

# INTERNATIONAL COMPETITIVENESS AND REGIONAL EXPORT COOPERATION NETWORKS

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## Abstract

The enlargement of the European Union with new members in Eastern Europe is changing the business situation in the Baltic Sea region between old EU members in the Western rim and new member states in the Eastern Rim. A main question is then how the competitiveness of firms is influenced by this change in international business conditions. In comparison with large companies, small and medium-sized enterprises (SMEs) usually are at a disadvantage because they are traditionally home-market oriented and are therefore characterized by a low degree of internationalization. But this could be compensated for by cooperating through forming networks in order to develop common competitive advantages. By sharing resources, synergies enjoyed by large firms can be achieved.

The main issue taken up in this paper is how the international competitiveness of SMEs can be improved through export cooperation. A vital question is then whether the SMEs involved in such international marketing activities are operating alone or cooperating. To what degree does the limited resource-base of SMEs favour joint actions? And how are firm-specific competitive as well as network-specific competitive advantages influenced by such networking among SMEs?

Based on these issues, the purpose of the study is to describe and explain how SMEs try to increase their competitiveness by establishing joint networks using local resources and competences in order to exploit international markets. Furthermore, the purpose is also to contribute to the understanding of how these activities effect the internationalization of the SMEs homeregion. To specify how such linking of competitiveness at the firm level and the network level takes place with the regional level, a regional network model is developed in the form of an export cooperation platform. The article mainly presents the main result of the study, which is the theoretical framework developed for connecting firms and regions on regional export platforms. The empirical background of the framework is briefly taken up as well as the methodology used. Finally, major conclusions and implications are stated.

As shown by previous research on clusters and industrial districts, successful cooperation between SMEs in the form of regional networks is based on geographical proximity. A regional network is in this study defined as an actor with own intentions, e.g. expressed through a deliberate strategy based on network-specific competitive advantages. This definition differs from the more common one of seeing the network or cluster as not having any strategic intention of its own, rather being a spatial agglomeration of firms. Why some groups of firms are more successful than others is here explained by the fact that there are favorable economic and social factors, e.g. a benevolent environment supporting the network. The regional network defined above is viewed from the perspective of the individual membership firm. The focus is on firm-specific competitive advantages and how these can be improved through being part of a regional grouping, benefiting from the network-specific competitive advantages. This means that the study focuses on initiatives endogenous to the network, treating public network initiatives as an exogenous factor.

**Keywords:** regional networks, export cooperation, internationalization processes

## **INTRODUCTION**

The enlargement of the European Union with eight new members in Eastern Europe is a major shift in the European business world, which creates business opportunities and threats for the firms there. European businesses across the continent now share a common set of rules and benefit from increased trade, greater efficiency and more competition. There are structural changes in each new member states' markets, inter alia speeding up the transition process. This is changing the situation in the Baltic Sea region between old EU members in the Western rim and new member states in the Eastern Rim. Vast sums are contributed to regional development in these countries in order to lift them to the European level, for example improving infrastructure and starting a number of projects to reduce pollution of the environment. These investments create business opportunities for the member country companies. Trade between the East and West will be influenced, e.g. across the Baltic Sea as international business activities between firms along both sides of the rim will increase. A main question is how the competitiveness of firms is influenced by this change in international business conditions. In comparison with large companies, small and medium-sized enterprises (SMEs) usually are at a disadvantage because they are traditionally home-market oriented and are therefore characterized by a low degree of internationalization. This further adds to the problems of small firms of doing international business. But this could be compensated for by cooperating through forming networks in order to develop common competitive advantages. By sharing resources, synergies enjoyed by large firms can be achieved. This change improves business opportunities but also creates new threats. E.g., international trade over the Baltic Sea is rendered more difficult by the great differences in business environments between transition economies and Western economies. But will the SMEs have enough internal strength to take advantage of the change. Or will they loose out because of too many weaknesses? How the competitiveness of firms and networks are influenced decide which regions benefit from this development, thus affecting regional development among the EU countries. Certain regions will be ill-favoured by this development, perhaps regions dominated by small and medium-sized firms.

## **RESEARCH ISSUES AND MAIN PURPOSE**

The main issue taken up in this paper is how SMEs can cooperate in order to improve their international competitiveness, especially concerning exporting and importing. A vital question in this context is to what extent the SMEs involved in international business activities such as marketing and purchasing are cooperating. Their limited individual resource-base is one motive joint action. We know from earlier (see for example the theories of industrial districts and entrepreneurial milieus) that SMEs which have developed in a local or domestic market tend to use complementary external resources from cooperation with partners in close geographical proximity. Such cooperation often occurs in the form of networks. This study is therefore focusing on such local networks in order to see how they can function as platforms for development of SMEs import and export.

The purpose of the study is to describe and explain how SMEs try to increase their competitiveness by establishing joint networks using local resources and competences in order to exploit international markets. Furthermore, the purpose is also to contribute to the understanding of how these activities effect the internationalization of the SMEs homeregion. The methodology used for this study is described below followed by a presentation of the theoretical framework developed for connecting firms and local networks. Thereafter, the empirical results of the study is described and analysed by using the theoretical framework. Finally, some major conclusions and implications are stated.

## **METHODOLOGY**

The methodological strategy behind this research is mainly abductive approach based on case studies, being a mix of deduction and induction (Alvesson & Sköldbberg, 1994; Boye, 1999; Dubois & Gadde, 2002; Jansson, 1994). The combination process starts from a more preliminary frame of reference, using the case-study approach (e.g. Merriam, 1998; Yin, 1991). This framework is continuously refined through changing perspectives between deductive and inductive approaches. The aim is to create a solid

theoretical and empirical base at the same time as strengthening the practical validation of the research, by making the results relevant for organizations and society. In addition, the aim should be to use research results for educational purposes. The research process behind this article started from the deductive end by putting together a preliminary theoretical framework based on previous research (e.g. Boye, 1999; Hedberg & al, 2000; Jansson, 2005). This framework was confronted with reality through making case studies of export/import networks in Sweden.

