT

This thesis investigates the internationalization process of family firms. This topic has been an object of widespread research efforts. In order to explore how family companies expand abroad it would be rational to consider internationalization theories, which show how company starts expansion and which factors affect the decision-making process and the speed of internationalization. Firms prefer different pathways: some expand gradually, while others are globally-oriented from their birth. In practical part internationalization of several Russian family firms is considered. It is a qualitative case study based on interviews and it's findings help to analyze internationalization process and to indicate the role of networks, distance-creating and distance-bridging factors.

**Key words:** Internationalization, family firm, the Uppsala model, the Network model, the International New Venture model, networks, pathway, born-global, entry mode.

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# 1. INTRODUCTION

*The introduction chapter of this thesis provides the background including the problem statement, objectives of study and research questions. Furthermore, this chapter presents the area of research.*

## **1.1. Background and problem statement**

Nowadays in order to survive family firms should prepare good strategies and enter new markets. In general, internationalization is a complex process and family firms are mainly cautious in each step they make in order to avoid mistake. But however, there are family enterprises that are international from scratch. First of all the company should decide is internationalization needed at that moment and what are key objectives. So, possible reasons of expansion will be summarized in this research. Secondly, the company should evaluate what are the strengths and weaknesses: are there enough networks, market knowledge and financial resources; are products quite innovative and on demand in a particular market. For family enterprises expansion can be especially challenging especially social capital. In this research it would be investigated to what extent do networks affect internationalization, and possibly lack of ties in a foreign market can be an obstacle of expansion. Generally, a big amount of networks accelerates the process of internationalization. When the company chooses where to expand, it should carefully analyze economic situation, competitors in the same market niche and demand; and further to choose a suitable entry mode. One issue that comes to each company's mind during internationalization is about which foreign market to enter, when to enter, scale of entry, and which entry mode to choose (Hill, 2007). Usually firms favor countries with a similar environment in order to avoid problems concerning language, culture and law. While expanding to far away markets company can meet many distance-creating factors, such as language and cultural differences, and if those exist than how to overcome these barriers?

The choice of a particular entry mode and a whole pathway depends on many factors, for instance, the innovativeness of the product, competitors, ownership issues, finance, networks, entrepreneurial talent, vision, economic and political environment, laws and other issues. Root (1998) assumed that "it is common that managers make a mistake of using the same entry mode for each market" (p.160), so each market needs to have unique approach and preliminary research. Mistakes come usually from lack of experience. In addition, while entering new markets firms should concern about the control of management, because only good management will allow meeting firm's strategic goals.

## **1.2. Aims and objectives of study**

This thesis investigates the internationalization process of family firms. Theoretical part will include definition of family firms, internationalization, psychic distance and types of knowledge. Besides, different internationalization theories, pathways and entry modes will be considered. And in order to give a clear explanation to problems mentioned above, several Russian family enterprises with international experience are selected to be case studies for discussing about internationalization.

The study will help in deep understanding of how do family firms internationalize. Key objectives of the study are following:

- to find out why do firms go abroad
- to consider internationalization models
- to identify the role of networks and how do family firms bridge social capital
- to describe possible entry modes and which do family firms give a favor
- to consider internationalization pathways
- to find out peculiarities of family firms
- to identify distance-creating and distance-bridging factors

According to the interest of studies, there are following research questions:

1. How do family firms start internationalizing?
2. To what extent does social capital affects the internationalization process?
3. What are the main barriers for family SMEs during internationalization and how do they overcome them?

## **1.3. Area of research**

Internationalization process of small- and middle-sized companies (SMEs) has been an object of widespread research efforts, and expansion of family firms is a developing a significant research area (e.g. Sciascia, Mazzola, Astrachan & Pieper, in press). Usually this issue is more generalized and only SMEs without mentioning the presence of the family in a company are considered or SMEs in developed countries. This thesis will include not just description and analysis of previous theoretical findings, but it also contains practical evidence obtained from the interviews with Russian family firms. Companies will be selected from different industries. This thesis is relevant not only for Russian family

companies that are planning to expand; it is also useful for SMEs in developing countries. Besides, this study is beneficial for students, who are interested in internationalization process.

## **2. THEORETICAL FRAMEWORK**

In this chapter definition of internationalization, description of different trade theories and internationalization models are presented. The Uppsala model, the Network model and International New Venture models are applicable for firms of different size, but this study is focused on family firms, which also will be defined in this chapter. Besides, reasons of internationalization, entry modes, internationalization pathways, psychic distance and obstacles during expansion have been described.

### **2.1 Definition of internationalization**

Welch and Luostarinen (1988) define internationalization as “the process of increasing involvement in international operations”. Another definition given by Calof and Beamish (1995) says internationalization is “the process of adapting firms’ operations (strategy, structure, resources) to international environments”. Based on dictionary definitions it can be generalized that the internationalization is the process of planning, designing and implementing products and services so that they can easily be adapted to specific local demand, languages and cultures.

### **2.2 Traditional theories of internationalization**

The importance of international trade to a country’s economic welfare has been heavily explained in the economics literature since Adam Smith’s (1776). The main idea was that economies should export goods and services in order to generate revenue to finance imported goods and services which cannot be produced indigenously (Coutts and Godley, 1992; McCombie and Thirlwall, 1992). Adam Smith developed his theory of international trade supporting of free trade against mercantilist foreign trade policies of protectionism. Adam Smith developed the law of absolute cost advantage for international trade. According to him, trade occurs between two countries if one of them has an absolute advantage in producing one good and the other country having absolute advantage in producing another good. An absolute advantage existed when the country could produce a product with less costs per unit produced than could its importer (Ingham, 2004). Because of this reason a country should import goods which it had an absolute disadvantage. His argument can be implemented not only in international trade, but it also can be within the country. According to Smith free international trade promotes international division of labor, because each country specializes in a particular group of products.



As labor becomes more divided and specialized, productivity grows dramatically. Smith claimed that we all are talented, but we learn by doing and find out how to produce goods at a lower cost and we start having higher returns.

In contrast to Smith, David Ricardo (1817) claimed that it not necessary to have an absolute advantage to gain from trade, only a comparative or relative advantage. According to Ricardo absolute advantage means greater efficiency in production, or the use of less labor factor in production. Comparative advantage means that the parity of the labor involved in the two goods differed between two countries, such that each country would have at least one good where the relative amount of labor involved would be less than that of the other country (Hunt, 2002).

Further, on the basis of Ricardo's theory the Heckscher-Ohlin model (Eli Heckscher, 1966 & Bertil Ohlin, 1952) was created. The authors from the Stockholm School of Economics stated that countries export products that utilize their abundant and cheap factor(s) of production and import products that utilize the countries' scarce factor(s) (Blaug, 1992). Wassily Leontief tried to prove this model empirically and found out an interesting aspect, called Leontief paradox (1954), the idea of which is that the country with the world's highest capital-per worker has a lower capital: labor ratio in exports than in imports.

Staffan Linder Burenstam has tried to find a solution to the Leontief paradox and thus created a theory known as Linder or demand-structure hypothesis. Staffan Burenstam Linder (1961) wrote: "The more similar the demand structure of the two countries the more intensive potentially is the trade between these two countries." So, according to him, international trade can occur between countries that have identical preferences and factor endowments.

The next well-known theory is called the New Trade Theory (late 1970s - early 1980s). It contains several economic models in international trade with a focus on the role of network and increasing returns to scale. One of these models, created by Paul Krugman in 1979, two countries are considered and in each of them consumers prefer variety, but the tradeoff between variety and cost exists. Because of economies of scale a firm's unit costs decrease while it's production increases; so, more variety means higher prices. Economies of scale cause in the direction of less variety. Nevertheless, trade raises welfare and scale of production will grow, and this in turn will cut costs and prices. In addition, the growth of variety for customers even in case when a world variety goes down is a core factor of globalization, when particular brands become well-known all over the world. Also, Krugman assumed the benefits of

capital and labor migration in order to reduce costs. Some New Trade scholars argued that protectionist measures will help certain industries to dominate worldwide. To sum up, the idea of this theory is that it might be beneficial for countries that have the competitive advantage in producing some goods to protect the trade of their products; and this will increase economic position of the firm. Those companies that can produce more of a specific product at lower cost than their rivals, may exploit comparative advantage and dominate in the market.

Michael Porter also contributed to the research of international trade by creating Diamond Theory. He had attempts to explain how does the company create and sustain competitive advantage. According to Porter the organization of the firm is considered as nine generic activities creating a value chain, and by many connections among them an independent system is formed. The result how one activity works influences on others. Manager's responsibility at that point is to connect and coordinate these activities. Porter says that competitive advantage is achieved by carrying out the activities in a more cost-effective way than competitors, better value and coordination (Porter, 1990). According to Porter innovation is related not only to product, but also to process and all these nine generic activities. Also he defines competition by five competitive forces: the threat of entry, the power of buyers, the power of suppliers, the threat of substitutes, and competitive rivalry. So, the company should create a strategy in order to have a good performance. Porter claims that these tools are: cost leadership, differentiation, and focus (Porter, 1990).

In international competition Porter considers configuration and coordination as important factors. Configuration refers to the places where each activity in the value chain exists. The implementation of configuration or coordination matrix helps to identify geographic positioning and the integration of value activities. According to Porter there are four broad combinations of configuration and coordination. The first one is called the "export-based" strategy, when configuration is geographically concentrated and there is low coordination of activities. In that case a firm gains profit by logistics and marketing. The second combination is called the "country-centred" strategy. It contains geographically disseminated configuration and few coordinated activities. The next one is "high foreign investment" which refers to coordination on a high level with geographically disseminated activities. This strategy is considered as costly one. And the fourth strategy is called "purest global" and it exists in geographically concentrated and well-coordinated activities (Porter, 1990).

