Relationship of Internationalization and Firm Performance: Empirical Evidence From SME Perspective

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Abstract
Firms internationalize in order to capture potential profit opportunities outside the home market or to withstand its competitive pressure, i.e. the factors that influence the firm to internationalize contributing to its increased profitability. It was in other words assumed that the more inclination towards internationalizing a firm, the better is its performance. The results from the previous research studies has confirmed a positive, but marginally, significant relationship between internationalization and performance of the firm. In this study, we lay emphasis on SMEs (small and medium manufacturing enterprises) of pumps and motors in Coimbatore district that have an international exposure in terms of foreign sales. This article proposes an extension of the internationalization performance based on the ‘Entrepreneurship Theory’ variables in relationship with the firm’s sales and profit growth. For this purpose, 143 firms in Coimbatore were surveyed and the findings revealed that these firms show a significant inclination towards the financial predictors such as Sales volume, Profit growth, Enterprise value and Asset value for assessing the total performance of the company. To assess the performance and growth of the internationalization firms, Pearson Correlation of firm’s export performance variables, Multiple Regression Analysis and Correlation of subjective and objective performance variables were applied in this study.

Key words: Entrepreneurship Theory, Internationalization, Enterprise Value, Asset Value

I. Introduction
Internationalization can be broadly defined as the outward activity of a firm. Exporting is said to be a firm’s international market entry in the internationalization process of a company. Only a few studies have investigated whether firm’s performance has an effect on its internationalization. Many different ways of measuring internationalization associating the performance and growth of a firm exists. Beamish also predicted that firm’s growth is an important dimension of firm performance, especially for SMEs, to understand the influence of internationalization on the growth of SMEs. Exporting has been extensively employed by firms as a growth strategy. By selling directly or through an agent to the customers in a new geographic area the firm broadens the customer base and can potentially achieve higher growth in sales volume. In turn increase in sales volume leads to higher production volume and expansion in production capacities leads to the growth of the firm. Export is an especially popular means of firm growth for SMEs.

Exporting is the main mode of internationalization for the select sample of SMEs to enter into foreign markets with low commitment and moderate control requirement. Based on the research, it is found that for exporting, an SME does not have to make substantial resource commitment like other modes of foreign entry. Exporting is a less risky strategy because at any moment the firm can withdraw its foreign activities such as a political instability or fluctuations in the market conditions. The firms can more easily change and adapt their foreign activities to other geographical area and scope by adjusting their resource and commitment. Furthermore, for the
study, ‘export’ is taken as a prime mode of internationalization and how possibly it impacts on the firm’s growth through the ‘International Entrepreneurship’ theory.

1.1 International Entrepreneurship theory

The theory states that it is the study of cross-border entrepreneurial behavior and it supports the idea that internationalization is an act of entrepreneurship, because internationalization cultivates a search for opportunities to achieve firm’s wealth and growth by expanding into new markets. McDougall and Oviatt’s (2000, p. 903) introduced their definition of international entrepreneurship as a “combination of innovative, proactive and risk seeking behavior that crosses national borders and is intended to create value in organizations”. For the study, the entrepreneurial variables identified are: Growth Opportunity, Creativity/Innovation, Managerial motivation, Technological advancement, Management’s ability to take risk, exploitation of foreign opportunities and previous international experience of the entrepreneur were considered as important factors affecting the firm’s internationalization process. Also entrepreneurial theory variables are taken as subjective measures in analyzing the performance of the firm.

