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How Strategic Market Entry Modes Influence Internationalization of Small Medium Enterprises in Kenya

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Abstract:
The purpose of this paper is to establish how strategic market entry modes influence firm's ability to expand from the local to the international market. The study looked at how different entry modes determine the level of firm internationalization. Some of the strategic entry modes which medium sized firms have used include exporting, direct investment, licensing and franchising, outsourcing and subcontracting, collaborations and partnerships. The study targeted CEOs and senior managers for 100 Top Medium firms in the category of 2012. Structured questionnaire was administered and both descriptive and inferential statistics were used. The findings revealed that though the mode of entry affects the firm's ability to internationalize, there are multiple factors that should be considered when deciding to go international as opposed to only one or a few.

Keywords; *Collaborations, mode, partnerships, strategic*

1. Introduction and Background

The one problem that comes to every company's mind when they are expanding to a new market is about which foreign market to enter, when to enter, scale of entry and the choice of entry mode (Hill, 2007). The other possible problem is that firms may lose control of their international operations. Medium enterprises that pursue rapid internationalization experience very high failure rate and a lot of their challenges relate to liabilities of newness, foreignness and smallness (Zahra, 2005).

What makes the entrepreneurial SMEs different from the other ordinary SMEs and what determine the speed of internationalization include; extreme proactivity for international ideas , strong personal drive , drive and inspiration for internationalization, international risk-taking behavior, international networking behavior, high alertness to profitable international breaks, positive international attitudes and international orientation and a great need for international achievement (McDougall *et al*., 1994)

Etemad (2004), postulates that internationalization is facilitated by environmental factors such as international communication and transport, removal of trade barriers and technological advancement besides the other factors that are associated with international entrepreneurship phenomenal.

1.1. Internationalization of Medium Enterprises

The internationalization of MEs has significantly increased all over the world in the recent times (Etemand, 2004; Andersson, Gabrielsson & Wictor, 2004). Firms Internationalization is no longer an option but an economic imperative which has a major role in the competitiveness of SMEs in all economies (Rutashobya & Jaesson, 2004).The significantly increasing role played by Small and Medium Sized Enterprises in driving Economic development has resulted in a growing interest in the study of Internationalization of SMEs (Kula & Tatoglu, 2003). SMEs from the growing markets in Africa have internationalized into developed countries and similarly the developed countries have increased their business undertakings in developing markets as a result of globalization and decline in the market barriers as well as the attraction for foreign investment (Cavusgil,2002).

1.1.1. Study Objective

The main objective of the study is to determine the influence of the types of modes used by medium sized firms in their internationalization process.

1.1.2. Research Hypothesis

- H_0: There is no relationship between the entry mode used by medium enterprises and internationalization
- H_1: There is a relationship between the entry mode used by medium enterprises and their internationalization

2. Literature Review

International market entry mode can be defined as;

"an institutional arrangement that makes possible the entry of a company's products, technologies, human skills, management or other technologies into a foreign country" (Root, 1994, p. 24).

Entry mode can also be explained as organizational structure of how a firm establishes itself in a foreign market (Chetty and Agndal, 2007). With respect to internationalization of firms, entry mode is one of the frequently researched areas There are also studies focusing on how entry mode choice affects performance (Devine, 2010; Lu and Beamish, 2001) as well as the relationship between international strategy of the firm and the entry modes (Pehrsson, 2008).

Firms adopt a wide range of modes of operation during the process of internationalization and many of these modes fit the traditional classifications i.e. contracting, exporting, foreign direct investment and licensing (wild et. al. 2003). A lot of literature collaborates in that networking influences the choice of the entry mode which SMEs adopt. A firm may chose different entry forms when penetrating similar markets dependent on the options that may be availed by the network relationships (Moen & Servais, 2002). Network relationships are the determining factor when deciding the form of entry to a foreign market. The choice of the market entry mode in the international market is mainly determined by an attempt to reduce uncertainty (Maskgard and Sharma, 1998).

Coviello and Martin (1999) show the importance of both informal and formal relationships in the selection of firms' first market and the choice of entry mode to geographically close markets. This finding collaborate with the studies of Coviello and Munro (1995, 1997), regarding New Zealand based small software firms suggest that a firm's informal and formal network relations facilitates the firm's entrance to psychically near markets and determine its mode of entry. These findings are consistent with the study done by Moen et al. (2004) which contend that small software firms first gain entry to foreign markets that are psychically in near. Zain and Ng (2006), and Moen et al. (2004) in their studies found that network relation influence market selection and entry mode of small software firms and therefore influencing the process of internationalization of firms.

