



**UNIVERSITY OF GOTHENBURG**  
**SCHOOL OF BUSINESS, ECONOMICS AND LAW**

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## **Internationalization as a Necessary Evil**

Why Japanese SMEs Hesitate to Expand Internationally and the Manager's  
Influence on Internationalization Decisions

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## ABSTRACT

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Small and Medium-sized Enterprises (SMEs) have traditionally been restricted to their domestic market but as the world becomes increasingly globalized, so do also SMEs. SMEs represent over 95 percent of the business population in most economies, and thus contribute significantly to both domestic and global economic well-being. Japan is a country facing protracted economic stagnation and a shrinking domestic market; factors that ought to drive SMEs to expand internationally. However, Japanese SMEs are in fact less international than SMEs in comparable countries. This study aims to understand and explain why Japanese SMEs hesitate to expand overseas and how managers influence internationalization decisions. The research consists of a multiple case study, incorporating interviews with managers from five Japanese SMEs. The main finding of this study is that internationalization is perceived as a "necessary evil", primarily caused by factors driving SMEs to expand overseas. These factors include the shrinking domestic market, the fact that internationalization often is a result of a suggestion from a network partner rather than an intrinsic desire to expand overseas, and an outspoken domestic focus among SMEs. Moreover, Japanese SMEs lack internal resources, in particular language skills, and find international networking troublesome. Managers were found to greatly influence internationalization decisions, which largely depend on the manager's own capabilities to engage in international business, attitude towards international markets, previous international experience and degree of proactivity in searching for internationalization opportunities.

**Key words:** Japan, SMEs, internationalization, decision-making, and managerial influence.

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## LIST OF ABBREVIATIONS

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FDI	Foreign Direct Investment
FTA	Free Trade Agreement
IB	International Business
JETRO	Japan External Trade Organization
METI	Ministry of Economy, Trade and Industry
MEXT	Ministry of Education Culture, Sports, Science and Technology
MNE	Multinational Enterprise
R&D	Research and Development
RBV	Resource-Based View
SME	Small and Medium-sized Enterprise

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# 1. INTRODUCTION

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*The chapter begins with a background to the research area, followed by a problem discussion highlighting existing research gaps. The purpose of the thesis is then presented along with the research question guiding the study. Finally, delimitations of the thesis are outlined.*

## 1.1 Background

With the fragmentation of global value chains, technological advancements and better means of communicating, engaging in international business is no longer a privilege restricted to large multinationals (Hashim, 2015). The increasingly integrated world economy, as evidenced by the growing number of Free Trade Agreements (FTAs) (WTO, 2016), facilitates foreign market entry for SMEs. SMEs have traditionally been restricted to their domestic market but are becoming more and more involved in cross-border activities (Oviatt & McDougall, 1994, 1999; Ruzzier et al., 2006). SMEs play a crucial role in the global economy by contributing substantially to economic growth, employment, social and economic development and ultimately to an improved global economic vitality (Kogut & Chang, 1996; Préfontaine & Bourgault, 2002). SMEs constitute more than 95 percent of the business population in most economies (Lejárraga et al., 2014), and thus contribute significantly also to domestic economic well-being.

SMEs' internationalization is contingent on both internal and external factors to the firm (Olejnik, 2014). Gilmore et al. (2013) point out that the geographical context surrounding SMEs is important to consider in relation to internationalization, which is why SMEs' international expansion has largely been studied in different national context (e.g. Abdullah & Mohd Zain, 2011; Crick & Crick, 2014; Hashim, 2015; Ojala, 2009; Tang, 2011; Thai & Chong, 2013). SMEs' overseas expansion is of particular interest in countries seeking to boost economic growth, considering SMEs' ability to contribute to national income (Ruzzier et al., 2006). A country recognized worldwide for its protracted economic stagnation and "two lost decades" of economic growth is Japan (Breene, 2016). Japan's macroeconomic climate is characterized by slow growth, a rapidly ageing and since the year of 2010 even shrinking population (SMEA, 2014). The outlook is unfortunately also rather gloomy as the population is expected to continue declining from 126.6 million today (UN, 2015a), to 107.4 million in 2050 (UN, 2015b). Large-

scale efforts to revitalize the Japanese economy and reinvigorate their role in the world economy are currently being undertaken (Gillispie, 2013). While it may not last long, Japan still retains its position as the world's third largest economy (World Bank, 2016). Further, encouraging SMEs' expansion into foreign markets has become an increasingly important tool for Japanese policy makers to promote growth and raise productivity, highlighting SMEs' crucial role for Japan's future economic well-being (Cabinet Public Relations Office, 2014; SMEA, 2014). Japan does in fact have the highest proportion of SMEs among industrialized countries (Blair, 2010), evidencing the importance of studying SMEs in the Japanese context. Moreover, Japan's FTA coverage was 18.2 percent in 2013, but could grow to 84.2 percent if ongoing FTA negotiations come into force, which would represent one of the highest coverage rates in the world. With better access to international markets and a shrinking domestic market pushing SMEs to seek demand overseas, Japanese SMEs' ability and willingness to enjoy the benefits of internationalization are alarming concerns (SMEA, 2014).

SMEs' global expansion has received growing interest from international business scholars in recent years (e.g. Mejri & Umemoto, 2010; Olejnik & Swoboda, 2012; Ruzzier et al., 2006). This reflects the notion that SMEs face different challenges than large firms in their efforts to expand overseas (e.g. Fillis, 2001; Hashim, 2015). Often, SMEs' managerial style, ownership structure and scale and scope of operations differ from larger firms and cause their structures and processes to be less rigid, sophisticated and complex. Mudambi and Zahra (2007) suggest that SMEs' liability of newness and smallness hinder them from entering foreign markets. According to Gilmore et al. (2013), SMEs are often defined by what they lack; namely capital, human resources, rigid management structures and access to international markets. Barriers to overseas expansion can be external and contingent on the environment or internal and exist in the form of lack of capital, time, experience and information resources (Rialp & Rialp, 2001). Also, Zhao and Hsu (2007) point to SMEs' insufficient management capabilities. In particular, the manager's central role in small firms' international expansion is reflected in the growing body of literature on the subject (e.g. Axinn & Matthyssens, 2002; Jones & Coviello, 2005; Kyvik et al., 2013; Omri & Becuwe, 2014). Osei-Bonsu (2014) suggests that managerial factors such as entrepreneurial orientation, knowledge, experience and networking abilities of managers have a substantial influence on the development of organizational capabilities required for SMEs to

internationalize. In the case of Japan, Todo and Sato (2011) found that managerial characteristics, such as risk preference and prior international experience of the manager, play a significant role in SMEs' internationalization.

## **1.2 Problem Discussion**

Japan has been a popular object of study in international business (IB), much thanks to the giant manufacturers Toyota, Nissan, Sony, Matsushita and Honda to mention a few (e.g. Cusumano, 1985; Donoghue, 2014; Kotter, 1997; Marksberry, 2011; Takanori, 2002; Wickens, 1987). These multinationals grew and enjoyed enormous success overseas before the burst of the Japanese “bubble-economy” in the beginning of the 1990s. Large Japanese Multinational Enterprises (MNEs) have continued to attract attention of scholars also in recent years (e.g. Horn, 2016; Tang, 2013). This has contributed to that smaller Japanese firms have remained in the shadows of larger firms and received less academic interest. Wakasugi (2014) for example describes internationalization of Japanese firms but fails to account for SMEs' unique characteristics and challenges. Ruzzier et al. (2006) stress that trying to apply theories based on large firms to SMEs may generate awkward results, as ideas developed for large firms do not necessarily work in an SME setting.

Japanese SMEs have not enjoyed the same international reach and success as their larger peers and their focus remains primarily domestic. Westhead et al. (2002) connect SMEs' domestic focus to attitudes, resources, and behavior of the entrepreneurs and firms involved. Firms and their managers may refrain from internationalization as they are reluctant to commit their limited resources to expand internationally (Westhead et al., 2001). Japanese SMEs are in fact less international than SMEs in many comparable countries; they display a lower export propensity than SMEs in the U.S., most of Europe and many OECD members (EIM, 2010; OECD, 2013a). Direct exporting SMEs only represent three percent of all Japanese SMEs (SMEA, 2014), which can be compared to SMEs in the EU, where around 25 percent export to foreign markets (i.e. any market outside the domestic) and around 13 percent also beyond the internal EU market (EIM, 2010). Around ten percent of Japan's medium-sized enterprises are engaged in direct export, compared to 15 percent in the US and 32 percent in the EU (Yanagida & Ngiang, 2013). Moreover, the dominance of large firms in FDI activities is especially striking in Japan, where

around 80 percent of all foreign affiliates are owned by large firms and thus only 20 percent by SMEs. This can be compared to SMEs in the U.K., who own more than 60 percent of foreign affiliates, or the U.S., Germany and Korea, where the number is around 50 percent (OECD, 2013b). Considering the lower international activity combined with the growing need for Japanese SMEs to search for overseas customers when the home market is shrinking makes this case particularly interesting.

Already some 15 years ago, Lu and Beamish (2001) underlined the significance of studying internationalization of SMEs in the Japanese context. They stress the view of internationalization as an entrepreneurial activity, especially in the case of SMEs. As overseas expansion demands additional resources and involves higher risk-taking, SMEs embarking on this path display an entrepreneurial character. The authors chose to study Japanese SMEs specifically as this entrepreneurial trait was reinforced in the Japanese setting. Japan is a culturally isolated country, without any close counterparts (Ronen & Shenkar, 1985), and firms therefore face greater obstacles whenever business is conducted outside the domestic border, as it must be done in a very culturally, socially and linguistically different context. The greater the differences between the domestic context and the context into which the SME is expanding, the greater will the obstacles be and the more entrepreneurial spirit is required (Lu & Beamish, 2001). Also, Anderson and Eshima (2013) chose the Japanese context in their study of how entrepreneurial orientation influences firm performance in SMEs, as contextual and cultural factors are believed to influence firms' entrepreneurial orientation and entrepreneurship in Japan is largely under-researched.

Emphasizing the important role of managers in SMEs' internationalization, Jones and Coviello (2005) conceptualize internationalization as an entrepreneurial process connected to behavior, with the entrepreneur being a key influencing factor. Wright et al. (2007) call for more studies incorporating the behavior and characteristics of the manager when studying SMEs' internationalization. Various aspects of cognition have been thoroughly researched in the entrepreneurship literature but are less exploited in the internationalization literature. Cognition has predominantly been investigated at the firm level, why calls for studies on an individual level have emerged (Acedo & Jones, 2007). Zahra et al. (2004) also point out the need for more

research on the mindset of managers, and argue that their mental models influence decision horizons and risk preferences. Similarly, Zahra et al. (2005) observe that the cognitive perspective in the internationalization process has not received enough scholarly attention, and thus constitute an interesting aspect to explore. Consequently, they argue that further research on what goes through entrepreneurs' minds as they explore their firm's competitive global landscape, their motivations to expand operations abroad and how these motivations influence the internationalization design is needed.

In the case of Japan, Anand (2013) studied the internationalization of a family-owned SME, but only focused on mapping the process of internationalization itself. Todo and Sato (2011, 2014) take a starting point in recent research stating that the performance of firms determines whether or not they engage in international business. Suggesting that other factors than productivity in fact influence internationalization, the authors studied the effects of managers' characteristics on the internationalization of SMEs in Japan. They point out that SMEs with a risk-tolerant and forward-looking manager are more likely to internationalize, while managers' risk-aversion and myopia lead to an unwillingness to internationalize. After having found this correlation however, the authors do not make any effort in explaining the phenomenon any further, commenting on the extent to which these managerial characteristics prevail among Japanese SMEs and if so, why, and what implications this has for SMEs' level of international activity. In fact, little empirical evidence exist that addresses the reasons behind Japanese SMEs' low level of international engagement. With reference to the quoted studies on Japan, a more holistic understanding of the challenges facing internationalizing Japanese SMEs is needed. Moreover, Kuivalainen et al. (2012) call for more research on how external environmental factors affect internationalization decisions, and point out that evidence from non-Western markets could offer new insights. Against the background of the current economic situation in Japan, the low level of international activity among Japanese SMEs deserves academic attention. Given the importance of managers in SMEs' internationalization decisions (Axinn & Matthyssens, 2002), and especially in Japan (Todo & Sato, 2014), the extent to which the manager encourages or discourages overseas expansion should be clarified as it could offer important explanations for SMEs' internationalization behavior.

### **1.3 Research Question & Purpose**

The purpose of the study is to explain why Japanese SMEs hesitate to expand internationally and to analyze how managers influence internationalization decisions. The research question that will guide our study is as follows:

*Why do Japanese SMEs hesitate to expand internationally and how does the manager influence internationalization decisions?*

The study seeks to fill research gaps in the IB literature in the context of SMEs in Japan who are about to embark on expansion overseas or increase their commitment in overseas markets. This will be attempted by offering explanations to why SMEs hesitate to expand outside the Japanese market, given the benefits of internationalizing and the gloomy economic conditions domestically. Since contextual factors are believed to influence SMEs' internationalization (Jones & Khanna, 2006; Zahra et al., 2005), the need arises to conduct country-specific research from which conclusions can be drawn for that particular context.

### **1.4 Delimitations**

This study is conducted by interviewing practitioners in Japanese SMEs as well as external SME support organizations and experts. Since the study is based on a small number of cases, the results are likely to be firm-specific, which limits the generalizability of the findings to other SMEs in Japan. Furthermore, our sample of Japanese SMEs is a convenience sample representing the SMEs we were able to access. As it was not possible to use any kind of randomization measures, i.e., drawing a random sample of SMEs from a business register or similar, the sampling process involved grabbing given openings and opportunities to access SMEs. Hence, this has implications for the representativity of the SMEs included in this study. Moreover, the fact that the case companies are operating in the manufacturing sector makes the findings to a certain extent also industry-specific. More importantly is however the delimitation to the Japanese context, which reduces the findings generalizability to other national contexts. The interviewed case companies are based in or around Tokyo, and the findings may thus even be region-specific as SMEs originating from other parts of Japan might reason or behave differently. Finally, the research is conducted on SMEs, thus making our findings less applicable to large firms.

## 2. THEORETICAL FRAMEWORK

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*This section provides a framework of theories relating to SMEs' internationalization by considering previous IB literature within the research field. The chapter first introduces the concept of internationalization and continues by describing how international business scholars have explained SMEs' internationalization by looking at internal, network and external factors influencing SMEs' ability and willingness to expand overseas. Thereafter, particular focus is directed to how the role of managers in SMEs' internationalization is described. The section is concluded with a conceptual framework that synthesizes applicable theories and builds a foundation for subsequent data collection and analysis.*

### 2.1 The Internationalization Process

Within the confines of this thesis, the concept of internationalization is defined as “the process of adapting firms' operations (strategy, structure, resources, etc.) to international environments” (Calof & Beamish, 1995: 116). In accordance with the reasoning by Olejnik (2014), this definition emphasizes that internationalization can be understood as a process, that it is dynamic and subject to changing conditions in the international market place. The phrasing further refers to adaptation of operations, implying a behavioral approach to internationalization, where firms learn from accumulating knowledge and experience. The decision to expand internationally is furthermore closely linked to organizational aspects and is by no means a detached strategic undertaking; it is both dependent on and has implications for internal operations.

Theories on the internationalization process have mainly developed through two streams of research: one economic and one behavioral stream. While the economic approach (e.g. Buckley & Casson 1976; Dunning, 1980, 1988; Rugman 1980) is focusing on the company and its environment (Andersson, 2000), the central point of the behavioral approach is the individuals within the firm and their learning (e.g. Johanson & Vahlne, 1977, 1990). The economic approach presumes rationality and leaves a limited role for the manager to influence internationalization decisions (Andersson, 2000). The behavioral approach has its root in organizational theory and replaces the economic man with the behavioral man (Andersen, 1993; Andersson, 2000). Being the seminal paper of the behavioral school, Johanson and Vahlne (1977) were influenced by and

sought theoretical explanation from Cyert and March's (1963) behavioral theory of the firm. Johanson and Vahlne's (1977) theory describes a step-by-step approach taken by firms in which they acquire, integrate and use knowledge about external markets and operations gradually through commitment of resources and learning by doing. Individual learning and the role of the manager are thus important factors shaping a firm's international expansion path (Andersson, 2000). The stage model of internationalization has however received criticism for being deterministic (Reid, 1981) and as depriving individual managers of their strategic choices (Andersson, 2000). Moreover, there is a growing body of literature suggesting that firms do not follow the predetermined internationalization pattern suggested by the stage model.

## **2.2 SMEs' Internationalization**

Ruzzier et al. (2006) point out that mature large MNEs have dominated previous IB literature, while SMEs, and in particular their international activities, have only recently emerged on the agenda. Internationalization research has largely centered around large MNEs and the applicability of conventional theories to smaller firms has been questioned (Jones, 1999; Mtigwe, 2006; Zhao & Hsu, 2007). SMEs meet different obstacles and barriers when internationalizing, as for instance their ownership structure, culture and decision-making processes are different than in large firms (Coviello & McAuley, 1999). For this reason, it is important to distinguish internationalization of small and large firms. During the past decade, increasing scholarly attention has been paid to SMEs' international activities (e.g., Preece et al., 1999; Wolff & Pett, 2000), reflecting the growing importance of SMEs in international business (Colapinto et al., 2015).

In sharp contrast to the stage model, conceptualizations of the internationalizing SME as a Born Global (Knight & Cavusgil, 1996), International New Venture (Oviatt & McDougall, 1994) or International Entrepreneur (McDougall & Oviatt, 2000) have emerged. The Born Global literature observes that certain firms internationalize soon after inception and to distant markets at once; not as an incremental learning process suggested by the stage model (Knight & Cavusgil, 1996; McDougall & Oviatt, 2000; Oviatt & McDougall, 1994). The two approaches represent the opposite ends of a spectra, with the stage model suggesting that a firm concentrates



on few markets, while the Born Global concept suggests rapid diversification into a large number of international markets (Mas et al., 2006).