The article builds on a survey of the companies in the Kalmar County trading with East Baltic Sea countries reported in Boye & Jansson (2004). In this survey, the one mentioned above and in other studies, the Kalmar County has been scanned for networks of cooperation in exports and imports. Initial attempts to initiate such cooperation were found in a few cases. But these networks have mainly been formed for other reasons, and have not yet got started with international business (Boye, 2000). One such export network with approximately 25 members was found in the environmental industry, cooperating in industrial marketing activities. A short account of this Environmental Technology RIO (ETR) will be presented later in the article. To know more about how exporting RIOs form and develop, another RIO was studied, namely the Woodhouse Aurora Borealis (WAB) with approximately 40 active members in Northern Sweden. Despite the high importance of wooden industry in the Kalmar County only some examples of export collaboration with 3 to 6 companies in their early stages could be found here, whereas it became interesting to study a more developed cooperation in another part of Sweden. A region was selected, where there is an industry cluster similar to the one in the Kalmar County and an export platform selling to similar markets, in this case Japan instead of to the emerging markets in the Baltic Sea region. Based on these studies, the preliminary theoretical framework has been developed into a more refined framework, presented in this article.

## **THEORETICAL FRAMEWORK: THE INTERNATIONAL COMPETITIVENESS OF REGIONAL NETWORKS**

### ***THE STRATEGIC APPROACH***

Porter (2000, p. 16) defines a cluster of companies as: "...a geographically proximate group of interconnected companies and associated institutions in a particular field, linked by commonalities and complementarities". The success or the competitiveness of such a network is decided by these commonalities and complementarities or the internal characteristics. But it is also determined by the external environment of the network: the geographical setting and environments beyond the region. Both these major strategic aspects behind network-specific competitiveness are developed below. Regarding the internal conditions behind the competitiveness of clusters, economic factors dominate in the literature. There are classical economic geography reasons for the spatial closeness, e.g. Marshall's self-contained networks in traditional industries focusing on the economic efficiencies of clusters in supply chains, labour markets and subcontractors. But it has also been explained by that a common and shared regional knowledge is developed through rapid formal and informal communication across firms, employees, and the community. This regional common knowledge base is the main factor behind cluster or network-specific competitive advantages, particularly the non-transferable knowledge that creates a dedicated and specific geographically bound capability: a kind of regional non-tradable public good for which there exists no market mechanism. From a social perspective such an untraded interdependency is socially driven, e.g. taking place within a community of practice (Brown & Duguid, 2001) or through the build up of social capital (Coleman, 1988). Such a mix of economic and social explanations is a common research perspective. According to Piore & Sabel (1984), for example, industrial districts consist of relationships-based firms that get institutional support in a close community, where social factors provide the context for economic success. The industrial district is a socio-geographic entity, where economic factors are socially embedded.

The growing importance of clusters in industrial development has made them popular industrial policy instruments. Increasingly, the establishment and operations of networks are supported by outside public parties. Such network initiatives manifest themselves as cooperative projects in networks consisting of

firms, government bodies and the research/education community. In 2003, 509 initiatives for such clusters all over the world were identified in the Global Network Initiative Survey (Lindqvist, 2004). This aspect is taken up in the present study in order to research the importance of such initiatives regarding clusters involved in international business. Whether public bodies are included in the network or not depends on how the initiative is organized. In case their task is limited to initiating or serving a specific network, they are normally left outside the cluster/network. In case they participate in the international business operations of the network, they are included.

Based on this literature, three major perspectives on the competitiveness of a regional network are taken in the present research:

1. The network does not have any strategic intention of its own. Why some groups of firms are more successful than others is explained by the fact that there are favorable economic and social factors, e.g. a benevolent environment supporting the network.
2. The network is seen as an actor with own intentions, e.g. expressed through a deliberate strategy based on network-specific competitive advantages.
3. The network is seen from the perspective of the individual membership firm. The focus is on firm-specific competitive advantages and how these can be improved through being part of a regional grouping, benefiting from the network-specific competitive advantages.

In this article, perspectives 2 and 3 are combined. This means that it focuses on initiatives endogenous to the network, normally treating public network initiatives as an exogenous factor. However, in case such initiatives result in public units participating in the intended operations of the network, they are included.

In order to give an overview of the theoretical model used in this study the following theoretical discussion relates to the schematic figure below. The Regional imaginary organization (RIO) functions as a vehicle for SME internationalization, supporting individual SMEs with limited resources to reach international markets. The SME internationalization process is described by Cavusgil (1980) as a five step development. The RIO with its action and organization networks, knowledge and resource base and institutional structures is the platform from which international relationships are built. The development of such relationships follows the five step process described by Ford (1980). The RIO is anchored in a regional setting, making it a part of an industrial region which as a whole will be influenced by the new international relationships built and, as a consequence becoming more internationalized.

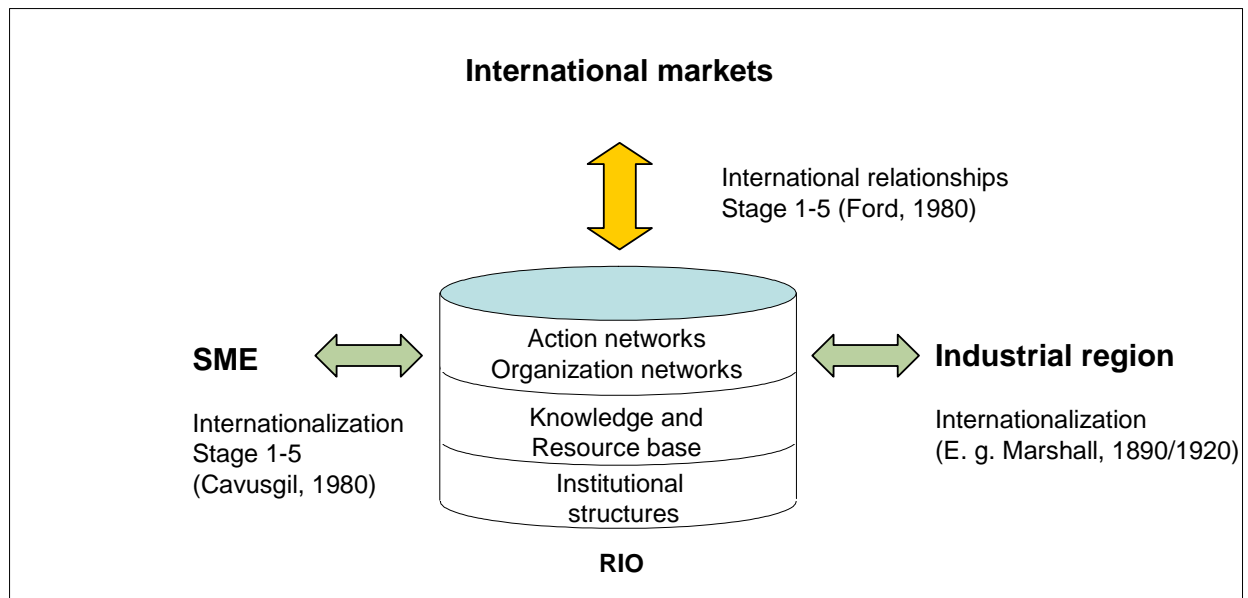


Figure 1: The regional imaginary organization as an export/import platform for SMEs and industrial regions.