The next well-known model is called Oli-Model, and was presented by Dunning in 1980. Mainly it was based on transaction cost theory, but the author has added 3 important factors to the process of interna-

tionalization: ownership advantages, location advantages and internationalization advantages. In order to compete with host country companies in their domestic markets, a firm should demonstrate its superior assets that will help company to gain profit that can cover costs. A firm's ownership advantages are reflected by its size, international experience and ability to develop differentiated products. The size of the company shows its capability to cover costs of marketing, for achieving economies of scale, and therefore, larger organizations can favor high commitment entry modes then low commitment ones. Also, the international experience affects entry choice. Firms with higher international experience tend to choose investment entry modes because they have enough experimental knowledge and social networks that help to follow more risky pathway of expansion. For companies that possess good abilities to develop differentiated products, it may be more efficient to choose higher control modes with higher levels of product differentiation (Stopford and Wells 1972). Company's location advantages include market potential and investment risk, which characterize market attractiveness. Generally, firms tend to prefer investment modes when they enter high market potential countries because they can provide long-term rents. Internalization advantages refer to contractual risk. On the one hand, when firm chooses low control entry mode it can benefit from the scale of economies of the specific marketplace, while not taking into account bureaucratic drawbacks. But on the other hand, when a firm prefers low control entry mode it will have higher costs in comparison with assets and skills integrated within the company in a case when the owner or management team has difficulties in predicting future events and act in the situation of uncertainty or in a case when there are no good opportunities in the specific market. Lack of opportunities, the problem of bounded rationality, and the situation of uncertainty can make the signing and observance of contracts senseless and more expensive (Andersen and Weitz 1986). In a case when there are no competing options and signing contract seems to be irrational decision because of the lack of possible partners or the presence of uncertainty it would be better to choose such entry modes like exporting or sole venture that will provide higher control because all the assets will be within the company.

### **2.3** The Uppsala model, the Network model and the International New Venture model

In contrast to the traditional view there are other internationalization theories which try to explain the process of internationalization and the behavior of middle- and small-sized firms. In contrast to majority of traditional theories these models, that include the Uppsala model, the Network model and the International New Venture model, have dynamic nature.

The most well-known model of internationalization behavior, the so-called **Uppsala Model**, has been claimed to be very general and therefore applicable to many different firms and different situations (Pedersen and Petersen 1998). Moreover, it is also relevant for explaining internationalization of family firms. In 1977, Johanson and Vahlne introduced the Uppsala model on the basis of arguments developed in the behavioral theory of the firm (Cyert and March, 1963; Aharoni, 1966; Carlson, 1966), in the theory of the growth of the firm (Penrose, 1959) and in the incremental decision-making process (Carlson, 1966). Based on empirical observations researchers explain theoretically an internationalization of firms and describe expansion from a learning viewpoint, because according to Johanson and Vahlne internationalization is tightly connected with knowledge acquisition and learning.

In 1959 Penrose has assumed that there are two types of knowledge: objective knowledge or “know-what” and experiential market-specific knowledge or “know-how”. Experiential knowledge is difficult to communicate and share with others, because they are based on personal experience. In comparison, general objective knowledge can be easily communicated and described by using printed or electronic media. Market-specific knowledge cannot be replaced by objective knowledge, because first one is related to theory, while second type is focused on particular opportunities, which keep firms consistent with the present and future activities (Johanson and Vahlne, 1977). However, both types of knowledge are essential during internationalization. For example, objective knowledge includes general information about foreign customers, their common traits or some methods of expansion, whereas the experiential knowledge knows contains information about traits of a particular customer or a firm. According to the Uppsala model role of the market-specific knowledge achieved through own experience is especially important. Experience generates business opportunities and constitutes a driving force in the internationalization process (Johanson and Vahlne, 1990). On the other hand learning through experience from a firm’s own operations is one of the main reasons why internationalization is often a slow process (Johanson and Vahlne, 1977). While going abroad a firm learns by doing. It is quite common that an entrepreneur does not have any preliminary international experience of expansion and that is why he chooses incremental internationalizing. For instance, Ingvar Kamprad was only 17 years old when he started selling farm implements under the name Ikea. Without business experience before setting Ikea he decided to expand step by step, he learned by doing. In the beginning he gave a favor to indirect market entries like franchising, which require less knowledge about country. Now Ikea is the world’s largest furniture retailer with 254 stores in 35 countries as of May, 2007.

Another important issue within the Uppsala model is market commitment, which is closely related to market knowledge. Market commitment is composed of all tangible and intangible assets that a compa-

ny accumulates in the individual country and the degree of commitment. Degree of the commitment is high if there are more specialized resources in the particular market (Johanson and Vahlne, 1977). A favorable situation is when a firm already has huge resources that help it to skip some intermediate stages of internationalization process; and market situation is quite stable and a company possesses good experiential knowledge reached through current operations that are the source of experience; or if a firm has already an experience from markets with analogical environment and the risks can be partly predicted. Unfortunately, in practice it is difficult to transfer resources to another market. Research and pre-testing should be done in order to reduce a risk of failure. A company should take into account the fact that countries have different management styles, culture, language, habits, attitudes to time, money, ways of communication; religion, and temperament. Before an expansion to a chosen market a firm should increase market specific knowledge, which includes knowing local competitors, customers attitude to the problem, a company solves, and purchasing power. One of the ways how to get market-specific knowledge is to hire personnel with international experience. While possessing good market-specific knowledge then there will be low probability of market risks and the market commitment will be stronger. In common, commitment decisions are made incrementally because of market uncertainty, risks, and opportunities (Johanson and Vahlne, 1977).

According to the Uppsala model firms are expected to go through the stages, from low to high commitment entry modes. There are four stages, called the “establishment chain” (Johanson and Wiedersheim-Paul, 1975), that includes: No regular export activities—Export via independent representatives—Establishment of an overseas sales subsidiary—Overseas production (Andersen, 1993). A company stores knowledge and enhances its presence in a foreign country by passing these stages. In stages 1 and 2 market-specific knowledge are not that needed as in further stages. When a company has learned more about a foreign market, it moves to Stage 3 and 4. However, the model does not include joint-venture operations which are widely-spread in the foreign operations and require intermediate levels of knowledge and commitment (Kontinen and Ojala, 2010). In market selection firms usually choose firstly nearby market, and then distant ones. Companies tend to favor nearby countries within a low psychological distance when they start internationalization and after that expand to psychologically distant markets (Kontinen and Ojala, 2010). According to Benito and Gripsrud (1992: 464): “Firms are predicted to start their internationalization by moving into those markets they can most easily understand, entering more distant market only at a later stage”. Psychic distance is the disturbance in information flows between organizations and foreign markets caused by psychological issues, whether they are actual, potential, or perceived (Ojala 2009, Oviatt, 2005, Child, Ng and Wong, 2002, Johanson and

Wiedersheim-Paul, 1975). Psychic distance is not totally the same as cultural distance due to the fact that it is based on individual perceptions. Psychic distance cannot stay always the same, there are constant changes due to development of trade, communication system, etc. (Johanson & Wiedersheim-Paul, 1975). Distance-creating factors can be related to differences in language, culture, education, political system, level of industrial development, level of knowledge of human capital and business practices, etc. A firm goes through stages, and the psychic distance is gradually decreasing.

The Uppsala model has been criticized a lot. According to Andersen (1993) it has been criticized for lack of methodological rigor and that it does not have conceptual and theoretical frameworks to guide research; also he does not find the congruence between theoretical and operational model. The authors defend their model anyway saying that it is a model of rational internationalization, and therefore it is better used for prescriptive intentions (Johanson and Vahlne, 2009). Hollensen (2004, p. 55) says that the Uppsala model is too deterministic, and it neither takes into account interdependencies between different country markets as it views them as completely separate entities. The model either does not take into account mutual commitment in internationalization. In contrast, authors say that successful internationalization indeed requires in particular a reciprocal commitment between the firm and its partner. As the internationalization process has accelerated, some of the firms enter distant markets already at an early stage (Hollensen, 2000).

The next model of internationalization called **the Network model** was presented in the 1980s, when it was recognized that network relationships play an important role in the expansion process; because contacts can be a like a bridge to a foreign market (Johanson and Vahlne, 1990). In contrast to the Uppsala model the Network model is not gradually progressing in nature (Ojala, 2008). The core idea of network scholars is that modern high-technology firms do not exhibit the incremental process; they achieve a rapid internationalization through the experience and resources of network partners (Mitgwe, 2006). Researchers of the Network model do not mention psychic distance and target markets (Ojala, 2008). Internationalization is seen as a natural development from network relationships with foreign individuals and firms (Johansson and Mattson, 1988). According to the Network model a firm is dependent on resources controlled by other companies. The only way to get access to these resources is to develop its position in the network.

Each firm is a part of some kind of networks. Business networks are described by Hakansson and Ford (2002) as “a structure where a number of nodes are related to each other by specific threads” (Hakansson and Ford, 2002:133). Nodes are seen as companies and threads as relationships. According to Emerson (1981) a network is a set of two or more connected business relationships, in which each

exchange relation is between business firms that are conceptualized as collective actors. Networking is a source of market information and knowledge, which can help in further expansion. Moreover, through cooperation it is possible to gain access to products, reputation and competence.

Companies have common interests in establishing and maintaining relationships with each other in a way that will bring mutual benefits (Johanson and Mattsson, 1988, 1992; Johanson and Vahlne, 2003). Development of these relationships with other actors in the market can be passive and active (Ojala, 2008). In active networking, the initiative is taken by seller; in contrast, in passive networking the initiation comes from customer, importer, intermediate, or supplier (Johanson and Mattsson, 1988). Both types of networking can open new opportunities in foreign markets. Therefore, networks are a bridging mechanism that allow for rapid internationalization (Mitgwe, 2006). Axelsson and Johanson (1992) define three aspects that affect internationalization. Firstly, firm cannot be just an observer in its network; it should definitely participate in transactions. Secondly, building relationships is connected with investing resources. It means that entry to foreign market is a long-term process of creating dependencies of partners from each other. And finally, presence in a network is strategically important, because it leads to finding out new business opportunities.

According to the network model of internationalization (Johanson and Mattsson, 1988), a company can have relationships with various actors, for instance: suppliers, competitors, customers, distributors, governments, non-profit organizations, etc. And there can be different kind of structural connection between actors, for example, financial, social, communicative or strategic. Network relationships can be divided into formal, informal (Ojala, 2009; Birley, 1985; Coviello and Martin, 1999; Coviello and Munro, 1995; Dubini and Aldrich, 1991; Harris and Wheeler, 2005; Rialp and Knight, 2005), and intermediary (Ojala, 2009; Chetty and Blankenburg Holm, 2000; Ellis and Pecotich, 2001; Oviatt and McDougall, 2005). According to Birley (1985) formal relationships are related to financial sources available; and informal relationships are contacts between other business actors, friends, and family members. In comparison Dubini and Aldrich (1991) proposes that formal networks include relationships between all the staff, whose role is boundary-spanning; and informal relationships refer to all persons that an entrepreneur can meet directly. Despite of differences in defining terms, a common agreement has found that formal relationships are related to business activities between two or more actors in the network, the informal networks refer to personal relationships between friend and family members (Ojala, 2009; Coviello, 2006; Coviello and Martin, 1999; Coviello and Munro; Sharma and Johanson, 1987). In the third type of network, called intermediary

relationships, there is no direct contact between the seller and the buyer, but there is a third party, that facilitates the building of the relationships between them (Ojala, 2009). For instance, broker can connect buyer and seller.

