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Social capital dynamics and foreign market entry

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ABSTRACT

This paper explores the dynamics of social capital in 121 new foreign market entries (FMEs) of 24 Swedish and New Zealand small- to medium-sized enterprises in the early and later phases of their internationalization. Its main contribution is the systematic assessment of the roles and forms of social capital over time and across countries, thus providing greater insight into the social capital concept. We separate social capital into efficacy and serendipity roles (economic dimension) and direct and indirect relationships (structural dimension). Efficacious and direct social capital is associated with early FMEs, while serendipitous and indirect social capital is more prevalent with later FMEs, indicating that social capital changes with (and is dependent on) FME. Moreover, while geographical proximity does not appear to affect the economic dimension of social capital, it is important for the structural dimension.

1. Introduction

Small- and medium-sized enterprises (SMEs) often have limited financial and managerial resources available for international expansion (Chetty & Campbell-Hunt, 2003). They also often lack knowledge about foreign markets and have few international contacts. Consequently, SMEs may have to enter foreign markets consecutively rather than simultaneously, and may have to limit the number of foreign markets in which they operate. Therefore, the decision about *which* foreign markets to focus on is among the most pivotal for long-term success of internationalizing SMEs (Ellis, 2000).

One important explanation for how SMEs overcome resource limitations in order to internationalize is that they use relationships they have with other firms (Chetty & Wilson, 2003; Wilson, Chetty, & Shergill, 2004). For example, it is frequently argued that to succeed internationally firms must acquire information about foreign markets from external parties (Majkgard & Sharma, 1998; Presutti, Boari, & Fratocchi, 2007; Wilson et al., 2004). Relationships may then be used to identify and exploit specific business opportunities. Drawing on the expertise of other firms in a relationship network can, thus, improve international performance (Blomstermo, Eriksson, Lindstrand, & Sharma, 2004).

A firm's network of relationships and the resources that can be acquired from the network may be referred to as the *social capital* of the firm (Adler & Kwon, 2002; Bourdieu & Wacquant, 1992; Nahapiet & Ghoshal, 1998; Yli-Renko, Autio, & Tontti, 2002). There is a substantial number of studies that address how social capital impacts on SMEs' internationalization, not the least foreign market entries (FMEs), although not all studies actually use the term social capital. Some of this research focuses specifically on how social capital enables internationalization (e.g., Agndal & Chetty,

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2007), while other studies look at the importance of social capital *relative* to other factors in explaining FME (e.g., Andersen & Buvik, 2002; Ellis, 2000; Ellis & Pecotich, 2001).

Arguably, social capital is dynamic as it may increase as well as decrease over time. This happens as firms deepen existing relationships, establish new ones and terminate problematic ones (Rauch, 2001). For the internationalizing SME, this means that the social capital available when doing business only domestically is likely to be different from the social capital available when the firm has extensive international sales (Chetty & Wilson, 2003). While the dynamic nature of social capital is often implied in internationalization research, it should be highlighted that few studies explicitly consider how the social capital of the firm *changes* during the internationalization process (cf. Coviello, 2006). Consequently, there is a dearth of research on the dynamic interplay between social capital and international growth (Yli-Renko et al., 2002).

Social capital can both affect and be affected by FMEs, depending on when it is employed in the firm's internationalization process. To our knowledge, few—if any—studies approach social capital and international expansion in this way. Our aim is to address this gap. More precisely, the purpose is to study the dynamic influence of social capital on SMEs' FME at different points in the internationalization process. In addition, we extend our exploration of social capital dynamics by comparing Sweden and New Zealand, two small export-dependent countries with quite different spatial implications in terms of multinational investment and access to markets.

The remainder of this article is divided into six main sections. The next section reviews the literature on social capital and SME internationalization and develops five propositions. Here we contribute to the literature by combining theory of social capital, its dynamics, roles and forms, with the FME literature into one framework. The propositions are summarized in a theoretical model. To test the robustness of this framework, we undertake a systematic process of case study analysis and coding, as well as conducting exploratory statistical analysis on the sample comprising our study. This is described in the subsequent sections focusing on method of research and presentation of results. The major themes emerging from our data are further illustrated by exemplar case studies of FMEs. The final part of the article contains discussion, conclusions, implications and limitations of the study.

2. Literature review and propositions

2.1. Social capital and its dynamic nature

The social capital concept first appeared in sociology (e.g., Bourdieu, 1986) and then in economics (e.g., Coleman, 1988). Whilst numerous, sometimes conflicting, definitions can be found, Patulny and Svendsen (2007, p. 32) argue that, on a general level, research "… has consolidated around an understanding of social capital as norms and networks of social cooperation". With its transition into management, understandably social capital studies increasingly focus on the *resources* available through networks. Although some scholars emphasize resources and relationships that can be "mobilized in purposive action" (Lin, 2001, p. 12), others consider both "actual or potential resources" (Bourdieu, 1986, p. 248), the latter perhaps unknown but still present in the network. To include these, we draw on Nahapiet and Goshal's (1998, p. 243) frequently cited definition of social capital, i.e. "the sum of the actual and potential resources embedded within, available through, and derived from the network of relationships possessed by an individual or social unit […] social capital comprises both the network and the assets that may be mobilized through the network". Consequently, social capital includes the network of relationships, which is a *structural* dimension, as well as the usefulness of the network of relationships, which is an *economic* dimension. In effect, social capital allows firms to access intangible resources controlled by other firms and individuals, such as knowledge and contacts. They can also allow access to more tangible resources, such as means of production.

We contend that social capital is not static but highly *dynamic*, as its structural and economic dimensions change over time. Evidence from the extant literature supports this notion. For instance, studies show that early on in a firm's history, entrepreneurs benefit from social capital in the form of supportive resources from family and friends (Birley, 1985; Wilson & Appiah-Kubi, 2002). As the firm commences operations, it starts to develop more social capital in the form of relationships with customers and suppliers (Larson & Starr, 1993). As the number of relationships increases, the variety and the extent of resources that firms can access through these relationships also increase. For example, third parties can increasingly act as linkages to other networks (Burt, 1992; Granovetter, 1973). We can, therefore, expect a correlation between years in business and the social capital of a firm, both in terms of the nature of social capital and the extent of social capital available.

It can be difficult, however, to distinguish elements of social capital, the ways in which it is created and the benefits it yields (Woolcock, 1998). We deal with this issue in three ways. First, based on the notion that social capital is *dynamic*, we distinguish between earlier and later international market entries, recognizing that the latter will be informed by developments in social capital that did not benefit the former (cf. Johanson & Vahlne, 1977, 1990, 2003). This allows for changes in the firm's absorptive capacity (Cohen & Levinthal, 1990). More specifically, we distinguish phase of internationalization as earlier within the first 3 years of first FME, and later beyond 3 years since the first FME. Second, we consider the *economic* dimension of social capital, by recognizing two roles that social capital may play in internationalization, namely the efficacy and serendipity roles (cf. Chetty & Agndal, 2007), acknowledging that the internationalizing firm's support needs can differ over time and are likely to be related to its social capital. Third, we