SMEs follow distinctly different internationalization paths and a number of factors influence the variation. Olejnik (2014) argues that both external and internal variables affect SMEs' international activities. According to Kuivalainen et al. (2012), a number of determinants at the environmental, firm and managerial level influence a firm's internationalization strategy, where firm and managerial influences can be categorized as internal and environmental influences as external factors. Opinions differ as to whether the external environment or internal resources is the primary determinant of foreign expansion. Seifert and Machado-da-Silva (2007) importantly point out that the external environment and internal resources seem to influence internationalization decisions differently. The external environment constitutes a contingency factor, whereas internal resources are facilitators of internationalization. In line with the resource-based view (RBV), it is also believed that the more resources a firm possesses, the less influence is exerted by external factors.

## **2.3 Internal Factors Influencing SMEs' Internationalization**

### ***2.3.1 The Role of Internal Resources & Capabilities***

The RBV argues that the environment alone cannot explain organizational behavior but that internal resources are important to consider in this respect. Internal parameters refer to a firm's internal resources available for overseas expansion. The RBV has its starting point in that firms accumulate tangible and intangible resources, which come to represent their sources of competitive advantage (Barney, 1991; Wernerfelt, 1984). A firm's resources can be categorized as assets and capabilities, where assets constitute a firm's accumulated resource endowments and capabilities represent the accumulated knowledge and skills that allow the firm to combine and utilize its assets successfully (Zou et al., 2003). Within economic internationalization theories, internal variables such as ownership advantages, product characteristics and communication ability are pointed out, while behavioral internationalization theories emphasize experiential knowledge and learning (Seifert & Machado-da-Silva, 2007). The resources needed for internationalization has gained more attention in recent years (Ruzzier et al., 2006). Ahokangas (1998) proposes that the internationalizing firm can be viewed as mobilizing unique and

interdependent resources that enable and contribute to the firm's internationalization activities. At the firm level, internal resources may both encourage and impede decisions to enter international markets. SMEs expanding into new markets are often believed to be disadvantaged in comparison with established domestic actors since they suffer from liability of newness and smallness, which are quoted as obstacles to enter foreign markets (Mudambi & Zahra, 2007).

### ***2.3.2 Knowledge-based, Financial & Human Resources***

SMEs commonly experience limited resources as a major obstacle to enter international markets (Coviello & McAuley, 1999). Internal resources that are necessary to internationalize successfully include the availability of knowledge-based resources (Mejri & Umemoto, 2010), financial resources (Cernat et al., 2014) and human resources (Brush et al., 2002). Westhead et al. (2001) argue that firms with older principal founders, possessing more resources in the form of for example information, networks and management capabilities are significantly more likely to be engaged in international business. Accumulation of knowledge-based resources in the form of management know-how, information about overseas markets and networking capabilities thus serve as an important facilitator of internationalization (ibid.).

Theories within the RBV emphasize the importance of intangible knowledge-based resources for firms' competitive advantage. Mejri and Umemoto (2010) argue that SMEs' internationalization is determined by market, experiential, network, cultural and entrepreneurial knowledge. They suggest that the firm's knowledge accumulation over time shapes its internationalization. Hashim (2015) states that SMEs' limited knowledge and experience at the international level constrain their internationalization, implying that knowledge and experience of how to conduct business in overseas markets facilitate expansion. Connected to the possession of knowledge-based resources is the ability for organizational learning required to develop new resources. The stage model (Johanson & Vahlne, 1977, 2009) rests on the idea that organizational experiential learning increases market knowledge and lead firms to increase their commitment in overseas markets. By accumulating knowledge and learning from experience, firms develop capabilities. Market knowledge can be learned only through personal experience and in such learning through experience, firms' organizational capabilities become central (Ruzzier et al., 2006). Moreover, the importance of financial resources in relation to internationalization is continuously reinforced

(Cernat et al., 2014). Starting international business is typically associated with additional costs and firms must therefore have financial muscle and maneuvering space to be able to internationalize. Greenaway et al. (2007) suggest that exporters exhibit better financial health than non-exporters. Strong financials is however no motivation in itself to start exports and export starters typically display poor financial health as a result of having to bear the sometimes high costs involved with the starting phase. Furthermore, sufficient human resources are in many aspects a prerequisite for firms to start international business. Brush et al. (2002) found that human resources were in fact the most crucial resources associated with internationalized SMEs compared with peers who remained domestic. Colapinto et al. (2015) further emphasized the importance of human resources to succeed internationally and found that language skills, knowledge of product innovation and marketing competences to meet the needs of customers in overseas markets facilitate internationalization.

#### **2.4 Networks as Facilitators of Internationalization**

Johanson and Mattsson (1988) suggest that interdependence between firms through networks has a strong influence on their internationalization process. The emphasis of network theory centers around the impact of informal and formal relationships on firms' internationalization (Coviello & Munro, 1995; Sullivan Mort & Weerawardena, 2006). A business network can be understood as the relationships a firm has with its customers, distributors, suppliers, competitors and the government. Participating in networks is frequently said to facilitate SMEs' internationalization. As a firm expands abroad, the number and strength of the firm's relationships increase and also extend to counterparts abroad; enabling access to resources and markets overseas (Johanson & Mattsson, 1988). Networks help firms to identify new market opportunities and contribute to accumulate market knowledge (Coviello & Munro, 1995). Chetty and Holm (2000) note that business networks may help firms to find new international opportunities, obtain knowledge, learn from experiences, and pool resources with other actors. Networks are important for all firms regardless of size, but due to SMEs' resource constraints, networking is particularly important as SMEs can pool resources with other actors. In networks, firms are no longer constrained by their internal resource limitations, but can utilize networks for resources and opportunities to internationalize (Chetty & Holm, 2000; Sullivan Mort & Weerawardena, 2006).

In describing the network approach, Johanson and Vahlne (2003) go as far as saying that there is in fact nothing outside the relationship and all relevant business activity is channeled through network relationships. Is it no longer country borders that constitute barriers to internationalization; only hinders in relationship establishment and development (ibid.). A *process* of international expansion is nevertheless to be expected. Similar to the conventional stage model, this process involves experiential knowledge development and commitment but instead about needs, resources and strategies of network relationships. Relationships develop gradually when firms learn from interaction with each other and commit themselves stronger to the relationship (Blankenburg Holm et al., 2015). In Johanson and Vahlne's (2009) revisited stage model they state that today's business environment consists of a web of relationships or business networks and suggest that entrepreneurs recognize opportunities much thanks to previous experiences from participating in such networks. It is opportunity recognition and exploitation that drive firms to internationalize, and in this process, they go from being outsiders to insiders in the foreign business network. Johanson and Vahlne (2009) found outsidership in relevant networks to be an even stronger determining factor for uncertainty than psychic distance. The lack of network knowledge constitutes a liability of outsidership just as lack of market knowledge constituted a liability of foreignness in their earlier model. Crick (2007) points out the challenge for exporting SMEs to ensure adequate representation in overseas markets and Kneller and Pisu (2011) similarly found that identifying the first contact overseas is problematic for internationalizing SMEs. Establishing a dialogue with potential customers and partners as well as nurturing networks overseas often constitute obstacles.

## **2.5 Using Networks to Overcome Internal Resource Constraints**

Relationships with external partners are believed to be at least as important as internal resources to realize market opportunities. Network theory thus assigns the firm's network position a strategic value, and regards this position as a resource in itself (Glückler, 2006). The network approach breaks with the strategic choice perspective and reduces the role of the manager's strategic decisions in explaining internationalization. Instead, it is network activities that are decisive in shaping internationalization. The decision to expand internationally typically arises as a result of partner initiatives, rather than a strategic decision taken by the firm itself (Johanson & Vahlne, 2003; Mtigwe, 2006). SMEs may be 'pulled' into overseas markets by partners in their

network, typically customers, who are themselves engaging in international activities. To not lose their position in the network, SMEs are therefore forced to internationalize, rather than that the decision originates from within the firm itself (Wright et al., 2007).

Ahokangas (1998) suggests that SMEs' internationalization is conditioned on the development or adaptation of internal and external resources. Resources can be adapted both within the firm (firm-oriented) and between the firm and its environment (network-oriented). This conceptualization results in four modes of adaptation that SMEs attempt when trying to internationalize. Adjustment of internal resources in a firm-oriented mode is displayed by the firm that alone tries to internationalize by learning from experience. If internal resources are adjusted in a network-oriented mode, firms engage in cooperation with external firms to develop for example R&D activities jointly. Similarly, adjustment of external resources in a firm-oriented mode involves for example help from support organizations, while adjustment of external resources in a network-oriented mode involves sharing control over resources in for example a joint venture. Considering this idea developed by Ahokangas (1998), it is argued that the RBV and network theory are in fact intimately intertwined. The combination of a firm's internal and external resources arising from network participation constitutes the entire set of resources available for internationalization. Firms' ability to combine and leverage their own internal resources with external resources residing in their network thus largely determines their ability to internationalize.

## **2.6 External Factors Influencing SMEs' Internationalization**

External parameters influencing SMEs' internationalization highlight the impact of the environmental context in which the SME is embedded. Zahra et al. (2005) voice the importance of recognizing the context when studying internationalization decisions and activities, and refer primarily to firms' geographical context. Kuivalainen et al. (2012) argue that environmental factors are important to consider as they may push firms to internationalize or on the contrary hinder entry into foreign markets. Wright et al. (2007) point out that the domestic environmental context may influence SMEs' internationalization. Motivation to engage in international trade may arise from a limited size of the domestic market (Kaynak & Kothari, 1984) and/or protection against an economic slowdown at home (Morgan & Katsikeas, 1997). The size and

stability of the home market influence whether a firm expands overseas. Olejnik and Swoboda (2012) explain that SMEs from large economies are more likely to internationalize later than SMEs from small economies as the vast size of the domestic market can be exploited for a longer time before the SME is pushed to internationalize in search of overseas opportunities. Dimitratos et al. (2004) noted in the example of Greece that SMEs internationalize first and foremost as a response to the uncertainty of the domestic environment. A firm's growth orientation, understood as the motivation to seek growth overseas, is further positively correlated with the scope of international expansion (Nummela et al., 2005).

Relating to SMEs' external context, Peng et al. (2008) consider the role of institutions in shaping firms' strategic direction. They argue that institutions have been assumed in the 'background' but that the influence of formal and informal institutions can be considerable in shaping international activities. Adhering to the institution-based view, DiMaggio and Powell (1983) coined the term institutional isomorphism and argue that organizations that operate in the same environment are pressured to become homogeneous, thereby highlighting the importance of external influences. As firms face similar external conditions, they also adopt similar practices, i.e. internationalization strategies, as other firms around them. Formal institutions also play a significant role, where for instance policy measures and government support can facilitate SMEs' international expansion (Hashim, 2015; Wright et al., 2007).

## **2.7 International Entrepreneurship: Managers' Role in SMEs' Internationalization**

When researching internationalization of SMEs, Ruzzier et al. (2006) stress that one should not fail to account for the importance of entrepreneurs, who are often suggested to be the most important factor in SMEs' internationalization. The manager can accumulate human and social capital, which generate important know-how, physical and financial capital necessary to grow the firm, and organizational capital to sustain the firm's competitive advantage (Brush et al., 2002). Axinn and Matthyssens (2002) state that the role of managers in internationalization decisions is undervalued, and that managers play an increasingly important role for internationalization strategies. Already in earlier internationalization research focusing on a firm's export process (e.g. Leonidou et al., 1998; Reid, 1981), emphasis was placed on the central role played by top management teams.

A fairly new stream within the internationalization literature is International Entrepreneurship, which entails the “combination of innovative, proactive, and risk-seeking behavior that crosses national borders and is intended to create value in organization” (McDougall & Oviatt, 2000: 903). Zahra and George (2002) explain international entrepreneurship as the process of creatively discovering and exploiting opportunities that lie outside a firm’s domestic market in the pursuit of competitive advantage. Jones and Coviello (2005) conceptualize internationalization as an entrepreneurial process connected to behavior, with the entrepreneur being a key factor influencing the structure of the firm. The firm structure then shapes the internationalization behavior and ultimately the firm’s performance. In contrast to the stage model, which fails to acknowledge that managers have the possibility to make strategic choices, international entrepreneurship recognizes that managers indeed make strategic decisions (Ruzzier et al., 2006). Similarly, Foss et al. (1995) point out managers' strategic decision-making and the need to identify which international activities the firm should undertake among possible options. In joining the entrepreneurship literature and the RBV, Alvarez and Busenitz (2001) view the entrepreneur as an important resource that builds competitive advantage within the firm and thus moves away from the firm-level analysis which dominates the RBV towards an analysis of strategic resources on an individual level. From the perspective of the entrepreneur’s social network ties and how these enable firms to identify opportunities to internationalize, Ellis (2011) found that opportunities more often were ‘discovered’ than ‘sought’ but point out that discoveries seldom were accidental but on the other hand to some degree deliberate.

### ***2.7.1 Managers’ Experience & International Orientation***

Olejnik and Swoboda (2012) point out that the manager’s capabilities, characteristics, experiences, and orientation are important factors influencing SMEs’ internationalization patterns. More specifically, Acedo & Jones (2007) suggest that managerial factors such as international orientation, growth orientation, proactivity and attitude towards risk and ambiguity shape international activities. Using ideas from psychology and strategic management, managerial cognition helps to explain why some firms rush into foreign markets and why others hesitate. Managers who are proactive, internationally orientated and tolerant to ambiguity perceive internationalization as less risky and expand quicker. Managers who, on the other hand, perceive risk as high may slow down or even prevent internationalization. Expanding overseas is

riskier than staying domestic and the manager's perception of risk and risk tolerance is thereby influencing internationalization as managers perceive opportunities, resources and risks in different ways, resulting in different internationalization behavior (Acedo & Jones, 2007). Olejnik and Swoboda (2012) suggest that a manager with international orientation displays a positive attitude towards international activities. They further state that the concept of international orientation includes the international outlook, which in turn relates to the perceived psychic distance and the global mindset of the manager. Sato and Todo (2014) investigated managers' influence on internationalization in Japanese SMEs and found that when managers are more risk-tolerant and forward-looking, firms are more likely to be internationalized. Managers' risk aversion and lack of foresight on the other hand caused an unwillingness to be internationalized.

Suárez-Ortega and Álamo-Vera (2005) suggest that management characteristics, attitudes and perceptions influence SMEs' export behavior and refer to objective characteristics such as language proficiency and overseas experience and subjective characteristics such as risk and change aversion, dynamism and flexibility. Export propensity and intensity were found to be positively related to management attitudes to exporting, level of experience in geographic market development, as well as foreign language skills and previous experience abroad. De Clercq et al. (2005) point out that international experience plays a crucial role for the pace and direction of internationalization, highlighting the importance of organizational knowledge in forming internationalization strategies. Manolova et al. (2002) found evidence that managers with previous personal experience from overseas markets develop an international orientation, which makes them more inclined to internationalize.

### ***2.7.2 Managerial Decision-Making in SMEs***

The manager's perception of internationalization is likely to be influenced by his or her external context. Zahra and George (2002) place the individual at the start of the internationalization process but emphasize that individuals are influenced by external environmental factors as well as strategic factors in their decision-making. The mindset of managers can thus be said to be connected to the environment in which the firm operates and context in which it is embedded. The notion that managers act on deliberate, strategic decisions can however be questioned. SMEs



are often characterized by informal structures and processes and act on opportunities presented to them rather than follow a strategically outlined path. A relevant question is thus to what extent SME managers actually pursue strategic choices or whether the internationalization rather could be described as haphazard and opportunistic (Fillis, 2001). Papadopoulos and Denis (1988) note that few SMEs in fact analyze the market systematically before internationalizing. The decision-making in relation to internationalization is better described as fragmentary and subject to bounded rationality (Björkman & Forsgren, 2000).

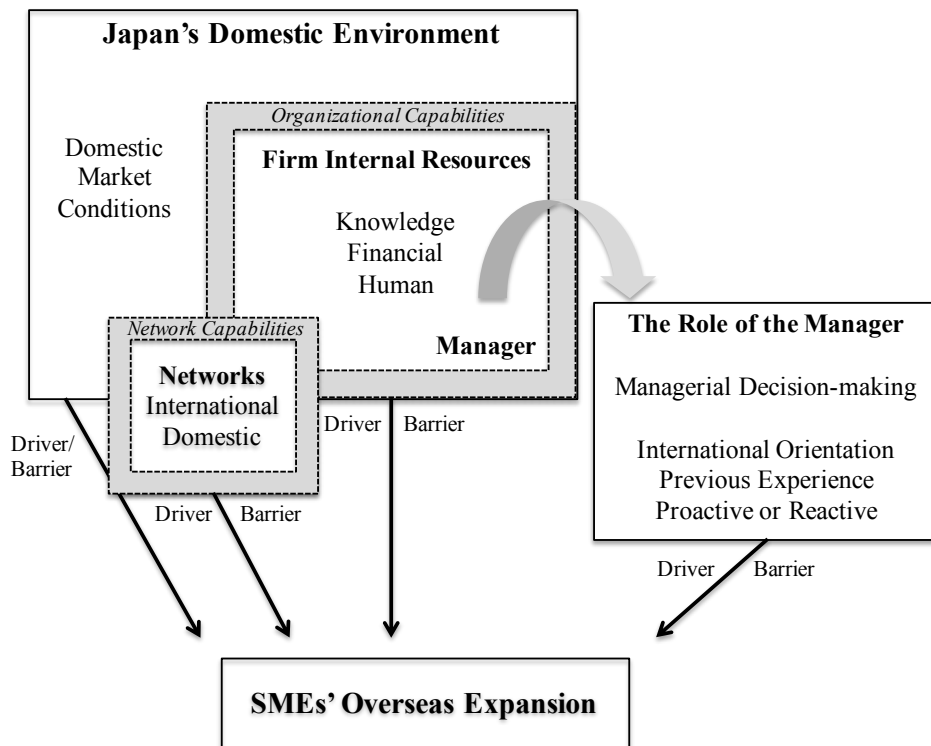
Managerial perception of internationalization can act as a barrier to internationalization; managers may carry misconceptions of prevalent conditions on international markets and lack accurate knowledge about overseas business environments. Smith et al. (2006) found in a comparative study of managers from the U.S. and India that differences in managerial perception of export barriers could explain differences in their level of export activity. This indicates that limitations in the actual or perceived resource requirements to internationalize appear to differ depending on the regional context.