According to the Network model (Johanson and Mattsson, 1988), there are three elements, including actors, activities and resources. Main actors in the internationalization process are the institutions, companies and individuals. They interact with each other and exchange resources in a way to provide mutual benefits (Johanson and Mattsson, 1988, 1992; Johanson and Vahlne, 2003). Activities are related to the forms of exchange between actors: direct or indirect. According to scholars Foster and Holstius (2009) from Turku School of Economics and Business Administration, direct activities are those that directly affect the exchange process as in the case of individual firms, whereas indirect activity links are those that are latent and derive from actions of governments and multilateral organizations. The access to the resources controlled by other actors is secured by the activities in the network (Johanson and Mattson, 1988). Resource elements within the network include products, raw materials, information, market access, finance, technology, research and even the network itself (Foster and Holstius, 2009).

The first step a firm must follow in order to internationalize is the understanding of the market where it operates, its environmental conditions and the firm's relationships (Madsen & Servais, 1997). When the commitment and the number of networks is increasing; and firms gains penetration abroad, companies can reach international integration by using various ties. Johanson and Mattsson (1988, p. 212) have defined four categories of firms: the early starter, the lonely international, the late starter and the international among others. The early starter is the company that has few networks in the foreign country and little market-specific knowledge. This type of firms uses agents to enter the foreign market. In the lonely international category are the firms that are highly internationalized but in a market environment with a domestic focus (Johanson and Mattsson, 1988). This firm has acquired prior knowledge and experience in a foreign market. Later starters are in a market that is already internationalized. The firm has indirect relationship with the network. By making use of those relationships the firm is able to internationalize. They have the drawback over the competitors, since they have more experimental knowledge. For this type of firm it is difficult to get a place in the existing network (Johanson and Mattsson, 1988). International among others is concentrated on a highly internationalized firm, where



market and the firm are highly internationalized. They have a lot of international networks that helps them to find new opportunities.

Ties can be strong and weak. Granovetter (1973) defines the strength of ties as a combination of time, emotional intensity, intimacy and the reciprocal services of the ties. If there is a frequent tight interaction and relationships based on trust then these ties are strong. Weak ties are those, where the distance in relationships takes place, and parties need time to get adapt to each other. Ties are not static: they can be changed from weak to strong and vice versa. Ties play an important role in the internationalization process; actors exchange the information, company gains knowledge.

Networks should be based on mutual trust, knowledge and commitment towards each other. Trust is developed over time; leads to deeper understanding and creates willingness to cooperate in future. It is based on past performance, friendship and social bonds and is gained through day-to-day interaction. According to Anderson and Weitz (1989:312) trust is “one party’s belief that its needs will be fulfilled in the future by actors undertaken by the other party”. Mutual trust is more probable than one-way trust (Anderson and Weitz, 1989). Zaheer, McEvily and Perrone (1998:143) describe trust as “the expectation that an actor can be relied on to fulfill obligations, will behave in a predictable manner, and that he or she will act and negotiate fairly when the possibility for opportunity is present”. Also scholars claim that trust can be represented between people and organizations.

The next model of internationalization is **International New Venture (INV) model**. According to this model young small and medium enterprises (SMEs) expand rapidly, and moreover they start internationalization from start-up. Instead of gradual internationalization, companies prefer to enter foreign markets immediately. In order to internationalize rapidly they use such factors as founder-entrepreneur’s knowledge (Oviatt and McDougall, 2000) and network of contacts (Crick and Jones, 2000) and their corporate relationships with public and private agents (Simoes and Dominginhos, 2001). These firms have proactive international strategy, offer unique products and services; they are willing to take risks. Frequently such SMEs are firms that produce highly specialized technology-intensive goods and occupy narrow specific market niche. But despite this common association with high-tech industry it would be correct to say that there are no limitations related to industry. For instance, international new ventures can be found in such sectors as arts and crafts (McAuley, 1999), management services (Oviatt and McDougall, 1995), manufacturing (Rennie, 1993) and sea products

(Knight et al., 2001). They are innovative and creative not only in technology, but also in conducting business. According to Knight and Cavusgil (1996) and Zahra, Ireland and Hitt (2000) INVs are those firms whose foreign trade activity constitutes more than 25% of their sales over a period of less than 6 years since they were established.

These enterprises were called differently in literature, for instance they were first called innate exporters (Granitsky, 1989), then born internationals (Ray, 1989), subsequently infant multinationals (Lindqvist, 1991) and high-technology start-ups (Jolly et al., 1992). Further proposed were the terms global start-ups (Oviatt and McDougall 1995), instant internationals (Litvak 1990; McAuley 1999; Preece et al. 1999) and international entrepreneurs (Jones 1999). More frequently used were the names: born global (Rennie 1993; Knight and Cavusgil 1996; Moen 2002; Chetty & Campbell-Hunt 2004) and international new ventures (Oviatt & McDougall 1994; Bloodgood et al. 1996; Shrader et al., 2000; Zahra et al., 2000). Regardless of the name firms of this type have in common that they “coordinate many organizational activities across many countries” (Oviatt and McDougall, 1995). Scholars define an INV as “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”.

Actually, international new ventures have existed for centuries (Oviatt and McDougall, 1995). However, only since 1989, scholars have started publishing reports based on case studies of international new ventures. Some case studies have shown that born global is established because internationally experienced and alert entrepreneurs are able to link resources from multiple countries to meet the demand of markets that are inherently international (Coviello and Munro 1992; Hoy, Pivoda and Mackrle 1992; McDougall and Oviatt 1991; Oviatt, McDougall, Simon and Shrader 1994; Ray 1989). Other reports have shown that the prosperity of international new ventures is related to international vision of the company from inception, an innovative product or service sold through a strong network, and a tightly managed organization oriented on international sales growth (Granitsky 1989; Jolly et al., 1992; McDougall, Shane and Oviatt, 1994).

According to Oviatt and McDougall (1995) there are four types of international new ventures distinguished by the number of countries involved and by the number of value chain activities that are coordinated. The first type is export/import start-up, which operates in few markets with which entrepreneur is familiar; and besides there is a small number of value chain activities coordinated across countries. The second type called multinational trader cooperates with many countries and also has few val-

ue chain activities. They are constantly searching new trading opportunities where their networks are established or where they can quickly be set up (Oviatt and McDougall, 1995). The third type is geographically focused start-up, which is the company that operates with few countries and has a big number of value chain activities. In comparison with multinational traders they are “geographically restricted to the location of the specialized need, and moreover, the activities of inbound and outbound logistics are coordinated” (Oviatt and McDougall, 1995). They use foreign resources; and meet the demand of a particular market. The competitive advantage of geographically focused start-up is in the coordination of various value-chain activities, for instance, research and development, and human capital. A company can be innovative in coordinating, and changing routines. Coordination is a complex process, because it involves social impact, organizational skills, and market-specific knowledge. The fourth type is called a global start-up that interacts with many countries and has plenty of value chain activities. It has significant competitive advantage, because it is not geographically restricted; it meets the requirements of globalizing markets; and moreover, it is in constant search of new opportunities. A success depends on good market-specific knowledge, well-structured coordination, human resources, financial resources, active scanning of new opportunities, technological development and strong network.

Oviatt and McDougall (2005) suggest four main factors, which determine the speed of internationalization process. These variables include the technological level of the industry, international networks, psychic distance and geographical distance between countries.

The technological level is an important factor, explaining the emergence of international new ventures (Oviatt and McDougall, 1995). According to Harveston et al. (2001) and Andersson et al. (2004) there is more probability that enterprises in a high technology industry will be international from start-up. The majority of international new ventures have a technological base. All product updates will be rapidly spread in a form of knowledge transfer. Another important factor is the number and the quality of international networks, which support and accelerate expansion. A number of international contacts before establishing firm shows opportunities, and directions of expansion. According to Keil *et al.* (2008), international networks help companies to become more innovative and open access to new knowledge and extra resources. The next factor is psychic distance. For born global it should not be the obstacle, because the majority of enterprises have well-trained employees, international experience before establishing the company, international contacts for export support, and knowledge of foreign languages. Some international new ventures export to nearby markets with a short psychic distance, while others have an aggressive approach and sell products far away. The second type of entrepreneurs

can be called venture capitalists, or risk-lovers. Many companies do not consider geographical distance when they are deciding where to sell products. Geographical distance affects the internationalization process. An enterprise can have wide network, knowledge of foreign countries, well-educated employees, and therefore reduce cultural distance, but it cannot reduce geographical distance. The costs of transportation should affect the choice of target countries. Nevertheless, some enterprises choose exporting to distant markets; and they can be more likely called international new ventures. Moreover, size of the firm (Jovell, 2005) can be considered as one of the factors affecting the speed of its expansion. Small companies have a shortage of all kinds of resources, so they do not have an opportunity to explore in detail foreign markets, to make pre-testing, or to hire a big team of professionals. In contrast, large companies can invest more money to hold a marketing campaign, to hire experts, to train employees, or to make a research.

### 2.3.1 **Born-globals' strategies**

New ventures set various strategies in order to find new business opportunities. Scholars Park and Bae (2004) define seven types of new venture strategies that help companies to survive in a constantly changing environment. The first type called reactive imitators includes SMEs that are concentrated on existing market in the maturity or decline stage of market development. These enterprises are not innovative by nature; they do not invest money into research and development. Reactive imitators copy already existing technology, products and services. The second type according to Park and Bae (2004) is import substitution, or local pioneers in the local existing market. A competitive advantage of these enterprises may be found in technologically sophisticated products, or good level of technological knowledge. They produce expensive goods; and in order to be more attractive for local consumers in a case when there are several competing companies, they should think about decreasing the price by substituting some components. "The opportunity for import substitution exists here where local firms demand local suppliers with low-priced and comparably functioning products" (Park and Bae, 2004). The third type is proactive localization or local followers in the local emerging market. In order to reduce uncertainty and investment into various researches new venture can use already existing technology. These firms develop a new local market, and use developments of other companies. They can be local partners of some foreign corporation. The success will depend mainly on the size of the target market and entries of other companies. The fourth type according to Park and Bae (2004) is creative imitation. Companies can imitate either for local or global market; also they are the followers in the existing global market. In contrast to import substitution they have technological capabilities in new young in-

dustries in the local market; and also they are in the boundary of competition is the global market (Park and Bae, 2004). The fifth type of strategy is global niche or global pioneers in the global existing market. These new ventures are focused in some specific sectors, and serve customers with some unique products or services. Their competitive advantage can be found in technological capabilities and innovativeness that will satisfy customers' specific needs. The next type of new venture strategy is early market entry or global followers in the global emerging market (Park and Bae, 2004). New ventures follow leading global innovators by imitating the technology; and if their reaction to technological changes is fast then they have a high probability of growth. Finally, the seventh type of strategy called global innovator is used by global pioneers. These new ventures can create new markets, new products and technology; they are the source of innovation. According to Park and Bae (2004) the success of global pioneer is related to sustainability of first-mover advantages, emergence of competitors, complementary assets, and entry timing of rivals.