### **REGIONAL IMAGINARY ORGANIZATIONS (RIO)**

The regional network model is developed for collaborative networks for exports from and imports to a region. They are separated from market networks and hierarchies (Powell, 1990). In the former case, collaboration takes place in the market in vertical or horizontal market networks. The former case concerns how firms are inter-related along the vertical value added chain, while the latter takes up relationships between competitors. Such collaborative inter-organizational networks or imaginary organizations also work in another way than intra-organizational networks within a firm. This means that the network of interest here consists of hierarchies and operates in market networks. So the structure of this collaborative network is decided by the characteristics of the firms involved in it and the market network where it operates. This type of collaborative network is defined as a regional imaginary organization (RIO). It is based on a platform of various structures and held together by regional concepts. Here, we stress that the foundation of the competitiveness of the network concerns how resources, capabilities are integrated through the network into network-specific capabilities. The competitiveness of a RIO is decided by how it is organized: its strategic identity, network organization and resource/competence base. These factors are influenced by outside factors in its geographical setting. This is illustrated in Figure 2, where the network is seen as a regional platform consisting of three layers placed in a geographical setting. The first layer consists of inter-organizational relationships between firms in a regional network. These relationships are connected to a second layer - the knowledge and resource structure -, which in its turn is related to the institutional structure. These layers and factors located in a geographical setting are all held together through the identity of the network defined as a regional concept.

The competitiveness of the RIO is thus determined by three layers of factors related to one another located in a geographical setting or region. The first layer of *the regional network* is viewed to consist of nodes connected by relationships or linkages. This network has a dualistic quality of both serving the interests of individual organizations, i.e. influencing firm-specific competitive advantages, at the same time as they are part of a larger collective with the right to carry out work on behalf of the whole network, i.e. influencing network-specific competitive advantages. A member of a network therefore feels that it serves the own interest simultaneously feeling to have common interests with the other organizations of the network. Actually, this trade-off needs to be right for each individual member in order for the network to persist for any longer period. This means that networks describe and explain entire social structures and comprehend particular elements within the structure. Three aspects of a firm's network structure are important: the number of direct links and the number of indirect links it has together with the connectivity, i.e. the degree to which the partners are linked to each other (Ahuja, 2000). According to the latter dimension, a distinction is made between open and closed networks. An example of an open network is where the firm has direct contacts with all its partners but who do not have any direct contacts with each other. Many such structural holes mean that the network consists of few redundant contacts and that it is information rich, since people on either side of the hole have access to different flows of information (Burt, 1992). The structure of an open network is suitable when the purpose of cooperation regards market information and in maximizing the number of contacts. The opposite is the closed network, where all partners have direct and strong ties with each other. This network is centered on social capital, which is built through trust and shared norms and behaviour (Coleman, 1988). This type of network is suitable where the partners' objective is to collaborate in action, e.g. collective marketing actions. This latter network is made up of two major types of networks: organization and action networks. (Aldrich & Whetten, 1981; Jansson et al, 1995). The organization network is a larger more permanent social structure, from which members are drawn for participation in temporary action networks. The action network is a temporary set of units, which has been formed out of different units in the organization network for a specific purpose. A value constellation, for example, is an action network that is established for the temporary task of marketing a product/service package involving a certain combination of competences from the units of the organization network. A value constellation is a group of actors representing different

units that work together to create value for the customer (Norman&Ramirez, 1993), implying that interdependent marketing activities link actors and their competences together. When the task is completed, the action network is dissolved, the units remaining in the organization network awaiting formation of future action networks

The regional imaginary organization is a separate organization or core unit through which firms cooperate with one another. The definition of the RIO is based on Hedberg (2002):

(Imaginary) organizations are cooperative enterprises that attempt to balance exploitation and exploration through combinations of systems for vertical integration with processes for interorganizational collaboration. A core unit assumes leadership through the elaboration of shared visions and elements of communal culture. Although information technology mostly serves as an important enabler, the social texture of trust-building processes, interdependencies and synergies, mutual respect and learning, together with transparent exchange mechanisms are what make these loosely-coupled networks organizations. (p. 12)

The RIO is a horizontal network, which consists of organization networks and action networks, where the latter network is a value constellation involving a number of formally independent organizations in a region. From a *regional industrial platform* perspective (Boye, 1999), competitiveness is created through the strategic capability to develop and position teams of complementary resources, thus creating regional core competencies. This capability depends on how activities are structured and organized and how individual knowledge is integrated through social interaction. Institutional structures, in the form of cognitive frames, norms, values, incentives, and sanctions, play an important role in structuring and organizing this social activity. Region concepts tend to play central role in the formation of horizontal networks or regional imaginary organizations, since they contribute to the crucial knowledge integration, as well as to the positioning of regional resource constellations on the competitive arena. The shared capabilities of the platform are the outcome of knowledge integration (see Grant 1996) through the social networking activities of local actors built on social capital and trust. These activities are embedded and formed in a context of role-related social expectations (normative institutions), mental patterns and symbols (cognitive institutions) (see Tsoukas 1996), and constraints and regulations by current rules and laws (regulative institutions). These kind of social activities are possible within a local community that has a high spatial proximity, which enables the substantial interaction between individuals.

