

INTERNATIONAL DIVERSIFICATION STRATEGIES AND THEIR ORGANIZATIONAL AND EXOGENOUS ANTECEDENTS

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ABSTRACT

International operations, with its multiplicity of objectives, can be seen as a diversification strategy, sometimes even as a strategic option taken as an effective alternative to product diversification. Focusing on a sample of SMEs of Portuguese manufacturing industries, this study analyzes the international diversification strategies and their organizational and exogenous antecedents. Specifically, entrepreneurial orientation and dynamic capabilities of the firm are two factors of organizational nature, while the environmental uncertainty arising from the diversity of the different markets is studied as an exogenous antecedent. Data collected in 390 companies through an online questionnaire, its processing and analysis through the use of a structural equations model suggest the existence of different types of influence of the antecedents, according to companies' options in various dimensions of the international diversification strategies. These results provide guidelines for managers and generate directions for future research.

KEY WORDS: international diversification, entrepreneurial orientation, dynamic capabilities, environmental uncertainty.

1. INTRODUCTION

Global international transactions have grown since 1990 at average annual rates, generally higher than the world's Gross Domestic Product (World Trade Organization, 2014). In line with the practical importance of the phenomenon, research has addressed different aspects of this theme, focusing the most important currents in the study of the relationships between different types of antecedents and the process of international diversification (eg Preece *et al.* 1999, José Acedo and Florin, 2006), on one hand, and the effects or consequences that, on the other hand, the implementation of such a strategy can have on the competitiveness of the company. Despite the large volume of research in this field, authors such as Hitt *et al.* (2006a) and Lu and Beamish (2006), either it in terms of establishing relationships between some types of antecedents and international diversification, or their influence on competitiveness and performance, given the enormous complexity of all this causal linkage, new factors and approaches should be investigated.

International diversification “may be defined as expansion across the borders of global regions and countries into different geographic locations, or markets”

(Hitt *et al.*, 1997: 767). It's a concept referring to the geographical scope of company's international presence (Goerzen e Beamish, 2003), which reveals the extent of its dependence on external markets (Thomas e Eden, 2004). According to Contractor (2007), the use of “international diversification” instead of “degree of internationalization” should be avoided, unless it is a reference to an explicit purpose of the company's global risk reduction. Nevertheless, researchers more related to the strategic management field have a broader perspective of international diversification strategy than the simple risk reduction through the geographic scope increase (Hitt *et al.*, 1994), considering it a way of improving competitiveness, which is why this research area has dedicated so much attention to the study of the relationship between international diversification and performance. (Hitt *et al.*, 2006a). Being this the prevailing perspective on the subject, international diversification strategies were here investigated along the two following dimensions: intensity and scope (multinational and multiregional).

2. THEORETICAL BACKGROUND AND HYPOTHESES DEVELOPMENT

2.1. Entrepreneurial orientation

The phenomenon of entrepreneurship has long been an intense object of study for several areas of knowledge, such as economics, sociology, psychology, etc. However, the primary justification for this lies in the widespread belief that the entrepreneurial activity, besides stimulating economic development in general, is also an important factor for the development of the business activity at the level of each individual business unit (Covin and Slevin, 1991). The concepts of entrepreneurship and entrepreneurial orientation, although closely related, refer to diverse realities, interposing themselves in the same way as content and process in the field of business strategy (Lumpkin and Dess, 1996). Thus, while entrepreneurship refers to the content, that is, to the type of “new entry” carried out, the concept of entrepreneurial orientation refers to the process adopted to achieve this entry (Lumpkin and Dess, 1996). Lumpkin and Dess (1996) further clarify that the designation “new entries” refers to actions to launch new entrepreneurial initiatives such as entering a new market through new or existing products (or services). In this study, in agreement with other works of the area (for example, Covin and Slevin, 1991; Lumpkin and Dess, 1996; Wiklund, 1999; Jantunen *et al.*, 2005), entrepreneurial orientation will be centered at the level of the company itself, considering it as the basic unit of analysis. Accordingly to Covin and Slevin (1991), this perspective reveals advantages in relation to the models centered on “traits” or individual characteristics because the effectiveness of an entrepreneur always ends up being evaluated through the performance of the organization in which it is inserted.