In conclusion, an internalization process of SMEs has been of much attention to the scholars during recent years. Firstly, researches explained internalization as a slow process, when company goes step by step. Such is the case of the Uppsala model introduced by Johanson and Vahlne. After the criticism of this theory Johanson and Mattsson proposed the network model, in which the important role of international contacts is explained. Further, McDougall and Oviatt offered the International New Venture model, when they realized that some companies are global from start-up. For the past few decades scholars have been arguing about existing models and trying to explain internalization behavior. In my opinion, in order to succeed in the internalization a company should have proper strategy, good market-specific knowledge, well-educated employees, networks, and financial capital. Also the success depends on chosen entry mode, the size of the company, and the role of the owner.

## **2.4 Entry modes**

Root (1987) defines entry mode as an “institutional arrangement that makes possible the entry of a company’s products, technology, human skills, management, or other resources into a foreign country”. More narrowed view was offered by Anderson and Gatignon (1986) who describe entry mode as “a governance structure that allows a firm to exercise control over its foreign operations” (Sharma & Erramilli, 2004). This definition accents the role of the control, but it does not reflect all the aspects like the transaction of resources or capabilities. Luo (2001) tried to combine concepts from transaction cost theory and the resource-based view. His definition says that there should be the combined fit be-

tween the internal capabilities of the company, its strategic goals, and environmental unpredictable circumstances. To sum up, entry mode is a governance form that modifies in degree of ownership structure (Mani, Antia & Rindfleisch, 2007) from non-equity modes like exporting to high equity modes like Greenfield investment according to resources, strategy, environment and other transactional features.

Firms seeking to enter a foreign market face a strategically important decision on which entry mode to choose. According to Dunning the choice of the specific entry mode is influenced by three factors: ownership advantages of a company, location advantages of a market and internalization advantages of integrating transactions within the company. In order to compete with host country companies in their domestic markets, a firm should demonstrate its superior assets that will help company to gain profit that can cover costs. A firm's ownership advantages are reflected by its size, international experience and ability to develop differentiated products. The size of the company shows its capability to cover costs of marketing, for achieving economies of scale, and therefore, larger organizations can favor high commitment entry modes then low commitment ones. Also, the international experience affects entry choice. Firms with higher international experience tend to choose investment entry modes because they have enough experimental knowledge and social networks that help to follow more risky pathway of expansion. For companies that possess good abilities to develop differentiated products, it may be more efficient to choose higher control modes with higher levels of product differentiation (Stopford and Wells 1972). Company's location advantages include market potential and investment risk, which characterize market attractiveness. Generally, firms tend to prefer investment modes when they enter high market potential countries because they can provide long-term rents. Internalization advantages refer to contractual risk. On the one hand, when firm chooses low control entry mode it can benefit from the scale of economies of the specific marketplace, while not taking into account bureaucratic drawbacks. But on the other hand, when a firm prefers low control entry mode it will have higher costs in comparison with assets and skills integrated within the company in a case when the owner or management team has difficulties in predicting future events and act in the situation of uncertainty or in a case when there are no good opportunities in the specific market. Lack of opportunities, the problem of bounded rationality, and the situation of uncertainty can make the signing and observance of contracts senseless and more expensive (Andersen and Weitz 1986). In a case when there are no competing options and signing contract seems to be irrational decision because of the lack of possible partners or the presence of uncertainty it would be better to choose such entry modes like exporting or sole venture that will provide higher control because all the assets will be within the company.

Generally, the options available to the firm are exporting, contractual agreements, equity joint ventures and wholly owned subsidiaries. The first entry mode, which is the low-commitment one, is exporting. It is a strategy of producing products or services in one country and selling and distributing them to customers in another country. The main difference between exporting and other entry modes is that in that case a firm still leaves its manufacturing process outside the target market and accompanies the transfer in a successive step (Root, 1987). Exporting is especially popular among SMEs. A firm can prefer exporting in a situation when there is a limited sales potential in target country, or when there are high target country costs.

Also exporting would be the effective strategy when there is a high political risk. A firm can benefit from exporting, because it increases its profits, sales, and economies of scale. Another advantage is that through exporting a company widens its customer base, and decreases the dependence on the home demand. Also, with the help of exporting a firm can stabilize fluctuations connected with seasonality of products or services and economic cycles. Moreover, exporting is low risk, low cost, and the most flexible entry mode. It does not require any investment in foreign production facilities. The majority of the costs related to exporting can take the form of marketing charges. Thanks to exporting a firm can develop international network. Besides a large number of evident advantages, a firm can lose in several positions when it chooses exporting. For instance, when a company decides to expand through exporting it will have few opportunities to learn about target country, its customers and competitors. In addition, sensitiveness to different trade barriers, tariffs and exchange rate fluctuations can create a considerable disadvantage. The company should recognize that expansion through exporting requires changes within the company; it should gain new knowledge and redirect organizational resources. Exporting can be implemented in two ways: directly and indirectly. Direct exporting applies when a home-based company either contracts with intermediaries such as distributors and agents located in a foreign country to accomplish export functions or conducts the exporting activity itself (Sharma and Erramilli 2004). Indirect exporting means contracting with intermediaries such as an Export Management Company or a Trading Company located in the firm's home country to perform export functions. These intermediaries help company to find customers in a foreign country, ship products and get payment. Johanson and Wiedersheim-Paul (1975) define exporting as the best method of reaching the foreign market for companies that do not have yet any international experience, because it will cut down risk of international operations.

According to Root (1987) contractual agreements that include licensing, franchising and strategic alliances are "long-term non-equity associations between an international company and an equity in a for-

foreign target country that involve the transfer of technology or human skills from the former to the latter". Through these agreements that act as channels partners exchange innovations and knowledge. For instance, through licensing agreement one firm known as licensor permits another firm called licensee the right to use its intellectual property in exchange for compensation designated as a royalty. Licensing and franchising include the idea of one-way transfer of knowledge and know-how, while alliances refer to mutual exchange. A firm tends to choose licensing when it faces import and investment barriers, or when there is a low sales potential in target market. Also, a firm can choose licensing if there is a large cultural distance between countries, and therefore, it would be better to transfer the license to a foreign company that is familiar with local environment. Through licensing a firm can test a foreign market without capital investment and market specific knowledge. Another considerable advantage of licensing is that a licensor receives additional return on already made investments on research and development in a form of royalty. Also, licensing increases protection of intellectual property rights. Among the main disadvantages is that a firm creates its own competitor and moreover, it gets limited expertise, because it does not contact directly with foreign customers and will not get experimental knowledge. In addition, a firm will have lack of control over use of assets. Franchising is similar to licensing but differs in terms of duration, service and motivation. Generally, licensing involves trade secrets and intellectual property while franchising is a transfer of trademark and operating know-how (Hoy and Stanworth 2003). In contrast to licensing the duration of franchising agreements tend to be longer. Also, the franchisor offers a broader package of rights and resources. A strategic alliance is a term that characterizes various cooperative agreements, which include shared research, formal joint ventures, or minority equity participation (Bartett 2009). The main advantages include risk reduction, technology exchange and industry convergence in order to create new globally competitive product. But on the other hand, there are risks of competitive collaboration, for instance, when one or both partners establish alliance in order to obtain the technology of its rival and create a competitive advantage in future. Generally, strategic alliances are often only established for short term duration.

The next entry mode is an equity joint venture. It is a "particular type of strategic alliance in which two or more firms create, and jointly own, a new independent organization" (Besanko, Dranove, Shanley & Schaefer, 2007, p.151). It involves certain degree of control and it seems to be rather risky entry mode based on collaboration, which means that in order to succeed relationships should be based on trust. Among the main challenges are possible conflicts, decision-making process, cultural differences and mistrust. The strong side of this entry mode is that firms combine their resources, technology, ideas, finance and knowledge in order to be competitive.



Wholly owned subsidiaries are the most risky in comparison to other entry modes. This mode involves the highest stake of equity ownership and control in contrast to others (Root, 1987). The dominant equity interest can be gained through acquisition or by setting up a new venture (Pan & Tse, 2000).

Generally it should be acknowledged that before choosing a particular entry mode the company should evaluate its knowledge about the target country, psychic and physical distance, competitors, ownership issues in order to decide whether to start firstly with low-commitment entry modes or to favor more risky high-commitment ones.

#### Motives for internationalization

According to Dunning there are four main motives for companies to expand abroad: market-seeking, resource-seeking, efficiency-seeking and strategic asset-seeking.

Company chooses those markets where their products will be on demand and company's capabilities will fit they key attributes of a foreign market. Generally, firms are more interested in markets where few efforts are needed in order to succeed. So, the choice of a target market depends on strengths and weaknesses of the company. Also target market is expected to have a rapid economic growth, strong stable exchange rates, good law and political systems, weak competition and cultural proximity. Unpredictable and non-transparent legal system can be a big problem. Intellectual property of recently internationalized company can be stolen by local companies, for instance, existed trademark can be used without the permission of the copyright owner. It frequently happens in emerging markets. So, companies should be careful when they expand to developing countries and should protect their patents, trademarks and industrial designs. But anyway, there is a risk that even complicated technology that is on the basis of an innovative company's product can be stolen. Another characteristic that makes foreign market attractive for market-seeking companies is physical distance. Geographically faraway markets mean high transportation costs, especially if the company sells heavy goods.

Diversification is also one of the good motives for internationalization. The idea is the same as one behind diversification of financial portfolios. The core idea is to reduce risks. A company expands to several countries that have different environments, and if the market for a company's products declines in one of the countries, it will expand in another country. Such strategy requires high costs in order to localize, but in future it can bring benefits for the company.

Next aspect in market seeking is target customers. Obviously, company will localize in a country, where there is a plenty of customers. And customer segments for some goods can grow rapidly if there is a growth of overall economy, because money is needed to buy those goods.

