

# **BANK RELATIONSHIPS AND EXPORT SHARES**

Lundberg, Helene, helene.lundberg@miun.se, (Mid Sweden University, Sundsvall, Sweden)

## **ABSTRACT**

The present study addresses the internationalization of small and medium-sized enterprises by relating their share of export to funding, transaction services, advice, knowledge and contacts that banks can offer. It thus contributes to SME internationalization research by addressing knowledge acquisition from institutional actors such as banks but also by taking this one step further, differentiating between the contributions from different types of resources and services that banks can provide. The study method is an on-site survey, encompassing 135 manufacturing Swedish SMEs. The results provide a more nuanced picture of the ways that banks support the internationalization of SMEs.

## **INTRODUCTION**

Internationalization is a way for small and medium-sized enterprises (SMEs) to grow, especially for those that originate in small country markets, and export share, i.e. the percentage of the total sales that are exported, is the most common measure of their degree of internationalization (Bell et al., 2001; Lu & Beamish, 2006). Some SMEs internationalize from inception and quickly develop high export shares (Kalinic & Forza, 2012; Knight & Cavusgil, 1996). Others initially focus on their home market and only gradually enter other markets, slowly increasing export shares (Johanson & Vahlne, 1977). Decisions on international expansion are affected by several factors but a key aspect is funding. While the limited scale of SMEs can imply flexibility and facilitate adaptation to the requirements of foreign markets, their lack of resources poses severe challenges and may reduce the pace and extent of internationalization (Coviello & McAuley, 1999). Furthermore, there are many practical financial aspects to handle in entering a new market. It is therefore argued that banks play an important role not only in the financing of SMEs, but also due to their ability to facilitate financial buyer-seller transactions (Durkin et al., 2013).

Internationalization not only implies financial challenges. As entering a new market entails considerable risks (Sapienza et al., 2006), knowledge acquisition has for a long time been seen as fundamental to successful foreign market entry (Johanson & Vahlne, 1977; Liesch & Knight, 1999; Musteen et al., 2014). Knowledge can be developed by learning from experiences (Johanson & Vahlne, 1977) but also result from deliberate search actions (Arthur & Huntley, 2005) or unprompted transfers during interaction with business partners (Tolstoy, 2009). Direct and indirect connections to other business actors function as conduits of information. The presence of knowledgeable actors within a firm's business network is therefore beneficial to internationalization, as they may indicate new opportunities (Bradley et al., 2006) and contribute to bridging the knowledge gap vis-a-vis foreign markets (Loane & Bell, 2006). Banks may be such a source of knowledge and business advice (Binks et al., 2006).

Very few studies have however focused on actual contributions from institutional actors such as banks (Lindstrand & Lindbergh, 2011), especially not regarding specific bank services (Boot & Thakor, 2000), and the results have been contradictory. While some studies report

that SMEs view banks as a key partner that is used for obtaining information on international markets (Boter & Lundström, 2005; Lewis et al., 2007; Meyer & Skak, 2002), others have reached the opposite conclusion (Lindstrand & Lindbergh, 2011). Consequently, there are unfortunate gaps in our knowledge regarding to what extent, and in what ways, banks assist SMEs in their internationalization process. Addressing these gaps, this paper reports the findings of a survey that investigates how SMEs with varying export shares experience different forms of support potentially offered by their bank relationships. The study is based on an on-site survey of 135 Swedish SMEs that have entered a new foreign market within the last 7 years.

## FRAME OF REFERENCE

### **Small and medium-sized enterprises**

SMEs typically account for more than 90 percent of all firms and two-thirds of a nation's workforce (Baas & Schrooten, 2006). Not surprisingly, they are considered crucial for economic development at national as well as regional and local levels of society (Porter, 1990). Their well-being and growth is thus an important topic, both for practice and research.

For SMEs with limited home markets, international expansion is not only a way to spread investment costs, but also key to growth. It is however a development step that comes with challenges due to their limited resources (Coviello & McAuley, 1999; Lu & Beamish, 2001), for instance in terms of funding and knowledge about foreign markets. Entering a new market requires coping with paper work as well as finding information and ways to finance exports. The larger the firm's export share, the more important the international business and the challenges related to it. In the manufacturing industry, the export share has previously been related to factors like technology, R&D and innovation (Ioannidis & Schreyer, 1997), product quality (Brooks, 2006), international orientation (Moen et al., 2016), human capital and managerial factors (Bianchi & Wickramasekera, 2016) and top management team composition (Acar, 2016). This study addresses gaps regarding to what extent manufacturing firms with varying export share have received beneficial support from banks (Lindstrand & Lindbergh, 2011).

