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THE SIGNIFICANCE OF FIRM INTERNAL BARRIERS TO THE INTERNATIONALIZATION OF SMES

Bachelor’s Thesis
International Business
November 2016
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1 INTRODUCTION

This thesis is a literature review into the subject of internal barriers to the internationalization of small and medium-sized enterprises. The intention is to review previous subject literature and to identify the key internal barriers to internationalization and their significance to small and medium-sized enterprises in the process of international growth.

1.1 Introduction to the research subject

Internationalization and globalization of markets have been strengthening their significance in the world of business for many decades now and their presence continues to be emphasized in economies around the world. Internationalization has become a medium for growth in all markets and a phenomenon, which is further assisted by decreasing regulation and evolving technology (Leonidou 1995, Rodriguez 2007). Consequently, due to decreased amount of obstacles related to internationalization also small and medium-sized enterprises (henceforth SMEs) have been able to gradually increase their participation in international trade especially in the form of exports (Fliess & Busquets 2006, Rodriguez 2007). This has made it possible for small and medium-sized enterprises to realize such advantages as enlarged markets and a shift in the dynamics of competition to their benefit (Lee et al. 2012). The rapid movement towards a global market place has resulted in companies needing to take international growth into consideration earlier in their life cycle than before, which has lead to an increasing amount of internationalizing SMEs. Internationalization is discussed in this thesis, for all means and purposes, as an intertwined concept with company growth.

Traditionally it has been the view of subject literature that larger firms hold a considerable advantage over smaller firms when it comes to internationalization. However, recent decades and many studies on the subject have started to show contradictory evidence to this once dominant notion (Katsikeas & Morgan 1994). The amount of obstacles, or barriers, to internationalization faced by SMEs is indeed bigger, but the measures taken against these barriers can be implemented in a more
agile way due to simpler organizational structures and smaller size (Smolarski & Kut 2011). Although SMEs may be more agile, their ability to absorb consequences of risk is smaller than that of larger firms, which have several possible strategies to overcome barriers by leveraging their size, influence and resources (Requena-Silvente 2005, Fliess & Busquets 2006). The agility of SMEs is better utilized in proactively avoiding internationalization barriers than trying to recover from the realized risk that said barriers bring forth (Francis & Collins-Dodd 2000). As a result SMEs must be proactive towards those trade barriers, which they can affect by their own actions, consisting mainly of factors relating to resources existing within the company (Leonidou 2004). Accordingly, the importance of researching barriers, which are related to especially SME internationalization is imperative, in order provide tools for SMEs to recognize the potential obstacles in their internationalization. These tools can be utilized not only by SMEs but also by policymakers and external service providers that seek to help SMEs in their international growth. While currently many countries offer various types of support to internationalizing SMEs, the amount of SMEs entering international markets still remains low, posing a problem for policymakers. This thesis can also provide answers regarding the problem areas, which SMEs and external parties should address in order to advance SME internationalization.

This research focuses on the internal barriers of SMEs’ internationalization processes. Firm internal barriers are a collection of barriers that arise from companies’ internal capabilities and resources as well as companies’ approach to internationalization, rather than from the external environment (Leonidou 2004). SMEs were chosen as the focus of the research because the SME-segment has proven to be a vital entity in many nations’ economies. For example in Finland SMEs comprise 99,8% of all businesses, create more jobs in a year than large companies and produce 53% of the nation’s GDP (Statistics Finland 2013). SMEs are also one of the biggest potential sources of economic growth and are thus constantly increasing their importance in national economies (Lamb & Liesch 2002). It is not as appropriate to review large companies in the context of internationalization barriers because they often have more abundant resources, which they can use to obtain foreign assets and leverage their influence, therefore they do not meet as much barriers to internationalization as SMEs (Liesch & Knight 1999). In addition, many
larger businesses possess previous experience in international business, which decreases facing problems such as lack of information about international markets, financial, legal and tax related barriers (Kneller & Pisu 2011).

In the context of internationalization, literature often refers to the importance of understanding barriers and their effect on internationalization activities (Leonidou 1995, Arteaga-Ortiz & Fernández-Ortiz 2010). Even though among researchers there is wide consensus about the increasingly important role of SMEs in the international markets, the same consensus is lacking in terms of what defines successful SMEs market entry (Requena-Silvente 2005). Still, internationalization barriers are widely acknowledged to affect the SMEs’ path to international markets significantly (Kahiya 2013). More specifically, the discourse of this research focuses on firm internal barriers to internationalization and their significance on the success of SMEs’ market entry into international markets. This thesis applies the division of export barriers, created and revised by Leonidou (1995, 1998, 2004), into external and internal barriers as a tool to identify relevant firm internal barriers from the empirical research related to the subject.

Literature on SME internationalization is heavily focused on export activity, as it is the primary first step of SMEs when expanding their business abroad (Johanson & Vahlne 1977, Katsikeas & Morgan 1994, Leonidou 1995, Rodriguez 2007). This also means that a dominant portion of the barriers found from previous research is related to SME internationalization by exporting. However, while most of the previous subject data is focused on the export barriers of SMEs, they can still be applied to many other forms of internationalization. This is due to the fact the internal barriers that need to be considered in export ventures ultimately have to be considered in other, more commitment requiring, entry modes as well.

1.2 Motivation for and purpose of the research

This thesis aims to provide a more concentrated view on SMEs’ internal barriers to internationalization than previous subject literature. The research is motivated by the fact that smaller firms perceive internal barriers as larger problems than big firms (Acs et al. 1997, Katsikeas & Morgan 1994) and that because of their resource
limitations, the impact of barriers can be more severe on SMEs (Fliess & Busquets 2006). Research on internationalization barriers is important in determining why companies fail or succeed in the international markets and can diminish the negative effects of barriers. The emphasis on internal barriers is appropriate in order to get a comprehensive view on barriers that can be proactively prevented by a company’s own actions. External barriers, however, are often a given set of obstacles provided by the exogenous environment such as political and economical factors, which cannot be affected by SMEs themselves. When SMEs become aware of internal barriers they are bound to face, they can prepare for and even avoid their adverse impact on internationalization and growth. (Leonidou 1995.)