In terms of how internationalization opportunities are recognized, managers can be described as taking either a proactive or reactive stance. Proactive managers are believed to search for opportunities, take initiatives and be change-oriented (Bateman & Crant, 1993). Similarly, Wright et al. (2007) state that the entrepreneur's cognitive processes may play a significant role in international opportunity identification and evaluation. Entrepreneurial behavior related to internationalization further implies being able and prepared to identify and exploit opportunities in foreign markets (Simon et al., 2000). Yet, to understand the behavior of more traditional SMEs, it may be appropriate to discuss the lack of such orientation to explain why some firms expand slowly, gradually or not at all. Traditional SMEs display a more reactive internationalization behavior by first exploiting their domestic marketplace before being pushed or pulled into foreign markets.

## 2.8 Conceptual Framework

To make sense of the outlined theoretical perspectives and illustrate how they guide the forthcoming empirical evidence and analysis, a conceptual framework is presented. This conceptual framework, as seen in Figure 1, positions the thesis in the body of literature on the topic.

*Figure 1: Factors Influencing SMEs' Overseas Expansion*



Note: Figure compiled by authors.

A number of external and internal factors are believed to influence SMEs' internationalization. External factors relate to the environment or context in which the firm operates, and constitute the prevailing domestic market conditions surrounding SMEs. These aspects can both act as drivers, either facilitating or pushing SMEs out of their home market, or as barriers to internationalization. Internal resources available to the firm also influence SMEs' internationalization. Adequate internal resources are in many ways a prerequisite to

internationalize, and lack of such thus act as a barrier. The most important resources for internationalization are assumed to be knowledge about how to internationalize as well as knowledge about overseas markets; financial resources to be able to bear the additional costs associated with internationalization; and human resources with sufficient skills, experience and willingness to help the firm expand overseas. Moreover, internationalization can be conceptualized as a learning process requiring organizational capabilities to adapt and develop resources to overseas markets. This means that SMEs' resources are not considered to be static but rather dynamic and subject to adaptation, depending on the nature of SMEs' organizational capabilities.

SMEs' most crucial internal resource to expand overseas is assumed to be the manager. Managers play a central role and their entrepreneurial spirit is believed to shape the international direction of SMEs. Decision-making depends on the manager's international orientation, previous international experience and the degree of proactivity or reactivity in regards to opportunities to expand overseas. These managerial parameters can thus drive internationalization as well as constitute a barrier.

Domestic and international networks act as a bridge between internal resource endowments and overseas markets. Networks are believed to provide resource-scarce SMEs with additional resources and opportunities to interact with business partners in overseas markets. Participation in networks may drive internationalization decisions and lack of such networks consequently acts as a barrier. Also, SMEs' network position is dynamic and subject to adaptation and development over time. SMEs' network capabilities thus influence their ability to utilize resources and opportunities embedded in networks, which in turn shape their ability to internationalize.

### 3. METHODOLOGY

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*This chapter describes the methodology used when conducting the research and collecting the empirical data. The techniques and approaches applied when analyzing the data and ensuring reliability and validity of the empirical findings are outlined and discussed.*

#### **3.1 Research Approach**

##### ***3.1.1 Explanatory Purpose***

This study aims to add explanatory insights about the apparent hesitant attitude among Japanese SMEs towards internationalization by considering the determinants and underlying reasons behind their internationalization behavior. The study further investigates *how* managers influence internationalization decisions. According to Yin (2014: 10), *how* and *why* questions are often explanatory in nature. To be able to conduct this explanatory study, a qualitative research method is used to show a nuanced picture of the phenomena being investigated.

##### ***3.1.2 Theory & Research***

This research is in many ways using theory as a starting point by allowing previous research to guide the data collection, and formulate approaches that could be applied to the observed phenomenon. A deductive approach is thereby permeating the study (Eriksson & Kovalainen, 2016) as the rich theoretical body about firms' internationalization was drawn upon and applied to the context of Japanese SMEs. During the data collection phase, the empirical evidence were however found to contrast the probable hypothesis suggested by theory. The relevance to theory was not always distinct and gaps that were not accounted for in the literature were identified. Japanese SMEs seemed to view and approach internationalization in a different way than suggested by theory and there seemed to be a research gap concerning the perception of internationalization among these firms. Instead of simply testing existing theories by applying them to the Japanese context, this research incorporates the observed phenomenon and seeks to explain it, following an more inductive approach. The conceptual framework, developed from previous research, is updated and modified according to the observed phenomenon and thus feed this piece of empirical finding back into theory. In this way, the link between research and theory can be described as abductive; a more pragmatic approach where elements of both deduction and

induction are incorporated. Their limitations are overcome as the research alternates between the literature and the social world (Bryman & Bell, 2015). With a research process moving back and forth between theory and empirical data, this helped us to critically reflect on the theoretical framework and to evaluate its applicability and relevance in the Japanese setting.

### ***3.1.3 Considerations from a Philosophy of Science Perspective***

When researching social actions and behaviors, it is useful to reflect on the epistemological perspective taken regarding the observed findings and the reality in which these are produced. This thesis positions itself in connection to the interpretivist research philosophy, which considers how actors experience and interpret social settings and how this influences their behavior (Snape & Spencer, 2003). The aim is to *understand* rather than *explain* social behavior and subjective meaning, and in particular to understand individuals' perception and experiences from their own point of view, leaving out the researchers' own preconceptions and biases (Bryman & Bell, 2015). The firm's perception of its surrounding, its resources and external environment will affect how it views international entry or expansion and consequently the action taken by the firm in this regard. As perception is a highly subjective construct, efforts have been taken to, in the best way possible, capture individuals' subjective experience. This resonates with the idea of a cognitive scheme residing in managers as argued by Seifert and Machado-da-Silva (2007), which influences how external factors and internal resources are perceived. By adhering to the interpretivist philosophy, and collecting Japanese SMEs' own words and opinions, the research design enables us to capture and understand the subjective experiences residing in our research objects.

Closely related to the epistemological viewpoint is the ontological assumption, which instead concerns the conception of reality. This thesis holds a subjective, or constructionist assumption, in which reality is understood as a social construct, subjective and different depending on the individual or group (Eriksson & Kovalainen, 2016). It is important to shed light upon the assumed subjective nature of knowledge and reality, as our empirical findings per definition constitute managers' subjective perception of internationalization.

## **3.2 Research Design**

Qualitative research has the ability to capture perspectives and views of participants in a study (Yin, 2011), which is what this research sets out to do. Further, qualitative research enables contextual conditions to be studied, as well as their impact on the situation being analyzed. For example, both social and institutional conditions in the Japanese context are assumed to impact firms' internationalization in this study. Since this study aims to explain why Japanese SMEs hesitate to expand internationally, a qualitative study is appropriate as it enables deeper understanding of the phenomenon itself, the contextual influences and the subjective experience held by managers and external parties. The complexity of the field and the diversity of participants in the study are other reasons for choosing a qualitative approach in which data from different sources can be compared, analyzed and presented (ibid.).

The primary empirical data is gathered through a case study format. Case studies are suitable when the research sets out to generate in-depth, holistic and contextual knowledge as they investigate the case in relation to its historical, social, economic and cultural context (Eriksson & Kovalainen, 2016). According to Yin (2014), a case study design is suitable when the research is guided by *why* and *how* questions and when a current phenomenon is being studied in a real life context where the researcher has little or no control. It allows an object to be studied in its natural setting and is therefore especially useful in international business research, when data is collected in cross-cultural settings or when the impact of the national context is being investigated. The depth enables theory building in addition to theory testing and the holistic viewpoint allows the research object to be studied from several angles and perspectives (Ghauri, 2004). Yet, this research follows a multiple case study logic, where 'thick description' from a single case is not the primary undertaking. Rather, this thesis aims to map common patterns, mechanisms and properties in a certain context to be able to develop and elaborate on existing theories within the field, as proposed by Eriksson and Kovalainen (2016).

### **3.2.1 Research Unit**

The empirical data was collected through studying multiple firms in an extensive case study, where the purpose is to extend existing theory by using more than one case (Eriksson & Kovalainen, 2016). The case itself is not the highlight but rather the phenomenon common

among the cases. It is the shared experiences between firms rather than the contrasting differences that are the basis for analysis. Multiple case studies have an advantage of giving more robust and generalizable findings than a single case, which increases the external validity of the findings (Marschan-Piekkari & Welch, 2011), and allows us to provide a more comprehensive picture of Japanese SMEs' internationalization. Similar questions were asked in the organizations and then compared in order to formulate findings and conclusions as suggested by Ghauri (2004). Collecting data from several cases and a number of external expert opinion-holders greatly strengthens the thesis as similar evidence was found across all interviews. Nuances naturally prevailed, but many experiences and perceptions were in fact shared among the respondents.

As the research question aims to understand why Japanese SMEs hesitate to expand internationally, the empirical evidence is gathered from Japanese SMEs. Five different Japanese SMEs were selected, representing the five cases in this study. The number of cases reflects Eisenhardt's (1989) recommendation of between four to ten cases for a multiple case study. Two categories of SMEs were picked; SMEs that are internationalized, either through exports or a foreign affiliate, and SMEs that are not yet active in international business but who wish to expand overseas in the future. Interviewing two types of SMEs allowed us to shed light both upon how internationalization is perceived by SMEs that have not yet taken the step into foreign markets and by SMEs that have. It provides a dynamic perspective by employing companies in different stages of their internationalization. The companies are all operating within the manufacturing industry, allowing us to limit for industry-effects. The firms are of very different age, with the oldest being established already in 1872 and the youngest in the year of 2000. Another relevant aspect is the ownership structure of the case companies. Apart from one firm, which the manager founded himself, the rest of the firms were all family-owned and had passed on from older generations. Moreover, the enhanced importance of the manager in SMEs is emphasized by e.g. Jones and Coviello (2005). By interviewing the manager of the case companies, we were able to discern the role played by the manager in shaping internationalization decisions and answer the second part of our research question. The managers interviewed were thereby in themselves research units, in addition to the companies they represent.

To complement the evidence from the case companies, a number of external parties were included in the research to provide additional perspectives on internationalization of Japanese SMEs. Two organizations who work intimately with and support SMEs were interviewed along with two professors who have in-depth knowledge about Japan's corporate environment. The Director General and one Deputy Manager from the semi-governmental agency Organization for Small and Medium Enterprises and Regional Innovation (SMRJ) provided interesting insights from an institutional perspective and from their vast experience of helping SMEs wishing to internationalize. An interview was further conducted with the founder of the non-profit organization Hasekura Program, who provides international business exchange and training programs for Japanese SMEs. The two professors, Professor Suzuki at Meiji University and Assistant Professor Edman at Hitotsubashi University in Tokyo, provided a scientific perspective with insight from academia about the behavior of Japanese firms and the structures of corporate Japan. The external perspectives contributed to giving a more balanced view and to increase the generalizability of the findings as the respondents called upon their accumulated knowledge from many different SMEs. Besides, they added valuable insights into the characteristics and structure of the Japanese economy and explanations with cultural and historical connotations.

### ***3.2.2 Data Collection Method***

Primary data was gathered through nine interviews, out of which seven were face-to-face interviews in and around Tokyo and the other two were held electronically over Skype. The interviews took place in the period between March 9 and April 1, 2016. The seven face-to-face interviews were conducted at different locations, typically at the organization being interviewed. For more information about the interviews, see Table 1.



*Table 1: Interview List*

Company/Organization	Respondent	Position/Job Title	Interview Method	Location	Duration	Date
Anything Co., Ltd	Kazuhiro Nishimura	President	Face-to-face, English	Tokyo, Japan	60 min	March 9, 2016
Nihon Shinkan Co., Ltd	Naoyasu Hosonuma	President	Face-to-face, Japanese (translator)	Saitama, Japan	120 min	March 14, 2016
Kojima Senshoku Co., Ltd	Hideyuki Kojima	President	Face-to-face, English	Saitama, Japan	50 min	March 22, 2016
Wakoh Co. Ltd	Hiroshi Kokubun	Executive Director	Face-to-face, English, Joint Session	Tokyo, Japan	60 min	March 22, 2016
Azumaya Ltd	Maki Kido	Representative Director				
SMRJ	Shinichi Murai	Director General	Face-to-face, Japanese (translator), Joint Session	Tokyo, Japan	120 min	March 10, 2016
Business Partners K.K.	Toshiyuki Ookubo	Certified SME Management Advisor/Consultant				
SMRJ	Masaya Yaguchi	Deputy Manager	Face-to-face, English	Tokyo, Japan	60 min	March 23, 2016
Hasekura Program	Renata Piazza	Founder and Director	Skype-Interview, English	Gothenburg, Sweden (authors) & Barcelona, Spain (respondent)	60 min	April 1, 2016
Meiji University	Kenji Suzuki	Professor at School of Global Japanese Studies	Face-to-face, English	Tokyo, Japan	60 min	March 18, 2016
Hitotsubashi ICS	Jesper Edman	Assistant Professor in International Business Strategy	Skype-Interview, Swedish	Gothenburg, Sweden (authors) & Tokyo, Japan (respondent)	60 min	March 30, 2016

Note: Table compiled by authors.

With reference to the Japanese business culture, which largely builds on relationships and network belongingness, contacting SMEs directly without having a common reference person to establish a connection is very troublesome. Introduction through a shared business contact will greatly facilitate the process, and this was therefore the approach taken. Most interviews were booked prior to the research trip to Japan. Yet, additional interviews were scheduled through interviewees that referred us to other contacts that they believed would be valuable to our study, a method referred to as ‘snowball sampling’ (Yin, 2011). This greatly facilitated the access to research objects because of the importance of networks and relationships in Japan. As a first step to approach suitable case companies, we reached out to the organization Japan Institute of Scandinavian Studies in Tokyo. We were able to utilize the relationships and contact network of members of this organization, and subsequently the three case companies currently involved in international business were selected. The two SMEs not yet involved in international business, were referred to us by one of the respondents.

The number of research units and consequently the number of interviews was determined by a combination of data saturation (Bryman & Bell, 2015) and our limited network in Japan, which constrained the number of companies we could reach out to. Time constraints also had an impact

since it was necessary for us to be physically present in Japan to conduct interviews. The possibility of conducting electronic interviews with SME managers instead of face-to-face interviews was not realistic in most cases. This relates to the Japanese business etiquette, where relationship and trust building should preferably precede the formal interview. The conducted interviews were typically associated with a ceremonial greeting, extensive introduction and small talk before the interview process began. At several occasions we were also given a tour of the factory or office. Such relationship building activities are not possible during an electronic interview, which is why the duration of our *sejour* in Tokyo constrained the number of case companies.

The interview approach chosen for this study was semi-structured interviews as this approach allowed us to retain structure and stick to important themes, while at the same time allowed respondents to share the experiences and ideas they believed to be important. Because of the multiple case study design, a certain degree of structure is needed to be able to compare the gathered data across cases. An interview guide (see Appendix 1) was therefore developed. At the same time, it is important to grasp each individual's experience and subjective opinion about the themes discussed, which may require the researcher to depart from the interview guide (Bryman & Bell, 2015). Additional questions were asked in instances when we wanted to follow up on something the interviewee said. The interviewee was free to answer the questions in the way preferred but if language barriers became too pressing and the meaning of the question did not come through to the respondent, we clarified the purpose of the question in more detail.

As a complement to the primary data gathered through interviews, secondary data was collected in the form of written documents such as case reports and publications on the studied topic, allowing for triangulation of the findings (Yin, 2014). This secondary data describes the current situation that Japanese SMEs face with regards to internationalization and serves as a context to the primary data.

### ***3.2.3 Interview Protocol & Interview Process***

Data was collected and analyzed using an interview guide designed for the purpose of obtaining deep and rich qualitative insights into the phenomenon under investigation. The guide was

adapted to suit the type of respondent, the supporting organizations were for instance asked somewhat different questions than SME managers, but the themes and key concepts remained the same. The interview guide designed for SMEs contained a number of structured questions designed to gather data for classification purposes as well as a series of open-ended questions to examine the strategic directions of firms and underlying motives for internationalization decisions. Particular focus was placed on examining the manager's orientation towards internationalizing; whether it was found important, how it was perceived (e.g. as an opportunity, a necessity or as a challenge), to what extent it entailed risk-taking and the experienced barriers to expansion. Questions relating to the manager's role, background and previous international experience were asked to assess how the manager influenced internationalization decisions. For the not yet internationally active SMEs, focus was placed on investigating their perceived barriers. The interview guide designed for the external organizations and professors covered the very same themes but aimed to capture their external perspective and experience of SMEs' internationalization to give a more balanced and nuanced picture.

The physical interviews were in all cases but one conducted at the factory or office of the responding firms. Field notes were taken during and after interviews to ensure that we captured what we saw, heard and experienced and to avoid being too dependent on memory, in accordance with Bryman and Bell (2015). Both researchers were present during all interviews and split the task of posing interview questions between us. Six interviews were held in English, two in Japanese and one in Swedish. Except for Mrs. Piazza, the founder of Hasekura Program who is Italian and Professor Edman who is Swedish, the respondents are of Japanese origin. During the two interviews when the respondent spoke Japanese, an interpreter was used between the Japanese and English language. Professor Kenji Suzuki was the interpreter during the interview with Mr. Murai and Mr. Ookubo, and Eriho Fujita, Husqvarna Zenoah Co., Ltd. was the interpreter during the interview with Nihon Shinkan. Using an interpreter may influence the data collected as the words and meanings expressed by the respondent is filtered through a third person, who may add or remove meaning during the translation due to a predetermined bias (Temple & Young, 2004). Therefore, we paid careful attention to ensuring that the interpreters were well informed about the purpose of our study, understood the questions posed and the importance of interpreting 'exactly' what the respondent said without modifying the meaning.

The interpreters were fluent in both English and Japanese, had considerable experience from working in Japan and internationally and good insight into the business of the responding firm or organization as well as the purpose of our study. We are therefore confident that the use of interpreters kept alteration of the data to a minimum and that this did not compromise the trustworthiness of our findings.