II. Review of Literature

Burgel et al (2001) detected that firms with international operations reported higher productivity and sales growth but not employment growth. From the previous literature it is clear that, Internationalization has a positive link between the firm’s growth in terms of sales, international operation and its reportedly superior performance by higher quality products, market expansion and profit maximisation. But Brush (1992) found no significant relationship between age of internationalization and new venture performance (usually sales growth or employee growth). In contrast to Brush’s findings (1992), Autio et al. (2000) demonstrated that the age of a high technology firm at international entry is negatively related to its subsequent growth in international sales because international growth happens through various factors and it is not dependant only on profit and sales growth. Bloodgood et al. (1996) found a positive but marginally significant relationship between internationalization and performance (sales growth). Recent studies, however, have shown a positive and linear relationship between internationalization and performance (Dhanaraj and Beamish 2003; Qian, Yang et al. 2003; Qian and Li 2003).

All these empirical findings in the international business literature point out to one conclusion: the results on the effect of internationalization on performance are mixed, and far from conclusive (Bloodgood, Sapienza et al. 1996; Zahra and George 2002; Sapienza, Autio et al. 2006). Yet it can be found through analyzing the performance indicators of a firm. As a consequence, there is a great deal of room for further investigating the effects of internationalization on SME development (Chiao, Yang et al. 2006).

According to the findings of McDougall and Oviatt (1996) in their longitudinal study, no relationship between internationalization and ROI (return on investment) was observed. However, they brought evidence that greater internationalization was associated with greater relative market share, which is to some extent a measure of firm performance. Also they have found ventures with increased international sales recorded higher performance over a two-year period, in terms of both return on investment and relative market share. McDougall and Oviatt (1996) noted that firms that had increased international sales exhibited superior performance. Further, Bloodgood et al. (1996) found that internationalization was fairly associated with ventures that reported higher profits. Hence increase in profits and sales volume can be associated with internationalization. Based on the studies of Jase R. Ramsey, Livia L. Barakat and Sherban L. Cretoiu (2012), the performance indicators are measured through categorizing them into ‘subjective’ and ‘objective’ performance variables.

2.1 Objective measures of performance

Objective indicators are represented as numbers or percentages directly found in financial statements, balance sheets or market/sales reports. Recent studies by Andersson, Forsgren and Pedersen, (2001) have used a combination of these variables. Bouquet, et al. (2009) found that the amount of time and
effort in activities, communications and discussions concerning the global marketplace was correlated with the firm’s performance.

2.2 Subjective measures of performance
The excerpts from the studies of Jase R Ramsey et al (2012) defines the subjective measures from various researches and supported their study. According to Wall et al. (2004), using subjective measures is a cost-efficient choice, additionally, executives are more amenable to evaluating performance on a Likert scale than reporting confidential information (Sousa, 2004). And also subjective measures provide a broader assessment of the results of internationalization as well as a useful comparison between firm’s expectations and the success achieved. A study by Geringer and Herbert, (1991) on the international joint ventures of United states provided an empirical evidence that subjective measures are adequate for assessing firm’s performance. Thus, scholars have been increasingly applying subjective measures as a complement to objective measures and also a solution to recurrent issues with objective indicators (Al-Khalifa and Peterson, 2004; Brouthers, Brouthers and Werner, 2008; Nielsen, 2007). Specifically, managers are more willing to give subjective results than hard numbers and both the size of the operation and how long it has been operating can both be taken into account when the manager responds to subjective measures.

III. Objectives of the study
1. To find the relationship between the export performance variables and the overall growth of the company.
2. To find the impact of enterprise value on the performance indicators
3. To know the relationship between the subjective and objective performance variables towards the firm’s international growth.

IV. Research Methodology
The study confines the selected sample to manufacturing firms of pumps and motor industries since, Entrepreneurship theory of internationalization is aptly applicable to the selected industry. 143 manufacturing firms were identified as sample for the research for the study of internationalization process and the performance of those firms. Simple random sampling method was used to select the sample from 272 firms based on the subjective measures such as age of the business, export intensity, sales turn over, line of business, number of countries exported, entrepreneurial scope and the previous international experience.