The second layer consists of *the knowledge and resource structure*, which plays a pivotal role in the strategic process of the network, then being a regional competence platform (Boye 1999). There are several similarities with the resource-based theory of strategic formulation (e.g., Wernerfelt 1984, Barney 1991, Grant 1991) in which strategy aims to enable the exploitation and upgrade the organization's resources and capabilities in the best of ways. However, in a network the strategy process is not in the hands of a single manager or a firm. Rather, it is a collective strategy formed through the network. As for the local industrial knowledge base, it is possible to view the network as a "distributed" knowledge system (Tsoukas 1996). In highly integrated networks, for example, the knowledge/resource structure is combined through the industrial network into distinctive network-specific capabilities or core capabilities, which create synergies for the units involved in the competence network. Thus, core capabilities are networked knowledge. Such resource sharing through combining knowledge, skills, and physical assets most efficiently takes place within a closed network, since it involves significant conversion of tacit knowledge, which normally requires repeated and regular meetings, a focus on specified objectives, close and trustful cooperation, and mutual dependency. When access to new information is the primary goal, on the other hand, open networks are the most suitable (Ahuja, 2000).

*The institutional structure* is the third strategic fundament of the regional network. Here, regional actors, seeking economies of scale and scope, take initiatives to reduce regional barriers and harmonize systems. Firms' and other organizations' perception and interpretation of their environment go through individual and common cognitive frames, including industrial recipes and definitions of their local region and competitive context. In addition, values, norms, and regulative mechanisms have a significant influence on how organizations act in relation to their environment. Consequently, a great many organization strategies are based on beliefs, ideas, and concepts shared by others in society. The more institutionalized these factors are, the more integrated or tight is the network.

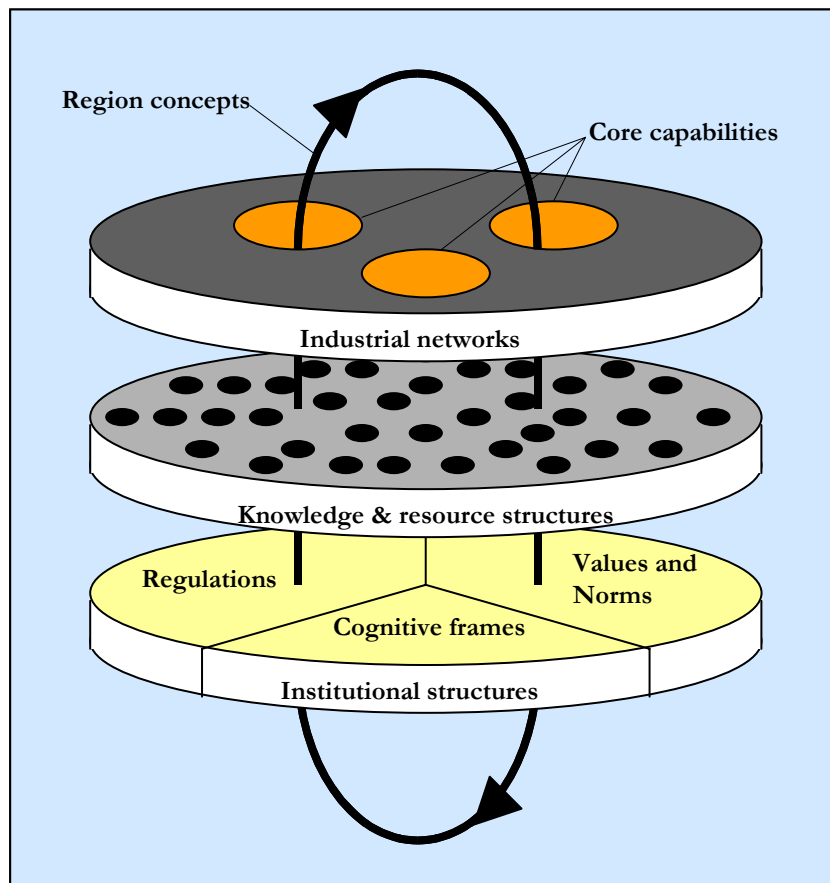


Figure 2: The anatomy of the regional export/import platform (Based on Boye, 1999).

Thus, trust, shared meanings, identity and routines as well as conformity are key aspects of the institutional structure. Regional concepts are thereby examples of concepts framing and defining the strategic arena for local firms and other organizations. The identity of the network is therefore expressed through *the regional concept*. It embodies the network, since it functions as a nexus between the various platform layers. The intentional development of the regional concept is seen as a cognitive strategic networking process. It is a collectively shared fundament for the network-specific strategy as well as for firm-specific strategy, as the regional concept influences the strategies of the individual firms of the network. Even if each company has its own interpretation, it adopts the prevailing regional concept into its strategic considerations. The agents participating in the collective strategic process of the network all influence each other with their own intentions and activities. So as region concepts are open to interpretation, the implementation of the network-specific strategy through the organization of the regional platform does not necessarily correspond to the initial intentions behind its creation. Various agents of the network have their own intentions, and the regional concept functions as a frame of reference for interaction and negotiation between these agents and their intentions and activities. The development of a network is therefore neither a strategic process that is planned nor that has simply emerged, but it is a process of interpretation and negotiation. The regional concept is embedded in the cognitive structures of the platform, elucidating it. It is a way of seeing and a way of thinking and making sense, triggering action. The regional concept does not only constitute the base for the process, but is also a product of the process in that it keeps undergoing change. When actors gain new experience, new action patterns develop and new ideas evolve. Over time, a strong concept becomes institutionalized and is taken for granted, becoming so convincing that it provides a common view of the network.

The regional concept (a cognitive frame) is influenced by values and norms, for example, social expectations of what the network will look like in the future. These expectations, in addition to cognitive structures, influence the way in which people participating in the development process act. The regional concept relates to the layer of resources and knowledge structures, as a specific concept supports the formation of teams of resources and the development of shared knowledge. E.g. the regional concept gives the collective competency or core capability of the network an identity, profile or a "name".

### **The network-specific capability**

The strategic issue is how to develop network-specific capabilities based on complementary resources supported by shared cognitive frames, values and norms. This is a collective strategic network (institutionalization) process critical for competitiveness and regional growth. This capability is the distinctive competence of a network, embedded in products and services, which creates value to customers through improved effectiveness and quality, and which are unique or rare compared to competitors' capabilities. It is created through the integration of knowledge and the development of constellations or teams of complementary resources. Resources and capabilities that can be trajected over time but not in space can sometimes create enduring differences in competitiveness between regions (Maskell & Malmberg, 1999). Some of these resources are tangible and articulated, which makes them easier to identify, and some are intangible or tacit, which makes them difficult to discover and trade.