The intent of this thesis is to help contribute to what Wright et al. refer to as “a positive platform for internationalization” (Wright et al. 2007: 1023), which can be achieved by successfully combining resources and sufficient knowledge. External barriers to internationalization have been excluded from this study because of their tendency to vary more intensely when the point of view is changed from country, or region, to another.

A gap can be found in previous research regarding the focus on specifically the internal barriers to the internationalization of SMEs, which this thesis addresses. Internal barriers to internationalization are often mentioned as a side-note in a more vast research entity, or quite conversely other studies are focused on a single internal barrier. This thesis aims to be the middle ground between the two research perspectives on SME internationalization barriers. Most importantly, the objective of this thesis is to help SMEs identify internal challenges in the company’s internationalization process and give a more comprehensive review on what internal barriers a company might have to overcome when expanding business across national borders. It is important to identify these barriers, because they help understand factors affecting business failure and success, and ultimately diminish the effect of barriers to internationalization (Leonidou 1995).

This thesis attempts to answer the following research questions:

*What are the common internal barriers to the internationalization of SMEs?*
What is the significance of the recognized internal barriers to the international growth of SMEs?

1.3 Methodology

This thesis is a literature review to the previous research related to internal internationalization barriers of SMEs. A literature review was chosen as the research method mostly due to a lack of resources to conduct an empirical study on a subject that would require such a large sample to be valid. This thesis acts as an introductory research to the subject matter and as a theoretical basis for the research in my following Master’s Thesis. A literature review is an excellent means of acquiring a comprehensive picture of the previously conducted research related to the topic.

The research is solely based on articles found from the ProQuest Business databases and EBSCO Business Source Complete. Articles have been searched mainly with the following topical words: “internationalization”, “barriers”, “SME”, “Small and medium-sized enterprises”, and “internal barriers”.

The amount of subject literature found regarding the research topic was satisfactory. Various studies on internationalization barriers and SME international growth were found and were suitable as the source material for this research. Especially the extensive empirical studies conducted mostly in the form of questionnaires provided valuable insight on SME internationalization and the barriers that SMEs perceive as the most hindering to their international growth. The large quantity of material did, however, provide a challenge in terms of limiting the amount of references to an appropriate level.

1.4 Framework and structure of the thesis

As a framework, this thesis applies the resource-based view by Barney (1991) together with Leonidou’s characterization of firm internal barriers, which are “associated with organizational resources and capabilities and company approach” to internationalization (Leonidou 2004: 281). The resource-based view states that the competitive advantage of a company is comprised of its internal resources, with
which it can form and execute its strategy (Barney 1991). Here, resource-based view is applied to view insufficient tangible and intangible resources of the SME as the causes of internal barriers to the execution of internationalization strategies. However, it must be noted that not all internal resources of an SME necessarily contribute to its internationalization, and accordingly internal barriers are regarded as insufficiencies in those specific internal resources, which are crucial to SME internationalization. This research has its emphasis on viewing the barriers that can be identified in the preface and beginning stages of the internationalization process: including stages of awareness, interest, intention and adoption of internationalization strategies (Cavusgil 1980, Lim et al. 1991, Wickramasekera & Oczkowski 2006). This way the research focuses on barriers that are integral to successful internationalization.

In chapter two the characteristics of SMEs and their significance to national economies will be deliberated. Furthermore, internationalization, growth and SMEs’ passiveness towards international opportunities will be discussed in relation to SME survival. The purpose of chapter two is to create a knowledge-basis about SMEs and internationalization for the reader in order to provide an outline for the topic of internal barriers to internationalization, which will be brought under discussion in chapter three. In the third chapter, internationalization barriers as an aggregate will be shortly viewed before concentrating into internal barriers more thoroughly. The main groups of internal barriers will be individually discussed before their importance and significance to SMEs is evaluated. Lastly, in the conclusions, the results of the literature review will be presented as well as limitations and implications for future research.
2 SMES AND INTERNATIONALIZATION

In this chapter the concepts of small and medium-sized enterprises and internationalization are defined, explained and discussed in order to create a conceptual understanding of the matters important to this research. The relationship between SMEs and internationalization is discussed as well as the important implications that internationalization has to firm survival.

2.1 Definition of SMEs

The definition of small and medium-sized enterprises varies to some extent and there is no commonly accepted definition among the WTO member countries (Lucian et al. 2014). In their research Freeman et al. (2006) define SMEs as companies with less than 100 employees working for them, while the most common definition for American SMEs states SMEs to be firms employing less than 500 people (US International Trade Commission 2010). Between these two, lies the definition of SMEs by the European Union, which defines SMEs to employ anywhere from one to a maximum of 249 people and to fulfill one of the following conditions: the company has a turnover of less than two million euros, or a balance sheet under two million euros (Lucian et al. 2014). This research reviews studies made in multiple countries around the world, so ultimately SMEs in this thesis are defined by the American definition, as it is the most comprehensive of the widely used definitions.

SMEs are a major source of economic success, growth and job creation in national economies and all in all comprise 99% (21.6 million) of non-financial businesses in the European Union and employ two thirds (88.8 million) of all the employees in the EU (Fliess & Busquets 2006, Muller et al. 2014). SMEs account for more than 80% of all exporting firms in the European Union with a number of over 600 000 exporting businesses employing over six million people in the EU (Lucian et al. 2014), which however, can be regarded as quite a small percentage in relation to the overall number of SMEs operating in the EU. Exporting tends to be the first choice of SMEs to internationalize as it requires relatively low amounts of capital and includes relatively low risk compared to other modes (European Commission 2010, Narayanan 2015). Therefore the export ratio of European SMEs can be used as an
approximation of the ratio of European SMEs internationalizing through outward activities.