Resource-seeking motive for internationalization means that certain market can attract a company with natural resources. From efficiency-seeking perspective company goes abroad because it needs to decrease costs. Such diversification can be done directly, when a company sets a production unit in a country where wage level is low and hires local people, and indirectly, for instance, by outsourcing. In turn, strategic asset-seeking motive exists when a company wants to obtain technology or some other valuable intangible assets. Usually it is done through presence in a foreign country.

## **2.5 Internationalization pathways**

Bell et al (2001) propose a number of stereotypical trajectories or pathways, which include a 'born global' pathway, a 'traditional pathway' (the incremental models), and a 'born-again' pathway.

Many firms now do not internationalize incrementally stage by stage. Firms often start international activities from their birth; they enter distant markets, and expand without prior experience. Such firms have been called International New Ventures (Oviatt & McDougall, 1994), High Technology Start-Ups (Jolly et al., 1992), and Born Globals (McKinsey & Co., 1993); (Knight & Cavusgil, 1996); (Madsen & Servais, 1997). Gabrielsson (2004) proposes that born globals are similar to INV because they appear due to cutting edge technology and access to the borderless market. The Born Global concept was first coined about 10 years ago in an Australian report by the consultants McKinsey, (McKinsey & Co., 1993), and it has been used and discussed together with similar concepts, for instance International New Ventures (McDougall et al., 1994); (Oviatt & McDougall, 1994); (Oviatt & McDougall, 1997); (Zahra et al., 2000); (Shrader et al., 2000).

According to McKinsey & Co (1993) born globals in common start to expand less than two years after the establishment of the firm: "these firms view the world as their marketplace from the outset and see the domestic market as a support for their international business". Another important characteristic is that born globals tend to be small manufacturers with average annual sales less than \$100 million. They export at least a quarter of total production. In common, born global is established by an active innovative entrepreneur who has applied cutting edge technology to create a unique idea of product/service or a new way of doing business.

Knight and Cavusgil (1996) define "born globals" as "... small, technology-oriented companies that operate in international markets from the earliest day of their establishment". Rennie (1993) describes born globals as competing on quality and value that is created through innovative technology and product design. Such firms may have no domestic market at all (Bell 1995). The born globals start internationalizing immediately; sometimes circumventing domestic market. Born globals are often as-

sociated with entrepreneurial knowledge-intensive firms (McKinsey 1993; Oviatt & McDougall 1994; Knight & Cavusgil 1996). However, such an internationalization pathway is not limited to high-technology industries (Madsen and Servais 1997; Borghoff 2005). For instance, trading companies can be international from their birth. Also the participation of the firm in high-technology sector does not mean that the company is a born global, because firms can face many barriers during expansion. In a case of family firms the small size can be compensated with their technological progress, for instance, they find foreign customers through the Internet. Moreover, the use of technology was found as a key factor in explaining expansion of new ventures (Andersson, 2000; Davis and Harveston, 2000; Gallo and Pont, 1996).

Small companies can act as born globals when a founder or management team has an experience in industry they are in and in the expansion. Calof and Beamish (1994) claim that an individual's geocentricity is associated with international experience. Internationally experienced management team can be considered as a key resource that affects the degree of internationalization (Reuber and Fischer, 1997). Previous experience influences on entrepreneur's behavior and can be the reason of alertness to new possibilities. McDougall et al. (1994) claim that founders of INVs are more alert to new business opportunities in foreign markets because of the capabilities they have developed from earlier activities. In practice, entrepreneurs have unique capabilities based on previous international experience and ties. According to McDougall only entrepreneurs with this kind of capabilities can establish INV.

The intention of founder and managers to go global accelerates internationalization and reconstructs organizational process. Their decision rules and routines do not depend only on national demand and environment. Routines, decision rules, and capabilities can be called the 'genes' of a company (McKelvey, 1978). When the domestic firm is planning to expand, it should make changes in routines in order to fit international environment. Entrepreneurs with global vision avoid domestic path-dependence by setting up born global, which have routines for co-coordinating international resources, controlling multicultural staff, and for targeting clients located in different countries.

The competitive advantage of SMEs depends on their network resources, especially on the international level. Generally, born globals have international networks and market knowledge from their birth. According to Johannisson (1995) the most important ties are considerably older than the venture itself. Study by Birley (1985) shows that entrepreneurs tend to come from smaller profit-oriented companies and tend to set up similar businesses in the same location with previous colleagues as partners. Networks help entrepreneurs to gain new knowledge, to find new partners and clients, and to internationalize rapidly. SMEs are more competitive on the international level if they have networks.

According to Oviatt and McDougall (1995) there are seven characteristics of successful global start-ups:

- 1) A global vision has existed since inception.
- 2) Managers are internationally experienced.
- 3) Global entrepreneurs have strong international business networks.
- 4) Pre-emptive technology or marketing is exploited.
- 5) A unique intangible asset is present.
- 6) Product or service extensions are closely linked.
- 7) The organization is closely coordinated worldwide.

The next trajectory called “traditional pathway” means that SMEs expand incrementally, stage by stage. First of all firms focus on domestic markets or start with irregular export activities. SMEs often lack financial and human resources, and innovations to expand rapidly. The obstacles during internationalization can be handled if entrepreneur has an intention to extend his entrepreneurial, network, and evolutionary capabilities (Borghoff and Schulz, 2005a, 2005b). SME entrepreneurs should develop innovative approach in order to expand. Generally, entrepreneurs are motivated by access to foreign markets, extension of their own capabilities, cost reduction; some of them internationalize because they do not have enough customers in a domestic market. Entrepreneur should choose an appropriate entry mode in order to achieve customer demand, knowledge, and cost advantages. Commonly, entrepreneur, who follows the “traditional pathway”, favors first indirect entry mode because it is less risky, it requires less costs and knowledge about the country in comparison with other entry modes. In market selection, companies prefer to expand firstly to nearby markets that have similar culture. Nevertheless, for many SMEs, expansion beyond export is still an unknown stage of business.

Theoretically, SME has no more than 250 employees and strong position of the entrepreneur and management team, who set goals, create strategies and make decisions in the internationalization process. According to Schulte (2002) the idea and its translation into international business activity are typically combined in one person. This phenomenon is called “internationalization made by boss”. Generally, SME entrepreneur is involved into daily routines and planning process. Internationalization issues can cause overloading because of the lack of knowledge, strategic awareness, cultural awareness, time, financial and human resources, and know-how. The typical mistake is that during the ongoing expansion process entrepreneur continues to do business as usual, because he or she is not aware of the necessity to gain new knowledge, to find new networks, to learn more about target market, to hire em-

ployees with knowledge about internationalization, and to reconstruct rules and routines. Commonly, the existed background is transferred spontaneously to the foreign environment without clear perception that it is a completely new environment with special rules, demand, culture, relationships and language. This will cause the view that the internationalization process is a pressure or a burden for a company, because at first expansion was regarded only as an additional activity without revising goals, opportunities, resources and strategy. In order to handle this burden entrepreneurs will try to "muddle through" (Schulz, 2007; Lay et al., 2001).

Scholars have found that family SMEs are less likely to internationalize than non-family firms (Fernandez and Nieto 2005; Graves and Thomas 2006). The possible obstacles can be narrow growth objectives (Donckels and Fröhlich 1991), risk avoidance (Claver et al. 2008), restricted financial capital (Gallo and Pont 1996), bounded managerial capabilities (Graves and Thomas 2006) and a shortage of bridging social capital (Graves and Thomas 2004). In addition, all decisions are made among family members that can cause lack of innovative new ideas. Firms, that have decided to expand, basically follow the "traditional pathway"; they internationalize incrementally step by step (Claver et al. 2008; Graves and Thomas 2008). They act cautiously and slowly with a focus on interpersonal trust (Roessl 2005).

The next trajectory called "born-again global pathway" is followed basically by firms in traditional sector than high technology industry. These are SMEs that have been well established in their domestic markets, without great motivation to expand, but which starts to internationalize suddenly (Bell et al. 2001). The possible motivation or trigger leading to such a strategy can be change in the management team, when after the succession of the family firm to the next generation, someone becomes a new owner and decides to change strategy. Another motivation to internationalize can be a case of acquisition of SME with international networks that will help company to find new clients, gain new knowledge and to adapt in a foreign environment. The next trigger can be related to client followership, when domestic client internationalizes.

To sum up, a firm chooses which pathway to follow on the basis of financial resources available, the willingness toward expansion, the managerial capabilities, networks and knowledge. On the one hand, there are born-globals that start their international activities from their birth. On the other hand, firms that follow "traditional pathway" internationalize incrementally step by step. Some SMEs become global after sudden appearance of motivation. Before the firm will enter the foreign market it should realize that there is a need of revision of the strategy, goals, resources and opportunities.

## **2.6 Definition of family firms**

Before considering the internationalization process of family companies it is essential to agree on definition of family firms. Researchers generally agree that family involvement in business is what makes the family business different (Miller and Rice, 1967). The presence of the family in a business affects decision-making process, amount of networks, the speed and the choice of certain pathway of internationalization. Family firms are unique. Since family firms differ from non-family firms internationalization process of family enterprises should be investigated as a distinct entity. Many scholars define family firms with the notion of ownership and management (Handler, 1989). Babicky (1987) defines family business as a small business started by one or few individuals who had an idea, worked hard to develop it, and finally achieved, usually with limited capital, growth while maintaining majority ownership of the enterprise (p.25). Barnes and Hershon (1976) also mention ownership; scholars define family business as a controlled ownership, rested in the hands of an individual or of the members of a single family (p.106). According to Welsch (1993) a family firm is one in which ownership is concentrated, and owners or relatives of owners are involved in the management process (p.40). In some articles vision and continuity criterions are mentioned in addition to ownership and management.

Since there is no general consensus on the definition of family firm companies in my thesis would be considered as family firms according to following characteristics:

1. Ownership control (at least 15 percent) by two or more family members
2. Influence or active involvement in management of the company and at least one of family members is involved in governance of the firm
3. Concern for family relationships
4. Thoughts about continuity across generations

Family businesses come in many different shapes and sizes, but it is not strategically important criterion in selection case companies for this research. Some businesses are extremely old and some are even owned by more than one family. Family businesses can come in many forms such as sole proprietorship, partnership, limited liability company, corporation, holding company; and can be publicly traded (Poza,2007).

## **2.7 Russian business culture**

Before considering Russian family firms and their internationalization process, it is good to mention peculiarities of Russian business culture. When a company localizes in a foreign country it should try to adapt by changing habits. Russian culture differs from western cultures in a lot of aspects and that is why foreigners especially non-Slavic ones have problems with understanding and communicating with their Russian business partners.