Once established, competitiveness can be sustainable due to that the interconnectedness between different knowledge and resource structures creates a socially complex capability, which is often difficult to understand, codify, or imitate for competitors. For the individual firm-specific competitive advantage, these resources and knowledge are found within the firm or with its partners in the competence network. This collective or architectural capability to use teams of resources in certain purposeful ways might lead to sustainable competitive advantage of the network, since they create synergies for the firms involved. Such a regional industrial platform could be compared to a corporation, in which the core task is to make its different companies share activities or competencies across industry boundaries (Porter 1987) or share with resource-related industry groups (Farjoun 1994). Through the development of a network, such regional capabilities are made explicit, thus facilitating their further development and positioning.

The regional concept which has developed under the influence of a large number of network actors play a crucial role both in facilitating and supporting the integration of local knowledge and in the formation of a network-specific collective strategic capability, as it provides the network with a shared mental frame. The development and institutionalization of the regional concept both trigger and stabilize the strategic development process of the network, inter alia contributing to the positioning of regional knowledge and resource constellations on the competitive arena.

### **The geographical setting**

The possibilities of the firms of the network to discover, combine, and utilize individual firm knowledge and resource structures to form network-specific core capabilities are dependent on the institutional structures in the region. Some institutional structures support this process, while others may restrict it. Proximate institutional structures in the region, in the form of industrial recipes and other cognitive frames that have developed through collective experience, may shape the formation of strategic capabilities. At the same time, background institutional structures, in the form of nation-specific or regional cultures and traditions, supported by values and norms as well as regulations and legal systems, tend to have a strong influence on how intentions and activities of the firms of the network are structured and organized.

Thus, the network is anchored in a broader regional context, making it a regional platform. The region is defined as an external network and institutional context, which consists of networks in organizational fields and societal sectors. The region influences the regional network and the network influences the region. In relation to such a geographical context, the regional concept, for example, creates a territory within the larger geographical area as well as a center and a periphery. Inversely, the region becomes partly defined by the regional concept. Moreover, the network and the region are also influenced from outside by larger



geographical entities, e.g. a geopolitical context such as the Baltic Sea region. Regional networks are embedded in larger and larger geographical contexts, meaning that regional resources are identified, developed, and positioned within different geopolitical settings.

## **INTERNATIONALIZATION PROCESSES**

RIOs meant for international business operations like exporting and importing are, as firms in general, involved in internationalization processes. They take place in a stepwise manner (Jansson, 1989; 1994b; 2005). Companies commit themselves through a gradual learning process. Learning is incremental and takes place by doing. Firms learn about doing business abroad, e.g. about the conditions in particular markets. Companies tend first to establish themselves in geographically and culturally proximate markets and increase their commitment more and more, starting with agents, and passing through sales companies to manufacturing companies (Johanson & Wiedersheim-Paul, 1975; Johanson & Vahlne, 1977). This has mainly been studied for MNCs but also for SMEs (Hohenthal, 2001). Research on the export of mainly North American both small and large companies have reached similar results (Bilkey, 1978; Cavusgil (1980); Reid (1981), Czinkota (1982). However, 'Born globals' or 'International new ventures' (that are international from inception) tend to follow another pattern (Oviatt & McDougall, 1994; Madsen & Servais, 1997, Sharma & Blomstermo, 2003a). A basic assumption in internationalization process theory is that knowledge accumulation is continuous and dependent upon the duration of foreign operations (Forsgren, 2002; Sharma & Blomstermo, 2003b). The longer the firm has been involved in foreign operations, the more knowledge firms accumulate about such operations. There is a relation between knowledge accumulation and risk so that the more knowledge the firm has, the less uncertain it perceives the foreign market to be. Firms that lack knowledge about foreign markets even tend to overestimate risks. This corresponds to what Jansson (1989, 1994b) found about establishment processes in a regional emerging market perspective, namely that the pace of investments in Southeast Asian countries accelerated the more experienced the firms became of this area, at the same time as the mode of establishment became slightly more direct for the later establishments.

### ***INTERNATIONALIZATION THROUGH NETWORK RELATIONSHIP DEVELOPMENT***

Traditional internationalization processes are mainly about marketing activities. This aspect is, however, not very much developed, especially when it comes to industrial marketing in emerging markets, which is a matter of building and handling network relationships. According to another branch of the Uppsala School, relationships constitute the core of the internationalization process (Axelsson & Johanson, 1992; Hammarkvist, Håkansson, & Mattsson, 1982; Jansson, 1994, 2004a,b; Håkansson, ed., 1982; Håkansson & Snehota, 1995; Jansson, 1989; Johanson & Vahlne, 2003; Majkgård & Sharma, 1998). Internationalization takes place through establishing and maintaining network relationships in foreign environments. An exporter/importer network is a temporary set of units, which has been formed out of different units in the organizations of the buyer and the seller, i.e. a value constellation established for the task of marketing/purchasing a product/service package involving a certain combination of competences from the units of these organizations. A value constellation is a group of actors representing different units at the buyer and the seller that work together to create value for the customer (Norman & Ramirez, 1993), implying that interdependent marketing and purchasing activities link actors and their competences together. This international marketing and purchasing of products and know-how through this direct exporter/importer network means that a vertical network in the exporting region (e.g. a supplier's supplier network) is indirectly connected to another vertical network in the importing region (e.g. a buyer's buyer network). This larger vertical network, in its turn, is embedded in other regional and national networks, e.g. a financial network (Jansson, 2005). The exporter/importer network is then part of a larger value constellation consisting of a supplying export network connected to a buying network in the emerging market.

## **STAGES OF INTERNATIONALIZATION**

Based on the experiential knowledge process, internationalization processes are often divided into different degrees of internationalization or stages. According to Johanson & Mattsson (1991) inexperienced firms follow the traditional slow and gradual pattern (e.g. the “late starter”), while the internationalization of the more experienced company is less gradual and slow (e.g. the “international among others”). A classical grouping of firms is made by Cavusgil (1980), which has been found to be valid also for exporting small and medium-sized enterprises (Gankema, Snuif & Zwart, 2000). According to their study, the internationalization of SMEs takes place in five stages. During the first stage, firms have a domestic market focus. Next follows the pre-export stage, when the firm evaluates the possibilities to start exporting. The third stage is experimental involvement, when exporting is a marginal activity. The fourth stage is active involvement, when international business is a normal activity, e.g. an important share of the turnover is exported. A suitable organization structure is also in place for this activity. The fifth and last stage involves committed involvement in exporting. The firm can now be called international, since it is heavily dependent on foreign markets.

