Internalization and types of entry modes

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Internationalisation makes a firm's managing skills better facilitate the resources usage and it gives greater flexibility for undertaking any intricate business risks (Katsikeas and Skarmeas, 2003; Young et al., 1989). Operating in a foreign country markets may allow a firm to face international competition and that yields a better concern in foreign markets thereby becoming a stronger player in its home-market (Lages and Montgomery, 2004). Outstanding to their lack of experience, skill and know how small and medium-sized enterprises (SMEs) need to be very vigilant in the entry route (Oviatt and McDougall, 1994 ; Collinson and Houlden, 2005). There are two types of entry modes in the world of business, the first is equity mode and the other is non-equity mode. In the market 78%, have restricted their internationalisation in non-equity mode to exporting alone, but remaining 22% of SME's goes for equity participation and other cooperation based modes (Young, 1987).

Previous works on the entry mode is done for the firm's domestic environment but particularly governmental support, which has not been examined, may well be an important driver of SME entry mode choice with that a country risk analysis is done for the target market. In this research we learn how the Indian textile SMEs choose their entry mode for their internationalization with the target market as Canada along with the government support that they get for the internationalization. A major drawback associated with using cross-sectional data is that it does not capture dynamic processes. For example, an SME could start with an exporting strategy and then progress towards a JV. Examining the switching behaviour and its optimal timing within a longitudinal perspective is an area

of research that has received little attention. Although consistent with other studies, the inclusion of the two broad categories of equity and non-equity may underestimate the effect of potential differences existing within each category.

This research may be useful when SMEs choose their entry for internationalization with the government support. Results in the present study concerning the impact of several managerial characteristics on the type of foreign entry mode have not been conclusive; an important line of research could explore this dimension more extensively. This study could be enriched and complemented by applying several measures of experiences. Since, the objective of decision-makers is to select the highest performance entry mode, the principal challenge is to discern which entry mode choice has a potential impact on performance and most importantly, which entry mode is more efficient under a particular set of market conditions.

This chapter is composed into three parts; first part will review literatures first part is for choosing the most feasible entry mode for Internationalisation; second part will review the country risk analysis for the target market the and then third part will review literatures the government support that SMEs they require for successful establishment.

2. 1. Entry modes for Internationalisation:

At the domestic level, internationalisation endorses socio-economic development, generates foreign exchange, increases employment opportunities and reduces the national deficit (Katsikeas and Skarmeas, 2003; Lenidou et al., 1998). When a company moves to the international

market they should have some kind of initiative to start the internationalization process (Hollensen, 1998). Internationzlization process increases the social prosperity and boosts the output of the industry (Lages and Montgomery, 2004). Research surrounding firm internationalisation has stressed that the recreation of foreign expansion is concerned with the organisation of overseas operations and the various costs and benefits associated with each foreign market entry mode. Companies classified as SMEs are defined as having fewer than 50-100 employees. Although SMEs have restricted their internationalization to exporting alone, there are other modes of entry, particularly those involving equity participation and other cooperation based modes that can also be considered by these types of firms (Young, 1987).

The most complex thing in choosing the entry mode is decision making. Different types of entry modes exist but they have both advantages and disadvantages in which selection process involves greater complexity. By analysing the entry mode of an SME facilitate its organisational activities with three aspects, which is the level of dissemination risk, control and resources allocated (investment) for the foreign markets by the SME (Young, Hamil, wheeler & Davies, 1989). Some initiatives are there for the SMEs internationalization and that was developed by Hollensen (1998) and Burca, Fletcher and Brown (2004) and that can be explained as internal and external causes. In this research, focusing on specific market segment, we are assessing the risks, level of control and the resources allocation which helps to structure their investments through which SMEs can make their entry ease. According to (Pan and Tse, 2000), for the first level entry can be

made with low investment that is with low risk of investment by focusing on specific market but the control may not be up to the mark. Those who prefer high control can go for equity entry mode consequently, to use more investment-intensive foreign modes of entry (e. g. JV, wholly owned subsidiaries), which enable them to have an exercised high level of control (Nakos and Brouthers, 2002). Control generally refers to the level of authority a firm may exercise over systems, methods and decisions in the foreign affiliate (Ekeledo and Sivakumar, 2004). So, organisations need to analyse in depth and breadth about the host country in regards to risk involved, time and cost to design their strategy.