Gorrill J.R. (2005) assumed several key concepts: collectivism, soul and egalitarianism. Russian people have a strong communal spirit that was reflected not only critical moments but also in business. In order to survive it is better to be collaborative than to have competitions. Ability to cooperate is one of the features distinguishing Russians from many foreigners. Another important concept called egalitarianism refers to equality and mutual benefits. It is a social philosophy that promotes the idea of removal of unfair inequity. The next concept is soul or in Russian “dusha”, which is the central to behavior, actions and relationships. When a foreigner wants to do business in Russia and build strong ties, than he should cause good emotions, sympathy from his partners. So, continuity and personal relationships in negotiations are important factors, because through long discussions and meetings in different places helps Russians to learn more about the person and to decide is it possible to have relationships based on trust and openness. Generally, Russians tend to be direct and informal in communication.

Russians typically have three names: first name, middle name and last name. First names or given names are usually used by family members and close friends. Middle name, which is a patronymic or father’s name, is formed by adding “-vich” or “ovich” for a male and “-ovna” for a female. Colleagues address each other with the first name and patronymic. In formal situation tree names are used. It is also possible to refer to Russian by “gaspodin” which is the same as Mr. or “gaspazhah” similar to Mrs and plus family name.

Another interesting aspect is attitude to time. Russians have the opposite attitude to time in comparison with Americans, to whom belongs the well-known saying “Time is money”, because there is no quick tempo in doing business. With such a relaxed relationship to the concept of time negotiations can occupy much more time than it is common for in Europe. Russians have a focus on the moment, and it is hard for them to plan events that will be later than in two weeks. If the meeting is arranged the foreigner is expected to be on time, but if he is being late than, for example, traffic jam can be considered as a good explanation of delay. It is possible that Russian partner can miss the meeting if something urgent will come up, and this case can test the patience of foreigner, since patience is regarded to be even

more important than punctuality. If there is a social event than it is possible to be late on 15 to 30 minutes.

When Russians see each other they shake hands. It is typical for formal and informal meetings, with strangers and friends. Shaking hands in gloves is considered as a bad manner. Generally, Russians are very demonstrative people, for whom physical contact in public, expressive body language and eye contact is common. Also, Russians stand close to each other when they talk. To stand with hands in pockets is considered rude. When you meet the person for the first time it would be good to exchange business cards, which preferably should have two sides: one side should be printed in English and another in Russian, because some Russians do not speak foreign languages, especially old generation. However, nowadays English is taught almost in each school, but still some entrepreneurs hire interpreters in order to explain all specific terms.

The first meeting is usually held in order to find out if the company and the potential partner deserve trust and are credible. The best way to show it is to appear very confident, firm and dignified. Besides, hierarchy is important, Russians respect age, rank and position, and that is why the most senior person makes decisions. Meetings are frequently organized for information dissemination and clarifying strategy and instructions rather than for open debate of business issues that is more common for one-to-one meeting or for small group. Generally, formal meetings are structural and serious, where humor can be considered as inappropriate. Pitches and presentations tend to be simple and straightforward, and the use of visuals sometimes is not essential, because the key aspect on which Russians pay attention are professionalism and knowledge, but still it is good to have written material in English and Russian. Also a good advice would be not to use high-pressure business tactics.

In Russia management tends to be centralized and directive. Because of the key role of hierarchy boss delegates tasks for subordinates and have last word on everything. Making a final decision can be also done without consultation with top manager because it can considered as lack of decisiveness and weakness. In addition, there are very few women in senior management positions in Russia, and because there are no yet equal rights between sexes women can be less respected in meetings.

Networks play an important role in business. The Russian word “svyazi” means weak and strong ties that help you to succeed. And when the person has friends in high positions, it might help him to find a good job. Besides, if you are familiar with someone successful it can affect reputation in a good way. So, it is necessary to make contacts and try to build relationships based on trust.



Russians are good hosts, they love entertain guests in their place. If you are invited at a family residence it would be a good idea to bring a gift such as bottle of wine, flowers or dessert. The gift for a kid is always appropriate. When the guest comes he should leave his shoes and he will be offered to wear slippers. Usually Russians put more food on the table than can be eaten. To decline an offer of food or drink can be considered rude. While drinking people say different toasts, and it is not allowed to drink until the first toast has been offered. After someone will say the toast people clink their glasses with alcohol together. But in general table manners are the same as in Europe.

Dress etiquette is another important aspect. Men usually wear suits that are dark and well-tailored along with tie and highly polished shoes. Wearing too bright cloths can make a person look unreliable and not serious. Women mainly wear business suits or blouses with skirts. Generally, style is formal and conservative. The is well-known Russian proverb “Meet by cloths see off by mind”, that means that when we see the person for the first time we evaluate the cover, and only further find out what kind of person he is. By appearance we can make some outputs about person’s traits, for example is he or she neat, and we even can hazard a conjecture about income. So, for foreigner in business meeting it is important to be well-dressed in order to enhance credibility.

### 2.7.1 **Russian SMEs**

Russian’s entry into a global economy leads to the development of SMEs as a strong economic and political force. There are still main problems in strategic planning on micro level and it is not conducive for foreign investment. Moreover, high level of crime, corruption, law instability, frequently changes “rules of a game”, lack of legal guarantees of equality for all forms of ownership, extra taxation and non-fulfillment of laws and regulations, also affect doing business in Russia and opinion of foreigners about Russian market. Corruption on the different levels is one daunting problem for foreign investors and local business community. That is one of the reasons why Russian market is considered to be risky and therefore not attractive for foreigners. But despite unfavorable environment, Russian private and family businesses are much more likely than global ones to have experienced growth in the last year and to be looking for growth over the next five years. 92% have grown in the last 12 months (compared with 65% globally) and 22% are planning to grow quickly and aggressively over the next five years (compared with 12% globally) (PriceWaterHouseCoopers, 2012).

Short-termism can be considered as a typical trait of Russian SMEs. Such kind of mindset appeared in Soviet Union, where short-term oriented people were good survivors in a frequently changing environment. The current generation of businessmen thinks how to sell a company ignoring an opportunity to transfer control. In turn, young generation also does not show intention to take responsibility and run the company. So, lack of family business succession planning can cause a business failure. For sure, succession brings stability and benefits. In addition, many businessmen advice their children to choose living abroad and to study in a foreign university, after which they probably will lose a feeling of Russian business culture. Also it means that good professional will stay living abroad, where there are good life conditions and favorable business environment. So, 57% of private and family businesses in Russia plan to sell or float their company, compared with only 17% worldwide (PriceWaterHouseCoopers, 2012).

Obviously, it is hard to do business in Russia in existing conditions. It requires many efforts to operate in the domestic market and therefore, lack of finance and time is left to plan expansion. And since Russia is a vast country and a “country of contraries” expansion to another region may need almost same efforts as internationalization. Regions can be geographically distant that mean necessity of transportation of goods and there might be even different cultural differences because in Russia there are about 160 various ethnic groups. So, regionalization also requires financial resources, networks and knowledge.

### **3. METHODOLOGY**

This chapter describes research method that has been applied in the thesis. Moreover, there is a description of data collection and explanation why this research is reliable and valid.

#### **3.1 Research approach**

There are two kinds of research approaches: qualitative and quantitative. Mainly researcher chooses one kind which to follow. After formulating research questions when the nature of research is clear researcher can choose approach, but sometimes there can be a combination of both. The choice depends on the aim of research, for example if the goal is to have a complete detailed description than probably qualitative approach should be chosen. Qualitative research has explanatory nature and is quite subjective, because it is based on participants' observation. For scholars who choose this approach individuals' interpretation of events is important. It helps to have better understanding or in-depth interviewees (Fisher, 2007). An approach is based on interviews and observations. In contrast, quantitative approach aims to clarify features, count them and create statistical models, so as a result there might be figures, which will help to generalize some processes. In qualitative research there also can be generalization, but reached through comparison.

According to Yin (2003) case studies as a tool should be chosen, for example, if a research gives answers to "how" and "why" questions or if there is an intention to cover contextual conditions if it is clear that they are relevant to the phenomenon considered. So, due to explanatory nature of research questions, it will be a multiple-case study, in which several interviews with Russian family firms will be conducted for further analysis and comparison. Firms are chosen based on some specific criteria. In order to be objective, companies are from different regions and industries, because the country is rather vast and each region has its own peculiarities.

#### **3.2 Data collection**

Fisher (2007) has identified five ways of collecting data: interviews, panels, questionnaires, observation and documentary. In turn, interviews can be open, pre-coded and semi-structured. Interview hold as an informal conversation is called open interview. In contrast, in pre-coded interview questions are defined beforehand and the process is flowing according to plan with a degree of control. And semi-structured interview is a mixture of two types (Fisher, 2007).

In writing thesis, semi-structured interview method was chosen. Questions were listed beforehand but at the say time conversation was quite informal, that allows getting long answers.

In overall, thesis contains primary and secondary data, gathered from credible reliable sources of information that include books, articles and websites. Ghauri and Gronhaug (1995) assume that secondary data helps in formulating research questions, and besides it is good for comparison, for example if we consider research with the same goal that we have, but it contains case studies in other country or there are observations in other companies. That is why secondary data should be examined and are a good basis for a research. In this study secondary data is used to explain internationalization process and to show it from different researchers' perspectives. It was important to define key concepts before making a multiple-case study. In contrast to secondary data, primary data is more relevant because it is intentionally collected for this study due to research questions. In this study primary data is based on communication in a form of interview. Interviews will be conducted via e-mail, in person and by telephone.

### **3.3 Validity and Reliability**

Validity refers to defining whether the research covers all the issues that it was planned to consider. According to Carlsson (1988) high validity depends on how appropriate is a method chosen. In turn, reliability means that if someone will repeat the same research he gets the same result.

Since this research is qualitative it is hard to guarantee validity and reliability because study is based on individual perception. In order to ensure validity and reliability interviews were hold in the national language otherwise there could be some inaccuracy. Also, the same questionnaire was used for all the respondents. So, reliability and validity were strongly taken into account.

## 4. EMPIRICAL DATA: THREE CASE STUDIES

*This chapter is devoted to the empirical study conducted. It includes brief presentation of Russian family firms and description of their internationalization process. The data for these case studies were collected through face-to-face interviews.*

### 4.1 JSC Danlen

JSC Danlen was founded in 1994. The company is located in St. Petersburg ([www.danlen.ru](http://www.danlen.ru)). It is mainly known as a wholesale trade of professional equipment for agriculture (aviculture, animal husbandry), but it also sells equipment for car wash, metalworking, construction, sanitation and hygiene, printing house and crop. Among products offered by Danlen is a multipurpose injector Dosatron (France), spray Gloria (Germany), gas heater Gasolec (Holland), LED- lightning LUMO (Lithuania), Socorex (Swiss), artificial insemination of pigs and birds IMV Technologies (France), Indrobase (Italy), MOEL (Italy), Verschuuren (Holland), Zoo-Techniques (France), Lyon (the USA), Desvac (France), Indrabase/Indrotech (Italy), Reno (Denmark), Delto Trak (the USA), ventilation and climate control system SKOV (Denmark), Lubing (Germany), Salter (England), diagnostics of eggs' quality Futura (Germany) and VEIT electronics (Czech Republic).