### **Bank services**

The bank relationship is key to firms' businesses (Tyler & Stanley, 2007); not the least, banks play an important role in the financing of SMEs (Durkin et al., 2013). Entering a new market entails handling a new situation which implies additional costs, for instance regarding search for suitable business partners, investments and customer credits, and absence of adequate funding is a major obstacle to such entrepreneurial processes (Westhead & Wright, 2000). While small firms may choose to, or simply have to, rely on loans from their family and friends (Hussain & Matlay, 2007), growth oriented firms usually depend on funding provided by banks, financial institutions or venture capitalists (Donckels, 2000; Kumar & Rao, 2015). This leads to the first hypothesis:

*Hypothesis 1: SMEs with high export shares find banks' loans or credits to be of high importance to the funding of their international business.*

Banks offer a variety of financial services, not only funding in the form of loans and credits, but also services related to payments and letters of credit (Binks et al., 2006). This complexity is however often not recognized in bank studies (Norberg, 2016). Moreover, SMEs cannot be

expected to act in the same manner and have the same needs. It seems likely that the more international business a firm undertakes, the more it will need to rely on various transaction and currency services for conducting its business in an efficient and profitable manner. Banks can then assist in making SME international operations and financial transactions flow more smoothly and efficiently. Addressing the variety of services offered by banks, the second hypothesis goes:

*Hypothesis 2: SMEs with high export shares find transaction- and/or currency services provided by their banks of high importance to their ability to do business abroad.*

### **Internationalization knowledge**

Many resources that are crucial for international business are knowledge based. While pursuing a business opportunity in a foreign market, firms cope with uncertainties to the best of their abilities, using their existing stock of knowledge (Barkema & Drogendijk, 2007). The knowledge residing in a firm or otherwise accessed by a firm will thus affect the feasibility of foreign-market-entry strategies and thereby the resulting scale and scope of the firm's internationalization (Saarenketo et al., 2008).

Some information needed is of a formal character, i.e. hard facts, and can be obtained from secondary sources. However, often also tacit knowledge developed from experience, so called experiential knowledge (e.g. Reid, 1984) is of importance, such as knowledge of foreign markets' norms and business cultures. Taken together, experiential knowledge and formal knowledge form a knowledge corridor that decides whether opportunities can be identified by a specific firm or not - and if so, how these opportunities will be evaluated and possibly acted upon (Shane, 2000; Venkataraman, 1997). The presence of internationally experienced management is therefore seen as a key ingredient in SME internationalization (Reuber & Fischer, 1997). When that resource is limited or not available, knowledge acquisition from external sources becomes fundamental to successful international market entry (Liesch & Knight, 1999; Musteen et al., 2014). Not surprisingly, small firms often rely on outside advice (McGee & Sawyerr, 2003; Silver et al., 2015).

### *Network relationships as conduits of knowledge*

Banks can be a source of business advice for SMEs (Binks et al., 2006). Nevertheless, bank interactions have usually been studied from the viewpoint of "transaction banking", that is, in the form of discrete exchange episodes, somehow isolated in time (Proença and de Castro 2000b). Only a minority of studies (Carson et al., 2004; Susan et al., 2004) have viewed banking relationships as including a mix of transaction-based and relationship-based interactions. Furthermore, although numerous business network studies have shown the importance of firms' relationships with business customers and suppliers, very few studies have dealt with the content of, and perceived contribution from, SMEs' bank relationships (Murray & Wallbridge, 2000), and the results have been contradictory.

Meyer and Skak (2002) found that the bank is a key networking partner for many SMEs, and one fifth of their respondents used their bank to obtain information on international markets. Lewis et al. (2007) found that for SMEs, bank representatives were among the most frequently turned to sources of support. Likewise, in the Swedish context, Boter and Lundström (2005) found that in comparison with auditors and legal advisers, employment service agencies, county administrative board, and national business-support organizations, banks were the most frequently mentioned source of advisory services. In fact, half of the

SMEs were in regular contact with a bank for advice. In contrast, however, Lindstrand and Lindbergh (2011) found that for internationalizing Swedish SMEs, in comparison with customers, competitors, suppliers, newspapers/magazines, trade organizations, databases, consultants and authorities, banks were the least used source of information, and banks did not participate in SME business networks during SME internationalizing. The majority of these SMEs did not consider banks to be valuable counterparts in their business networks.