Although the choice of the mode of entry for a market is mainly seen as a result of network relationships, some studies have altered this view (Bell, 1995; Sharma & Blomstermo, 2003). The network model of internationalization does not say anything on how network relationships influence the choice of entry mode in the target market neither does it give direction on how firms enters geographically or psychic distant markets(Johanson & Mattsson, 1988; Johanson & Vahlne, 2003).

2.1. Network Theory of Internationalization

Network theory originates from sociology and it is also known as the social capital theory (portes, 2003). Johanson and Mattsson, (1988) explored the influence of network relations on the firm's internationalization based on the stage theory (Johanson & Vahlne, 1977). The Stage theory envisages that entering into international markets is single effort of the firm and thus the need to acquire knowledge and the requisite resources to internationalize; the firm develops and builds this knowledge and resources through its own effort. Network theory, on the contrary contests this premise by holding a view that internationalization is achieved through collaborative efforts and creating relationships between firm and the other actors in the market. The network approach postulates that internationalization of firms is achieved via affiliations of the firm to other counterparts ((Johanson & Mattsson, 1988; Johanson & Vahlne, 2003). The network viewpoint defines industrial markets as "networks of relationships between firms" (Johanson & Mattsson, 1988, p. 287).

Networking speeds the firm's internationalization capacity and this neutralizes the incremental assumption in the stage theory. The privilege of being in a pool of network relations enables the SMEs' to gain capacity to respond positively to the prompts of export initiatives and the firm can easily achieve internationalization.

Networking invalidates the need for the SMEs to have prior experiential knowledge and requisite resources before gaining entry into the international market; this is the claim of the stage model that the firm should possess these two attributes before contemplating internationalization. Networking enables SME to access many resources from the other actors both locally and abroad through association. The requirement of the psychic distance by the stage theory becomes irrelevant as a prerequisite for the choice of the foreign market since SMEs profits from network relations. Consequently, the variables like; the age of the firm, the firm size, the age of its owner manager or the key decision maker ceases to become determinants of firm internationalization. Network theory postulates that it is the type and amount of network ties that a firm possesses which mainly determines whether the firms will entre foreign markets.

As a way to counteract stage model, the network perspective has made an attempt to explain internationalization of industrial firms through associations and relationships among firms and their equivalents (Johanson & Mattsson, 1988; 1992, 1995). Network model proposes two prerequisites for the process of internationalization: 1. the gradual acquirement of market knowledge and experience and; 2. learning from colleagues in a network (Elango and Pattnaik, 2007). To this extent, network model is therefore regarded as an extension of the Uppsala model because it outspreads the unit of analysis to the market level. Chetty and Campbell-Hunt (2003),claim that although firms gradually learn about international markets as they enter into these foreign markets, the process of learning happens in a network.

3. Research Methodology

Descriptive research design was used for this study. Descriptive research design is characterized by existence of considerable knowledge and information about a specific phenomenon (Chisnall, 2001). The target respondents were CEOs and senior managers for Top 100 medium companies' category of 2012. A structured questionnaire tool was used to gather primary data. Both Descriptive statistics and inferential statistics were used. The responses gathered were coded in order to process using the computer. The analysis was done by the use of statistical package for social sciences (SPSS) software version 21 (Nicole, Kemp and Sneglar, 2000). Pearson Correlation analysis was used to test the strength of the relationship between independent and dependent variables.

4. Findings

4.1. Whether Firm Operate Foreign/International Business Activities

The table below shows results on internationalization of the firms

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Yes	41	56.2	56.2	56.2
	No	32	43.8	43.8	100.0
	Total	73	100.0	100.0	

Table 1: Internationalization of Firms

Out of the 73 firms that participated in the survey, 41 (56.2%) had internationalized and 32 (43.8%) were local. A majority of the firms that were studied therefore had international operations as compared to the ones with only domestic presence.

4.2. Foreign Countries of Operation

The respondents were asked to indicate the foreign countries where their firms had operations. The results are presented in the table below

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Uganda	15	20.5	20.5	20.5
	Tanzania	15	20.5	20.5	41.0
	Rwanda	11	15.1	15.1	56.0
	Southern Sudan	9	12.3	12.3	68.3
	Burundi	7	9.6	9.6	77.9
	Western Africa countries e.g. Nigeria, Ghana…	8	11.0	11.0	88.9
	Europe	4	5.5	5.5	100.0
	Others	4	5.5	5.5	100.0
	Total	73	100.0	100.0	

Table 2; Foreign Countries of Operation

When the participants were asked which foreign countries their firms has operated, a majority said Uganda, 15 (20.5%) and Tanzania 15 (20.5%). Rwanda followed at 11 (15.1%) and Southern Sudan at 9 (12.3%). Only a few firms had international operations in Europe, 4 (5.5%). This implied that cultural distance especially geography played a major part in making the decision on the foreign country to enter.