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To find the internationalization and its performance the pump and motor manufacturing Industry was taken for the research study. A known population of 272 firms from the available sources of data were chosen. The firms that fit into the definition of SMEs and those who have internationalized were chosen for the study. Firms selected for the survey were based on the SME definition by the European Commission and the exporters of the same business. The sample size of 143 firms comprising of both organised and unorganized sector were chosen for the study based on simple random sampling method. The subjective measures such as age of the business, export intensity, sales turn over, line of business, number of countries exported, entrepreneurial scope and the previous international experience are collected for knowing the firm’s international growth. For this study, data was collected through a questionnaire from the selected sample which are exporting pumps and motors from Coimbatore to Indian sub continents and to various other countries. The collected data were analysed through applying multiple regression and correlation by using SPSS software.

V. Empirical Views
For finding the empirical results, the analysis was done through conducting Pearson Correlation and Multiple Regression. The relationship between the performance variables and the impact of enterprise value on the performance indicators are found through applying regression analysis. The method of analysis are as follows.

1. Pearson Correlation of firm’s export performance variables
2. Multiple Regression of enterprise value on other growth variables
3. Correlation of subjective and objective performance variables.

5.1 Relationship between Export performance variables
From the table 5.1, it prompts the correlation coefficient between share of profit from International growth with all the other factors that shows a value more than 0.5 and the result for asset value shows a highest correlation value of 0.914. The values indicates close to 1 or 90% which shows a positive relationship or a perfect direct relationship between profit from International growth and other variables at the significant level of 1%. The P value(0.000) is less than 0.01 which shows that the results are significant. Also from the table-5.1 almost all the results show a direct positive relationship with other factors selected in growth table with respect to the financial year 2010-2011.

Hence it is concluded that, the enterprise value is having a positive relationship with all the other performance variables and the results found to be statistically significant of the p value which is less than 0.001.

5.2 Enterprise value on other growth factors
Multiple regression is used to measure the impact of the identified dependent and independent variables i.e.,

(i) Enterprise value as dependant variable
(ii) Increase in profit, increase in foreign sales, and asset value are the independent variables identified for the study.

From the table 5.2.1, it shows that the r value is 0.815 and R² value is 0.665 and hence exists a positive relationship between the dependent and independent variables. The multiple correlation coefficient is 0.815 from the table 5.2.1, measures the degree of relationship between the actual values and the predicted values of the Adjustment. Because the predicted values are obtained as a linear combination of enterprise value (X₁) and the growth indicators (X₂), the coefficient value of 0.815 indicates that the relationship between the dependent and the independent variables are quite strong and positive.
The Coefficient of Determination R-square, measures the goodness-of-fit of the estimated Sample Regression Plane (SRP) in terms of the proportion of the variation in the dependent variables explained by the fitted sample regression equation. Thus, the value of R square is 0.665 simply means that about 66% of the variation in adjustment is explained by the estimated SRP that uses growth indicator variables and enterprise value as the dependent variables and R square value is significant at 1 % level.

From the table, 5.2.2, based on the Unstandardised coefficient the regression equation is, 

\[ Y = 2.837 + 0.123X_1 + 0.643X_2 + 0.052X_3 \]

Here the coefficient of \( X_1 \) is 0.123 represents the partial effect of growth opportunity on enterprise value as constant. The estimated positive sign implies that such effect is positive that adjustment score would increase by 0.123 for every unit increase in asset value and this coefficient value is not significant at 1% level. The coefficient of \( X_2 \) is 0.643 represents the partial effect of increase in profits variable holding enterprise value as constant. The estimated positive sign implies that such effect is positive that adjustment score would increase by 0.643 for every unit increase in profit volume on enterprise value and this coefficient value is significant at 1% level. The coefficient of \( X_3 \) is 0.052 represents the partial effect of growth variables holding enterprise value as constant. The estimated positive sign implies that such effect is positive that adjustment score would increase by 0.052 for every unit increase in sales volume and this coefficient value is not significant.