Knowledge acquisition is often both time consuming and resource demanding. Cooperation with experienced firms, such as established multinational firms, is therefore an important option (Bradley et al., 2006). Banks can contribute to the development of the knowledge base through adhering or enriching the management vision and cognitive map (Basly, 2007), especially in relation to small firms and firms with limited experiential internationalization knowledge (Boter & Lundström, 2005). It thus seems likely that firms that have developed extensive international experience perceive a lesser need for banks' advice and gain lesser benefits from banks' knowledge than firms that only have limited experience of international markets. Hypothesis three and four thus read:

*Hypothesis 3: SMEs with low export shares find advisory services provided by their banks of high importance to their ability to do business abroad.*

*Hypothesis 4: SMEs with low export shares derive a high degree of benefits from their banks' knowledge of international markets.*

Moreover, banks may have valuable contacts with other international actors to share. For an SME with limited international experience and a small number of international actors within its network horizon, such recommendations could be a valuable contribution. In entering a new market, unfamiliarity with actors and relationships in that market, the liability of outsidership (Chetty et al., 2015; Johanson & Vahlne, 2009), is often a major obstacle that banks thus could assist in remedying. This line of reasoning thus leads to hypothesis five:

*Hypothesis 5: SMEs with low export shares derive a high degree of benefits in their international business from their banks' contacts with other international actors.*

## METHOD

### **Sample**

The sample consists of manufacturing SMEs (applying the European Union definition of less than 250 employees) that had entered a new international market within the last 7 years at the time of the survey. Based on data from Statistics Sweden, all firms fulfilling these criteria and located within five Swedish counties (Jämtland, Gävleborg, Västernorrland, Västmanland and Halland), in total 214 firms, were contacted by phone to check the criteria and set up a meeting for making the survey on site. In total, 168 firms (78,5%) agreed to participate in the study. However, some questions were left unanswered, resulting in a sample of 135 firms (63%). The main part of the unanswered questions is caused by the fact that the respondent lacked detailed knowledge of the bank relationship. Since there is no reason to believe that the choice of respondent made by the company is related to the questions, no bias is supposed to occur from the omitted observations.

### **Data gathering**

Each visit lasted between one and two hours. It began with a semi-structured, qualitative interview lasting about 20–30 minutes. Next, the survey was conducted. Making the survey on-site meant that we could check who completed the survey, provide explanations, and enhance their motivation by explaining the importance of the questions and assuring the respondent that there are no right or wrong answers, which improved data reliability (Holbrook et al., 2003; MacKenzie & Podsakoff, 2012). The respondent was usually the CEO (68%) or the sales manager (24%). Addressing the risk of systematic biases related to a common rater of both dependent and independent variables, we applied several remedies suggested by Podsakoff et al. (2003) and MacKenzie and Podsakoff (2012). First, we checked the ability to understand and answer the questions by pre-testing the survey on ten firms. Second, we separated the measurements of dependent and independent variables into different parts of the questionnaire to avoid answers based on the respondents' implicit theories on causal relationships and/or aims for consistency. Third, also reversed scales and different formulations of statements were used to disrupt undesirable response patterns and reduce the impact of social desirability in answering the questions. The latter effect was also achieved by the use of a self-administered method of data collection, that is, a traditional paper and pencil questionnaire.

### **Measures and control variables**

The dependent variable *export share* was taken from the information provided by the respondents in the survey as it cannot be found in any public records.

The items on the bank relationship are related to the most important bank in cases when a company has more than one bank relationship. The main variables measured are funding (bank loans and credits), transaction- and/or currency services, advisory services, knowledge shared and contacts provided. The items used are presented in Table 1. For the answers, a Likert scale (1-7) was used with 1 representing “I completely disagree” and 7 representing “I completely agree”.