The internationalization process is normally divided up into two parts: an external part dealing with the geographical spread to the international country markets and one internal part focussing on types of establishments or entry modes in a country. The customer aspect is developed here by looking at how relationships are established with customers. Establishment points in networks are defined as entry nodes, e.g. directly with the customer or indirectly through an intermediary. In the latter case, the entry node is also an entry mode.

The development of international buyer/seller relationships tends to follow a certain pattern (Ford, 1980, 1997, 1998), being separated into five stages. Each stage in the entry node is described according to a number of relationship factors, e.g. how the experience, commitment and adaptations of the parties increase and how the distance and uncertainty between them are reduced. The first stage takes up marketing/purchasing activities before the relationship begins. The next three stages show how direct buyer-seller relationships within networks are established: their beginning and deepening. This development can be described according to a number of relationship factors, e.g. how the experience, commitment and adaptations of the parties increase and how the distance and uncertainty between them are reduced. The variable experience indicates the amount of experience the respective parties have of each other. Both parties will judge their partner's commitment to the relationship. Commitment is to a large extent shown by the willingness to make adaptations. The variable distance is multifaceted and can be split into the following types of distance: social, cultural, technological, time and geographical distance. Uncertainty deals with the fact that at the initial stages, it is difficult to assess the potential rewards and costs of the relationship.

Ford's model complements Cavusgil's model. While the latter concerns how the international experience of the firm is developed, the former is a good approximation of how international experience is gained in a country. The more developed the customer relationships, the more experience the firm has of the particular foreign country market. During the pre-relationship stage, the experience of the customers/suppliers is none or very low, uncertainty high, distances large and commitment and adaptations zero. According to Cavusgil's five-stages model, for a SME that has a domestic market focus and starts to internationalize its relationships to a foreign country, the pre-relationship stage corresponds to the pre-export or pre-import stage for the first foreign market (Gankema, Snuif & Zwart, 2000). The development of the relationships in the foreign country market starts in the early stage, when commitments and experience increase somewhat. In the five-step model, this is similar to the experimental export stage or import stage for an internationally inexperienced firm. This establishment of relationships is a mutual learning process, where the parties learn to know more and more about each other. The first adaptations are made, but are still few. High uncertainty is experienced and high distances prevail between the parties. The early stage is followed by the development stage, during which business between the customer and the supplier starts to grow and resources are increasingly shared. In this stage, there is a further development of the buyer/seller relationship signified by a delivery build-up and the signing of contracts. Intensive mutual learning results in increased experience on both sides, as well as in reduced uncertainty and distances. Trust and

commitments increase, which are signified by both formal and informal adaptations as well as cost savings. Relationships change character and become entirely focused on the dyad, in that way becoming deeper and broader. Next, after several major purchases or deliveries, the relationship is developed and settles in a stable stage of the long term stage with continuous business going on between the parties. The exporter and the importer have now learnt to know and trust each other, which gives high experience and that the uncertainty is perceived as being low. Distances are small and commitment high. Adaptations are extensive and cost-savings considerable. The main aim with building relationships is to reach the long term stage, to get an on-going long-term relationship. If this is not accomplished, the relationship may retract to an earlier stage, even to the pre-relationship stage. In the latter case the relationship building may start all over again, perhaps this time with a new buyer/supplier. In the final stage, the relationship is extensively institutionalized and habitual with commitment being taken for granted. The downside is that the relationship might get stuck and become hard to adapt to on-going environmental changes. The high trust, low distances and uncertainty might also lead the parties to become complacent. Despite the high degree of institutionalization, this makes the relationship sensitive to being broken, due to environmental changes and attacks by competitors.

Thus, relationships being at the core of the internationalization process of SMEs follow a similar pattern as the internationalization process as a whole as showing how the gradual build up of international experience takes place. The more relationships in a foreign country that have reached later stages, the more internationally experienced and the higher the degree of internationalization of the SME. Further, the more countries with established relationships, the more internationally experienced the firm is.