Theoretical background

The study of firm's development into foreign markets has received increasing attention at both conceptual and empirical levels. There three different rules for choosing the entry modes, they are naive rule, the pragmatic rule and the strategy rule.

According to Albaum, strandskov and Duerr (1998) if a company adopts same entry mode for all the country it comes under naive rule. Often SME mangers use this rule to enter international markets.

The pragmatic rule says that " one entry mode for one market entry but they won't investigate on the different entry modes, but the selected one must not be the most suitable one. Due to lack of investigation the cost of information and management is small". (Albaum, Strandskov and Duerr, 1998). They often begin with export and export is not the only way to yield profit but the company changes their entry mode once they established

themselves in the international market (Hollensen, 1998). The advantage of this rule is that it minimizes the types of entry modes and its disadvantage lies to lead managers to the selection of the entry mode (Albaum, Strandskov and Duerr, 1998)..

Strategy rule states that companies evaluate their experiences when making the final decision (Hollensen, 1998). The decision rule is to choose theory mode that can enrich the profit level with the previous experiences.

The firms undertake international activities on an incremental basis to gain experience, to adopt a more positive perception of risks and to develop know-how for entry into additional markets (Johanson and Vahlne, 1977, 1990). Specifically, Johanson and Vahlne (1990) state that the firm's engagement in a specific foreign market develops according to an established chain, i. e. at the start no export activities are performed in the market, then export takes place via independent representatives, later through a sales subsidiary and finally through full engagement.

Ownership-specific advantages

When a firm decides to enter into a new foreign market, it should be directed by its ability to effectively exploit its own competitive advantages (Prahalad and Hamel, 1990). Existing literature holds that, if an ownership advantage could be relocated internationally without losing its worth, the firm would prefer high-control modes of entry, which make sure that an efficient implementation of the firm's unique advantages and provide a enhanced protection of its knowledge and differentiated products (Nakos and Brouthers, 2002). Furthermore, by gaining control over external operations,

firms can substantially reduce the dissemination of risk (Anderson and Gatignon, 1986). Several authors have recognized various SME specific resources and capabilities that provide significant ownership advantages including firm size, extent of international experience and ability to produce differentiated products (Calof, 1994; Nakos and Brouthers, 2002; Agarwal and Ramaswami, 1992). A number of authors, however, have renowned that size, competency and resource availability may differ rudely among SMEs in such a way that the medium-sized firms are expected to possess greater managerial and financial resources than their smaller counterparts (Osborne, 1996; Nakos and Brouthers, 2002). Therefore, it is likely that medium-sized firms tend to prefer equity-entry modes, while smaller firm's go for non-equity entry modes (Osborne, 1996). Due to this SMEs go for exports and the theories suggests that a number advantages are there when using the export entry mode such as low risk, resource allocated can be predicted before the project and big disadvantage is lack of control (Bennett, 1998, Hollensen, 1998).

International experience is defined by Johanson and Vahlne (1977) as practical knowledge attained by doing business in the host country which is also measured as an important driver for determining the choice of a specific entry mode (Agarwal and Ramaswami, 1992) and with that managers in the company who look for the business opportunities must update their knowledge and the author further adds that through international visits they can get more opportunities for their company (Hollensen, 1998). Thus, firms having greater international experience are able to face the risk associated with doing substantial resources into the foreign markets and, at the

sequential time, have developed more complicated processes and systems for efficiently managing their international operations (Gatignon and Anderson, 1988). Such international experience, particularly that of geographic experience which is rooted in the firm's familiarity with a region of the world (Gomes-Casseres, 1989), as well as attendant (network) relationships, offers greater control leading to a move from non-equity to equity investments (Anderson and Gatignon, 1986).

Location-specific advantages

Location advantages consign specific factors to the host country and are believed by appropriate literature to act as potential drivers for the firm's internationalisation. Although location-specific advantages are there to all firms in a host country market (Dunning, 1988), not every firm is able to maximise its return in an equal way. The literature holds that markets with high-current demand and high potential for future demand provide a firm with long-term investment potential (Brouthers et al., 1996). Therefore, the estimated growth of a particular market may lead SMEs towards a greater degree of obligation.