#### TABLE 1 ABOUT HERE

In the hypotheses tests, 8 variables were controlled for in order to explain their respective effects on the export share, thereby isolating these effects from the effects of the main variables. Firm size, perhaps the most common control variable, was controlled for by firm *turnover* for the year preceding the survey (Bonaccorsi, 1992). In addition, firm *turnover per employee* for the year preceding the survey was calculated and controlled for in order to capture the possible influence of the type of firm. The number of years that have passed since firm inception (*firm age*) is an often-used predictor for the likelihood of firm internationalization. Moreover, in relation to banks, firm age is of further relevance as older firms have developed a track record and a reputation that is taken into account in funding decisions (Van Caneghem & Van Campenhout, 2012). Older, well-established firms are thus more likely to receive bank funding than new, small firms. The length of the relationship with the main bank (*relationship duration*) was included as a longer time period of interaction facilitates relationship development, which in turn increases the propensity to share information and give advice (Ford, 1980; Forsgren, 2016). The bank relationship duration was captured by the use of four intervals (years): <5, 6-10, 11-15, >16.

The firm's experiential knowledge was measured in terms of two dimensions: time - the number of years the firm has been conducting export (*years of export*) - and scope - the

number of international markets exported to (*number of markets*)). The longer the experience of acting on international markets, the greater the experiential knowledge is expected to be (Schweizer, 2012). Due to varying resource availability and varying strategies, some firms can be expected to act more proactive and actively search for information, for instance by contacting their banks asking for various services or advice, while others act more passively. Firm *proactiveness* in the form of amounts of time and resources dedicated to finding new international opportunities was thus included as a control variable using the item “In our company, we dedicate significant amounts of time and resources to finding new international business opportunities” (Likert 1-7).

## RESULTS AND CONCLUDING DISCUSSION

The results (table 1) provide a more nuance picture of the ways that banks support the internationalization of SMEs. The importance of bank funding was confirmed and so was the importance of transaction- and/or currency services provided by banks for SMEs’ ability to do business abroad, but with the important limitation that the effect diminishes as the number of markets increases, is absent when the level of about 30 markets is reached, and thereafter the effect turns negative. Furthermore, the results indicate that SMEs with a low export share attach a high importance to the advisory services that banks can offer regarding international business. Banks thus seems to support SMEs in certain respects but not to their full potential.

TABLE 1 ABOUT HERE

### **Managerial implications**

Technical advances facilitate the gathering of many forms of customer information, but the results from the presents study further underline the remaining challenges in building efficient relationships supporting both parties (Durkin & Kerr, 2016). SME managers could support this change by proactively inviting various forms of bank support.

### **Limitations and suggestions for further research**

The present study has limitations that can be addressed in future studies. Firstly, the sample only encompasses firms originating in Sweden, i.e. a developed country, and Swedish SMEs are likely to develop bank relationships with Swedish banks. Banks and SMEs originating in other countries may have developed other ways of interacting that lead to different results. The findings of this study should thus be examined against alternative samples. Furthermore, although this study has contributed to increased nuances in research on SME-bank relationships, there are still many aspects of banking services and the SME-bank relationships that have not been covered. In particular, a longitudinal study examining trends by addressing these issues over time would be welcomed.

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Table 1. Linear regression estimations for different models

Logarithm of export ratio is the dependent variable in all the models. Model 1 is a model with all the variables but with no interaction variables. In Model 2 to Model 10, one interaction at the time is tested in addition to the variables in Model 1. The p-values are calculated with heteroskedasticity-consistent covariance matrix estimation (White, 1980). Standard error in parentheses.