4.3. Foreign Sales as a Percentage of Total Sales

The participants were asked to provide approximate foreign sales as a percentage of total sales

	Frequency	Valid Percent	Cumulative Percent
Below 10 %	11	26.8	26.8
11 - 20%	11	26.8	53.7
21-30%	9	22.0	75.6
31-40%	7	17.1	92.7
41-50%	3	7.3	100.0
Total	41	100.0	

Table 3: Foreign Sales as a Percentage of Total Sales

Out of the 41 firms that had internationalized, 22 (53.7%) had below 20% foreign sales as a percentage of total sales. Only 9 (22%) of the firms had 21-30 percent foreign sales as a percentage of total sales. Of the firms that participated in the survey, 7 (17.1%) had 31- 40% of their total sales coming from the foreign market while only 3 (7.32%) had 41-50%. Out of the 41 firms that had internationalized none had more than 50% of the foreign sales as a percentage of total sales.

4.4. The Mode of Entry That the Firm has used to Access Foreign Markets

Entry mode	Freq.	%
Exporting	30	73.17%
Direct investment (Wholly owned operations abroad)	7	17.07%
Licensing and franchising	22	53.64%
Outsourcing and/or subcontracting	19	46.34%
Collaborations and partnerships e.g. Joint venture	25	60.98%

Table 4: Mode of Entry

On the mode of entry that the firms has used to enter international market, a majority 30 (73.17%) of the firms studied used exporting followed by collaborations and partnerships 25 (60.98%). Only 22 (53.64%) firms used licensing and franchising modes. Direct investment was the least considered mode, 7 (17.07%) followed by outsourcing and/or subcontracting 19 (46.34%).

4.5. Inferential Statistics

- H_0: There is no statistically significant relationship between a Firm's Mode of entry and its ability to internationalize.
- H_a: There is a statistically significant relationship between a Firm's Mode of entry and its ability to internationalize.

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.897[a]	.805	.802	3.741

Table 5
Source: Primary Data 2013
a. Predictors: (Constant), Mode of Entry

ANOVA[b]						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	4096.849	1	4096.849	292.788	.000[a]
	Residual	993.471	71	13.993		
	Total	5090.320	72			

Table 6
Source: Primary Data 2013
a. Predictors: (Constant), Mode of Entry
b. Dependent Variable: Internationalization

The coefficient of a Firm's mode of entry into a foreign market was found to have an estimated standard error of 3.741, F-statistic of 292.788 and an associated p-value of 0.00. The relationship between a company's mode of entry into a foreign market and its capacity to expand internationally is statistically significant at significance level $\alpha=0.05$ given that $p<0.05$. As a result, the Null hypothesis is rejected since the p value is less than the critical value while the alternative hypothesis is accepted.

4.5.1. Hypothesis Testing

- H_0: There is no statistically significant relationship between a Firm's Mode of entry and its ability to internationalize.
- H_a**:** There is a statistically significant relationship between a Firm's Mode of entry and its ability to internationalize.

The findings established that the coefficient of a Firm's mode of entry into a foreign market had an estimated standard error of 3.741, F-statistic of 292.788 and an associated p-value of 0.00. The relationship between a company's mode of entry into a foreign market and its capacity to expand internationally is statistically significant at significance level $\alpha=0.05$ given that $p<0.05$. As a result, the Null hypothesis is rejected since the p value is less than the critical value while the alternative hypothesis which stated that there is a statistically significant relationship between a Firms's Mode of entry and its ability to internationalize was accepted.

5. Conclusion

The empirical investigation revealed that firms use different entry modes for different reasons but mainly the network relationship available. The results of the study supports the study by (Moen & Servais, 2002) which argued that a firm may chose different modes of entry when penetrating similar markets dependent on the options that may be availed by the network relationships. The choice of the market entry mode in the international market is mainly determine The

Recommendation to the government of Kenya is that it should build a forum where domestic firms will have the opportunity to network with foreign businesses to build business alliances (e.g. by sponsoring local and abroad business development forums). Such forums would enable the domestic firms to explore any opportunities to build partnerships with foreign associates. Additionally, in the field of policy, the government of Kenya should sponsor a variety of trade fairs and subsidize international businesspersons who are willing to take part in such proceedings. By hosting the event locally, the cost will be low and therefore attract domestic firms to participate and thus showcase of what they do and thus stand a chance of forming alliances with foreign partners. The reason for this is that, results from the study show some firms did not have the capacity to participate in trade fairs and they felt that foreign trade is a preserve for large businesses.

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