In cases when the respondent felt comfortable with the English language, there were nonetheless language barriers that influenced how questions were interpreted and the respondent's ability to express his or her opinion or experience (Tsang, 1998). This led to that certain questions needed to be simplified and that answers did not entail the full complexity of the situations. We did our best to optimize the interviews where language barriers prevailed by encouraging the respondent to take the time he or she needed and to express themselves in the way they felt most comfortable. Given language challenges as well as the interactive process of all interviews, the possibility of 'interview artefacts' prevails, i.e., that we as interviewers were influencing the content of given responses.

### ***3.2.4 Data Analysis Method***

All interviews were recorded and transcribed one to two days after the interview had been conducted to permit a thorough examination of the data (Bryman & Bell, 2015). The interview held in Swedish was translated to English during the transcription phase. Xian (2008) notes that translation is more of an interpretative process rather than simply a technical procedure as the researcher interacts with the data. We ensured data accuracy by translating as close to the meaning as possible. In accordance with Ghauri (2004), the data analysis ran parallel to the data collection phase. This allowed theory to develop simultaneously to data collection and helped us to identify shortcomings in our data collection technique, as learnings and experiences of the first interview helped us to improve how we conducted the following interviews.

The nine interviews were transcribed and then coded and categorized in a systematic manner, which was facilitated by the semi-structured interview approach. The coding ensured cross case comparability, which is highly relevant in multiple case studies (Bryman & Bell, 2015). Transcripts were coded individually and compared with the field notes taken to avoid that data

was misinterpreted. The scope of the transcripts allowed for coding and categorization to be performed manually, in which every paragraph was read and analyzed thoroughly to detect the areas and points discussed. According to Saldana (2009), manual coding gives the researcher better control over and ownership of the work, and adds a literal perspective that is not always possible when using electronic coding. In addition, moving from coding to categorization of data into themes and concepts was made easier thanks to the manual process.

### ***3.2.5 Qualitative Assessment***

The external validity of qualitative research is often referred to as the generalizability of the findings, i.e., the extent to which the findings can be applied to contexts outside the immediate study (Yin, 2014). Even though all our case companies are based Tokyo, we have tried to ensure external validity by sampling case companies with different levels of internationalization experience, companies of different ages and with different types of international business. The external perspectives included in the research are furthermore greatly contributing to the external validity of the findings as this data reflects the tendencies and trends of Japanese SMEs *in general*.

Ghauri (2004) argues that triangulation is a defining feature of the case study approach. Triangulation offers a more holistic and contextual understanding of the research object as it allows the researcher to view the same phenomenon from several angles. Collection of data from case companies, external respondents, and secondary sources allows us to triangulate our empirical findings, which increases reliability and reduces the risk of misinterpretation (ibid.). The concepts of trustworthiness and authenticity have been suggested as replacements to validity and reliability in qualitative research (Guba & Lincoln, 1994; Lincoln & Guba, 1985). Trustworthiness has been accounted for by ensuring that the research process is fair and transparent, that respondents have been able to freely express their opinions and that the data analysis is performed with as little interference from predetermined bias as possible. The multitude of respondents, with varying backgrounds and experiences contributes to the authenticity of this study.

## 4. EMPIRICAL FINDINGS

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*This section presents the primary data collected through interviews with the five case companies and with external respondents such as SME support organizations and professors. Before addressing the primary data, an introductory section is presented, consisting of secondary data derived from publications and reports about Japanese SMEs' internationalization. This introduction helps the reader to get a better understanding of the current situation that Japanese SMEs face with regards to internationalization and serves as a context to the primary data.*

### 4.1 Using Secondary Data to Describe the Situation for Internationalizing SMEs in Japan

#### 4.1.1 Drivers behind SMEs' Internationalization

Securing demand appears to be an increasingly important objective for Japanese SMEs (see Table 2 for the definition of an SME used in this study) to internationalize. More than half of Japanese SMEs have the intention to expand overseas in the coming three years; with the primary reasons being falling demand domestically, increasing demand overseas and higher profitability in overseas markets.

*Table 2: Japanese Definition of an SME*

<b>SME Definition</b>	<b>Manufacturing</b>	<b>Wholesale Trade</b>	<b>Services</b>	<b>Retail Trade</b>
<b>Capital Size (Million Yen)</b>	300 or less	100 or less	50 or less	50 or less
<b>Number of Employees</b>	300 or fewer	100 or fewer	100 or fewer	50 or fewer

Note: Definition of an SME according to the Small and Medium-sized Enterprise Basic Act and used by METI.

Another common reason for SMEs to internationalize is if their client company internationalizes (JETRO, 2015a). Following a client company overseas has been a common way for SMEs to internationalize due to a unique feature of the Japanese corporate structure; the so-called *Keiretsu* production networks. A *Keiretsu* can be described as an informal business group or intercorporate network, typically with one large manufacturer surrounded by a layer of smaller suppliers tied to the client company. Well-known examples include Toyota, Nissan or Mazda (Grabowiecki, 2006). This interdependence between large and small firms is however decreasing in strength and SMEs can no longer rely on supplying large firms to the same extent as

previously. It will therefore become more important for SMEs to proactively face the market on their own and undertake efforts to secure business opportunities (SMEA, 2015). The rationale behind establishing overseas subsidiaries has shifted from lower labor cost, which dominated in the past, to tapping into markets with substantial demand. Hence, securing demand has become a more important objective to engage in FDI than reducing costs for SMEs (SMEA, 2014).

#### ***4.1.2 Internal Resources to International Expansion***

##### *4.1.2.1 Inadequate Language Skills*

English proficiency is poor in most Japanese firms, which makes it very difficult for Japanese firms to conduct business in the English language (Blair, 2010; EF, 2014). Martin (2004) estimates that an upper secondary level student in Japan will have had at least three hours of English per week for six years, and on completing university usually another two years of English. Nonetheless, their English proficiency tends to be disappointingly low and few Japanese students are able to engage even in a simple English dialogue. Moreover, the total number of young Japanese studying abroad has been following a downward trajectory since 2004 (MEXT, 2015). The number of Japanese students studying in the U.S. has for example dropped from 46,900 in 1999 to 19,300 in 2014. This can be compared with Korea, which has a much smaller population, but sends about 68,000 students to the U.S. each year (Lippert, 2015). Bradford (2015) does however present a more nuanced picture, and states that the number of students going to the U.S. has declined more rapidly than other destinations. Regions that have seen a significant increase in the number of Japanese students are for example Latin America, the Middle East and Asia. In terms of the prevailing English proficiency, Bolton (2008) estimates the share of English speakers in Japan to be around 20 percent.

##### *4.1.2.2 Lack of Information about Overseas Business*

Another commonly reported barrier is the lack of knowledge and information about overseas markets and foreign customers' preferences and needs (Blair, 2010; JETRO, 2015b). JETRO (2014) identifies the lack of "Brain Circulation" in Japan as an obstacle to global business expansion by Japanese firms. The concept refers to the flow of talent to and from a country and the benefits that this entails, where people spend time in other countries and contexts and bring back new ideas and insights back to the home country. The lack of brain circulation in Japan

relates to the fear of brain drain, and failing to acknowledge the benefits of brain circulation. Part of the problem lies in that the economic growth in Japan after WWII offered plenty of opportunities for R&D to take place within the country's borders. Neither does the tradition of lifelong employment in Japan and cultivation of skills within organizations rather than across organizations help to promote brain circulation (ibid).

#### *4.1.2.3 Difficulties to Secure Financing*

Securing finance is another major challenge for many SMEs. A large part of the problem can be explained by the risk aversion among Japanese banks to give credits to SMEs and a preference for fixed assets as a measure of a firm's value. As fixed assets tend to be scarce in SMEs, this results in that SMEs face difficulties in accessing finance to expand overseas. SMEs' dependence on financial institutions becomes particularly evident during economic downturns. When credits are scarce, such as in the aftermath of the financial crisis in 2008, SMEs were hit harder than large firms in Japan (Blair, 2010). IMF (2012) suggests that Japanese SMEs could benefit from more effective financial intermediation and readiness to allow SME restructuring. The problem does not seem to lie in that credit is unavailable, but rather that Japanese banks perceive SMEs as riskier and thereby become reluctant to offer credit.

#### *4.1.2.4 Shortage of Human Resources*

The shortage of human resources, both regarding quantity and quality, has deteriorated in recent years for the primary reason of a lacking interest from applicants (SMEA, 2015). According to Yanagida and Ngiang (2013), a key internal constraint is the inward-oriented labor market in Japan. Japanese manager's face difficulties of finding young employees with a willingness to build business abroad since few young Japanese want to leave their comfort zone (Lippert, 2015). Almost 75 percent of Japanese SMEs that do not operate internationally are also lacking access to human resources capable of handling overseas operations, such as employees with foreign language proficiency or an international outlook; neither do they have access to foreign employees. Moreover, about 60 percent of Japanese SMEs that conduct business abroad report that they have no or few 'global human resources' (Yanagida & Ngiang, 2013).



With reference to the tradition of lifelong employment in Japan, Iwatani et al. (2011) point out that very few Japanese managers have experience from international assignments or even experience of working for another firm. They have typically spent many years working for the same company and thus understand the domestic situation very well but lack knowledge about how to succeed internationally. Moreover, securing human resources is especially difficult for SMEs since the preferred career path among young Japanese students is to work for governmental institutions or large established firms. Hence, it is a key challenge for Japanese SMEs to compete with governmental institutions and large established firms over young talent (Blair, 2010; Lippert, 2015).

Risk-aversion is another distinguishing feature of the Japanese business culture, and is especially evident in the SME sector. The fear of making mistakes is more apparent in Japan than in for instance China, Korea and Taiwan, where entrepreneurs tend to be more willing to accept risk (Blair, 2010). Lippert (2015) states that there is little room for failure in Japan implying that entrepreneurs seldom get a second chance. Risk-aversion and stability-seeking behavior lead Japanese people to look for secure employment, leaving SMEs short of experienced and skilled employees to help the firm go international (Blair, 2010). This is also evident when looking at the objectives of SME management policy (SMEA, 2012). Management policy among Japanese SMEs is first and foremost geared towards providing a place of employment, followed by a desire to contribute to society and thereafter to pass on the family business. Profit maximization came first at fourth place (ibid.).

#### ***4.1.3 Characteristics of Japan's Domestic Environment***

One way that the Japanese government is trying to revitalize the domestic economy and in particular to strengthen SMEs is through the so called *Cool Japan*-initiative. Formulated in 2012, it aims to increase foreign demand for Japanese culture and Japan-related products, both by distributing Japanese products overseas and by attracting foreign visitors to consume within Japan. The strategy involves transforming the appeal of Japanese culture and lifestyle into added value and thereby generate growth opportunities. The growing influx of tourists is seen as a golden opportunity to boost sales for SMEs domestically, and can later serve as a platform for future export. The types of goods selling well overseas and that are promoted through this

initiative include fashion, food, animation, daily goods and traditional craftwork of Japanese origin. It is thus less technologically advanced sectors of the economy that are promoted for having potential to generate overseas expansion. Many SMEs are found within these sectors (METI, 2012), thus emphasizing the potential for Japanese SMEs, also in less technologically advanced industries, to internationalize.

Against the background of Japan being an island, historically isolated from the rest of the world with a large domestic market, Lippert (2015) discusses the risk of that Japanese firms suffer from “the ‘Galapagos syndrome,’ i.e., the development of outstanding products by adapting to the peculiar needs of the highly competitive domestic market.” (2015: 16). This implies that firms who focus heavily on the domestic market face a risk of missing market developments and competitive dynamics overseas.

## **4.2 Empirical Findings from Case Companies**

After having shed some light on the current situation facing internationalizing SMEs based on secondary data, we will now turn to the primary data of our research. We start with a brief introduction to the SMEs interviewed, and thereafter present the data collected.

### ***4.2.1 Introduction to Case Companies***

#### *Anything Co., Ltd. - Manager Mr. Nishimura*

Anything is manufacturing *Maekake*, a traditional Japanese style apron typically carried by craftsmen and shopkeepers. The company was established in the year of 2000 by Kazuhiro Nishimura, who was determined to revive the *Maekake* manufacturing tradition. The production is carried out in a traditional way, using original Japanese weaving machines, which require several years to learn how to operate. The company has ten employees. Exports currently account for approximately ten percent of total sales and export markets include the U.S., Canada, Europe, Australia, China, Thailand, Malaysia and Singapore. Exports started in 2009, with the U.S. as first destination since Mr. Nishimura had experience from having studied there. The company finds customers in new market through participating in overseas exhibitions where Mr. Nishimura himself promotes the *Maekake* to potential customers and distributors. The company is exporting both directly and through distributors.

*Kojima Senshoku Co., Ltd. - Manager Mr. Kojima*

Kojima Senshoku was established in 1872 and manufactures *Aizome*; indigo-dyed textiles. Ten years ago, Hideyuki Kojima became manager of the family-owned company as the business was handed over to the fifth generation. Both the head office and the factory are located in Saitama Prefecture, and the company employs 40 people. They sell both textiles and products made from their textiles, such as *Kendo* uniforms (*Kendo* is a Japanese martial art), festival clothing and products for the apparel industry. Exports to China were attempted five years ago, thanks to Mr. Kojima's previous experience from working in China and his knowledge of the Chinese language. However, the expansion proved unsuccessful due to lack of adaptation to the Chinese market. Three years ago, the company again tried to export but this time to Europe. Currently, exports account for less than one percent of total sales, and their overseas customers are located in London, Paris and Milan. The company exports both directly and through distributors.

*Nihon Shinkan Co., Ltd. - Manager Mr. Hosonuma*

Nihon Shinkan is an aluminum processing company, established in 1967. The company is specialized in cold drawing of aluminum pipes for a wide range of applications, such as Shinkansen trains, optical equipment, vehicles and industrial equipment. In 2008, the respondent Naoyasu Hosonuma took over the business after his father, who founded the company. Nihon Shinkan has two production plants in Japan, and one in Ayutthaya, Thailand, which was established as a greenfield investment in 2012. The company has about 150 employees in Japan, and another 50 in Thailand. In 1995, Nihon Shinkan started to export to Korea, but stopped after some years due to declining demand. Exports to the U.S. started in 2003, followed by China, Vietnam, Thailand and the Philippines. Later this year, exports to India will start. Exports account for about 20 percent of Nihon Shinkan's total sales.

*Azumaya Ltd. - Manager Mrs. Kido*

Azumaya was established in 1914 and produces high quality leather goods such as wallets and small bags. Azumaya is located in Tokyo and is a family owned business with five employees. Maki Kido is the Representative Director, referred to as manager, and it was with her the interview was conducted. The company has no overseas business, but wish to start exporting in the near future.

*Wakoh Co. Ltd. - Manager Mr. Kokubun*

Wakoh was established in 1956, in Tokyo. It is a family owned apparel manufacturing company with eight employees. In 1968, the family established another company in Tokyo called Wakoh Knit Iwae Co. Ltd. This company is only focusing on textile sewing and employs 48 people. Hiroshi Kokubun is in charge of the daily operations of the two companies, and it is with him the interview was conducted. The companies are currently not involved in any business outside Japan but wish to expand abroad in the future.

#### ***4.2.2 Drivers behind SMEs' Internationalization***

##### *4.2.2.1 Replacing Falling Domestic Demand with Demand Overseas*

The shrinking Japanese market was recognized as a factor driving all case companies to expand their business overseas. Mr. Nishimura stated that it has become more difficult to conduct business in Japan today compared with the decades before 1990, when the Japanese economy was stronger. He now views overseas expansion as a necessity in order to continue his business. The objective of his firm Anything is first and foremost to preserve the Japanese *Maekake* tradition. As the domestic customer base for his product is decreasing, finding customers in overseas markets becomes increasingly important. Similarly, Mr. Kojima was concerned about his falling customer base and the declining textile market in Japan. Hence, he viewed the future growth opportunities in the Japanese market as very limited, and therefore saw expansion into foreign markets as an opportunity for his business to stay alive. Mr. Hosonuma was also concerned about the stagnating economy and shrinking population and expressed his concern by saying:

If something goes away, I want to replace that and that might be by going overseas (Mr. Hosonuma, manager of Nihon Shinkan, March 14, 2016, authors' translation).

He saw no place to grow in the Japanese market and although being unsure about whether to expand or not, it at least provided the company with a chance to survive. It became clear from the interviews with the managers of Anything, Kojima Senshoku and Nihon Shinkan that the primary reason driving them to expand overseas is not to grow their business *per se* by finding customers abroad but rather to compensate for the declining number of customers in the domestic market. Moreover, all three managers stressed the importance of *preserving* their firm

and being able to continue their business a long time in the future. Also, Mrs. Kido and Mr. Kokubun expressed an interest in expanding into foreign markets since the Japanese population is shrinking and this threatens their current business. Internationalization, in the form of export, was perceived by them as a way to compensate for falling sales domestically.

#### *4.2.2.2 Opportunities to Internationalize Arising from Networks*

Among the three internationally active case companies, overseas expansion was in one case found to be a result of the SME's own initiative, while in the two other cases rather the result of opportunities arising from SMEs' surrounding network. Different levels of proactivity could be observed with regards to internationalization; the ultimate decision to expand could either be an intrinsic desire arising from within the firm or manager or it could emerge as an opportunity proposed by another firm. In the latter case, the SME may not have considered internationalization from the outset but was introduced to the idea by an external party, often an interested customer overseas. Approaching distributors with an interest in helping the SME to expand overseas could then serve as a platform for further expansion. In this sense, the SME is more or less "pulled" into overseas markets by other firms in its network and the network is thereby becoming an important enabler of international expansion. Despite the acute awareness of the shrinking market, the ultimate factor leading Nihon Shinkan to expand overseas was not intrinsic; it came from outside the firm in the form of a suggestion from a network partner. Mr. Hosonuma explains why his family first started to export:

They [the family] didn't have so much of an interest in doing business overseas but they had an offer. It's not like they really wanted to expand their business but it just came and so they said okay (Mr. Hosonuma, manager of Nihon Shinkan, March 14, 2016, authors' translation).