2.2 Internationalization and growth

Internationalization can be defined as initiating, developing and sustaining operations in overseas markets (Fliess & Buquets 2006). It can be divided into inward and outward activities. Franchisees, licensees and importers are focused on the inward activities of internationalization. The outward activities of internationalization are the main activities of exporters, licensees, franchising companies and companies taking part in foreign direct investment activities. (Rodriguez 2007, Wright et al. 2007.)

This research focuses on outward internationalization, with the reviewed studies often restricted to export. This is due to outward activities providing a more abundant source of international growth opportunities for SMEs compared to inward activities, which have the restricted demand of a single market. The outward expansion to foreign markets can allow smaller firms to escape the difficulties of competing with larger firms in the domestic markets and allow SMEs to reach completely new markets and demographics. (Lee et al. 2012.)

There are two main theories to SME internationalization: the traditional, gradual internationalization and the born global approach. Gradual internationalization was first characterized by Johansson and Wiedersheim-Paul (1975), further developed into the Uppsala model by Johansson and Vahlne (1977) and added onto by other researchers like Cavusgil (1980) with the innovation model. The basic notion of these models is that SMEs should have a strong position in the home market before internationalization, and when internationalizing, SMEs should incrementally move to foreign markets starting with the physically and culturally closest countries. This way internationalization knowledge and commitment develop incrementally in the process (Andersen 1993).

Traditional models have been claimed outdated by born global theories e.g. the theory of International New Ventures (INVs), which have gained popularity in the past decades. Born global theories claim that SMEs need no share of the home market before internationalizing, but instead can internationalize from inception.
Much of the recent progress in international trading conditions, which has torn down many trade barriers, has resulted in a growing number of born global firms that are able to internationalize from birth. (Oviatt & McDougall 1994, 1995, 1997, Chetty & Campbell-Hunt 2004, Bell & Loane 2010.)

It holds true for all firms that at some point for the firm to be able to achieve further growth, internationalization of operations is required (Calof 1994). This is the case when the domestic market achieves saturation and foreign markets are the only available direction for the company to grow. However, there are statistical implications to the benefits of internationalization even before home market saturation. Research suggests that SMEs’ participation in internationalization activities increases their business performance. Accordingly, internationalization has been found to correlate positively with higher turnover growth, revenue growth, employment rate, process innovations and introduction of new products (European Commission 2010, US International Trade Commission 2010). In other words, earlier internationalization enables potential for faster growth of SMEs. Internationalization activities thus increase the chances of SMEs’ survival and simultaneously produce economic growth for countries with international SMEs (Lee et al. 2012).

While the correlation of internationalization and positive growth seems evident, not all SMEs decide to expand their business internationally. In fact, the participation of SMEs into the international trade activities is disproportionally small compared to the overall provision of economic growth and job creation provided by the SMEs in national economies (Fliess & Busquets 2006). Research by the European Commission (2010) concluded that merely 4% of European SMEs have actual plans to internationalize. The reluctance, insufficient resources and inability of SMEs to internationalize are persistent problems, which impose a challenge for policymakers (Wright et al. 2007). The disinterest in internationalization can stem from a multitude of reasons. One explanation for the reluctance of SMEs to grow is the data gathered by Almus and Nerlinger (1999) to support a hypothesis, that firms are started in a size and scale that is below the optimal size for the market and once the minimum level of optimal size is reached, firms have little incentive to pursue further growth. Another explanation would be the fact that internationalization can create more
complexity into SMEs’ organizational structure and processes demanding them to have capabilities and human resources to manage internationalization effectively (Lee et al. 2012). Increasing resource demands can pose a problem for SMEs, which have a disadvantage compared to larger firms in terms of resource availability (Calof 1994). SMEs may also serve a local niche market, which cannot be realized in international markets and thus discourages internationalization (Acs et al. 1997).

Aghion et al. (1998) recognize the possibility of situations where internal growth incentives are scarce. However, they provide evidence, which shows that for most SMEs there is an external incentive for steady, continuous growth. This evidence is derived from the Schumpeterian theory of creative destruction by indicating a need for growth and innovation in order for businesses to stay relevant while competition tries to make them obsolete. Consequently, firms that cannot achieve a certain level or quality of innovation can be discouraged to internationalize (Acs et al. 1997). The constant introduction of new technologies makes product life cycles constantly shorter, which should encourage growth in order for firms to tap to as large a market they can globally before a product is made futile by new innovation. This is the case especially for many SMEs that rely on a small spectrum of products or services and cannot rely on product portfolio diversity for protection against competition. (Kazanjian 1988.)

SMEs, which are often hindered by their limited resources, should learn to see past the sunk costs of international ventures, whether successful or unsuccessful, and realize the value of the knowledge and experience provided by the process. Failed attempts at internationalization should not discourage future attempts but in fact create confidence because of the accumulated knowledge from previous attempts. (Wright et al. 2007.) Encouraging internationalization is imperative because the move towards global markets and the resulting increase in competition sets a pressure for SMEs to grow internationally in order to stay competitive (Flies & Busquets 2006).
3 INTERNAL BARRIERS TO INTERNATIONALIZATION

In this chapter the core subject of the thesis will be brought under thorough discussion. The chapter will include analysis on the internal barriers to SME internationalization found in research literature and deliberation about the significance of internal barriers to SMEs.

3.1 Overview on barriers to internationalization

In their attempt to enter international markets, SMEs regularly encounter significant barriers to trade, which can stem from the firm itself or the surrounding external environment (Fliess & Busquets 2006). Barriers to internationalization are “all those constraints that hinder the firm’s ability to initiate, develop or sustain business operations in overseas markets” (Leonidou 2004: 281). These barriers, such as the considerable cost of resources, affect SMEs disproportionately in comparison to large companies (Requena-Silvente 2005, Fliess & Busquets 2006, US International Trade Commission 2010).