All manufacturing companies, whose representatives they are, have leading positions in global market, and most of them are certified by ISO 9001 quality system ([www.danlen.ru](http://www.danlen.ru)). Since Danlen has direct long-term contracts with manufacturers they have significant discounts and therefore, they are able to offer their customers all products at competitive prices. Besides, Danlen has a diploma for socially responsible business, because of sustainability, concerns about social and environmental issues, and ethics.

Most of the products on the company's website, as well as spare parts for them are available at our warehouse in St. Petersburg, the goods that are not currently in stock, available by arrangement. Mainly they deliver goods throughout the territory of Russia. Danlen are able to deliver goods to any region in Russia. Mainly it is done by air transport, trains and trucks depending on the distance.

There is a plenty of big and small companies that are producers by themselves or just distributors of the products of the same industry, but the competitive advantage of Danlen is that it is generally the official

distributor of certain equipment in the Russian market, and in case of Dosatron, it is the only representative in Russia. And if another Russian company will buy a certain product in order to resell it in local market it could not give low price, otherwise there will be no profitability. In addition, products offered by Danlen are mainly innovative and some of them do not have analogue produced in Russia or somewhere else. For instance, Danlen is the official distributor of Dosatron that invented in France and was produced since 1974. This technology was very innovative and therefore, it was a global pioneer ([www.dosatron.com](http://www.dosatron.com)).

JSC "Danlen" regularly participates in exhibitions, seminars, together with representatives of manufacturers. Generally, the new exhibition season starts in the specialized trade fair in February organized in Moscow. Top regional managers of Dosatron from Western and Eastern Europe are there to answer customer's questions about the product. Also, Danlen concerns about problems in aviculture, for example, viral or bacterial diseases, drug safety and new developing technologies. In April 2013 it took part in the International Veterinary Congress. The conference was held in Moscow and it was dedicated to actual issues in aviculture.

In May 2013 Danlen participated in the International Exhibition of Innovative Technology and Advanced Research "Meat Industry. Chicken King / VIV Russia 2013 "that is the largest industry event of the year for manufacturers and distributors. JSC Danlen where has presented their partners: Dosatron (France), IMV (France), Indrobase (Italy), Gasolec (Holland) and Socorex (Switzerland).

#### **4.2 Target and potential markets**

Danlen buys goods abroad and sells them mainly in Russia that is the main target market because this industry is developing and there is a big market volume. Besides, it exports equipment to countries of the CIS (Commonwealth of Independent States). The CEO of Danlen Muhamedshina about market choice:

“I would characterize position in a Russian market as a stable one. Export to Kazakhstan, Ukraine and Belarus makes less than 7 per cent of total sales, so, it is obvious that we should be more concentrated on local market” (Muhamedshina 2013).

However, the company has regular direct export activities to countries of the CIS. Muhamedshina claims that the reason of a trade abroad is not the lack of demand in a local market, but a potential ex-

pansion of sales market. It is in common that in market selection firms usually go first to nearby market, then to distant ones.

All the products offered by Danlen are mainly produced in Europe, so if someone from European countries will be interested in buying these goods than they will probably buy them directly from producers or distributors located in Europe. Also, distant markets such as Australia, Asian countries or the USA could not be potential markets for Danlen because this company is just a distributor which means it does not produce anything, and another reason is the high cost of goods delivery.

This position is even reflected on the website of the company. All the information there is only in Russian that means that the company is definitely not in search of partners from distant countries. Besides, the web site is not well-promoted in the internet and there are no reports.

### **4.3 The role of networks**

Networks usually play important role in the internationalization process, but in case of Danlen contacts so not have a critical role in choice of target country and certain entry mode. Indicators of market dynamics are the main factor that has influenced the choice of target market. Muhamedshina, the CEO of the company said:

“Networks does not affect strongly on the foreign market choice. I can know many people in Australia, but expenses of goods delivery can be higher than all possible limits of prices, and nobody will buy it. Than how can we consider Australia as a potential market and claim about helpfulness of networks?!” (Muhamedshina 2013)

Danlen is active in search of new partners including importers. They find potential partners mainly in exhibitions, seminars and private industry annual meetings. Danlen has several strong long relationships based on trust. Good interpersonal relationships are highly valued in business. Muhamedshina describes how to evolve trust between partners:

“In establishing trustworthy relationships not only informal meetings play important role, but also the quality of production, service and extra bonuses for clients” (Muhamedshina 2013).

#### **4.4 Speed of internationalization**

Since the founder and managers did not have any preliminary international experience, than the expansion can be a gradual process, done step by step, when they learn by doing. The lack of international experience can be called one of the reasons why they have not started selling abroad from scratch. Besides, Danlen is not a producer of the all the goods they sell, and generally, there are other representatives of the same equipment in many countries, and this fact also has affected the choice of exporting as an entry mode to foreign market. In addition, the internationalization strategy of the company is not risky at all, because they have chosen nearby countries, low-commitment entry mode and do internationalization slowly with constant analysis of dynamics in different markets. So, the internationalization process of Danlen was rather slow: it has started exporting to nearby countries only after about 11 years from establishing. Muhamedshina about the speed of internationalization:

“It depends on the size of the company. Some firms in order to start regular exporting need half of a year, while others require several years” (Muhamedshina 2013).

##### **4.4.1. Distance-creating and distance-bridging factors**

Distance-creating factors are not well-defined because these countries are nearby and have similarities in the environment and besides, Danlen has only direct exporting at the moment, so there is no need to learn about local laws and regulations. The language of negotiations is Russian. In contrast, if the company will internationalize to more distant markets than it should take into consideration the fact that countries have different management styles, culture, language, habits, attitudes to time, money, ways of communication; religion, and temperament. Before an expansion to a chosen market a firm should increase market specific knowledge, which includes knowing local competitors, customers attitude to the problem, a company solves, and purchasing power.

However, even the low-commitment entry mode to a nearby country requires time and efforts to be competitive in a target market.

Muhamedshina said that such factors as experience, high competence of executives, networks, good advertisement and promotion, products themselves (price, quality, guarantees and after-sales service) helped the company to internationalize.

##### **4.4.2. Recommendations for companies planning to internationalize given by Danlen**



There should be a well-done preliminary research of market, for example, trends and dynamics, and current and potential competitors.

By Muhamedshina:

“You should understand can you be competitive in certain market conditions. Analyze the quality of products, productive capacity, prime cost, service and delivery. And then choose a right strategy of expansion. Also, consider possible actions in case of failure in order not to lose business” (Muhamedshina 2013).

Also, from the recommendation given it is visible that a company is risk-averse, because it expands only after long preliminary research, it chooses low-commitment entry mode such as exporting, it internationalizes to nearby countries and thinks a lot about future.

If a big amount of sales is in a local market it can be assumed that the company will not change its strategy and starts rapid internationalization to distant markets. And since it is not a manufacture, but just a distribution of professional equipment, than it cannot choose high-commitment entry modes such as licensing or joint venture. Potentially it can have more export activities in future because they have direct connections with manufacturers without any intermediaries that usually have its margin, so they can sell goods at competitive prices.

#### **4.5 Company X**

Company X is located in a small town of Rybinsk. Originally, the company has been selling trucks, but since the demand on them is seasonal, entrepreneur came up with an idea of creating websites and their promotion that means putting a client’s company in top 10 list after browsing in Google. The idea was quickly accepted by all team members, because it requires really few investment and there will be fast financial return (around 4500 rubles will bring 50000 rubles after 2 months). Technical Director Petr Shor, who gave me an interview, has shared an idea with his friend, who is a good IT specialist, and he joined their team. Petr’s uncle is a business manager of a company. He is responsible for negotiations and other financial issues. They deal very well with each other and all decisions are made together. Company’s main clients are local companies. About 70% of clients were found through freelancing exchange, 5% from advertisement given in a newspaper, and rest are personal contacts.

In April 2012 intention to expand has appeared. Their first foreign client was from Holland. He was found through personal network. Generally, the decision to internationalize was made in order to increase profit, to find interesting collaboration, to travel, to develop language skills and simply to find something new.

Poor marketing and lack of finance were seen as main obstacles. Petr about local companies:

“Small firms here do not intend to internationalize much and mainly people want to have “easy” profit without big efforts. Besides, you should have really unique product, you should have networks and be aware of foreign market, and it is time and money consuming. That is why local small companies are mainly focused on domestic market” (Shor, 2013).

Other target markets considered by Company X are Scandinavian countries, Central Europe and Baltic countries. Knowledge about these potential markets will be obtained through the internet, and foreign clients will be found without any professional help that is costly. Petr sees an advantage in central location that they are located not far from Moscow, but at the same time in a small town wage level is low. At the moment there are 5 people in a company, but if there will be need they have a reserve to hire more specialists.

#### **4.6. Konung Ltd.**

Konung Ltd was established in 1997 in Yaroslavl region by Sergey Rastorguev. Company became well-known because of innovative idea to pack sunflower seeds. Earlier seeds were sold by weight on the market place, and the idea of selling seeds in small colorful packages was completely new in the Russian market. Company presented their product in the exhibition and got award of the best product of the year in Moscow. Due to the fact that roasting and packaging sunflower seeds does not require big investments, in a short period of time many competitors have appeared, and moreover, company's product was counterfeited that really spoiled the reputation of the company. Rastorguev about counterfeiting:

“In Yaroslavl region there were about three counterfeiters. Clients called us with complaints that we have bad quality. And once when we checked the package we found that it was totally the same as our, but there was wrong street title, instead of “Sysoevskaya” it was written “Sovetskaya”. It was hard to struggle with it. And since sunflower seeds have already brought us really good profit, I started looking for new business ideas”. (Rastorguev, 2014)

Counterfeiting really has caused a sales decline in the domestic market, and company started exporting seeds to UAE in 2005. The decision to export was done by accident after an offer from one person to make sales abroad with his help. Due to the choice of indirect exporting there was no need for a company to learn a lot about target market, so everything was done smoothly without any involvement and obstacles. At the same time company was concentrated on production of other products, and in small period of time Konung Ltd started producing pasta, groat, nuts and further coffee and tea. Such shift was done gradually and it has required a lot of investments. Company had to hire new people, expand a plant, build new stores, create a website and even to set up an office in Moscow. Now in total there are 35 employees and company's team really consists of professionals. Rastorguev describes expansion within the company:

“When I feel the growth of our market share I have to think about changes within the company. I evaluate each step, for example, it was really a hard decision to set up an office in Moscow, because it is very expensive to rent an office and to hire to professional managers who already have a client's database. Wage level in Moscow is much higher and I need to pay a lot in order to keep professionals. Managers in local office have much lower salary, but they do not make such quantity of sales. Location means. Existence of office in Moscow helps to increase reputation and clients' trust. So, I am ready to pay more.” (Rastorguev, 2014)

Despite there is a good team of professionals the owner have to be present. Rastorguev that without his involvement in day-to-day routine and a certain degree of control nothing will work. He discusses all issues with family and managers but still he has last word on everything in a company. The owner clearly has faced improvements to be done, for instance, nobody in a company has international experience. Changes should be done not only within the company but also supply chains and procurement of raw materials should be reconsidered.