## **EMPIRICAL ILLUSTRATIONS**

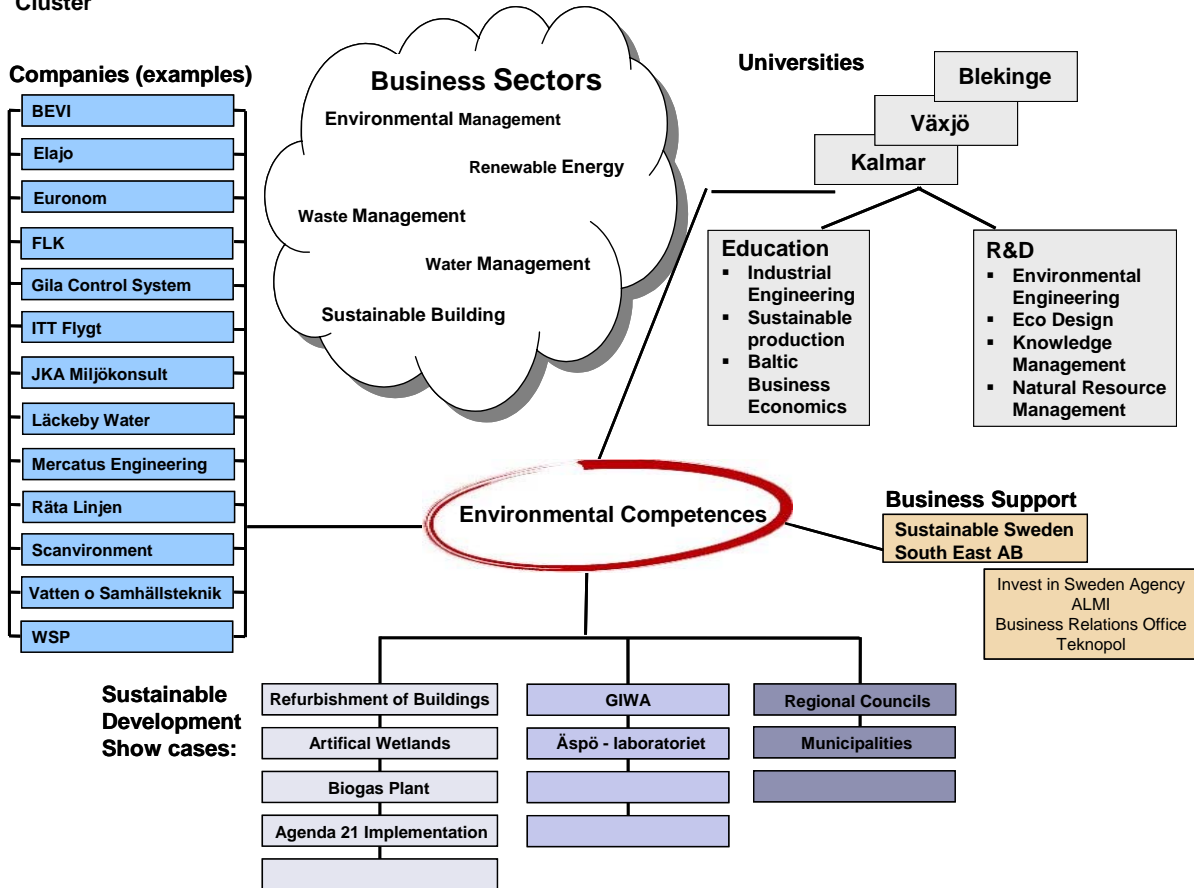
### *THE ENVIRONMENTAL TECHNOLOGY RIO*

Very few horizontal international trading networks or regional imaginary organizations (RIOs) oriented toward international business were found. There are some preliminary attempts to initiate such organization networks based on existing industry networks on the present export and import platform, e.g. within the plastic industry network, the woodwork industry network, and the glass industry network. But these networks cannot be classified as international business RIOs, since firms within these networks mainly cooperate in other areas than international business, e.g. manpower development and modernizing production. Although this cooperation mainly aims at increasing general firm-specific competitiveness, it may indirectly influence the competitiveness in international markets of the individual firms of the network. The main purpose behind the cooperation within these RIOs is mainly to develop the competitiveness of the individual firm of the network. The purpose is not to develop a common competitive advantage of the whole group of firms, i.e. a network-specific competitive advantage. The most advanced attempt to start a RIO in order to build network-specific competitive advantages was found in the formation of an export marketing network, which began a few years ago and has now reached a state where initial orders are received. A brief account of this environmental technology RIO is given below.

The Environmental Technology RIO (ETR) is an organization network that fits the description of an imaginary organization (Hedberg et.al., 2000). There is a distinct IO-leader ('spider') of the network ('web') in the form of a leader enterprise by the name of Sustainable Sweden South East (SSSE), which handles the strategic management of the network, e.g. by developing marketing strategies and defining core competences. The network is held together through informal contracts based on trust more than formal means. Other unifying factors are synergies, a clear vision, and a working business concept. IT also plays an important facilitative role. SSSE's main task is to market the products and services of the organization network's units by forming action networks or value constellations. The IO-leader heads a broad partner base (12 firms and 7 municipalities). The purpose of SSSE is to increase the customer base of the network through marketing of the products and competences of the network members. The insignificant marketing competence, and mainly the production competences of the network units are supplemented by an international marketing competence. This latter competence, mainly embodied in one full-time

manager, forms a kind of 'marketing department' for the organization network, heading its marketing activities. If successful, SSSE will establish an export platform by creating profitable export business through its marketing activities. SSSE has been formally established but is in the process of creating confidence (trust) among the members of the ETR by demonstrating that it

The IO:s Network Map of the **Environmental Technology Cluster**



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Figure 3

works as a marketing organization, inter alia producing orders for its members (legitimation). So far, the customer base is too small for this imaginary organization to have reached a long-term (legitimized) stage, more being found in the development stage. If the marketing of ongoing offers will result in orders, the organization comes closer to this 'firmly established' stage. A closer look is therefore taken at this potentiality by studying the organization of marketing of a few promising business deals. One concerns a Water and Sewage project in Panevezys, Lithuania, and another concerns smaller environmental projects in Kaliningrad. Two major opportunities are found for such projects, representing two major offerings. Either the whole project is supplied or bits and pieces of it. In the first case the action network will be a main contractor involving many and different competences of the network. In the second case only one or few firms are involved as subcontractors. However, as demonstrated by this case, there are definite limits on the project side for export platforms consisting of small firms. Although forming a larger organization and competence base, the network is too small to be able to compete with big companies over most types of projects. It lacks resources and competences for offering and constructing larger projects, e.g.

engineering competences, marketing skills, a main contractor capability consisting of project administration skills and other organizational capabilities. In addition the more short-term business outlook of small firms demanding more immediate results is too much of a drawback in this kind of long-term business. This situation is aggravated when exporting to the very foreign emerging markets in the Eastern Baltic Rim.

Another drawback in marketing and effectuating projects and probably marketing in general lies in the fact that this is a virtual organization competing with real organizations, e.g. having a more fuzzy identity and being more difficult to coordinate an inter-organization network than an intra-organization network. This drawback is even larger in the formation stage of an imaginary organization.

To market industrial products and service on the specific emerging markets firms need to have a broad and deep knowledge about the markets and the broader market environment. In short, they need to know about the societies there, e.g. having a cultural knowledge in order to interpret markets and understand how to build network relationships. Knowledge is required about the formal and informal rules or the institutions that drive the market as well as about how to act in these markets, i.e. how relationship marketing takes place through local networks. (Jansson, 2005). A smaller organization like SSSE and its network normally faces problems of acquiring such know-how. This market knowledge is mainly found with the IO-manager for certain markets and customers in the Eastern Baltic Area and to some extent with other managers at the firms involved in the network. The IO-manager has a long experience from marketing projects in emerging markets, which is shown by the realization that networking is the key marketing activity.

However, this is still a rather limited marketing capability, since it is mainly found within one person. It is not enough to establish a customer base of the size that will satisfy the members of the ETR. Outside marketing assistance is therefore required, for example to monitor the fast transformation of these markets and to help with certain networking activities. SSSE is also in the process of recruiting agents and possibly also distributors. This is a further extension of the external network with more marketing competences, e.g. to help out with market research, customer and government contacts. This development fits with theories on internationalization processes, which show that internationalization is a gradual and slow process, particularly on emerging markets. Marketing, for example, in the beginning more takes place through indirect entry nodes than direct, smaller organizations, in particular, use entry modes such as agents, distributors and other intermediaries, even more so on emerging markets. However, for high technical competence organizations like SSSE, where the knowledge linkage is critical, it is more a question of combining direct and indirect customer relationships.