The significance of barriers to internationalization is evident in the amount of time and resources that SMEs often need to sacrifice in order to surmount the barriers and realize international growth benefits such as stability and diversification (Freeman et al. 2006). Nevertheless the process of overcoming internationalization barriers is often an inevitable part of an SME’s path to growth and internationalization in order to survive (Kazanjian 1988, Lee et al. 2012, Kahiya 2013). Therefore the study of internationalization barriers has important implications for smaller businesses in order for them to be able to proactively prevent the effects of barriers or diminish their impact to the firm (Leonidou 2004).

Often the small size of SMEs is first and foremost considered as a barrier when discussing internationalization, and accordingly firm size has been largely focused on in previous research (Calof 1994, Shaw & Darroch 2004). However, while SMEs may perceive their size as a barrier for internationalization, recent research has indicated that, especially in the modern globalized markets, this is not the case. Despite the fact that SMEs are small, it does not necessarily influence success in the
international markets negatively (Calof 1994). It may be that SMEs use size more as an excuse than an actual reason not to expand and explore international business opportunities (Shaw & Darroch 2004). While it is true that smaller size implies the predisposition to face barriers related to internal resources, in fact a flat organizational structure can be a beneficial quality when internationalizing, especially in terms of agility and communication (Wright et al. 2007, Toulova et al. 2015).

3.2 Firm internal barriers to internationalization

Internal barriers to internationalization are barriers arising from within the firm itself and affecting the firm’s aspirations toward internationalization negatively (Leonidou 1995). SMEs have been found to rate internal barriers as a bigger obstacle to internationalization than external barriers. Often it is the case that a proportionally larger part of the barriers that affect the internationalization of an SME, are found in the firm itself and are in fact controllable as opposed to barriers that arise from the external environment. (Katsikeas & Morgan 1994, Leonidou 1995, Fliess & Busquets 2006, Kahiya 2013, Toulova et al. 2015.) The path to SME internationalization is to some extent dictated by the impact of internals barriers, and the fact that firms can affect the degree to which internal barriers impact them, makes the closer attention to internal barriers all the more necessary when discussing SME internationalization (Kahiya 2013).

The main reason why SMEs’ disposition towards internationalization differs from that of larger firms’ is the lack of internal resources to invest in international expansion opportunities (Requena-Silvente 2005). According to the resource-based view, organizations have heterogeneous resources that contribute to their competitive advantage at home and in the international market (Barney 1991). Consequently, it can be stated that the theory also has reversed implications, which suggests that inadequate internal resources diminish competitive capabilities and thus impose barriers to the organization’s growth and internationalization.

Fliess and Busquets (2006) analyze the results of a survey by The National Federation of Independent Business (NFIB) and conclude that SMEs with less
international experience emphasized the importance of internal barriers whereas more experienced SMEs were more worried about barriers set by the external business environment. The results of the research are in line with the aforementioned notion that knowledge about internal barriers is of the greatest use to SMEs who have recently began their international ventures, or have not yet internationalized, but intend to do so.

While the lack of especially financial resources, is often listed at the top of SME internationalization barriers, not all barriers are as obvious and based on tangible resources. When SMEs are faced with uncertainty, they will come to interact with other internal internationalization barriers such as attitudes, lack of information and marketing-related barriers (Wright et al. 2007). Besides sufficient financial and human resources, a successful internationalization requires skill and knowledge about international markets, and commitment by the firm to enter and sustain presence in the foreign markets (Calof 1994).

The results discovered by Shaw and Darroch (2004), when researching the internationalization of New Zealand–based firms, indicated that relatively few SMEs actually make their first international transaction as a result of deliberate planning or strategy. Instead SMEs end up internationalizing in a reactive manner, through unsolicited orders by foreign customers even though SMEs with a proactive approach have been found to perform better in the international markets. Proactive SMEs are likely to meet fewer barriers, especially relating to intangible resources, than firms with a reactive approach to internationalization (Campbell 1996, Francis & Collins-Dodd 2000). Accordingly, the following review of firm internal barriers attempts to help explain what factors SMEs would need to take into consideration in order to be more proactive towards internationalization.

The internal barriers to internationalization found in this research are categorized into informational barriers, managerial barriers, human resource barriers, financial barriers and marketing related barriers as demonstrated below in Table 1. Each of the categories is discussed next in dedicated subchapters.
Table 1. Internal barriers to internationalization

3.2.1 Informational barriers

Assets of knowledge and experience improve the economic outlook of SMEs’ internationalization operations, competitiveness and overall chances of survival in the markets (Mudambi & Zahra 2007, Saarenketo et al. 2008). Consequently the lack of information and experience has at times been stated as the main barrier to SME
internationalization (Toulova et al. 2015), and in fact Liesch and Knight (1999) propose that a company’s readiness for expansion to international markets can be measured by the amount of information that the company has about the overall internationalization process and about foreign markets.

Without a sufficient amount of current and relevant information about the foreign markets, the response to internationalization barriers can be insufficient and increase uncertainty in the firm’s operations (Katsikeas & Morgan 1994). SMEs often lack information about international business opportunities, have insufficient ability to analyze international competition and can poorly access relevant information about foreign markets (Leonidou 2004). The acquisition of knowledge and experience can be done most effectively through research, acquisition of human resources or through networks, which can provide insight to internationalization externally (Leonidou 2004, Freeman et al. 2006). The acquisition of knowledge is also often less costly when the target market is physically and culturally close, which would make similar markets the preliminary target for the first international activities when knowledge and experience are limited (Johanson & Vahlne 2009, Liesch & Knight 1999).