2.2. Dynamic capabilities

The capabilities derive from the resources and the way they are integrated and articulated to carry out the activities of the company. Within organizations, therefore, the use of capabilities presupposes the interconnection between resources according to complex patterns of coordination among all the assets involved. It is with the repetition in the use of their capacities and the resulting experience that the company is creating its organizational routines (Nelson and Winter, 1982). These routines constitute for the organizations what competences are in the case of an individual (Ruzzier *et al.*, 2006). Some organizations reveal that they are able to continually develop, update, expand, and reconfigure their organizational capacities, leading to higher ones that can replace them with benefit. In this perspective, the search for the sources of competitive advantage should be seen as an infinite and continuous process (Collis, 1994). It is to this continuous process that Teece *et al.* (1997) designate dynamic capacities. Specifically, dynamic capabilities refer to the process whereby skills and resources can be developed, deployed,

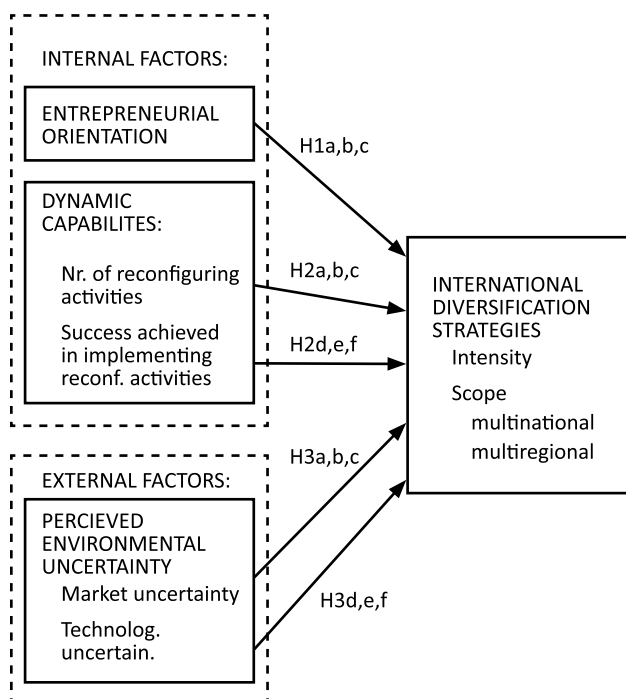
and protected so that they can best cope with rapid changes in their external context (Teece *et al.*, 1997).

By its nature, international activity requires the presence of dynamic capacities that allow the firm a certain compensation of the disadvantages of its condition of foreign entity (that is, of its liabilities of foreignness), having to compete with its local competitors and other origins (Luo, 2000; Luo and Mezias, 2002). That is, success in international diversification processes is closely associated, not only with the resources and capabilities available to the company, but also with its capacity to continually reconfigure and adjust these assets to the contingencies of the internationalization process (Kogut and Chang, 1996).

2.3. Perceived environmental uncertainty

One of the central aspects of the company’s environmental considerations is the inevitability of decision makers to deal with uncertainty in the analysis and interpretation of “signs to be removed” from this configuration of external conditions (Duncan, 1972). It is precisely this necessarily subjective realization of the existence of this uncertainty in the exogenous organizational environment, that authors of various scientific areas related to the management of organizations, have come to call it perceived environmental uncertainty (Duncan, 1972; Gordon e Narayanan, 1984; Waldman *et al.*, 2001; Dimitratos *et al.*, 2004; Matanda and Freeman, 2009). Accordingly to Ganesan (1994), uncertainty derived from the diversity of its external global environment encourages the strengthening of a company’s international diversification of strategies. Figure 1 presents the conceptual model of this study.

Figure 1. Conceptual model



Source: Authors

2.4. Entrepreneurial orientation and international diversification

Oviatt and McDougall (1995) report that internationalization is triggered by the entrepreneurial ability to identify opportunities in other markets. In other words, entrepreneurial orientation is recognized as an enabler of entry into new markets, in particular markets outside the domestic base of an organization, given the "important role it plays in determining the company's behavior when it is internationalized" (Baldegger and Schueffel, 2010). Consequently, the following hypotheses are put forward:

Hypotheses 1a, 1b, 1c: The degree of entrepreneurial orientation has a positive effect on international diversification in terms of (1a) intensity, (1b) multinational scope and (1c) multiregional scope.