The family reacted on an opportunity presented to them rather than actively sought to export. Through a technical exchange with a firm based in the U.K., they were introduced to their first customer in the U.S. A Chinese subsidiary to this American firm was furthermore the way into the Chinese market, illustrating how customers pulled Nihon Shinkan into overseas markets. Moreover, when Nihon Shinkan increased their commitment to overseas markets by establishing a production plant in Thailand, the policy from the chairman had in fact been to stay in Japan to develop the business domestically. However, a Japanese acquaintance with business ties to

Thailand contacted Mr. Hosonuma and asked if he was interested in a joint venture in Thailand. One month later, Mr. Hosonuma travelled to Thailand together with two other managers and later took the decision to open up a production plant in Thailand. In a similar way, Mr. Kojima's family business started to export after a customer suggested that their products could be suitable for overseas markets. He explained it in the following way:

At first, we thought of not doing foreign business. We produced shirts, bags and so on and then because the textile business is decreasing, I'm interested in the product business. Some customers looked at our products and said, "this is good for overseas business". Then, I went to China to sell the products (Mr. Kojima, manager of Kojima Senshoku, March 22, 2016).

Mr. Kojima started to export to the U.K. after a visit from a potential customer who looked at his fabric and later placed an order. Exports to his French customer, the well known fashion house Chanel to whom he sold his fabric last year, also started after the initial contact came from the customer that contacted him via a distributor, rather than the other way around. Thus, Mr. Kojima was inspired by a suggestion to engage in exports presented to him.

Without in no way reducing the extent, complexity or sense of initiative necessary to go international, Mr. Hosonuma and Mr. Kojima described a reactive attitude towards engaging in international business, where managers reacted on propositions rather than searched for opportunities on their own. Mr. Nishimura on the other hand described a more proactive and entrepreneurial attitude, where he actively sought to engage in exports and did so on his own initiative. Regardless of whether a reactive or proactive stance was taken with regards to internationalization, accessing international customers and building relationships were found to be key components to succeed overseas. For both Mr. Kojima and Mr. Nishimura, exhibitions arranged in foreign countries, in which they promote their products to potential customers and distributors are crucial to build relationships and function as a platform for expansion. Exhibitions are their main channel to establish contact with business partners, highlighting the importance of participating in such network events. For Mr. Hosonuma and Mr. Kojima who displayed a more reactive stance, network embeddedness and an ability to capitalize on opportunities arising from network relationships were important factors leading their firms onto

an internationalization path in the first place. For Mr. Nishimura, network embeddedness and his networking capabilities also constitute important ways into overseas markets.

#### *4.2.2.3 Overseas Expansion to Boost Domestic Reputation*

It became clear from the interviews that expanding into foreign markets generated additional effects than only access to an overseas customer base. Being an international company could improve the reputation in the home market and was perceived as something positive; it inspired respect and trustworthiness among Japanese customers. Three of the five case companies stated that they expanded overseas in order to boost their domestic business. When Mr. Kojima was asked if overseas business is something that he prioritizes, he answered:

Once we have sold a product overseas, the same product becomes very easy to sell in Japan because we sold them overseas. It is PR. Japanese people like this. ... Overseas business is good for domestic business. For example, this fabric was sold for 5,000 yen, and for a Japanese textile company 5,000 yen was too expensive. Then, when we had sold it to Chanel, the same Japanese company that before thought it was too expensive said “mmh very good“. That is a character of Japanese people (Mr. Kojima, manager of Kojima Senshoku, March 22, 2016).

Mr. Kojima believes that his products will sell better in Japan if he manages to create a reputation of how well they are selling in foreign markets. Similarly, Mrs. Kido considered it difficult to promote her products to Japanese people, but she thought that if she manages to create a good reputation of her products in foreign markets, then more Japanese customers would buy her products as well. Also, Mr. Hosonuma noticed how his greenfield investment in Thailand helped to boost his business by improving the firm’s reputation as being an international company.

Once we had a factory in Thailand, this changed the reputation against customers. ...Customers think that we are able to do business overseas because we already have a factory in Thailand. ... For example, Husqvarna [one of Nihon Shinkan’s customers in Japan], before when we only had a factory in Japan, they only talked about markets in a domestic stage but once we opened a factory in Thailand, Husqvarna became interested in giving us information about Europe (Mr. Hosonuma, manager of Nihon Shinkan, March 14, 2016, authors’ translation).

Expanding overseas thus opened up new opportunities both domestically and internationally for Nihon Shinkan as it reinforced customers' and business partners' perception of the firm's international capabilities.

In addition, for the case companies with traditional manufacturing techniques; being international was seen as a way to revive domestic interest in these old techniques, to retain and develop the craftsmanship within the firm in order to survive in the future. Mrs. Kido was very concerned with that the skilled craftsmen were losing interest in the Japanese traditional manufacturing techniques and lacked motivation to pass on their skills to a younger generation. Similarly, she noted a lack of interest in preserving these techniques among younger people. Expanding overseas was however seen as a way to reinvigorate interest; to show craftsmen that their products are appreciated overseas and that foreign customers value their skill. In this way, Mrs. Kido hoped to be able to continue her business in Japan, not only in terms of increasing brand recognition among Japanese consumers but also to preserve the traditional manufacturing process. Again, preservation of the business and maintaining the old traditional techniques were cited as the ulterior motive.

#### ***4.2.3 Internal Barriers to International Expansion***

##### ***4.2.3.1 Inadequate Language Skills***

Insufficient language skills was found to be a strong reason why Japanese SMEs hesitate to expand internationally as it was emphasized by all case companies. Mr. Nishimura believed that his previous experience from studying in the U.S., and especially the English skills he acquired helped him to start exporting. He explained that it is difficult for managers who cannot speak English to go abroad, and that most Japanese hesitate to communicate in English as they have little experience of speaking English. When Mr. Kojima was asked about whether he had experienced any barriers or difficulties to internationalize, he answered with only one word "language", followed by laughter. He explained that his company for instance has trouble to respond quickly to emails from current or potential customers written in English. Mr. Kojima was furthermore asked about his internationalization strategy, and replied that he will increase the number of English speaking staff to be better prepared to conduct business in English. Similarly, both Mrs. Kido and Mr. Kokubun considered the lack of English skills to be the



largest obstacle to expand abroad. Also for Mr. Hosonuma, speaking English was troublesome and an interpreter was therefore used during the interview.

#### *4.2.3.2 Lack of Information about Overseas Business*

Three of the five case companies expressed a perceived lack of information about *how* to internationalize. This disorientation was most prevalent among the SMEs not yet internationally active. Mrs. Kido and Mr. Kokubun are very interested in overseas expansion but do not know how or where to start. Mr. Kokubun states that his company is good at what they are doing, i.e., the production process but does not know how to expand overseas. Mrs. Kido expressed that she does not know anything about the export process itself or about foreign customer demand. Neither did they know where to turn to for advice or guidance. Similarly, Mr. Hosonuma faced a lack of information about overseas markets before his company took the decision to engage in international business. Interestingly, the decision to engage in international business brought access to valuable information about overseas markets since interested customers then approached him about overseas business. Mr. Hosonuma explained that people in his surroundings changed attitude when he established the factory in Thailand compared to when he was only involved in domestic business. Before he opened up the production plant, no one talked to him about international business opportunities. He explained this in the following way:

When we didn't have a factory in Thailand, all customers only talked about domestic business. ... I realized after we went to Thailand that when we decided to stay in Japan in 2008, to not expand business, we were making decisions with much less information (Mr. Hosonuma, manager of Nihon Shinkan, March 14, 2016, authors' translation).

This indicates that Mr. Hosonuma recognized that his company lacked information about overseas markets at the time the decision was taken to expand abroad, and did not get such information until when he had set up the factory in Japan. An example of how the attitude of his surroundings was change after having set up the production plant in Thailand is the following:

...some days ago I was at a golf practicing place and all of a sudden my friend came up to me and said "Do you want to do a joint venture with an Indian company?" If I didn't have a factory in Thailand that person would never come up to me and say that. So it is very interesting. Just because I have a factory overseas, the attitude of other people has also changed (Mr. Hosonuma, manager of Nihon Shinkan, March 14, 2016, authors' translation).

#### *4.2.3.3 Difficulties to Secure Financing*

The costs of expanding overseas were recognized as a barrier to internationalize by the three case companies engaged in international business and by one of the not yet internationally active case companies. Mr. Nishimura expressed difficulties with export costs such as shipping and insurance. He explained that the retail price of his product is as much as three times higher outside the Japanese market. However, he was able to overcome the financial barrier that he faced by receiving financial support from Ministry of Economy, Trade and Industry (METI). Mr. Hosonuma also talked about cost as a barrier when his company set up their production plant in Thailand. Mr. Kojima discussed the cost aspect as well, but rather the costs related to business trips to meet with customers. He explained that today, when exports only account for less than one percent of total sales, they cannot afford to meet customers face-to-face as often as he would like to. Also Mrs. Kido discussed taxes and shipping costs as potential barriers for internationalization.

#### *4.2.4 Lack of International Networks*

Network embeddedness and networking capabilities were found to be important enablers and facilitators of international expansion. Yet, SMEs' international reach when it came to networking was limited. Lack of international networks such as distributors and customers was recognized as a barrier to internationalization by all case companies. Nihon Shinkan did for example not have many business ties to foreign customers. The foreign customers that they export to are in fact Japanese customers located in foreign markets. In cases when Nihon Shinkan exports to non-Japanese companies, a Japanese trading company handles the export. When Mr. Hosonuma discussed his future thoughts about finding new customers he clearly expressed that he first and foremost wants to do business with Japanese companies in foreign markets and not with local companies. He stated:

...because if I would have business with a local, a non-Japanese company, I would think that collecting money and to make an agreement would be difficult. I'm not exactly looking for business with local companies. ... I hear a lot about non-Japanese companies, once there is a problem they stop payment and collecting payment from them would be very difficult (Mr. Hosonuma, manager of Nihon Shinkan, March 14, 2016, authors' translation).

Mr. Hosonuma's statement illustrates a rather closed mindset towards doing business with foreign customers, which has resulted in few international business partners. This mindset could be the result of bad experiences of doing business with foreigners. Mr. Hosonuma explained that he had faced difficulties when doing business with Korean and American firms:

Koreans first of all, they want to be superior to the opponent. So they started to shout during this agreement or in the meeting. And this is not how we do business here. ... I felt especially barriers when we started business in the U.S. The business culture there was completely different. It is very based on agreements and it takes a lot of time before they reach the agreement. And then, when the business starts, everything will be based on that agreement. But here it is a completely different culture, the agreement is not so important between Japanese companies. We just sign and then let's see how it goes (Mr. Hosonuma, manager of Nihon Shinkan, March 14, 2016, authors' translation).

Contrasting business cultures and difficulties in understanding each other's standpoint seem to have contributed to Mr. Hosonuma's reluctance to establish business ties with customers in overseas markets. It is here worth pointing out that Mr. Hosonuma speaks from experience and not about his perception of how other cultures do business. This points to a reluctance to enter business negotiations and partnerships with foreigners or at least a preference for keeping such partnerships with other Japanese counterparts. Mr. Hosonuma further stated that he did not experience a true global barrier to internationalization as his overseas counterparts are primarily Japanese and the trading house he uses is Japan based. In the U.S. and China on the other hand, the customers are local and in these cases he had experienced difficulties to expand.

Both Mr. Nishimura and Mr. Kojima use exhibitions as the primary channel to establish relationships with customers. The fact that no other significant channels are used for international networking limits their opportunities for network building. Furthermore, Mr. Nishimura discussed the importance of finding the right distributor, and stated that he had difficulties with this American distributor that negatively affected his U.S. business. He compared two of his distributors and the impact they have on the business:

The reason why the market in London is growing so much is because the distributor understands the product, the culture and what we want to do. The distributor there is very good. The American distributor is not so good and that makes it more difficult to expand there (Mr. Nishimura, manager of Anything, March 9, 2016).

This points to the importance of distributors and how they may influence export performance. Mr. Nishimura further emphasizes that it is important that the distributor truly *understands* the business, the culture and the product offered. A lack of mutual understanding and different perspectives on how to conduct business may problematize the partnership and ultimately the firm's performance. The fact that Mr. Nishimura has not changed distributor in the U.S. indicates that it is difficult to establish a relationship with another American distributor. Moreover, both Mrs. Kido and Mr. Kokobun talked about that they do not have any contact with potential foreign business partners today, and they were not sure how to establish such contact. Mrs. Kido believed that using a distributor is necessary when starting to export due to the difficulty of selling directly to foreign customers. She also expressed troubles of knowing whom to trust when it comes to potential business partners, pointing to a risk-averse and hesitant attitude towards doing business with foreign counterparts.

#### ***4.2.5 Managers' Influence on Internationalization Decisions***

##### *4.2.5.1 Managers are Responsible for Developing Overseas Markets*

The manager plays an important role in all case companies and has the ultimate responsibility for decision-making. None of the case companies employed staff with the explicit responsibility for developing international markets or hired staff based on their previous international experience. Instead, the responsibility of developing overseas markets rests entirely on the shoulders of the manager. Nihon Shinkan was the only case company that has one employee managing parts of the company's international business; the manager of the production plant in Thailand. All managers handle the contact with existing and potential international customers and distributors and thus have a large impact on decision-making regarding international expansion.

In the case of Kojima Senshoku, the ultimate decision to export was taken by Mr. Kojima himself. When he answered the question of how the decision was taken to start export, he stated:

At first, I like overseas... (Mr. Kojima, manager of Kojima Senshoku, March 22, 2016).

This illustrates that the decision to expand overseas was taken mainly because of his positive attitude towards international markets. Mr. Kojima also compared his own attitude with attitudes

of managers from other firms that are not interested in overseas business, and suggested that his positive attitude made the primary difference. He stated:

The reason why I think so is that it is another firm that is also interested in doing business overseas but the president does not like overseas. So that's the difference between us. For them, it is a kind of barrier and for me this is not a barrier (Mr. Kojima, manager of Kojima Senshoku, March 22, 2016).

This points to that the manager's interest in and attitude towards overseas business to a large extent influence whether the firm decides to expand overseas or not. There may exist a wish to be an international firm but if the managers do not have a positive attitude towards international business, the conclusive decision to internationalize is not likely to be taken.

#### *4.2.5.2 Previous International Experience Influence Decision-making*

The manager's previous international experience was found to be an important factor in SMEs' decision to expand overseas. This was evident in all case companies. Mr. Kojima had international experience from working in China prior to entering the family business and spoke Chinese, which he believed made him more open towards overseas business. China was consequently also the country that his company first started to export to. He stated:

... because we had some products and I could speak the Chinese language so I must go to China. So I went to China... (Mr. Kojima, manager of Kojima Senshoku, March 22, 2016).

This indicates that China became the natural choice for Mr. Kojima thanks to his experience. Mr. Kojima described how he learned from the first failed efforts to export products to China and how he consequently adapted the strategy when Kojima Senshoku a few years later tried again to expand to Europe. Their offering in China was developed to suit Japanese taste and little energy was spent on researching the preferences of the Chinese market. They had the idea that what worked in Japan would work in China, but this was not the case and their products sold poorly. When attempting to expand again a few years later, Kojima Senshoku went back to selling textiles instead of finished products, as this requires less adaptation to differences in taste. The company learned from the failure in China and adapted the future expansion attempts to only include textiles.

Mr. Hosonuma also recognized the impact of a manager's previous international experience and referred to the manager of Nihon Shinkan's production plant in Thailand. Mr. Hosonuma himself lacks previous international experience, but interestingly, the decision was largely influenced by another manager with international experience who advised Mr. Hosonuma and followed him to Thailand. He explained the situation in the following way:

One of the persons had experience from working in China before he joined this company and he is now president of the Thai factory. ... this person had the opinion that Nihon Shinkan should expand business overseas from the very beginning. Not officially, but he has been telling me that we should go out overseas if we want to keep business as Nihon Shinkan. He advised that we should go out (Mr. Hosonuma, manager of Nihon Shinkan, March 14, 2016, authors' translation).

The international experience of the other manager thus encouraged the decision to expand overseas. The choice of locating in Thailand was further motivated by the opinion held by one of the managers that the current market conditions in Thailand were similar to those that prevailed in Japan some decades ago. They could thus use their experience of the Japanese market in Thailand. Mr. Hosonuma explains this rationale:

Also, one of the management that went to Thailand with me felt that the situation in Thailand is very similar to what his experience was in Japan 30 to 40 years ago. So the knowledge that we already have, we could take all that to Thailand and do big business using our own experience. These are the main reasons or motives for why we decided to start business in Thailand (Mr. Hosonuma, manager of Nihon Shinkan, March 14, 2016, authors' translation).

Even if Mr. Hosonuma lacked previous international experience, he expressed that his first business trip to Thailand really opened his eyes and that he had to "see it to believe it". He was reluctant in the beginning of the expansion process and knew very little about South East Asia, but changed his mind after having visited Thailand and seen it with his own eyes. This points to that the little experience Mr. Hosonuma gained from his short business trip changed his perception of expansion and that it was rather the lack of knowledge that from the outset caused him to hesitate to expand to Thailand. Also, Mr. Nishimura based his first expansion decision on his previous international experience. He had studied in the U.S. and knew the language, and consequently chose to first export to the U.S. He stated:

The language helped me very much. It is difficult for managers who cannot speak English to go abroad. Most people hesitate to communicate in the English language; they have little experience of speaking English within Japan (Mr. Nishimura, manager of Anything, March 9, 2016).

Mrs. Kido and Mr. Kokubun both have previous experience from studying in New Zealand, which they believed had a considerable impact on their wish to expand overseas. Mrs. Kido believed that managers of other small companies in Japan who have not been studying or working outside Japan are not as likely to have the same desire to internationalize. She stated that her experience from studying in New Zealand changed her a lot and was a very good experience. Similarly, Mr. Kokubun believed that his previous experience from studying abroad was the main reason for why he wished to expand overseas.

### **4.3 Empirical Findings from External Respondents**

External respondents were also interviewed to gain an additional perspective on Japanese SMEs' internationalization. They will now be introduced, followed by a presentation of the primary data collected during interviews with them.