Andersen (1993) notes that internationalization requires the existence of two types of knowledge in a firm: market-specific knowledge and general knowledge on internationalization. The former includes the knowledge, which the firm acquires by operating in a certain market, whereas the latter is related to operations that are characteristic of the internationalization as a process in general (Andersen 1993, Kahiya 2013). General information about processes included in internationalization plays a bigger role in the success of SMEs’ international ventures than market-specific knowledge and it can include aspects such as knowledge about funding, networks, government policies and international trade law. Notably, general internationalization knowledge reduces the risk factor of SMEs’ international ventures more than market-specific knowledge and thus suggests a concentrated effort into learning about general processes related to internationalization. (Johanson & Wiedersheim-Paul 1975, Casillas et al. 2015.)

Especially the role of experiential learning and transparent communication is essential to the long-term success of SMEs’ international ventures. Even though existing foreign market knowledge affects the speed in which SMEs are able to start
internationalization, it appears not to have any effect to the prosperity of international ventures in the long-term. However, the lack of experiential learning and adjuvant communication seems to negatively affect SMEs’ ability to maintain intensity in its ventures. (Casillas et al. 2015, Karlsen et al. 2003.) Thus experiential learning is an essential part of the dynamic capabilities that help SMEs adapt to the needs of international markets (Campbell 1996, Eisenhardt & Martin 2000, Chetty & Campbell-Hunt 2004).

The implications of experience and information acquisition to managerial decision-making are evident: the experiential knowledge that managers accumulate during the internationalization process affects the way they make further decisions. Furthermore the expenditure and commitment to foreign market activity is dependent on how managers perceive the risks involved, and on the information about alternative options that are available to the firm (Johanson & Wiedersheim-Paul 1975, Mudambi & Zahra 2007, Casillas et al. 2015).

3.2.2 Managerial barriers

Managerial barriers to internationalization and growth have been recognized to deal with lack of commitment, lack of experience and skills, negative attitudes, and personality traits such as risk-aversion (Leonidou et al. 1998, Lamb & Liesch 2002, Shaw & Darroch 2004). The importance of managerial barriers to internationalization is highlighted by the fact that in smaller companies the contribution toward internationalization decisions is mainly in the hands of a few individuals, whereas larger companies usually have more parties involved in the decision-making process (Andersen 1993, Leonidou 2004). The role of a single manager can thus be pivotal in the decision of how an SME positions itself towards internationalization in terms of attitudes, entry modes and time to internationalization (Rodriguez 2007).

Managers’ previous international experience can provide a competitive advantage but it is not compulsory for a successful internationalization. However, what appears to be more definitive is the orientation of SMEs’ management towards internationalization (Freeman et al. 2006). Freeman et al. (2006) mention managerial
risk-aversion as one of the three main barriers to SME internationalization. The management of an SME is inclined to see the internationalization process as intimidating and with too much financial risk. Some managers may decide against internationalization because of the fear of management losing control over the company’s operations due to increasing complexity (Acs et al. 1997), while other managers fear the risks that are brought by cultural differences in foreign markets (Freeman et al. 2006). Firms with managerial incompetence and risk-aversion may perceive internationalization barriers to be more substantial than they actually are, which may result in a disinterest towards internationalization (Bilkey & Tesar 1977).

Rather than avoiding risk and remaining static, it is imperative that companies seek to manage risk and to move quickly in the dynamic market to achieve growth (Freeman et al. 2006). However, the shortage of information and resources can make managers abandon internationalization projects after experiencing initial failure and become discouraged about internationalization (Lim et al. 1991). Consequently an important managerial implication stemming from the subject research is that managers need to be more committed to a market, prepared to face uncertainty, accept initial failure and seek solutions to emerging problems (Chetty & Campbell-Hunt 2004). Although internationalizing may increase uncertainty in the beginning, it can be considered as a risk reducing procedure in the long term as it enables access to a larger market and divides economic risk across several markets (Czinkota & Ronkainen 2003).

The initial uncertainty caused by lack of internal resources often leads to negative attitudes towards internationalization in the SME’s management team. These negative attitudes and aversion towards risk can be considered as major deficits in the managerial resources, which build towards the positive platform for internationalization. Calof (1994) discovered an important correlation between the size of a firm and its attitudes toward internationalization: company size didn’t necessarily matter in the success of international ventures, but it affected how the firm approached internationalization. Larger firms were more open to internationalization and, accordingly, had diversified their operations to various different countries, whereas smaller companies had far less internationalized attitudes, were more uncertain and thus had operations in far fewer countries. (Calof
SME managers may also perceive that processes and policies regarding internationalization are biased towards larger companies and thus adopt an adverse attitude to internationalization (Fliess & Busquets 2006).

Factors of uncertainty, such as difficulty in enforcing contracts with foreign co-operators, asymmetrical information, physical and cultural distance, and ambiguous qualifications and capabilities of the foreign co-operator are perceived as intimidating risks by the management of SMEs. Uncertainty still maintains itself as a prominent cause for managerial barriers in the SMEs’ expansion to international markets, and this holds true with an even greater effect to firms, which have no international networks. The most effective way SMEs can avoid risk-aversion, is by acquiring experience and knowledge either through, market research, networks or by acquisition of human capital. (Leonidou 2004, Freeman et al. 2006.)

### 3.2.3 Human resource barriers

SMEs often underestimate the amount of human resources internationalization demands, in fact, the share of personnel engaged in exporting is often much lower than the proportional contribution of export sales to the total sales of the company (Leonidou 2004). Human resources can also pose a barrier to internationalization due to a lack of personnel with sufficient expertise with international business (da Rocha et al. 2008). Even the lack of communicational skills, such as insufficient language proficiency and a lack of cultural sensitivity, can act as a barrier to SME internationalization (Toulova et al. 2015).