5.3 Relationship between Objective and subjective performance variables

Objective indicators are represented as numbers or percentages directly found in financial statements, balance sheets or market/sales reports, whereas subjective indicators are the firm level performances. These results seem to suggest that the components of the subjective performance variables correlate more positively with the Objective performance measures. In the table 5.3 the correlation matrix also shows that all subjective performance measures positively correlate with each other. The highest correlation is growth in sales volume and profit volume with the firm’s asset value.

However, subjective performance variables (age of the business, number of countries the firm exports its products, Annual sales turnover) are positively correlated among themselves. (The results are based on table 5.3 ). This is possibly explained by the fact that the subjective construct is measuring the satisfaction with different aspects of performance as compared with the ones in the objective performance construct. It is interesting to note that international experience is positively associated with entrepreneurial activities suggesting that firms operating in international markets with previous international experience are better in obtaining their incremental sales.

Annual sales turnover and Age of the business firm shows a positive correlation of 0.340 at 1% level of significance. Number of countries exported shows a positive correlation with the subjective measures of Age of the business(0.620**) and annual sales turnover (0.378**). A positive correlation lies between entrepreneurial activities and export intensity (0.169*) and share of foreign sales (0.259**). If a firm operates with previous international experience, the asset value will also increase. This shows a negative relationship with these variables, which are asset value (-0.193*), profit growth (-0.166*) and growth in sales volume (-0.189*).

The objective growth measures shows a positive relationship with each other. Profit growth is strongly correlated with growth in sales volume (0.972**) and growth in enterprise value (0.814**). The firm’s asset value is influenced by many factors and not because of international sales alone, but due to the objective measures like gain of prior international experience, entrepreneurial skills, and adequate knowledge about the international markets.

Enterprise value is strongly correlated with the growth in sales volume which shows a value of 0.799 at 1% level of significance. Hence it can be concluded that the enterprise value is influenced by the growth in sales volume. The sales volume increases based on the impact of goodwill or the enterprise value.
VI. Findings

Although previous researches show that there is no direct significant relationship with degree of internationalization and performance indicators, the study would strongly recommend the following findings from the analytical views. There are firm level performances associated with the micro economic indicators to show the overall international growth. Yet the research finds the following relationship with the objective and subjective performance variables.

- It can be concluded that there is a negative relationship with previous international experience and the objective measures of performance. If the firm operates with prior international experience, it is evident that there is growth in terms of sales and profit.
- From the multiple regression the results reveal that there is an impact of objective measures of performance on the firm’s enterprise value.
- Enterprise value is strongly correlated with the increase in sales volume since the effect of the company’s value will show an influence on the sales volume.
- Previous international experience and the entrepreneurial abilities show a positive relationship.

From the Figure -1, the relationship of assessing the subjective and objective performance variables towards international growth has been clearly depicted. As said earlier, the growth starts in a firm when internationalization begins. The subjective measures are also the influential factors for international growth such as, resource commitment, firm specific advantages like market expansion, increase in demand and more sales volume which are said to be the growth indicators.

In this article, we attempted to examine the effectiveness of internationalization as an important growth strategy for SMEs; to explore the individual effect of internationalization strategy i.e., exports on firm’s growth in a sample of internationalized small and medium manufacturing enterprises of Coimbatore and further to assess how the subjective measures influence the growth indicators. Also it was found that the impact of enterprise value is dependent on the performance variables which also has an effect on the international growth.

VII. Conclusion

This article proposes an extension of the internationalization—performance relationship to include the firm’s performance indicators. It has attempted to provide a theoretical advancement in the international entrepreneurship theory, and it has a wider scope to further investigate how internationalization affects a firm’s performance towards its international growth. The ultimatum of the study proposes that the entrepreneurial abilities, capability of networking, prior international experience and the plethora of knowledge on the international markets speak upon the level of International sales volume, growth, enterprise value and the firm’s profits.

References:


Annexure

**Fig -1**
Conceptual Model

(Source : Self)