#### ***4.3.1 Introduction to External Respondents***

*Mr. Murai, Director General at SMRJ & Mr. Yaguchi, Deputy Manager at SMRJ*

The Organization for Small and Medium Enterprises and Regional Innovation (SMRJ) is a supporting organization for Japanese SMEs. The organization has its headquarters in Tokyo and employs about 800 people. The organization is for example supporting SMEs to expand their business overseas by giving advice on overseas business promotion and assistance for participating in overseas trade fairs. Two interviews were conducted, one with Shinichi Murai, Director General at the Marketing Support Department and one with Masaya Yaguchi, Deputy Manager. Mr. Yaguchi has been working for SMRJ for 15 years but even before that he worked for a large commercial bank where he also supported SMEs.

*Renata Piazza - Founder and Director at Hasekura Program*

Renata Piazza is the founder of the non-profit organization Hasekura Program, which is a business exchange and training program for SMEs, social entrepreneurs and local authorities

from the EU and Japan. The program is promoting cross-borders relations between the EU and Japan.

*Professor Kenji Suzuki - Meiji University*

Kenji Suzuki is a Professor at School of Global Japanese Studies, Meiji University in Tokyo. His current research areas are international comparison of welfare and corporate systems; public policy and organizational decision-making.

*Professor Jesper Edman - Hitotsubashi ICS*

Jesper Edman is an Assistant Professor in International Business Strategy at Hitotsubashi ICS in Tokyo. His research includes the internationalization strategies of Japanese multinationals, the impact of foreign firms on Japanese institutions and business practices, and innovation and change in corporate business practices.

**4.3.2 Drivers behind SMEs' Internationalization**

All external respondents recognized the shrinking Japanese market to be a very significant factor driving SMEs to expand abroad. Mr. Murai addressed this as the primary reason pushing Japanese SMEs abroad. Mr. Yaguchi talked about how many Japanese SMEs today have to sell to markets outside Japan due to the stagnating domestic economy and he believed that managers must cultivate new markets outside Japan in order to survive. Similarly, Professor Suzuki, Professor Edman and Mrs. Piazza were also concerned about the future of Japanese SMEs due to the shrinking Japanese population and economy and viewed this as an important driver for Japanese SMEs to expand abroad.

Four of the five external respondents recognized that opportunities for SMEs to internationalize often arise from participating in networks. They referred to the *Keiretsu* network structure in Japan and its importance for SMEs involved. Professor Edman discussed how SMEs often follow their client firm's internationalization path. Similarly, Professor Suzuki discussed the importance of networks by stating that some SMEs are forced to go abroad when their client company goes abroad. Also, Mr. Murai and Mrs. Piazza discussed this phenomenon by giving examples from the automotive industry in Japan, in which many small suppliers to larger



automotive firms historically have followed these large firms overseas. Professor Suzuki believed that although some of these networks or subcontractor systems have been dissolved, there is a tendency towards that large manufacturers are trying to reorganize and impose these subcontractor systems again.

Mrs. Piazza believed that Japanese SMEs use overseas expansion to boost domestic business. She explained that internationalization could be a way for Japanese SMEs to show the domestic market that their products are superior since the company is successful abroad. This shows that the focus for Japanese SMEs is still very much on domestic business, and that SMEs even consider using foreign markets as a channel to promote sales in Japan.

#### ***4.3.3 Internal Barriers to International Expansion***

Insufficient language skills were recognized by four of five external respondents as an importance reason why Japanese SMEs hesitate to expand internationally. Mr. Yaguchi explained that about 40 percent of Japanese SMEs are interested in overseas business, but that the poor language skills often come in the way. Professor Suzuki also considered the lack of English and other foreign languages to be a barrier to overseas expansion. Professor Edman and Mrs. Piazza stated that the lack of English skills is still a big obstacle that makes Japanese SMEs feel insecure about engaging in international business.

Three external respondents viewed lack of information about overseas business as a barrier for SMEs' international expansion. Professor Suzuki argued that many SMEs lack information of how to internationalize in practice. Mr. Murai explained that since SMEs often lack knowledge about how to internationalize, one of SMRJ's objectives is to provide Japanese SMEs with information about foreign markets. Similarly, Mr. Yaguchi believed that SRMJ plays an important role in providing SMEs with such information since this kind of information is necessary to have for a successful overseas expansion.

Mr. Murai voiced the financial concerns of Japanese SMEs since they in general have very little capital compared to their sales and that many firms are 'personalized'. By this he meant that many companies' credits are based on the manager's own credit. This in turn results in that it is

difficult to transfer the company to the next generation. Although this is not a financial problem directly associated with international business, it is a barrier for Japanese SMEs to survive and in the future be able to engage in international trade. In addition, Professor Suzuki, Professor Edman and Mrs. Piazza also considered financing to be a barrier for Japanese SMEs to internationalize. Professor Edman explained that firm size has an impact on a company's ability to get loans that could be used to expand overseas. The smaller the company is, the harder it is for the firm to receive loans from Japanese banks.

#### ***4.3.4 Lack of International Networks***

Professor Suzuki considered one of the main barriers for Japanese SMEs to expand overseas to be the lack of network and connection with local people in foreign markets. This is the primary reason why many Japanese companies, even though they go abroad, only conduct business with other Japanese companies. Professor Suzuki further stated that since Japanese people in general have little connection with people from other countries, they face difficulties of finding advisors or partners overseas. Professor Edman also pointed to the lack of business contacts and relates this to the importance of relationships within Japan, and how Japanese tend to view themselves as uniform. These features make it difficult for SMEs to build new relationships in overseas markets.

Mr. Yaguchi explained that the lack of integration with people outside Japan has led to that most Japanese SMEs and their management staff are afraid of going abroad because of the uncertainty it involves. Moreover, Mrs. Piazza emphasized the importance for Japanese people to find a trustworthy partner since the Japanese business culture to a large extent is based on trust. However, she stated that this is difficult for Japanese companies when doing business with Westerners due large differences in business culture, leading to miscommunication between the parties. For example, Mrs. Piazza stated that the Western counterparts grow tired of the Japanese managers' beating around the bush and do not understand why it takes such a long time to start doing business. She further explained that Westerners are typically seen as not trustworthy, and their restlessness is thus making relationship building even more difficult.

### ***4.3.5 Japan's Domestic Environment Impedes SMEs' Internationalization***

#### *4.3.5.1 History & Geography*

The external respondents believed that the Japanese history plays a role in explaining why SMEs hesitate to expand overseas. Professor Suzuki stated that Japanese people are quite isolated, by which he meant that they have a very strong identity of being Japanese. He believed that this is a result of that Japan has been closed for a long time, and therefore do not have any history of interacting with foreigners. Mr. Yaguchi explained the same feature:

Most of Japanese SMEs and their management staff are afraid of going abroad. As you may know, Japan was closed for more than 300 years until 200 years ago. We didn't know the foreigners. When I was young, I had never seen a foreigner in my town, a suburb of Tokyo (Mr. Yaguchi, Deputy Manager at SMRJ, March 23, 2016).

This statement explains that the historical isolation from the rest of the world has resulted in that many Japanese are afraid of interacting with foreigners. Similarly, Mr. Murai argued that the Japanese mindset has been largely affected by the fact that Japan is an island, causing people to think more about the differences than similarities between themselves and other cultures. This in turn has made it difficult for Japanese people to interact with foreigners. Mr. Murai also believed that Japanese people could be seen as rather uniform. In line with this, Professor Suzuki explained that Japanese people tend to follow the big mass and align strategies with how peers and competitors do, and since there is no current trend of internationalization among Japanese SMEs, most of them stay in the home market.

The more recent economic developments also play a role according to external respondents in SMEs hesitation to expand internationally. Professor Suzuki explained that being the most economically developed nation among their Asian neighbors, a gap has been created between Japan and the surrounding, less developed nations. He described the distance between Japan and their neighbors in the following way:

...from the Japanese point of view, those countries [other Asian countries] are less developed than Japan so Japanese people tend to look down on those local people. And that of course can be a very big barrier for making a network (Professor Suzuki, Professor at Meiji University, March 18, 2016).

Japan's isolation thus has created difficulties in building business relationships with people from neighboring countries. The divide between Japan and their Asian neighbors in terms of economic development has also made it difficult for Japanese firms to compete on the Asian market. Mr. Suzuki points out that the high-quality Japanese products that SMEs often specialize in are difficult to sell to other Asian countries, as their demand tend to be less sophisticated. This leads to that Japanese SMEs are more likely to find overseas customers in the Western parts of the world, which is far away both in geographical as well as cultural terms. The step to internationalize therefore becomes even bigger and Japan can be seen as an island in more than one sense; it is a economic power surrounded by less developed neighbors, even through nations such as South Korea is approaching.

Professor Edman addressed the influence of geographical factors by discussing how the vast size of the Japanese market has affected SMEs' attitudes towards internationalization. SMEs have not experienced a need to internationalize since domestic demand has been sufficient. Therefore, foreign countries are rather unknown for them, making interaction with foreigners uncertain and uncomfortable. He believed that Japanese SMEs therefore tend to perceive internationalization as a "necessary evil". It is not something SMEs want to do; on the contrary, they are dragged into overseas expansion because of the realization that they cannot sell enough in the Japanese market.

#### *4.3.5.2 Risk-aversion & Lack of Courage to Break with Traditions*

Professor Edman pointed out that the Japanese culture has little tolerance towards failed entrepreneurs and a mistake can more or less ruin a career. He further explained that since second chances are seldom given, failure is avoided at all times in Japanese firms. Internationalization is perceived as a great risk by many SMEs, and as a consequence of their risk-aversion, few SMEs are internationalizing. Mr. Yaguchi discussed the mindset of managers in Japanese SMEs and stated that many of them seem to be afraid of doing new things such as expanding overseas. An example of Japanese employees' risk-aversion is that few employees are willing to work for the company abroad. Mr. Murai stated that if a Japanese employee wants to work abroad at all, it is only for a shorter period of time. Professor Edman also recognized a lack of employees who are willing to work abroad. He explained:

... it is probably difficult to find people within the organization who wants to go. “Let's go to China – who wants to go?” And everyone takes one step back. It is difficult to find capable employees that the CEO can trust. They can take the decision but may not be able to find the people they need (Professor Edman, Assistant Professor at Hitotsubashi ICS, March 30, 2016, authors' translation).

This shows that the decision to internationalize might be taken by the manager but that it may be difficult to find employees willing to work for the company overseas. In addition, Professor Edman stated that since international operations tend to be centralized to Japan, being an expat is like having a long vacation. By this he meant that being away from the head office means that employees lose contact with what is going on at home, which causes the career to deteriorate. Many Japanese employees therefore hesitate to work for the company abroad. He believed this phenomenon to be even more outspoken in SMEs compared to larger firms since employees in SMEs to a larger extent want to stay close to the management.

Professor Edman further suggested that Japanese firms are currently lacking self-confidence, as the economic rationale by which they used to compete internationally is growing obsolete. The classic Japanese model worked very well, where firms focused on the domestic market and developed it. They had superior technology and quality and could simply export around the world. This model is becoming increasingly outdated and competition on cost from for instance China and Korea amounts. To internationalize as an SME does however require courage to break with traditions. Due to the mindset created by the system that SMEs have clung to, breaking with tradition is a significant challenge. Also, Mr. Murai discussed the need for Japanese firms to shift focus from outperforming in terms of quality and instead pay more attention to the needs of the market. Adapting to the market was less important in the past, as the market simply accepted whatever they supplied. This necessary shift of focus also puts pressure on SMEs to understand foreign markets in order to succeed internationally, making expansion even more difficult. In addition, Mrs. Piazza noted a lack of self-confidence among Japanese SMEs, both in terms of how to enter overseas markets and an uncertainty about whether their products are good enough to succeed abroad.

#### 4.4 Summary of Empirical Findings

Table 3 illustrates a summary of the empirical findings collected both from case companies and external respondents. This summary lays the foundation for the way the following analysis chapter is structured. The rows present the main factors that were found to influence Japanese SMEs' international expansion, and they are presented in the same order as they are outlined in this chapter. The number of respondents who addressed each observed factor is also shown in the table. The respondents are divided into three categories: active case companies (i.e., the three case companies currently involved in international business), not yet active case companies (i.e. the two case companies not yet involved in international business), and external respondents (i.e., the five external respondents including representatives from SME support organizations and professors). The last column shows the total number respondents for each factor.

*Table 3: Factors Influencing Japanese SMEs' International Expansion*

	Active Case Companies*	Not Yet Active Case Companies**	External Respondents	Total
<b>Drivers behind SMEs' Internationalization</b>				
Replacing Falling Domestic Demand with Demand Overseas	3	2	5	10 (10)
Opportunities to Internationalize Arising from Networks	2	0	4	6 (10)
Overseas Expansion to Boost Domestic Reputation	2	1	1	4 (10)
<b>Internal Barriers to International Expansion</b>				
Inadequate Language Skills	3	2	4	9 (10)
Lack of Information about Overseas Business	1	2	3	6 (10)
Difficulties to Secure Financing	3	1	4	8 (10)
<b>Network Barriers to International Expansion</b>				
Lack of International Networks	3	2	4	9 (10)
<b>Managers Influence on Internationalization Decisions</b>				
Managers are Responsible for Developing Overseas Markets	3	2	-	5 (5)
Previous International Experience Influence Decision-making	3	2	-	5 (5)
<b>Japan's Domestic Environment Impedes SMEs' Internationalization</b>				
History & Geography	-	-	4	4 (5)
Risk-aversion & Lack of Courage to Break with Traditions	-	-	4	4 (5)

\* Case companies currently involved in international business

\*\* Case companies not yet involved in international business

Note: Table compiled by authors.

## 5. ANALYSIS

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*This section analyzes the empirical findings presented in the previous section against the background of the theoretical framework provided in chapter two. The analysis addresses factors causing Japanese SMEs to hesitate to internationalize as well as the manager's influence on internationalization decision. By comparing the findings with how the subject has been studied previously, the analysis clarifies to what extent the theoretical framework reflects the Japanese context. The analysis further provides a foundation for answering the research question in the final concluding chapter.*

### **5.1 Drivers behind SMEs' Internationalization**

In order to analyze why Japanese SMEs hesitate to expand internationally, it is important to first understand the factors driving them to expand, as this motivation determines the nature of their internationalization decisions. Factors originating from Japan's domestic environment were found to be the primary drivers of Japanese SMEs' overseas expansion. The most significant factors were found to be the shrinking domestic market which pushes SMEs overseas to replace falling domestic demand with demand overseas; opportunities to internationalize arising from network participation; and a wish to expand overseas in order to boost reputation in the home market. These factors contribute to that internationalization is perceived as a "necessary evil".

#### ***5.1.1 Replacing Falling Domestic Demand with Demand Overseas***

Japan's shrinking domestic market, as a result of the poor economic growth and declining population, was found to be the most evident factor driving Japanese SMEs to internationalize. It was recognized as a driver by all respondents, who were concerned about the future of their businesses in the Japanese home market. The shrinking market is a widely acknowledged concern, and found by JETRO (2015a) to be an important reason for Japanese SMEs to increase exports. The firm's domestic environmental context has been recognized to influence SMEs' internationalization (Kuivalainen et al., 2012; Wright et al., 2007; Zahra et al., 2005). A stagnating domestic market pushes firms overseas, with for example Morgan and Katsikeas (1997) stating that engaging in international trade could be an act of protection against an economic slowdown domestically and Kaynak and Kothari (1984) suggesting that a limited size

of the domestic market results in motivation to engage in international trade. Japan has faced economic stagnation during “two lost decades” (Breene, 2016), with the consequence that SMEs have been forced to seek demand overseas to survive.

From the empirical evidence, it became clear that the case companies were predominantly concerned with replacing lost domestic demand rather than seeking expansion *per se*. Expansion was perceived as a necessity in order to survive the difficult times ahead. Also, SMEA (2015) points out that securing demand has become an increasingly alarming concern for SMEs. It is more appropriate to explain SMEs' internationalization as something they were forced to do. The fact that internationalization is viewed as a necessity rather than an intrinsic desire helps to explain why Japanese SMEs hesitate to expand internationally, as the motivation to expand is weak from the outset. An outspoken growth orientation was thus not observed among Japanese SMEs. If connected with the findings by Nummela et al. (2005), which suggest that a firm's growth orientation is positively correlated with international expansion, this could help to explain SMEs' hesitation. All SMEs were primarily concerned with *preserving*, and *continuing* the business in a long-term perspective, and were afraid that this was threatened by the shrinking market. The long-term orientation that characterizes Japanese management style is reflected in the findings by SMEA (2012), where providing employment, contributing to society and passing on the family business are more important than profit maximization. When the mindset is to preserve rather than to grow the business, the thought of internationalizing is only entertained when preservation is no longer possible within the domestic borders.

### ***5.1.2 Opportunities to Internationalize Arising from Networks***

Opportunities to expand overseas were found to largely originate from participation in international networks. Network participation either pulled SMEs overseas, in the form of approaching customers, or the initiative originated from the firm itself but networks provided access to overseas business contacts. One internationally active case company took the decision to expand overseas as a result of being approached by a potential foreign business partner, another was inspired to engage in international business by a suggestion from a network partner, and the third expanded on the manager's own initiative. SMEs were thus sometimes pulled into overseas markets by customers, as also Wright et al. (2007) suggest. Moreover, two of the case



companies participate in exhibitions abroad to establish relationships with potential customers and distributors and therefore viewed international networks and events as very important for their ability to expand. The importance of networks for internationalization has been stressed by Johanson and Mattsson (1988) as well as Johanson and Vahlne (2003, 2009). Networks help firms identify new market opportunities and acquire knowledge about international markets (Chetty & Holm, 2000; Coviello & Munro, 1995; Ellis, 2011). The internationally active case companies largely used their network belongingness to establish relationships with overseas business partners and learn about overseas market opportunities. Domestic networks did however not constitute a significant driver for SMEs to expand overseas.