The European Commission (2010) found in their survey that SMEs already participating in internationalization activities list the lack of qualified personnel amongst the most important barriers to successful internationalization. One reason for this may be that highly qualified job seekers view contracts with SMEs more risky than those with larger companies and are therefore more inclined to seek employment in larger companies (Acs et al. 1997). SMEs may find it hard to acquire human capital from the labor markets also as a result of restricted financial resources to allocate into recruitment and salaries. Due to a lack of human capital and financial resources, many researchers emphasize the importance of networks as a source of

Human resources comprise the SME’s ability to navigate in the international market: the accumulated sum of employees’ personal competences and experiences form the firm’s expertise. Accordingly, the effect of human resources to internationalization is a vital factor for SMEs to consider even in the initial recruiting phase, even if their intention is not to internationalize yet. (Xie & Suh 2014.) This is an important proactive step that managers/owners can act on to make the firm more capable of internationalization from the inception. SME managers often consider barriers when they intend to start internationalization, however, to prevent the realization of barriers it is wise to diminish them from the moment that internationalization becomes a possible future option for the SME (Yang et al. 1992).

Human resource deficiencies have important managerial implications as well. Often the manager, who makes the final decisions in matters concerning internationalization, has no time to follow through and manage the operations (Leonidou 2004). As a result, managers often need to rely on other members of the organization to oversee parts of international operations. Because of limited human resources, communication throughout the organization plays an important role in SMEs’ success. It is important that information about internationalization is effectively communicated in the entire organization e.g. through personnel training in order to align employees’ actions with the company’s internationalization strategy. By doing so, companies can increase the amount of employees who are capable of overseeing of internationalization processes. (Liesch & Knight 1999, Lamb & Liesch 2002, Nonaka 2007.)

3.2.4 Financial barriers

One of the main barriers to SME internationalization is the fact that many SMEs have the inability to self-finance their expansion to foreign markets (Katsikeas & Morgan 1994). Financing is needed in the internationalization process of SMEs to acquire relevant resources and to finance the expansion of business operations (Smolarski & Kut 2011). As with most barriers to internationalization the issue of
inadequate financial resources is perceived more hindering by small firms than by larger firms (Shaw & Darroch 2004).

Because of limited internal resources and a higher income volatility compared to larger companies, SMEs have a restricted access to additional external capital and is thus limited in its ability to utilize debt money in their internationalization. Due to their resource limitations, SMEs may not be able to leverage debt money, which can result in negative effects on internationalization and growth. While debt money used alone may yield negative results, it can be combined with equity financing to achieve better results. Overall, equity financing through shares seems to have positive effects on SME growth when the consequential external monitoring doesn’t limit SMEs’ agility. (Smolarski & Kut 2011.)

SMEs, especially those relying on a single innovative product, can feel a high pressure to internationalize during their early years but often lack the resources to finance the expansion (Freeman et al. 2006). Many SMEs, especially start-ups, often need to rely on venture capital for the developmental phase of their internationalization operations. This often causes controversy in the company’s management because accepting venture capital usually means partial loss of control over the company. (Spence 2003.) Venture capital may also be difficult to obtain if VCs see the investment to hold too much risk. If the capital is acquired for the project, it adds to the pressure for the SME to realize fast and significant growth. (Smolarski & Kut 2011.) On the other hand, venture capitalists can also act as an ample source of information and experience relating to internationalization and thus tackle some of the knowledge related barriers when starting internationalization. Other ways of avoiding the distress of insufficient financial resources are e.g. engaging in joint ventures or strategic alliances, which again usually imply a partial loss of control over some aspects of the venture (Freeman et al. 2006).

In their research Shaw and Darroch (2004) concluded that the lack of financial resources is one of the most prominent barriers for SME internationalization preventing many SMEs from internationalizing. In fact, they found that only 11.8% of the SMEs they surveyed had access to external capital sources. This shows an important implication for policymakers about the importance of connecting investors to SMEs with lacking sufficient funds (Acs et al. 1997).
In the recent years some alternative ways of funding have surfaced to provide small companies access to capital, such as crowdfunding. Crowdfunding has steadily gained popularity especially in the startup world, and social media platforms such as Kickstarter and Gofundme have enabled companies to collect funds by offering a large pool of investors (and consumers) first rights to the company’s product or service, and often in a discounted price, in return for an investment. Besides financing their business, crowdfunding is a way for companies to get insights on the demand that the international markets have for their product/service, which increases their market knowledge. However, crowdfunding is often only viable to companies with a novel product or service to offer. (Belleflamme et al. 2011.)

SMEs have multiple sources for financing their operations, but often a limited access to those sources. Furthermore, if the access to finance is gained, the subsequent issue is the difficulty in combining debt and equity financing in a way, which enables leveraging debt while remaining independent and agile.

3.2.5 Marketing related barriers

Marketing efforts by SMEs is a major factor contributing to how well firms are able to penetrate foreign markets (Kahiya 2013). Marketing related barriers have to do with finding markets, adapting products, adapting marketing processes and distribution to international markets (Katsikeas & Morgan 1994, Liesch & Knight 1999, Leonidou 2004). Distribution can be elaborated to mean both finding suitable agents and distributors and also gaining adequate quantity of representation in the market (Leonidou 2004).

Before internationalization a company must make sure that its product is marketable in the target country. Companies have the option to differentiate and localize their product’s features according to each market, or aspire to efficiency and modify their product as little as possible, in a way that it meets legal and cultural standards in most foreign markets. The product adaptation includes pricing, design, packaging and labeling. Companies also sometimes need to take product usage differences into consideration when marketing their product abroad. (Leonidou 2004, Kahiya 2013.)

While seeking to expand to international markets, SMEs can see the price of their
own product as a major barrier to internationalization (European Commission 2010). Existing heavy competition in a target market may have driven prices low, which then makes it harder for SMEs to expand to those markets as a viable competitor (Leonidou 1995). SMEs should analyze the competitive advantage that competitors have in the market and decide accordingly whether market entry is sensible.

In the pre-face of internationalization, the main marketing barriers are related to the identification of markets and foreign partners, and adapting internal marketing processes to comply with international market requirements. Further along the process, after initial internationalization, a barrier can arise from the commitment intensity of the SME to the foreign market. If the commitment of the SME, both resource-wise and psychologically, to the market and its customers is lacking, it is difficult to gain a sufficient market representation to sustain business activity in the foreign market. (Lamb & Liesch 2002.)