Konung Ltd has quite many networks in different regions within the country. Rastorguev about geography of sales:

“Strangely enough, but we almost do not have clients in our town. And I have no idea what could be a reason. We have several clients within Yaroslavl region and many clients in Moscow and faraway parts of Russia. Of course, main income comes from sales in Russia, that is why I am not very focused on foreign markets”. (Rastorguev, 2014)

At the moment company is selling products to Belarus, Kazakhstan and Ukraine. Konung Ltd really has good stable quality and comparatively low prices. Since it a small company it is really flexible;

they quickly react on changes in demand, try to adapt and exploit almost each opportunity in order to expand and raise profitability. Rastorguev talks about advantages during expansion:

“For sure there are many aspects that help during internationalization, for example, highly qualified employees, proximity of raw material markets and good infrastructure. But sometimes even without such kind of advantages you can succeed. You just should in the right place at the right time” (Rastorguev, 2014).

The owner has mentioned luck, but did not talk anything about role of the leader. If he won't be so proactive, optimistic, sociable, smart and well-organized he probably won't be successful even on domestic market. Besides, he is very hardworking, he comes to work earlier than others and he is a last who leaves an office. Having ability to work for long hours can be typical only for a person who is highly-motivated and has strong personality. His phrase “Business is my hobby” explains why he invests a lot of time in it and why he talks about business as about game with a pleasure. In addition, it is noticeable, that while being a sociable person, it is easy for him to make contacts.

Konung Ltd finds international partners in exhibitions and through current networks: besides, many clients were found through company's website. In order the evolve trust owner of the company and top manager organize informal meetings with their partners. Rastorguev describes keeping in touch with clients:

“I know that I need to invest more time in expansion of social capital in Russia and abroad, but the problem is in lack of time. But still, I have warm relationships with my partners, for example last time when I was in St. Petersburg with my family I found time to meet my good client. We met in a restaurant and next day he invited us to his house. And for sure it has positively affected on our collaboration. I can say that it is an art to be in touch with business partners but it requires time”. (Rastorguev, 2014)

Owner's wife Olga has helped him a lot in decision-making and has given moral support during hard times. The decision to set up a company was made jointly. Now she works as a secretary and has very flexible time schedule. Her mother and sister also were involved in business for some period of time. Rastorguev's daughter is partly involved. Rastorguev about his plans:

“It would be easier if in future not only my wife will be involved, but also my daughter who can be a CEO. I hope she does not accept family business as a burden. We will share responsibilities and besides day-to-day routine I will be able to travel more. I identify new opportunities very quickly, and I admit there can be big changes in future. Also, I have big requirements to myself, I want to develop myself and to learn foreign languages. And as a result changes in myself will help me to find new solu-

tions for business and who knows, maybe I will sell it and move abroad or will change industry”.  
(Rastorguev, 2014)

## 5 ANALYSIS

In this chapter, the empirical data is analyzed. The case analysis has been done in order to detect common aspects during the process of internationalization among Russian family SMEs.

**Research question 1:** How do family firms start internationalizing?

All case companies follow traditional pathway, because they are internationalizing gradually and began expansion after several years from establishment. SMEs tend to choose low-commitment entry mode such as indirect or direct exporting. Generally, selling abroad begins with nearby markets, where psychic distance is rather low, but it is not always so. There are different motives that have affected on choice of a target market. In case of Danlen there is a preference to nearby countries with a small psychic distance, but not to the countries where they have networks; and its internationalization process better reminds the Uppsala model. In turn, Konung Ltd and Company X have chosen particular countries because of networks.

Chosen case companies did not have any preliminary international experience and moreover, all employees are Russians. Internationalization was not thoroughly planned and there was not any research done. Besides, companies gain more profit on domestic market and can operate without selling abroad. Connection between presence of a family and internationalization process is not well-defined from the first look, but still in all case companies business issues are discussed between family members and decisions are made rather fast. Moreover, family firms are long-term oriented and they cause trust and reliability from their partners. Also, it is noticeable that all case companies have lack of financial resources that prevents making very big steps and therefore, companies avoid risks. But generally, collaboration of different generations leads to balance between rationality and cool mind.

**Research question 2:** To what extent does social capital affects the internationalization process?

Impact of networks on the internationalization process depends on stage of company's development and on product. If a company exports products abroad it should be in search of new contacts that will help somehow to expand. Service companies like Company X are not in a active search of networks, and moreover, have critical view on expansion, because it needs not only good networks, but also company should provide really good service and also internationalization process is time and money consuming. But nevertheless, first foreign client was found through personal contacts. In case of Danlen networks also do not have a strong impact, and contacts have not affected on choice of target market. But still, company is in search of new clients and visit exhibitions and trade fairs in order to expand

social capital. They claim that tangible things as product itself matter more than relationships. Clients judge you according to quality of your product, stability and timeliness of delivery. Both companies do not strategically search for international ties and are more reactive than proactive. In turn in Konung Ltd the owner believes that networks really play an important role in business and spends time on maintaining existed networks. Despite lack of time, he holds informal meetings because they bring pleasure and really help to evolve trust between partners. Also, they regularly visit different fairs, where they look for new partners. Once the owner had to travel himself to Vietnam in order to sign an agreement for delivering raw material directly without any intermediaries. Generally they are not narrowly focused just on finding clients in the particular country; they are open for all coming negotiations to collaborate. But at the moment, it happens so that they export products to nearby markets and reason is not low psychic distance, but networks. So, networks already have a good influence on company's expansion and probably, in future, if there will be simultaneous improvement of quality, appearance of new ideas, new specialists; and finding new networks; than company can really succeed in its future expansion. To sum up, networks can help in internationalization, but company should not rely just on social capital, because being socially active without having really competitive product does not guarantee demand abroad. Based on experience of case companies, it can be assumed that sometimes networks bring benefits, for example new client can be found through existed network, but at the same time, building social capital is time consuming and the result of collaboration is not known beforehand. In addition, presence of a family can affect badly on bridging social capital to some extent. For family firms it is not an easy step even to hire first non-family member, not to mention collaboration abroad. Most of the family SMEs do not have international networks at all. And generally, contacts are found on the basis of alertness.

**Research question 3:** What are the main barriers for family SMEs during internationalization and how do they overcome them?

Low-commitment entry modes chosen by case companies include low risk and low cost. Since companies do not have prior international experience exporting was the best option. Manufacturing process is still left in the domestic market, so there is no need of huge investments, no political and economical risks; and moreover, exporting does not require constant involvement in operations abroad. Companies learn by doing, and through exporting they increase knowledge about target markets and moreover, they develop network.

Since Danlen has chosen exporting to nearby countries, where environment is similar, they have not faced any significant difficulties, but they have realized that even exporting requires time and efforts in

order to be competitive. Experience, high competence, networks, good advertisement, promotion and products themselves can help to overcome barriers during internationalization. Company X has defined that obstacles are within the company, and such as lack of finance and poor marketing can be barriers. Mainly, Russian SMEs have intention to gain profit during short period of time and without efforts. Interesting enough that it was not assumed by the company that obstacles can be abroad, such as different law system or cultural issues. Probably, company starts thinking about distance-creating factors when it is seriously planning to internationalize and chooses high-commitment entry mode.

Konung Ltd also did not have prior knowledge about internationalization and also has chosen exporting as an entry mode. The first target market was UAE that is faraway market, but sales were done indirectly and there was no need to learn about local environment. At the moment there is exporting to nearby country that is also done very smoothly. Company says that advantages within the company help to succeed during expansion, and these advantages are: highly qualified employees, proximity of raw material markets, good infrastructure and luck.

To sum up, case companies have really big requirements to themselves, and have intention to develop quality, hire good specialists and reduce costs. Since case companies are not ready yet to make investments in the internationalization and have good home demand they do not learn a lot about foreign markets. So, it can be assumed that Russian SMEs do not plan ahead on a long period of time. But nevertheless, there is an intention to learn languages and to find new contacts that will play a positive role in future expansion.





## CONCLUSIONS

The main purpose of this paper was to increase the understanding of the internationalization process of family firms through testing Russian family companies. Empirical findings demonstrate that family firms' internationalization process reminds combination of the Uppsala model and the Network model, because companies expand gradually and mainly with the help of social capital. And networks can even play more important role than psychic distance. Moreover, being a family firm gives advantage in establishing trustworthy relationships, because, in general, there is an opinion that family firms are reliable and long-term oriented.

In the beginning of expansion companies choose low-commitment entry mode that does not require permanent involvement and huge costs. Very often networks affect on market choice and help in expansion by providing with useful contacts and information, but case companies are not very active in search of new contacts as they can be. Generally, for family SMEs expansion of social capital is very challenging.

To sum up, case companies internationalize slowly because of several reasons. First of all, in all companies nobody has prior international experience. Secondly, companies are located in Russia, where it is hard to run business and businesspeople are involved in day-to-day routine in spite of planning the future of the company. Short-termism is a typical trait not only concerning avoiding early expansion, but also in intention to sell the company without succession to the next generation. So, mainly entrepreneurs just want to have "easy" profit at the moment without thinking about the future and such kind of behavior definitely badly affects on company's reputation. Thirdly, presence of the family might affect on openness to find new contacts. In fourth, internationalization needs financial investment, knowledge and time. The next reason is that Russia is a vast country and companies gain more profit from selling in domestic market than abroad, so there is simply no necessity to internationalize. Other reasons can include absence of governmental support, product itself and traits of the owner.

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