### ***5.1.3 Overseas Expansion to Boost Domestic Reputation***

A peculiar and somewhat unexpected factor driving internationalization was how international presence could help to boost domestic reputation and consequently firm performance. To the best of our knowledge, there seem to be little support in the literature for this driver, which may point to that it is especially pronounced, or even unique for the Japanese context. Some SMEs wish to export due to the positive effect on domestic business, which implies that they to a large degree are domestically focused. Being international gives SMEs a competitive edge and contributes to the firm's good reputation domestically. Among SMEs taking pride in their traditional manufacturing techniques, succeeding overseas was also recognized as a way to revive interest in these old techniques. If craftsmen understood that their products are appreciated in foreign markets, they would become motivated to pass on their skills to the younger generation and thereby enable the continuation of the business in its current form. Again, preservation was a key priority. This feature has received little attention in earlier internationalization research as a driver behind internationalization, and thus highlights an important aspect in Japan.

## **5.2 Internal Barriers to International Expansion**

In accordance with the RBV, the environment alone cannot explain organizational behavior, and internal resources available for overseas expansion are therefore important to consider (Barney, 1991). Ahokangas (1998) suggests that internationalization involves mobilizing unique and interdependent resources. At the same time, SMEs commonly experience limited resources as a major obstacle to enter international markets (Coviello & McAuley, 1999). In particular,

knowledge-based resources (Mejri & Umemoto, 2010), financial resources (Cernat et al., 2014) and human resources (Brush et al., 2002) are important considerations for internationalizing firms. In this study, all respondents recognized a lack of language skills. Information about overseas markets was another knowledge-based resource lacking. Insufficient financial resources were also addressed to inhibit the possibility to internationalize. Lack of human resources was however not pointed out to impede internationalization by the case companies themselves; only by external respondents who noted a lack of willing human resources to work abroad for the company and connected this to a risk-averse and inward-oriented labor market.

### ***5.2.1. Inadequate Language Skills***

What emerged as a recurring feature among Japanese SMEs was the lack of language skills, and especially English proficiency. Insufficient language skills is a major finding of our research to why Japanese SMEs hesitate to expand internationally as it was emphasized by all case companies and all but one external respondent. For example Mr. Nishimura noted that Japanese people hesitate to communicate in English. This insecurity about speaking English, as expressed by Professor Edman, is an obvious, but nonetheless vital explanation to why Japanese SMEs hesitate to expand internationally. Mr. Kojima even stated that in order to expand his overseas business further, he needs to hire more English speaking staff. Further, evidence from Blair (2010) and EF (2014) reinforce the low level of English proficiency in many Japanese firms. Language skills were also recognized in the literature as being necessary to succeed internationally when engaging in more complex international markets (Colapinto et al., 2015). Relating to management characteristics, Suárez-Ortega and Álamo-Vera (2005) point out how the manager's language proficiency is important to engage with overseas markets.

### ***5.2.2 Lack of Information About Overseas Business***

Information about overseas business was typically lacking in the case companies. The sought-after information included how to export, how to open up a production plant, where to open it, how to find new customers, what is demanded overseas and how to get financing. SMEs expressed how more information about how to actually start exporting or increase existing commitment was holding them back. The lack of such information was also recognized as an important reason for why the case companies not yet internationally active hesitated to

internationalize. Also, Blair (2010) and JETRO (2015b) observe a lack of information among Japanese SMEs about foreign markets and customers' preferences. Mejri and Umemoto (2010) found that a firm's knowledge accumulation shapes the firm's internationalization over time, and evidence of this could be observed among the case companies, who largely based their location decision on their accumulated knowledge. Mr. Nishimura had experience from studying in the U.S., which led him to start exporting to this country. Mr. Kojima had experience from China and therefore chose China as the first export market. Moreover, Hashim (2015) explains that SMEs' limited knowledge and experience at the international level constrain their internationalization, and this largely explained why the two case companies not yet internationally present had not taken the first steps out of Japan. This implies that knowledge and experience of how to conduct business in overseas markets facilitate expansion and lack of it acts as a barrier. Further, according to the stage model (Johanson & Vahlne, 1977, 2009), organizational experiential learning increases market knowledge and lead firms to increase commitment in overseas markets. Mr. Hosonuma gave an example and explained that after his firm had taken the decision to engage in international business, he received more information about international markets, which later on facilitated further expansion. The perceived lack of information about overseas markets points to that SMEs are eager to be knowledgeable and preferably rather sure about new paths they embark on. When undertaking an important strategic decision, SMEs wish to be certain that they will succeed. Since internationalization is perceived as a considerable risk and foreign markets are perceived as uncertain, the need for extensive information about overseas markets becomes even more pressing in order to succeed.

### ***5.2.3 Difficulties to Secure Financing***

Four out of five case companies recognized that internationalization requires sufficient financial resources and that lack of such prevents internationalization. Cernat et al. (2014) state that lack of financial resources is especially evident in SMEs. Governmental financial support helped one case company to overcome this barrier by enabling the firm to participate in overseas exhibitions. This shows that financial support helps firms to take the first step towards internationalization, and without this support the financial barrier might become too surmountable for SMEs to overcome. Johanson and Mattsson (1988) consider the government to be one of the stakeholders to which network ties are important. The importance of governmental

support in facilitating SMEs' international expansion is also recognized by Wright et al. (2007) as well as Hashim (2015).

#### ***5.2.4 Lack of Human Resources was Not an Outspoken Barrier***

Lack of human resources was not addressed as a barrier to internationalization by the case companies, only by the external respondents who pointed out a lack of willing human resources to work abroad for the company and connected this to a risk-averse and inward-oriented labor market. Sufficient human resources were recognized as a key factor for firms to start engage in international business (Brush et al., 2002; Colapinto et al., 2015). Brush et al. (2002) even found it to be the most crucial resource associated with internationalized SMEs compared with SMEs who remained domestic. None of the case companies had appointed employees explicitly responsible for developing international markets; instead the manager alone handled this. Why the interviewed managers did not highlight a need for 'global human resources' could be attributed to the central role of the manager in developing international markets. The manager was solely responsible for handling such strategic undertakings and only stressed the need for employees with English skills. In addition, the external respondents pointed out that there is a lack of human resources with the right attitude and willingness to work internationally. Without employees being open for internationalization, SMEs have a hard time expanding. This attitude may be a result of a lack of international skills and experience, leading Japanese employees to feel insecure about working abroad, in combination with the Japanese inward-oriented labor market (Lippert, 2015; Yanagida & Ngiang, 2013).

#### **5.3 Networking Internationally is Troublesome**

Lack of international networks, in the form of access to overseas business partners, was found to be a distinguishing feature among Japanese SMEs. The empirical findings pointed to a limited number of channels by which contact with potential international customers and distributors could be established. For two of the case companies active in international business, exhibitions in overseas markets constituted the only channel. Kneller and Pisu (2011) state that establishing contact with potential customers and partners is a major obstacle for SMEs wishing to internationalize but lack international networks, and Crick (2007) further notes the challenge with adequate representation overseas. The two case companies not yet involved in international

business were unsure about how to establish contact with foreign business partners and did not have any such connections today.

In the same way as network participation can open up opportunities for SMEs to internationalize, the lack of such network access limits SMEs' ability to enter and expand into foreign markets. As mentioned earlier, Johanson and Mattsson (1988) stress the importance of participating in networks to facilitate internationalization and state that the number and strength of a firm's relationships are related to their access to resources and overseas markets. Chetty and Holm (2000) found that networks are of particular importance for SMEs considering their resource constraints. Firms involved in networks are no longer restricted to their own resource limitations since they can use networks for resources needed to internationalize (Chetty and Holm, 2000; Sullivan Mort & Weerawardena, 2006). Hence, international networks can be seen as a bridge to overcome barriers to internationalization. The case companies did however not display a tendency to use their networks to bundle resources to be better prepared to enter foreign markets. The primary implication of network participation was that it enabled access to foreign markets and contacts. Domestic networks between firms are otherwise an important feature in Japan, and relationships are key to do business successfully. Firms tend to be keen to entertain their network ties domestically and it is therefore somewhat of a paradox that networking internationally is problematic. Seeing a firm's network position as a resource in itself as suggested by Glückler (2006) is to a large extent applicable also in the Japanese case as it serves as an enabler and facilitator of internationalization. The extent to which this resource is utilized and leveraged by Japanese SMEs is however rather limited. The case companies made few efforts to adapt or develop available resources in connection to their network. Revisiting the model by Ahokangas (1998), which suggests that internal and external resources can be adapted in a firm-oriented or network-oriented manner, an appropriate description of internationalizing SMEs in Japan is that internal resources are adapted in a firm-oriented manner. They make little use of external resources and do not develop resources in relation to other firms, but seek to internationalize on their own by learning from experience. Even though an SME has excellent domestic networking capabilities, these seldom extend to international networking. In fact, networking internationally appears to be rather troublesome. International engagements are perceived as difficult, and Johanson and Vahlne's (2003) statement that all relevant business activity is channeled through

networks would thus explain why SMEs hesitate to undertake internationalization decisions. Japanese SMEs remain *outsiders* in relevant international networks (Johanson & Vahlne, 2009).

The challenge of networking internationally appears to be connected to the difficulty of interacting with other cultures. Evidence from the empirical findings even showed a wish to, if possible, do business with other Japan-related firms present in foreign markets to avoid the obstacles associated with collaborating with foreigners. Kojima Senshoku was the only SME having overseas customers without connection to Japan, but it may here be relevant to point out that their foreign sales ratio was less than one percent. The external respondents described a hesitant attitude towards engaging in business with foreigners resulting from differences in business culture, which sometimes lead to miscommunication. They further explained that Japanese people have historically been exposed to little interaction with foreigners, which has resulted in uncertainty about collaborating with non-Japanese. Evidence of such uncertainty was expressed by Mr. Hosonuma, while Mr. Nishimura and Mr. Kojima displayed a more open and confident attitude. The more confident attitude was displayed by managers who had previous international experience; reinforcing how experience and having engaged with foreigners in the past reduce the perceived uncertainty.

#### **5.4 Japan's Domestic Environment Explains SMEs' Hesitation**

External parameters relating to the firm's domestic environmental context has been recognized to influence SMEs internationalization (Kuivalainen et al., 2012; Wright et al., 2007; Zahra et al., 2005). In this study, contextual factors were only addressed as drivers of internationalization by the internationally active case companies. None of the case companies recognized contextual factors to be a barrier impeding their internationalization. Instead, they referred primarily to internal resource limitations. Contextual factors such as Japan's history, geography and unique mindset were however addressed by the external respondents to be underlying explanations to SMEs' hesitant internationalization behavior.

##### ***5.4.1 A Large Isolated Island with a Uniform Population***

From the perspectives offered by the external respondents it became evident that a large part of the explanation to SMEs' hesitant internationalization behavior relates to Japan's history and

geography. Such contextual factors appear to have received little attention in earlier studies about barriers to SMEs' internationalization. The external respondents explained how SMEs' hesitant attitude can partly be seen as a result of Japan's long history of being isolated from the rest of the world. The isolation has created a strong identity of being Japanese, with a uniform population that is more inclined to focus on the differences between them and other cultures. This in turn makes interaction with overseas business partners difficult and limits SMEs' ability to create fruitful business ties with overseas counterparts. Also, the size of Japan's domestic market offers a significant explanation to why few SMEs internationalize. Despite the stagnation in recent years, Japan remains the third largest economy in the world (World Bank, 2016) and SMEs have thus enjoyed sufficient demand in the home market. Market size has been recognized by earlier literature, where Olejnik and Swoboda (2012) explain that SMEs from large economies are more likely to internationalize at a later stage than SMEs from small economies. Historical and geographical factors have resulted in a prominent domestic focus, where SMEs have not needed to consider internationalization. With a shrinking domestic market however, SMEs' long-term survival is threatened. They are now forced to expand internationally, but would rather remain domestic if they could. Moreover, institutional factors are found by Peng et al. (2008) to shape firms' international activities. In terms of informal institutions governing SMEs' behavior, the empirical evidence indicate that Japanese people have a tendency to follow the big mass, implying that since relatively few SMEs internationalize, there is no force dragging SMEs out of Japan. Following the big mass can be described as a kind of institutional isomorphism as suggested by DiMaggio & Powell (1983). In the case of Japan, it makes SMEs hesitant to internationalize as most SMEs only operate domestically and it is therefore safest to adopt a similar strategy as their peers.

#### ***5.4.2 Risk-aversion & Lack of Courage to Break with Traditions***

A risk-averse behavior, with little tolerance towards mistakes and failed entrepreneurs was pointed out to describe the Japanese culture by the external respondents as well as by Blair (2010) and Lippert (2015). Internationalization is perceived as a risk by many SMEs and as a consequence, few SMEs are internationalizing. There appears to be a fear of engaging in new, unknown activities such as expanding into foreign markets. These unknown activities become even more frightening considering that failing when embarking on such new paths is not

acceptable. Risk-aversion therefore impedes Japanese SMEs' willingness and readiness to expand overseas and requires courage to break with traditions. The fact that the case company Kojima Senshoku was established in the year of 1872 and internationalized only in the very last decade may illustrate how internationalization is not something that Japanese SMEs are eager to rush into. Also, the not yet active case company Azumaya that was established 1914 still remain domestic after more than 100 years in business.

Moreover, the classic Japanese model that used to work well in the past has grown obsolete and firms have not kept up with the changing market dynamics. Too much focus has been directed to developing the domestic market and attention has primarily been paid to ensure an excellent manufacturing process with superior quality and technology. This feature was recognized by Lippert (2015) who pointed to the possibility of too much domestic focus resulting in a “Galapagos syndrome”. As international competition amounts and Japanese firms have failed to sufficiently acknowledge the needs of the market, the self-confidence of Japanese firms have taken a hit as a result. The insecurity about what international markets demand, how to internationalize and whether the products offered will be good enough to foreign consumers contribute to SMEs' hesitation to internationalize. The case company Kojima Senshoku pointed to how their failure of properly adapting to the Chinese market lead to an unsuccessful venture and that they had to withdraw from China. As a result, their exports offering today consist of fabrics rather than products, which demands less adaptation and thus simplifies overseas expansion.

## **5.5 Managers' Influence on Internationalization Decisions**

### ***5.5.1 Managers are Ultimately Responsible for Internationalization Decisions***

All managers in the case companies were found to play a crucial role as decision-makers. They had the ultimate responsibility for the firms' decision-making and therefore also regarding internationalization decisions. Among the firms currently engaged in international business, the decision to expand internationally was taken by the manager himself. The case companies were family-owned businesses, which further reinforced the central role of the manager. The manager's role has been emphasized in existing literature already by Reid (1981) and Leonidou et al. (1998) who discussed the central role of the top management team in a firm's export



decisions. Managers are found to play an increasingly important role for internationalization strategies (Axinn & Matthyssens, 2002), and constitute the most fundamental resource in many SMEs (Brush et al., 2002). The empirical findings from this study strongly point to the unique positions of managers in SMEs, with the manager being solely responsible for internationalization decisions. No management *teams* were found to exist, and even if the manager was advised by other employees, the manager was in a sense found to be inseparable from the firm.

### ***5.5.2 Managers are Not as Entrepreneurial as Suggested by Theory***

The entrepreneur is recognized as a key factor influencing SMEs' internationalization (Jones & Coviello, 2005; Ruzzier et al., 2006). However, the extent to which the managers in Japanese SMEs are performing "international entrepreneurship" could be questioned. According to McDougall and Oviatt (2000: 903), international entrepreneurship can be seen as a "combination of innovative, proactive, and risk-seeking behavior that crosses national borders and is intended to create value in organizations". Moreover, Zahra and George (2002) explain international entrepreneurship as the process of creatively discovering and exploiting opportunities outside a firm's domestic market, in search of competitive advantages. This stream of research is describing a behavior that is proactive and risk-seeking, which does not always correspond to our empirical findings. The interviewed managers gave rise to a more mixed picture, where proactive decision-making sometimes prevailed but mostly, a reactive stance was taken and internationalization opportunities were not sought actively. On the contrary, opportunities often came to the managers. Risk-taking could be considered moderate, and the case companies' internationalization process typically followed a stepwise process with increasing overseas commitment over time and with experience. As entrepreneurial behavior is associated with proactive and risk-seeking behavior, and conceptualizes the manager as taking initiative and seeking change (Bateman & Crant, 1993; Simon et al., 2000), this characteristic has limited bearing on the Japanese managers interviewed in this case study. On the basis of the empirical evidence gathered, it may therefore be fair to question the extent to which the international entrepreneurship literature is fully applicable to SME managers in the Japanese context. Although the scope of the empirical base is limited, the collected evidence point to a greater variety of internationalization behavior than what is suggested in the international

entrepreneurship literature. Managers are furthermore conceptualized as strategic decision makers in the international entrepreneurship literature (Foss et al., 1995; Ruzzier et al., 2006), while the network models on the other hand deprive the manager of the ability to make strategic choices (Johanson & Vahlne, 2003; Mtigwe, 2006). The proactive manager shapes his or her own internationalization path and undertakes strategic evaluation of opportunities, while the reactive manager to a greater extent allows network partners to shape internationalization. Mr. Nishimura's entrepreneurial path is for example more of a strategic undertaking than Mr. Hosonuma's path, who rather reacted on suggestions from network partners to expand overseas.