Another barrier for SMEs is set by the difficulty in establishing market presence. Promotion in foreign markets is often listed by SMEs as a prominent barrier for SME internationalization (Toulova et al. 2015). As an internal barrier, the issue of promotion is related to finding compatible partners and with how the product can and should be represented in the international markets. Regarding SMEs’ representation in the international markets, Shaw and Darroch (2004) found a prominent barrier of unrecognizability and concluded it to be in the top six of the total 46 internationalization barriers that their survey results listed all together.

Freeman et al. (2006) discovered that most commonly managers have a lack of knowledge relating to marketing activities such as requirements on quality, quantity and supply frequency, processing and monitoring of the product, and the dynamic needs of the international key customers. Successful marketing in foreign markets often requires an internal adaptation of marketing procedures to work swiftly and seamlessly with distribution to avoid delays and costs resulting from them (Katsikeas & Morgan 1994).

In a similar way to many other internal barriers, internal marketing problems can sometimes be prevented or alleviated by the existence of networks. From a marketing perspective, networks are useful in avoiding problems related to organizational
adaptation, distribution, unrecognizability, insufficient marketing knowledge, financial issues and quality problems. Networks can e.g. act as sources of foreign market consulting, and providers of references to an SME by representing its products in the foreign markets. (Ghauri et al. 2003.)

3.3 Significance of internal barriers

SMEs consider internal barriers to be the most substantial barriers to internationalization. While external tariff and non-tariff barriers are largely out of the control of SMEs, internal barriers to internationalization are factors that SMEs are able to affect significantly and even prevent their occurrence. Even though barriers exist for large and small companies alike, the vulnerability of SMEs due to their size exposes them to feel the adverse impact of barriers more severely. (Fließ & Busquets 2006.)

A longitudinal study of 20 years by da Rocha et al. (2008) concludes that the lack of firm internal resources has throughout the years maintained its position as one of the top barriers to internationalization. The study of internal barriers offers implications for SME management in terms of preparation and proactivity measures, and equally importantly for external service providers and policymakers for identifying the core barriers with which SMEs require help (Leonidou 2004). The internal barriers to internationalization also act as barriers to firm growth and consequently, external support relating to internal barriers has also been found to positively affect the growth outlook of SMEs (Almus & Nerlinger 1999).

Internal barriers slow down the internationalization of SMEs and can thus provide further drawbacks for SMEs in terms of competitiveness. Modern, technologically advanced, markets bode better performance for firms that internationalize rapidly, which in turn imposes a challenge for the preparation to international operations (Crick & Spence 2005). There is a need for balancing between preparation activities and rapid internationalization: SMEs need to try to achieve speed and simultaneously determine an adequate level of preparedness that will help to avoid realization of internal barriers.

The highly developed information and communication technologies available to
companies have been found to diminish some barriers to internationalization to an extent. Development of ICT has lead to, for example, the constantly increasing amount of appropriable knowledge available to firms and easy access to that information. In spite of that, SMEs still maintain the difficulty in discovering what information is relevant. The development of ICT has also been found to reduce risk of internationalization, however, advanced ICT does not provide competitive advantages in aspects of market share or product pricing. There is some correlation found in knowledge intensive and technologically advanced companies having a higher intensity in ICT usage, which may provide them a competitive advantage in terms of time to internationalization. This is usually the case with knowledge intensive start-ups. (Aspelund & Moen 2004, Bell & Loane 2010.)

Many knowledge intensive SMEs have the ability to surpass the establishment of costly infrastructure and realize a diminished need for external capital by internationalizing via the Internet (Bell & Loane 2010). However, while knowledge intensive companies may experience lower financial barriers to internationalization, they can experience an increased impact of marketing related barriers such as unrecognizability and difficulty in gaining market share due to high creative destruction, which is characteristic to the knowledge intensive business sector (Bell & Loane 2010, Kuivalainen et al. 2012). Furthermore, knowledge intensive SMEs with a high degree of tacit knowledge and a rapid internationalization strategy, may find it difficult to standardize their complex product appropriately for international markets (Saarenketo et al. 2008). This goes to say that the increasing proportion of knowledge intensive SMEs does not inherently avoid the significance of internal barriers, but experience them in a different composition than traditional SMEs.

A research conducted by the European Commission (2010) shows that the significance of the internal barriers to SME internationalization is increased by the fact that a large portion of SMEs are unaware of the sources of non-financial and financial assistance that is available to them. Only 10-27% of SMEs, depending on firm size, are aware of the existence of public support programs suitable for them, bigger firms being more informed than smaller ones. The portion of SMEs actually taking advantage of the available support is even lower: the average portion depending on firm size being 6-16%. Smallest firms have found the non-financial
support more important whereas bigger SMEs have used financial support more frequently.

Regarding firm size it can be noted that small size in itself is not a barrier to internationalization (Calof 1994, Katsikeas & Morgan 1994). However, a smaller size implies that internal barriers can have a more significant effect to the firm, which in turn makes SMEs more vulnerable to their risks than larger companies (Requena-Silvente 2005, Fliess & Busquets 2006).
4 SUMMARY AND CONCLUSIONS

The intention of this thesis was to recognize firm internal barriers that significantly affect the international growth of SMEs. This was achieved by reviewing previous literature in order to compile a comprehensive overview of the significant internal barriers to the international growth of SMEs. The found internal barriers have been repeatedly recognized in various studies and have persisted in the empirical research through time.

4.1 Theoretical contribution

This thesis has applied the resource-based view (Barney 1991) with Leonidou’s (2004) definition of internal barriers as a framework to identify the most prominent internal barriers to SME internationalization from existing literature. Furthermore, this research has concluded that the internal barriers to internationalization have a significant effect on the internationalization of SMEs, affecting smaller firms more severely than larger companies especially by hindering growth.