	log(export share)									
	Model 1 (1)	Model 2 (2)	Model 3 (3)	Model 4 (4)	Model 5 (5)	Model 6 (6)	Model 7 (7)	Model 8 (8)	Model 9 (9)	Model 10 (10)
Constant	2.13** (1.03)	1.98* (1.03)	1.51 (1.03)	1.79* (1.06)	1.78* (1.01)	2.21** (1.09)	2.74*** (1.06)	2.15** (1.07)	2.14** (1.08)	2.27** (1.08)
<b>Main variables</b>										
Funding	0.09** (0.03)	0.14 (0.09)	0.09** (0.03)	0.09** (0.03)	0.21*** (0.08)	0.09** (0.03)	0.09*** (0.03)	0.08 (0.06)	0.09** (0.03)	0.09** (0.04)
Transaction services	0.13*** (0.03)	0.13*** (0.03)	0.29*** (0.07)	0.13*** (0.03)	0.13*** (0.03)	0.12 (0.08)	0.14*** (0.03)	0.13*** (0.03)	0.13** (0.06)	0.13*** (0.03)
Advice	-0.12** (0.05)	-0.11** (0.05)	-0.11** (0.05)	-0.01 (0.12)	-0.11** (0.05)	-0.12** (0.05)	-0.23** (0.10)	-0.12** (0.05)	-0.12** (0.05)	-0.19** (0.08)
Knowledge	-0.07 (0.07)	-0.07 (0.07)	-0.07 (0.07)	-0.08 (0.07)	-0.07 (0.07)	-0.07 (0.07)	-0.08 (0.07)	-0.07 (0.07)	-0.07 (0.07)	-0.06 (0.07)
Contacts	0.05 (0.07)	0.05 (0.07)	0.06 (0.07)	0.05 (0.07)	0.04 (0.07)	0.06 (0.07)	0.05 (0.07)	0.05 (0.07)	0.05 (0.07)	0.05 (0.07)
<b>Control variables</b>										
Relationship duration	-0.12* (0.07)	-0.11* (0.07)	-0.13** (0.06)	-0.11 (0.07)	-0.11 (0.07)	-0.12* (0.07)	-0.12* (0.07)	-0.12* (0.07)	-0.12* (0.07)	-0.12* (0.07)
log(Number of markets)	0.42*** (0.08)	0.51*** (0.15)	0.84*** (0.14)	0.57*** (0.14)	0.42*** (0.08)	0.42*** (0.08)	0.41*** (0.08)	0.42*** (0.08)	0.42*** (0.08)	0.41*** (0.08)
Proactiveness	0.11*** (0.04)	0.11*** (0.04)	0.11*** (0.04)	0.12*** (0.04)	0.22*** (0.07)	0.09 (0.10)	0.02 (0.07)	0.11*** (0.04)	0.11*** (0.04)	0.10*** (0.04)
log(Turnover)	-0.03 (0.06)	-0.03 (0.06)	-0.03 (0.06)	-0.03 (0.06)	-0.03 (0.06)	-0.03 (0.06)	-0.04 (0.06)	-0.03 (0.06)	-0.03 (0.06)	-0.02 (0.06)
Turnover per employee	0.02 (0.02)	0.02 (0.02)	0.02 (0.02)	0.02 (0.02)	0.02 (0.02)	0.02 (0.02)	0.03 (0.02)	0.02 (0.02)	0.02 (0.02)	0.02 (0.02)
Years of export	0.01** (0.01)	0.01** (0.01)	0.01** (0.01)	0.01*** (0.01)	0.01*** (0.01)	0.01** (0.01)	0.01*** (0.01)	0.01* (0.01)	0.01 (0.01)	0.01 (0.01)
Firm age	-0.01* (0.003)	-0.005 (0.003)	-0.004 (0.003)	-0.01 (0.003)	-0.01 (0.003)	-0.01* (0.003)	-0.01* (0.003)	-0.01* (0.003)	-0.01* (0.003)	-0.01** (0.003)
<b>Interaction variables</b>										
Funding:log(Number of markets)		-0.03 (0.03)								
Transaction services:log(Number markets)			0.09*** (0.03)							
Advice:log(Number of markets)				-0.05 (0.04)						
Funding: Proactiveness					-0.03* (0.02)					
Transaction services: Proactiveness						0.004 (0.02)				
Advice:Proactiveness							0.03 (0.02)			
Funding: Years of export								0.0001 (0.002)		
Transaction services:Years of export									0.0001 (0.002)	
Advice:Years of export										0.003 (0.002)
AIC	328.871	330.144	324.056	329.386	327.932	330.836	328.849	330.865	330.867	329.281
Observations	135	135	135	135	135	135	135	135	135	135
R <sup>2</sup>	0.49	0.49	0.51	0.49	0.50	0.49	0.49	0.49	0.49	0.49
Adjusted R <sup>2</sup>	0.44	0.43	0.46	0.44	0.44	0.43	0.44	0.43	0.43	0.44

Note:

\*p&lt;0.1; \*\*p&lt;0.05; \*\*\*p&lt;0.01