2.5. Dynamic capabilities and international diversification

International diversification is a process that usually occurs in a context of great uncertainty, involving high risks and costs that constitute serious obstacles to the implementation of this type of strategy (Hitt *et al.*, 2006a). In particular, in the case of smaller firms, due to their natural scarcity of resources (Buckley, 1989; Kuo and Li, 2003; Cerrato and Piva, 2010). Teece (2007) argues that for analytical purposes, dynamic capabilities can be disaggregated into the ability to detect and shape opportunities and threats, to seize opportunities, and also to maintain competitiveness through reinforcement, combination, protection and, if necessary, reconfiguration of the company's tangible and intangible assets. This way, firms with advanced reconfiguration capabilities (i.e. dynamic capabilities) will be able to identify and seize opportunities not only through new combinations of resources but also through well-organized processes and structures, for their global intervention (Jantunen *et al.*, 2005). In addition to the effect of the firm's own involvement in the company's recombination of assets, it will still be expected that the degree of effectiveness achieved in the implementation of these changes will, in turn, also have an influence (Edmondson *et al.*, 2001; Griffith and Harvey, 2001; Jantunen *et al.*, 2005). Consequently, the following hypotheses are formulated:

Hypotheses 2a, 2b, 2c: The level of involvement in reconfiguration activities has a positive effect on international diversification in terms of (2a) intensity, (2b) multinational scope and (2c) multiregional scope.

Hypotheses 2d, 2e, 2f: The level of success achieved in the implementation of reconfiguration activities has a positive effect on international diversification in terms of (2d) intensity, (2e) multinational scope and (2f) multiregional scope.

2.6. Perceived environmental uncertainty and international diversification

Several research works from various areas such as strategic management, international business, etc. suggest that the perceptions of top managers about the external environmental reality of their firms influence their strategy choices (Miller and Friesen, 1978, Milliken, 1987, Keats and Hitt, 1988, Milliken 1990, Miller 1993). According to Zahra *et al.* (1997), international intervention reduces the risk of fluctuations in the domestic market of the company, contributing, through the diversification of the market for greater stability. Confronted with the dynamism and instability of its environment, that is, the markets in which it operates at any given time, the company can try to reduce the uncertainty arising from these contextual conditions, reinforcing its international presence (Hitt *et al.*, 1994; Zahra *et al.*, 1997).

Following in the footsteps of Miller and Dröge (1986), two aspects of perceived environmental uncertainty will be investigated: market uncertainty and technological uncertainty. Firms in more turbulent market contexts and thus more uncertain, often show greater attention to changes in these markets (Jaworski and Kohli, 1993; Atuahene-Gima and Murray, 2004), and thus in response to those who are more pressured to make timely decisions about their strategy for international operations (Etemad, 2004). A more turbulent technological environment, on the other hand, can create in the companies, opportunities for the development of new products that can be used to expand its customer base (Sheng *et al.*, 2011), challenging them to improving and updating the products of its current range and maintain or strengthen its competitive position (Sheng *et al.*, 2011). Thus, the following hypotheses were established:

Hypotheses 3a, 3b, 3c: Market uncertainty has a positive effect on international diversification in terms of (3a) intensity, (3b) multinational scope and (3c) multiregional scope.

Hypotheses 3d, 3e, 3f: Technological uncertainty has a positive effect on international diversification in terms of (3d) intensity, (3e) multinational scope and (3f) multiregional scope.

3. METHODOLOGY

Sample selection was based exclusively on a database (of Portuguese exporter companies) from the AICEP - Agency for Investment and Foreign Trade of Portugal. As basic profile in terms of firm size, we adopted the SME definition according to the European Union and, so, the minimum number of 10 employees and a maximum turnover EUR 250 million were defined as requirements. Besides, in line with Beleska-Spasova e Glaister (2010), we established, as additional conditions, the involvement in international business at the time, and if this involvement should be, in terms of minimum previous time period, of at least five years, nevertheless, without defining a minimum value for the foreign sales to total sales ratio. The five years minimum period of involvement in international business was considered

sufficient to assess the impact of international diversification in performance (Beleska-Spasova and Glaister, 2010; Beleska-Spasova *et al.*, 2012). After adjusting the original database to the requirements, a list of 2895 companies were then compiled, and, so, the sampling frame used in the study was established. As final result of the data collection process, we obtained 390 valid questionnaires, corresponding to an effective rate higher than 16%, which can be considered as satisfactory, since the average percentage level of response in case of questionnaires sent to top managers is typically between 15 and 20% (Menon *et al.*, 1996).