The internal barriers found in this research are related to internal resource deficiencies and attributes of the SME. Barriers related to insufficient information, managerial attributes, human resources, financing and marketing were found to be the most prominent barriers as they were included, in some form, in most of the previous studies. These categories were compiled into Table 1 to provide a general overview of the most significant internal barriers that affect SMEs’ international growth. In the various research articles used as source material, internal barriers were often quite differently categorized and analyzed, but by the means of Leonidou’s (1995, 1998, 2004) definition of internal barriers, common denominators between various barriers were found and these barriers were then comprised into the five categories.

As mentioned before, the resource-based view suggests that firms’ resources are the building blocks of competitive advantage. This means a certain level of internal resources is needed by an SME to make internationalization a viable option. However, it is impossible to define the resources needed for successful
internationalization. This is due to the “casual ambiguity” of firm resources: every company has a combination of internal resources that is one-of-a-kind and the way companies can utilize these resources to carry out strategies is unique. (Barney 1991.) The internal resources for internationalization can differ considerably between different types of SMEs and consequently also the experienced internal barriers are different, e.g. knowledge intensive ICT companies can face more marketing related barriers while traditional manufacturing SMEs can experience financial barriers to be more prominent (Saarenketo et al. 2008, Bell & Loane 2010, Kuivalainen et al. 2012). Circumstantial aspects change the composition of internal barriers faced, but does not diminish their significance to SMEs.

By being commonly mentioned in most researches as the top barrier for SME internationalization, a cautious conclusion can be made about informational barriers being the most prominent internal barrier affecting SME internationalization (Casillas et al. 2015, Liesch & Knight 1999, Mudambi & Zahra 2007, Saarenketo et al. 2008, Toulova et al. 2015). While the configuration of other barriers and their significance can change to a large degree, informational barriers remain important for all firms as appropriable knowledge creates the foundation for a successful international venture. Although developments in ICT have made access to relevant information faster and cheaper, and enriched firm internal communication, ICT does not obviate informational barriers, but rather changes the means that appropriable information can be acquired and communicated (Aspelund & Moen 2004).

The uniqueness of required resources only enables a rather general categorization of the most prominent internal barriers to SME internationalization. However, the results of this research can help SMEs by making them aware of problems that internationalizing SMEs commonly face and giving them a possibility for preparation and proactive measures. In addition to SMEs, the results can also be utilized by policymakers and external service providers contributing to the international growth of SMEs.

4.2 Managerial implications

The importance of a proactive approach to internal barriers emerges from the
reviewed subject literature. Due to the vulnerability of smaller firms, the significance of proactivity is emphasized in order to decrease the levels of uncertainty and risk within SMEs (Campbell 1996, Francis & Collins-Dodd 2000, Leonidou 2004). Proactivity in practice means that SME manager should recognize the possible obstacles they may experience while internationalizing and strive to minimize their effects. By minimizing the effects and resource restraints of internal barriers, SMEs are more equipped to address external barriers and thus increase their chances of survival in the process of international growth. The proactive efforts by SMEs against internal barriers are on one hand resource consuming, but on the other hand also important positive triggers that prepare SMEs for their path to internationalization (Kahiya 2013). Being proactive against internal internationalization barriers can mean e.g. due diligence on general procedures required for internationalization, market analysis, adapting marketing processes and compiling an internationally oriented team.

The lack of internal resources is often exaggerated by risk-averse managers. SME management can be intimidated to begin internationalization if they perceive their resources to be insufficient in order to succeed. (Bilkey & Tesar 1977, Xie & Suh 2014.) Therefore it is important for SME managers to have tolerance for risk and accept occasional failure in order to improve their international growth prospects and learn from their mistakes (Chetty & Campbell-Hunt 2004). Ultimately internationalizing is considered crucial for the long-term survival of SMEs as stagnation in the home market often yields more risk than facing the uncertainty of internationalization (Czinkota & Ronkainen 2003, Lee et al. 2012).

To circumvent the negative effects of the lacking international experience, research implies that SMEs should utilize their external networks. Networks and other external support can convey information about internationalization to inexperienced SMEs and provide a way for SMEs to avoid some adverse effects of lacking internal resources (Wright et al. 2007). Consequently the benefits of external networks in terms of mitigating various different internal barriers are mentioned throughout the subject literature (Almus & Nerlinger 1999, Spence 2003, Shaw & Darroch 2004, Freeman et al. 2006.)
4.3 Limitations and future research

The limitations of this research are related to the all-embracing nature and ambiguity of the found internal barriers. This thesis states the most prominent internal barriers in the internationalization of SMEs, but is incapable of specific answers for example regarding the exact type of information SMEs should acquire or how to find the most suitable partners internationally. The specific aspects of the found internal barriers are variables that SMEs have to recognize themselves depending on situational circumstances. This problem exists also in the previous literature. The complexity and dynamic nature of the SME sector provides a challenge in producing generally applicable guidelines for proactivity measures in internationalization, even though the main barriers can be recognized. Additionally, the constant development of new business practices provides a challenge from the perspective of existing literature on internationalization barriers. For example, the growing phenomenon of software companies internationalizing through mobile application stores and the applicability of traditional barriers to this form of international growth could provide an interesting topic for future research.

By framing the research according to the resource-based view, this research somewhat inadequately examines the effects of factors, which are difficult to define as organizational resources, but which still undoubtedly affect the internationalization processes of all firms. Such factors include organizational cultures, entrenched organizational habits and paradigms existing within firms.

The significance of external networks, which has emerged from the subject literature, might be grounds for further research in my Master’s Thesis. The research could be executed, for example, in the form of a case study on how external partners and service provides, such as consultants, governmental agencies, venture capitalist and partner companies can help internationalizing SMEs mitigate the internal barriers to international growth.
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