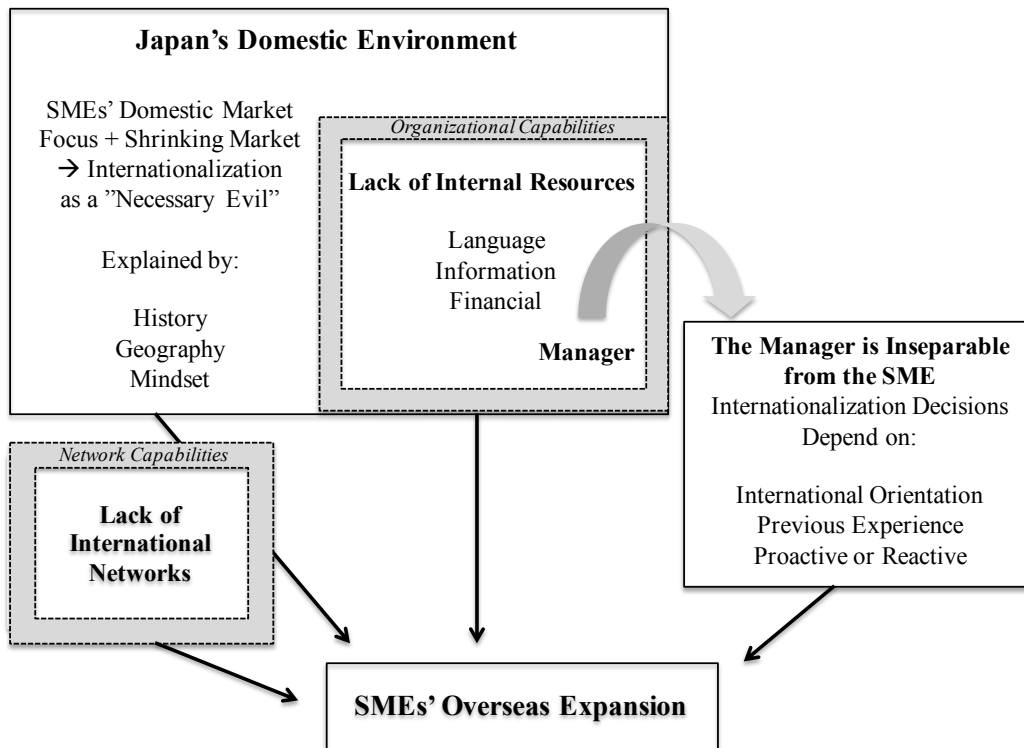
### ***5.5.3 Previous International Experience Shapes Internationalization Decisions***

Empirical evidence from the case companies showed that the manager's attitude towards international markets as well as previous international experience played a significant role in internationalization decisions. A positive attitude towards internationalization corresponds to what Acedo & Jones (2007) explain as international orientation. Managers with previous international experience exhibited a more open and positive mindset about international business in general. International experience also affected the decision of which country the firm started to export to or where investments were made. For example, since Mr. Kojima had previous experience from working in China he chose China as the company's first export market. Similarly, Mr. Nishimura had previous experience from studying in the U.S. and thus decided to first export to the U.S. Being knowledgeable of the local language and somewhat familiar with the country facilitated these two managers' internationalization decisions. Mr. Hosonuma was influenced by another manager's previous international experience when deciding to establish a production plant in Thailand. Furthermore, Mr. Kokubun stated that his previous experience from studying abroad was the main reason for why he wished to expand internationally. Having lived or worked abroad seemed to create a more positive attitude to international expansion and experience of interacting with foreigners reduced the perceived insecurity associated with doing business with foreign cultures. In this way, managerial capabilities, characteristics, experiences and orientation were important influences among the case companies in accordance with what Olejnik and Swoboda (2012) argues. Also, Manolova et al. (2002) as well as Clercq et al. (2005) point to that managers with previous experience from overseas markets develop an international orientation making them more likely to go abroad.

## 5.6 Summary and Adaptation of the Conceptual Framework

Figure 2 illustrates an adapted visualization to explain the factors contributing to SMEs' hesitation to expand overseas and how the manager relates to internationalization decisions.

Figure 2: Japanese SMEs' Hesitation to Internationalize and the Role of the Manager



Note: Figure compiled by authors.

A large part of the reason for why SMEs in Japan hesitate to expand internationally relates to the drivers of internationalization, which arise from Japan's domestic market conditions. The shrinking Japanese market was found to be an important force driving expansion as it threatens SMEs' long-term survival at home. Combined with the domestic orientation of SMEs and that international expansion is not always an intrinsic desire but that some SMEs were rather pulled overseas by network partners, this leads to that internationalization is perceived as a "necessary evil". The importance of, but difficulty associated with international networks was moreover established. SMEs made little effort to utilize international networks and did not pool or bundle their own internal resources with resources in their network, thus limiting the extent to which

international network participation was used as a way to overcome internal resource constraints. Lack of international network capabilities and access to relevant networks thus constituted barriers, as did lack of internal resources in the form of language skills, information about international business and financial resources. The underlying reasons why SMEs hesitate to internationalize relate to historical and geographical factors characterizing Japan's domestic environment as well as a unique Japanese mindset. Managers of Japanese SMEs were found to greatly influence internationalization decisions and could in fact be seen as inseparable from the firm. Managers can both drive and constitute a barrier to internationalization depending on the manager's international orientation, previous international experience and degree of proactivity in searching for internationalization opportunities.

## 6. CONCLUSIONS

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*This chapter presents the main findings and theoretical implications of the study. The concluding answer to the research question is based on findings drawn from the empirical evidence and analysis. Since the research question in fact consists of two parts, the different parts are presented separately. Thereafter, managerial implications are outlined followed by suggestions for future research.*

### **6.1 Findings and Theoretical Implications**

This thesis has studied SMEs' internationalization in the context of Japan and investigated why Japanese SMEs hesitate to expand internationally as well as managers' influence on internationalization decisions. Internationalization is a widely studied topic within the IB field, but as the set of internal and external influences on SMEs' internationalization are unique in each national context, country-specific studies are more fruitful to explain internationalization behavior. In the specific context of Japan, SMEs' internationalization remains largely uncovered, in particular their low level of international activity and reluctance to internationalize. Our findings are context-specific and constitute new knowledge in the Japanese setting. The findings add an updated empirical contribution for the Japanese context and could offer helpful implications for SME managers. Adhering to the growing body of literature acknowledging the important role of managers in internationalization decisions, this research looks specifically at how managers in Japanese SMEs influence decisions relating to international expansion. The qualitative nature of this research has enabled us to answer *why* there is a hesitation and *how* managers influence decisions in Japan; it has allowed for a deeper, contextual understanding of SMEs' behavior. At the same time, the multiple case study design has increased the generalizability of the findings.

By drawing primarily upon the RBV and network models to explain internationalization behavior, the findings show that the two streams of research are largely applicable to the Japanese case. SMEs' internal resources available for overseas expansion are important considerations and lack of sufficient resources therefore act as a barrier to internationalization. Moreover, network embeddedness is an important facilitator of international expansion and

consequently, lack of access to international networks and poor networking capabilities contribute to SMEs' hesitation. However, the findings also highlight that certain aspects are of little relevance and others have not been explored by existing theories. Japanese SMEs did for example make little use of their network embeddedness and undertook few efforts to share, bundle or pool resources with other firms in order to overcome their own resource limitations. The low level of network engagement is related to that networking internationally is perceived as troublesome. The use of external network resources as a way to complement internal resource constraints was seldom observed among Japanese SMEs. Findings specific to Japan include that drivers behind internationalization largely shape decisions to expand overseas. This connection is seldom made in existing literature. Also, the importance of historical and geographical factors as well as the unique Japanese mindset has been pointed out to influence the nature of internationalization decisions among Japanese SMEs. Moreover, theories on international entrepreneurship and managerial decision-making serve as the foundation for explaining how managers influence internationalization decisions. Conceptualizing internationalization as an entrepreneurial act is not fully applicable to the Japanese context as managers display varying levels of proactivity, international orientation and risk-aversion. This thesis has shed light upon internationalization behavior in a cultural setting where international entrepreneurship appears to be less pronounced. A more nuanced perspective is therefore needed to describe Japanese managers as they are largely influenced by the unique domestic environment.

The research question that has guided the thesis is: *Why do Japanese SMEs hesitate to expand internationally and how does the manager influence internationalization decisions?* The question will now be answered in the following two sections.

### ***6.1.1 Why Japanese SMEs Hesitate to Expand Internationally***

The reasons why Japanese SMEs hesitate to expand overseas is explained by the fact that they are driven to internationalize by forces that lie outside the firm, rather than an intrinsic desire to expand. The main force driving expansion is the shrinking Japanese market, which threatens SMEs' long-term survival at home. Internationalization was perceived as a way to compensate for falling domestic demand, and less connected to growth objectives. The long-term management objectives of *preserving* and *continuing* the business are key concepts in the

Japanese context and it is more appropriate to explain internationalization as a result of SMEs' survival instinct. Moreover, SMEs' network embeddedness played an important role in enabling internationalization opportunities. Network members, primarily customers, would sometimes pull SMEs out of their home market and SMEs did not always have an intrinsic desire to expand. In addition, drivers of internationalization largely had its roots in SMEs' domestic business, where case companies wanted to internationalize because of the good reputation that this created domestically. Expanding overseas to boost domestic business underlines SMEs' pronounced domestic focus, which contributes to a lack of dedication to overseas markets, which in turn contributes to SMEs' hesitation. The driving forces to internationalize result in that internationalization is perceived as a "necessary evil" by Japanese SMEs. This is the main reason explaining why Japanese SMEs hesitate to expand overseas.

Highlighting the importance of adequate resources available to internationalize, the case companies pointed to that a lack of internal resources acted as a barrier to overseas expansion. In particular, insufficient language skills, but also lack of information about international business and shortage of financial resources was recognized to be impeding factors. Inadequate language skills, especially English, make Japanese SMEs uneasy about communicating and interacting with foreigners, which contributes to their hesitation towards engaging in business overseas. Also the importance of, but difficulty associated with international networks constitutes a significant barrier. The number of international networking channels was limited and the act of networking was furthermore troublesome in an international context, which could be attributed to inexperience and uncertainty about interacting with non-Japanese business contacts. Since network participation is out of reach for many SMEs and a troublesome act for SMEs with access, the lack of international ties overseas constitutes a barrier to expansion and contributes to SMEs' hesitation to expand overseas.

The underlying reasons behind SMEs' perception of internationalization can be explained by historical and geographical factors as well as a mindset characteristic for Japan's domestic environment. These factors influence SMEs' ability and willingness to expand internationally. Japan's long history of being an isolated island has created a uniform population with a strong identity of being Japanese, resulting in that interaction with foreigners is both uncommon and

troublesome. Moreover, the Japanese market has generated sufficient demand at home, leading to that SMEs have not needed to internationalize until recently when the domestic market started to shrink. Also, the tendency of Japanese SMEs to follow their peers implies that as few SMEs have internationalized before, few take the step today. Risk-aversion and courage to break with traditions further add to that SMEs remain domestically focused and hesitate to expand internationally.

The most surprising findings include the extent to which SMEs' domestic focus influence internationalization decisions, and that expanding overseas could in fact be undertaken as a way to boost domestic business. The language deficiency was another finding easy to detect but no less surprising, considering how very pronounced this factor was against the background of Japan's level of economic development.

### ***6.1.2 How the Manager Influence Internationalization Decisions***

All managers of the case companies played a crucial role as decision-makers and were ultimately responsible for all major internationalization decisions. The decision to internationalize or not, as well as how, where and when to expand was up to the manager. Although we encountered examples of decisions taken with help from advisors, the central role of the manager cannot be underlined enough. In many ways, the manager was inseparable from the firm. Managerial characteristics such as international orientation, previous international experience and to what extent internationalization opportunities are proactively sought were found to largely influence the nature of internationalization decisions. A positive attitude and interest in overseas markets facilitated expansion, and was often the result of previous international experience from studying or working abroad. Previous international experience created an international orientation among managers, which lowered the perceived uncertainty associated with interacting with foreigners. Experience also largely dictated to which overseas markets the SME expanded. Moreover, evidence of reactive behavior dominated among SME managers. Rather than seeking opportunities to expand internationally themselves, some managers reacted on opportunities presented to them and expanded overseas as a result of a suggestion from partners within their network. With such reactive stance to internationalization, the extent to which overseas expansion can be seen as a deliberate strategic undertaking by managers is limited.



Connecting the manager's considerable influence on internationalization decisions with SMEs' hesitation to expand internationally, we can draw the conclusion that part of the hesitation is in fact the manager's hesitation. While drivers of internationalization were largely found to arise from factors external to the firm, internal resource limitations in the form of inadequate language skills and a perceived lack of information about overseas markets relate to managerial capabilities. Similarly, lack of international networking capabilities can be attributed to the manager, as the manager is ultimately responsible for developing overseas markets and establishing international business ties.

## **6.2 Managerial Implications**

This study has shed light on both firm-level and managerial influences on internationalization and offered explanations against the background of Japan's domestic environment. For SMEs who are internationally active or considering international expansion, these findings can serve as guidance to organizational internationalization requirements; i.e. internal and external resources helpful to expand overseas as well as the importance of networks. Managers of Japanese SMEs could greatly benefit from engaging with international markets and business partners in order to accumulate international experience, which facilitates internationalization. An undertaking such as improving the manager's and employees' language skills, in particular English, could lead to that more international opportunities are taken advantage of and interaction with overseas markets could be greatly facilitated. Improving the use of networks is another key takeaway for SME managers in Japan, seeing that they rarely utilize networks to bundle or pool resources to expand overseas. Collaboration and exchange of experiences between Japanese SMEs around difficulties associated with foreign markets could be a fruitful way to lower the perceived shortage of information of such markets. The hesitant attitude towards internationalization relates to that foreign markets are perceived as very different from the Japanese as well as uncertain and difficult to engage with. This perception does however seem to change as managers gain international experience. Undertaking efforts that facilitate the first step out of Japan is therefore encouraged, as this is likely to reduce the hesitant attitude towards overseas expansion.

### **6.3 Suggestions for Future Research**

Although internationalization is a widely studied phenomenon within the IB literature, its complexity and applicability to unique contextual environments need to be studied continuously due to the dynamic nature of such environments. This study has identified a number of features unique to Japan, which can explain SMEs' internationalization behavior. In terms of furthering the research within this field and in the specific context of Japan, a general recommendation is to conduct a broader study, incorporating a larger number of firms from different industries to be able to better generalize the findings. Including SMEs from a variety of regions in Japan is another recommendation to better reflect the plethora of perspectives and experiences, considering that this research only relied on SMEs in and around Tokyo. Moreover, when researchers study a specific national context with eyes belonging to another context and culture, the findings are to some extent colored by the researcher's lenses. This study has been conducted from a Western perspective, by researchers without any outspoken connection to Japan. Research from a Japanese perspective may emphasize other aspects and synthesizing such potentially different viewpoints would generate a more culturally dynamic understanding of Japanese SMEs' internationalization behavior. In addition, seeing that certain SMEs succeed to expand overseas, while other remain domestic, a better understanding of the differences between Japanese SMEs engaged in international business and Japanese SMEs only engaged in domestic business would clarify which key success factors that are important for internationalization.

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## APPENDIX

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### 1. Interview Guides

#### **Interview Guide for Case Companies**

##### *Background Information about the Firm and Manager*

1. What is your job title in the company?
2. How long have you worked for the company?
3. How long have you worked in your current position?
4. When was the company established?
5. Please describe briefly the business concept of the firm – what products or services are produced?
6. How many employees does the company have?
7. Who takes major decisions in your company?

##### *The Overseas Expansion Process*

8. When did you start overseas expansion?
9. How did you start overseas expansion? (Export, local incorporation, business alliance, licensing of technology, or other?)
10. How much (%) of your total sales come from foreign trade?
11. How has that percentage changed over time?
12. In which countries are you currently present?
13. When did you enter these countries?
14. What type of business do you conduct in these markets (exports/sales/production)?
15. If/When you are selling your products to foreign markets, are you changing/adapting your products to these markets?
16. If you are exporting, are you exporting directly on your own or through a distributor?
17. Who are your customers in the foreign markets?

##### *Internationalization Decisions*

18. Why did you take the decision to expand into international markets? What were the underlying reasons?
19. Have the motives for being international changed over time? If yes, how have they changed?
20. Is it important for you and your company to operate internationally? Why/why not?
21. Were there governmental incentives (e.g. loans, credits, governmental support) available to you when you first internationalized?
22. Are there currently governmental incentives available for expanding abroad?
23. Which barriers did you experience when you started to internationalize? How did you overcome them?

24. Are you experiencing barriers to further expand your business overseas?
25. Have you studied, worked or lived abroad?
26. Do you plan on further expanding your business abroad? Why/why not? What are the main reasons for this decision?
27. Where do you see your company in 10 years? More or less international?

### **Interview Guide for SME Supporting Organizations**

#### *Background Information about the Respondent and the Organization*

1. What role does your organization play in supporting Japanese SMEs' internationalization?
2. How has that role changed over time?
3. What is your personal experience from working with Japanese SMEs in general and their internationalization in particular?

#### *SMEs' International Expansion*

4. What are the motives behind internationalization of Japanese SMEs?
5. How have these motives changed over time?
6. Despite these motives, why do you believe that relatively few SMEs expand overseas?
7. How do you believe that Japanese SMEs perceive internationalization (e.g. important or not/difficult or easy)?
8. What are the main barriers for Japanese SMEs that want to expand abroad?
9. Do they manage to overcome these barriers? If yes, how?
10. What are the main issues for Japanese SMEs that operate internationally?
11. How would you say that Japanese SMEs' willingness to expand their business abroad has changed over time?
12. What do you believe is necessary for SMEs to become more international?
13. What role does the manager play in a firm's decision to expand abroad or not?
14. Has the role of managers changed over time?
15. Do you believe that managers facilitate or constrain expansion?
16. How do you believe that managers facilitate or constrain expansion abroad?

### **Interview Guide for Professors**

#### *Background Information about the Respondent*

1. What knowledge do you have about Japanese SMEs' internationalization and how is that knowledge related to your research?

#### *SMEs' International Expansion*

2. What are the motives behind Japanese SMEs' internationalization?
3. Despite these motives, why do you believe that relatively few SMEs expand overseas?
4. Have the motives for being international changed over time? If yes, how?

5. Which factors influence decision-making in an SME regarding internationalization?
6. Which barriers do you believe SMEs face when internationalizing?
7. How do SMEs overcome these barriers?
8. Have you observed a common way to internationalize among Japanese SMEs? If yes, how does that path look like?
9. How do you believe that Japanese SMEs perceive internationalization?
10. Is it important for Japanese SMEs to operate internationally? Why/why not?
11. Do SMEs perceive it as a high risk to expand their business abroad? If yes, what are the risks and how are they handled?
12. Is SMEs' approach to internationalization proactive or reactive, i.e., do they look for opportunities to expand the business abroad or is internationalization a result of demands from customers/suppliers or other stakeholders?
13. What role does the manager play in a firm's decision to expand abroad?
14. How does the manager's previous international experience influence internationalization decisions?