4. RESULTS

To assess the goodness of fit of the measurement model, absolute measures as the chi-square statistical significance (χ^2) and the RMSEA (Root Mean Square Error of approximation) were used. The overall chi-square was found significant ($\chi^2 = 385.46$; d.f.= 183; $p < 0.000$) and the RMSEA = 0.039, which is an indicative factor of a good fit. Additionally, three incremental measures of fit were assessed: Comparative Fit Index (CFI=0.99), Incremental Fit Index (IFI=0.98) e Tucker-Lewis Fit Index (TLI=0.98).

Table 1. Structural model results

Hypotheses	β	T	Supp./Not supp.
H1a: Entrepr. Orientation → International Diversification (Intensity)	0,09	1,46	Not supported
H1b: Entrepr. Orientation → Internat. Divers. (multinational scope)	0,38	7,25***	Supported
H1c: Entrepr. Orientation → Internat. Divers. (multiregional scope)	0,34	4,79***	Supported
H2a: Dynam. Capab. (nr. of reconfig.activ.) → Int. Divers. (Intensity)	-0,05	-1,22	Not supported
H2b: Dynam. Capab. (nr. of reconfig.activ.) → Int. Divers. (multinat. scope)	0,04	1,26	Not supported
H2c: Dynam. Capab. (nr. of reconfig.activ.) → Int. Divers. (multireg. scope)	0,02	0,41	Not supported
H2d: Dyn. Capab (success in impl. reconf. activ.) → Int. Divers. (Intensity)	0,02	0,62	Not supported
H2e: Dyn. Cap. (success in impl. reconf. activ.) → Int. Divers. (multinat. scope)	0,15	4,75***	Supported
H2f: Dyn. Cap. (success in impl. reconf. activ.) → Int. Divers. (multireg. scope)	0,13	2,84**	Supported
H3a: Perc. Environ. Uncert. (tech.) → International Diversification (Intensity)	0,51	7,57***	Supported
H3b: Perc. Environ. Uncert. (tech.) → Int. Divers. (multinational scope)	0,07	1,37	Not supported
H3c: Perc. Environ. Uncert. (tech.) → Int. Divers. (multiregional scope)	0,02	0,26	Not supported
H3d: Perc. Environ. Uncert. (mark.) → International Diversification (Intensity)	0,18	2,74**	Supported
H3e: Perc. Environ. Uncert. (mark.) → Int. Divers. (multinational scope)	0,22	4,14***	Supported
H3f: Perc. Environ. Uncert. (tech.) → Int. Divers. (multiregional scope)	0,16	2,14*	Supported
<i>*p<0.05; **p<0.01; ***p<0.001. Two-tailed test</i>			

Source: Authors

The conceptual model was tested using structural equation model. Results of this test suggest an acceptable fit of the model to the data: $\chi^2 = 461.68$; d.f.=192; $p < 0.000$; RMSEA = 0.046; CFI = 0.98; IFI = 0.96; TLI = 0.96. Table 1 depicts the estimates of the parameters and the T-values obtained for the tested hypotheses.

Table 2. Effect of the control variables

Control Variables	β	T
International Experience → International Diversification (Intensity)	0,10	2,41*
International Experience → Internat. Divers. (multinational scope)	0,05	1,42
International Experience → Internat. Divers. (multiregional scope)	-0,17	-3,48***
International Business Assistance → Int. Divers. (Intensity)	-0,13	-2,61**
International Business Assistance → Int. Divers. (multinat. scope)	0,28	6,71***
International Business Assistance → Int. Divers. (multireg. scope)	0,13	2,40*
<i>*p<0.05; **p<0.01; ***p<0.001. Two-tailed test</i>		

Source: Authors

The effect of the control variables used are presented in Table 2.