Managerial specific characteristics

A number of managerial-specific characteristics that may act as important drivers of SME entry mode decision. The relative weight attached to the role of decision-makers within the internationalisation process varies depending on the theory and conceptual framework that is cited, Whereas, at one end of the spectrum, internationalisation theory completely relegates the importance of decision-makers to an economic and transaction-based

rationale, network relationship theory approaches confirm the essential role played by individual decision makers (Collinson and Houlden, 2005). Lenidou et al. (1998) have examined the possible effects of a number of objective and subjective decision-maker characteristics and their attendant impact on the firm's internationalisation. Among the objective characteristics, particular emphasis has been placed on the decision-makers age and educational level (Schlegelmich, 1986). In a determining work, McConnell (1979) suggested that younger managers leaned a greater potential to be involved in international activities (Ursic and Czinkota, 1989).

Similarly, it has been suggested that more highly educated decision-makers have a greater likelihood of being more open-minded, interested in foreign affairs and willing to objectively evaluate the potential advantages associated with internationalisation (McConnell, 1979). Others have claimed that higher education level is crucial for guaranteed success in foreign undertakings since it reduces the degree of uncertainty associated with international markets (Schlegelmilch, 1986).

Ownership structure (family and non-family owned)

By considering the ownership structure and the most SMEs are family owned, it is expected that their strategic orientation, particularly with respect to internationalisation, is indivisible from the personal objectives of the owners reflecting their own personal needs, values beliefs and philosophies (Kotey, 2005). Growth in these types of firms takes place slowly and in a traditional manner since family-firms show a less liberal management style and react slowly to changes with informal management practices (Dyer and Handler,

1994). There is a lack of research covering the international obligation of family firms as compared to non-family firms (Fernandez and Nieto, 2005). Despite the scarcity of studies in this field, it is likely that family firms gradually commit to international markets by means of non-equity entry modes due to the aforesaid difficulties for accommodating growth, intrinsic conservatism and general dislike to risk (Harris et al., 1994).

2. 2. Country risk analysis

In addition, firms entering in to new foreign markets may be meeting with unstable economic, legal and political systems creating high-investment risk environments thereby discouraging their tendency towards international obligation (Agarwal and Ramaswani, 1992). In this sense, firms may not tend towards a high-involvement entry mode in risky markets due to the potential for loss of their assets and investments. Furthermore, once a financial commitment has been made, it may be very difficult for a firm to safeguard its investments, particularly in rapidly changing environments (Nakos and Brouthers, 2002).

Economical scale of the company increases when a company goes into the international market that the price of the product goes high and there will be increase in production (Hollensen, 1998). Due this company gains an advantage of competition with the lower cost (Albaum, Strandskov and Duerr, 1998). Reliable with Terpstra and Sarathy (1994), low-operating costs corresponds with marketing activities favour high international obligation to foreign markets leading to the choice of equity-entry mode.

The apparent cultural distance between home and host countries, conceptualised in terms of similar business practices, also contributes towards the choice of a specific entry mode (Ball and Tschoegl, 1982). Kogut and Singh (1988) suggest that the entry mode choice varies depending upon the cultural distance between countries. Therefore, it is assumed that the propensity for choosing an equity-entry mode arises out of a low-distance perception in terms of culture and business practices between the home and the host-countries.

Creating the present country risk work came from the obligation of finding conclusive answers on about accepting or not some credit risks, especially those ones represented by the possibility of restricting the payment, imposed by a country. These facts are getting more significant throughout the world, these has led the countries towards economic downswing, necessary for keeping them competitive. So, there is number growing of companies owing their advantage for the external trade, which shows numerous business choices as much as the option of buying products (Lynch, 2001).

Country risk studies are related to the future capability of enhancing wealth from the existing resources, in terms of capital, technology, natural resources and labour forces.

Dependency Level:

A country with an established economy in terms of industries, it can be the major leading controller in its world relationships. In the more an economy has a strong international trade in both ways, the better it could deal with its

international partners. It is sure that financial dependency to meet the needs of a country also is a strong and lasting concern for the analyst. In this case, the debts and, the existing sources of financing also calculate the grades of the country. Output is increased throughout the economy (Lynn, 2001).