The size of the ETR seems to be favourable for establishing a semi-closed network for common marketing activities through direct and mutual ties between the members at the same time as to keep it semi-open for having an efficient information network. However, as seen above the RIO is still far from this state, since it is in the experimental internationalization stage and early stage of building relationships to expand the customer base, particular the base common for the ETC.

### ***THE WOODHOUSE AURORA BOREALIS PROJECT***

The main purpose of WAB is to establish long-term cooperation between firms in this region and Japanese firms, mainly to export, but also to attract Japanese firms to invest in the region (Jacobsson & Strömberg, 2004). The plan is also to include the Chinese and Korean markets. This RIO is larger than the ETR. Of approx. 260 firms in the two most Northern Swedish counties, 50 are members, of which 35-40 are active. The number of employees of the firms varies between 5 and 500. The firms cover the whole value added chain of building material and house components, i.e. all inputs except raw material for wooden houses. The largest company in the industry in the area – 'Norra Skogsägarna' – is a passive member of the network, mainly contributing its marketing experience to the project. Collaboration partners are local governments, a few central government units and some organizations in Tokyo. WAB builds on

previous attempts by the Swedish Export Council to start export cooperation within this industry in the area and the experience of the short previous life of a sub-supplier network. The project is financed by the local partners and EU, and the fee of active members is SEK 20.000 and of passive members 10.000. The good finances have eliminated one of the main difficulties for SMEs that want to start exporting, namely lack of financial resources.

A main activity within the RIO is match making, i.e. identifying suitable suppliers in Sweden and customers in Japan and fit them together. Another activity is to provide market information through documentation and visits by Swedish firms to Japan and vice versa. These visits are an important part of the fourth activity, namely creating contacts. Support is also given. The project is primarily meant to create contacts, give advice, and follow up on the activities.

A house building network of 25 firms has been established within the WAB. WAB also cooperates with two other similar projects in Northern Sweden: Building Wood and Artic lumber group.

The activities in WAB are concentrated to the first stages of the internationalization process, mainly to make resource poor SMEs to help each other to start exporting to Japan: to leave the domestic market focus, pass through the pre-export stage and enter the experimental stage. In addition, the activities are primarily concentrated to the pre-relationship stage through match making and information, and to the early stage through helping with the building of contacts. The WAB is classified as a semi opened network. During the pre-relationship stage it works as an open network, where opportunity exposure, network mapping, and information collection dominate. Later, when marketing starts through contact building, direct links between a smaller numbers of firms become necessary. The network starts to close through the formation of smaller and more integrated networks. The separate and smaller house building network seems to be a good example of a more closed network, which has certain similarities with the action networks within the ETR. In the former case, there are more direct, interconnected and mutual relationships and probably more of shared meanings, trust, and routines. Other smaller networks have also been formed within the WAB. Then, the role of the IO manager is somewhat different than in the ETR. He works as a bridge between the internal network and external networks at the same time as he is coordinating mainly the internal network and inspires to actions within it. He is a broker, and also engaged in contact building and maintenance inside the network and outside in the Japanese vertical market customer network. This is more the task than making, closing and following deals up, which the IO leader of the ETR is more doing. The IO manager of the WAB also has extensive experience from how business is done in Japan. Through these abilities, he has been accepted as a leader by the members. In the initial stages it is also important to be able to create new business concepts for the SMEs.

The basic resources of the RIO are the high-quality timber growing in the region, long experience from making high quality products throughout the whole value chain, high class production facilities and an effective transport system. A good knowledge has been built up about the Japanese market and how to do business there. The network especially has establishment know-how. By combining the resources of highly niched SMEs a broad range of products can be offered. The marketing routines learned are shared within the network as success stories or best practices. The name of the network functions as a brand, giving the RIO a regional identity in Sweden and a common brand name for the international business in Japan.

## **MAJOR CONCLUSIONS AND IMPLICATIONS**

One more advanced regional imaginary organization was found in the region studied, which was compared with another RIO in a similar region. Even if there are some examples of more embryotic RIOs this kind of cooperation is insignificant for Swedish SMEs is in general. A major reason for this is probably that the total export volume is too low and the firms are too small. An industry structure dominated by small firms becomes fragmented, consisting mainly of 'stand alone' firms operating in the market. There are few leading firms (or flagship firms), which other companies could look up to, could work as role models, or which could initiate cooperation efforts. Still four export clusters exist in the county, since

exports are concentrated to two major industries (engineering industry, woodwork industry) and two minor industries (glass industry and plastic industry) in a few and often nearby places. There is one major import network of this type, namely in woodwork industry (co-location of importing companies). These industry clusters have a potential for future development of horizontal networks or RIOs, within which joint exporting or importing could take place. The slow processes of trade development were illustrated by the empirical examples. It takes time to establish an international trade platform, especially when there are great differences between countries.

As shown above the size of the two RIOs varies. In addition smaller networks emerged within the WAB. Size defined as the number of strong ties matters as it affects performance, in this case competitiveness (Uzzi, 1996). There also seems to be a U-shaped relation between closure and performance, i.e. when size relates to the structural properties of networks (Soda, Usai & Zaheer, 2004). According to their study of projects within the Italian TV industry the best performing projects were those with high past closure and high current structural holes. Network closure has a strong long-term effect, while brokerage structures have only short-lived effects. The effects of bridge ties are temporary, meaning that they decay and are unstable, which could be expected from weak ties. These are important implications for how to build open networks, e.g. that the cost of creating and maintaining bridge ties has to be evaluated in the context of their short-term (brokerage) advantages. Transferred to RIOs, this means that networks should be based on both past working relationships among members and simultaneous links to other firms/persons for best performance. This seems to fit with the structure of WAB and the strength of the IO leader and how he performs. Flexible forms of organization are most relevant in industries undergoing rapid change, and being instable and where uncertainty is high. There are also drawbacks with high closure. A too strong identity built on shared meanings and language, routines, and social norms like trust might make the network too inflexible, e.g. by having too many mutually connected people. It also means that information networks should be kept flexible and where exposure is critical for getting access to new bridges. Thus, match making should be made a continuous process.

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