5. DISCUSSIONS AND IMPLICATIONS

The results of this work reveal that the entrepreneurial orientation has different effects on the two dimensions of the international diversification construct investigated: intensity and scope. Although positive in both cases, the result of the stock assessment on the intensity of international diversification, in a somewhat surprising way, does not present significant values to support the hypothesis that there is an important role for that type of guidance. The explanation may be that the firms with the highest degree of international diversification are the ones that are most “installed” in terms of internationalization strategy. “Installed” in the sense that they have defined the guidelines for their overseas business for a longer period of time, and that they have therefore come to realize these types of options, already with more consolidated structures and processes. This “accommodation” could mean a less markedly entrepreneurial presence vis-à-vis those other companies that are more diverse in scope. Regarding the scope of international diversification, whether in the multinationality guideline (measured by the number of countries in which the companies operate) or in terms of the distribution of international business across the globe, degree of entrepreneurial orientation has revealed a very significant association with more diversified companies internationally. This suggests, therefore, the existence of an important role of this position as an enabler of international diversification in the “scope”, since companies in this situation have been “exposed” to a greater number of contexts (national and regional). In other words, they were more willing to adjust their practices and assume a greater diversity of risks, thus revealing more active entrepreneurial behavior (Lumpkin and Dess, 1996).

This work investigated the influence of dynamic capacities on the choices made by companies with regard to their strategies of international diversification, since any change in intensity or scope of that strategy is likely to be influenced to a greater or lesser degree by the type of use in resource constraints and organizational routines (Villar *et al.*, 2014). Therefore, although in many cases companies may be involved in reconfigurations of their resources and capabilities, with a view to strengthening their international diversification strategies, this effort may not be sufficient. In fact, as the results suggest, this commitment may not lead to success in this design, if the necessary skills and competences are not simultaneously present to effectively carry out these reconfigurations (Jantunen *et al.*, 2005). That is to say, also in this case, being active is obviously not the same as being effective. The lack of a significant effect of the success achieved with the reconfigurations carried out on the intensity of international diversification, as in the case of entrepreneurial orientation, may be due to the characteristics of the sample used.

Specifically, there was a significant and positive effect of market uncertainty on all the dimensions of international diversification studied: intensity, multinational scope and multiregional scope. The results suggest, therefore, that

companies subject to a greater degree of market uncertainty, being more attentive to their external environment, tend to implement international diversification strategies both more intense and broader, in the latter case in references the two perspectives investigated, number of countries and distribution of international operations by regions of the globe. Regarding technological uncertainty, there was a positive and significant influence only in the case of the intensity of the international diversification, hypothesis H3a, thus not confirming the hypotheses H3b and H3c that suggested the existence of a positive effect of this type of uncertainty on the two strands (number of countries and distribution by regions) from the scope of international diversification.

Adapting to these conditions of technological turbulence, and therefore developing the necessary skills and competences, companies can, when necessary, re-evaluate their product ranges and the markets for which they are intended. The eventual success in this continuous “confrontation” with its external technological context in the markets of the countries in which it already has international operations can, therefore, in a context of global economic turbulence, lead to decisions to strengthen the presence in these markets in terms of investment.

Therefore, particularly when the international diversification adopted privileges the scope dimension, managers of SMEs should pay special attention to the need to develop (or reinforce) an orientation of an entrepreneurial nature at the level of the organization. In addition, as a third recommendation, SME managers should, take into account the specific characteristics of the international operations in which they are involved, in order to identify carefully which activities are most critical to the continuation of these operations. Managers responsible for SMEs, making use of their dynamic capabilities, should also provide the effective reconfiguration of assets of those associated activities, a process for which, as previously seen, entrepreneurship will also be an important requirement. This way, we will try to avoid involvement in spurious reconfiguration processes, since, as we have also concluded, only the effectiveness of this involvement can influence international diversification strategies. The previous recommendations should also be complemented by the need for managers to strive for regular monitoring of the external environmental realities of their companies so that, in the context of their international business, they can accommodate the changes that this reality requires.

6. LIMITATIONS AND DIRECTIONS FOR FUTURE RESEARCH

Two main limitations of the study should be noted. First, its cross-sectional nature, since for many of the studied variables, involving processes over the time, the use of longitudinal data, therefore (related to a time-series), would allow a more appropriate assessment of relationships between the main variables. Secondly, with

regard to the central theme itself, the strategies for the international diversification of SMEs, despite the various dimensions used (one referring to intensity and two to scope), the non-investigation of the cultural dimension is potentially a limitation (Sullivan, Zahra *et al.*, 2000, Evans and Mavondo, 2002, Shirokova and McDougall-Covin, 2012).

Concurrently, two suggestions for future studies are presented. First, a longitudinal study, also focusing on SMEs, once the scarcity of research work of this type on the current theme is a major problem. Secondly, because of the additional contribution it could make to the study in terms of understanding the international activities of SMEs, the cultural dimension should also be the subject of research in future works.

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