The same approach is done for the international trade. For that, the analyst must divide each part of the trade balance in sectors, goods, countries and economic blocks, identifying its composition and level of concentration (Ray, 1998).

External Environment:

External trade has been an important factor to the development of societies since ancient times. Nonetheless, nowadays, globalization has brought important identification to the international business and so forth the external environment had became very important for all countries, including the ones where the external sector has not been so strong until now. Thus, a whole vision on what is taking place around the world (the economic trends, the behaviour of financial markets (flows and rates), the forecasts for clashes among nations, the improvement of the economic blocks, the level of openness of the world economy, (Financial crisis and international liquidity) is a framework over which the analysis is believed to start. So forth, the analyst must select those matters that are more closely linked to the country which he is dealing with, seeking to figure out about the impact of the most probable situation of them to apply over the country`s economic variables (Horne & James , 1998).

The new exchange rate carries a change in the prices of the whole domestic economy that could cause an impact in terms of internal prices and other macroeconomic collected as outcome, growth rate, interest rate, savings, consumption and so on. The dimension of the impact will be also defined by the stage of international liquidity, the bigger it is, the soft and cheaper is the adjustment process (International Monetary Fund, 1996).

2. 3. Government support:

Smaller firms usually dogged on their domestic market, and a majority of SMEs will most probable goes on to do so in the future. These SMEs contribute to 35% of global manufacturing exports. SMEs have a large unexploited potential to grow through internationalization. Policy may play a significant role in assisting SMEs in their internationalization process. The first objective of policy can be targeted at making the awareness about the internationalization and its benefits within this group of entrepreneurs. There should be minimizing entry barriers and lowering the cost of international expansion, and transaction costs. These barriers should be minimum than further increasing the administrative costs SMEs already have to pact with. Other important barriers relate to lack of information and finding reliable partners (Internationalization of SMEs).

Firms in different stages of internationalization have different needs for government expert help. Therefore, support should be modified to firms with different degrees of export obligation, rather than offering generic government assistance to all firms. For those firms that do not export, a distinction should be made between those that are ready to export and those firms that are not.

Policy frameworks need to be fit enough to react to the increasing difficulty and uncertainty SMEs face while competing internationally. Policy should take initiatives to develop an international entrepreneurial environment. Agencies should support other forms of internationalization than export. Since joint ventures are an emerging internationalization strategy for SMEs, support programs could play in vital role in helping SMEs in identifying foreign business partners and that should be secured by policies and laws. Programs providing direct and active support to SMEs should combine a number of factors, such as access to information, competency development and hands-on, individual service (Internationalization of SMEs).

Most countries offer information services and promotion, such as support for contribution in trade fairs. A more effective support measure would be more customized support, such as individual counselling. This advice may help them on export development, the establishment of subsidiaries abroad, competence development, the identification of partners and legal advice. However, there seems to be a significant gap between the need SMEs have for planning their international activities and the actions in relation to these activities. Therefore, SMEs could benefit from assistance in choosing, planning and deploying the right strategy. Support agencies should not restrict their role to information services and financial support. Follow up is needed to assess the impact of the aid on the SME’s internationalization performance (Internationalization of SMEs).

In India, textile SMEs they generally prefer exporting as their entry mode for internationalization and they restricted themselves to exporting alone. For

the target market government does supports in tax basis and by means of incentives for the differentiated products.

Government Policy of India

The government policies that have a bearing on global competitiveness of the

Indian textile and clothing sectors are explained as follows

Excise Policy:

The excise duties related to the textile industry are the basic excise Duty, Additional Excise Duty at 15% related on cotton yarn. Garments and made-ups that contribute 15% added share only 13% of excise burden. No duty for the grey fabrics.

Quota Entitlement Policy

The fact germane for competitive analysis in this policy is the fact of over-categorisation that has been practised through these policies, and the ' export tax' that the Indian textile and clothing exports have been subjected to owing to the quota policy of major importing markets. So that a firm to be able to export therefore, it must buy the quota from the market at the prevailing premium. This imposes a cost to the firm analogous to export tax.