

AN EXPOSITION OF RESOURCE CAPABILITIES FOR SMEs IN THE EMERGING MARKETS

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Abstract

Emerging markets' small and medium sized enterprises (SMEs), despite having enormous growth potential and significance in the economy, have not been able to harness the advantages of internationalisation and subsequently have fallen short in facing the challenges of globalised competition. The purpose of this study was to review and explore the importance of the resource capabilities, building on the literature from the resource based view (RBV), (core) competency and dynamic capabilities theory, as the main rationale behind their significance in the SME internationalisation. This study intends to provide conceptual clarity about the resource capabilities and their importance in providing the SMEs in the emerging economies, the competitive edge to sustain themselves in today's business environment. The study concludes with an agenda for future research.

Key words: SMEs, resource capability, emerging markets

JEL: M100, L200

1 Introduction

While most research concerning internationalisation strategy has focused on large and multinational corporations (MNCs), this issue is becoming increasingly important for small and medium sized enterprises (SMEs) (Filatotchev, Liu, Buck & Wright, 2009), especially for those that internationalise during the early stages of their organisational life-cycle (Wright; Westhead & Ucbasaran, 2007). The existing literature often refers to these firms as 'born global' firms in the existing literature (Rennie, 1993; Oviatt & McDougall, 1994; Autio, Sapienza & Almeida, 2000; Zahra, Ireland & Hitt, 2000). According to many scholars, even though numerous studies have analysed the factors that drive the internationalisation of smaller firms (Gabrielsson & Kirpalani, 2004; Knight & Cavusgil, 2004) the overall understanding of this phenomenon is still limited, and previous studies have not been able to capture the dynamic nature of internationalisation decisions that occur over many years (Kamakura, Ramon-Jeronimo & Grave, 2012).

Research that examines new ventures, "born-global" firms, small and medium-sized enterprises (SMEs), and multinationals enterprises (MNEs) has provided an array of findings regarding the drivers of internationalisation and the factors that contribute to the success and performance of firms in international markets. Management literature has examined top management team (TMT) characteristics; and entrepreneurship literature has examined the innovativeness, risk-taking, and competitive aggressiveness of individuals and organisations as the first to act upon opportunities given various conditions of market risk (Radulovich, 2008). Concurrently, innovation research, encompassing new product development (NPD) and new service development (NSD), has shed light on the adaptation of a firm's products/services to enhance market share and create performance advantages (Radulovich, 2008). However, with regard to the effects of internationalisation on firms, empirical results are mixed (Hitt, Hoskisson & Kim, 1997). Researchers have a limited understanding of the performance benefits of intangible resources (Radulovich, 2008), and how firms attain sustained competitive advantage (Parayitam &

Guru-Gharana, 2010). Proponents of the resource based view posit that superior intangible resources provide sustainable competitive advantages and superior performance. However, the means by which advantages are created in international operations involves an understanding of firm resources and differences in consumer/clients' needs across borders.

In emerging markets, like Asian, African and Latin American countries (e.g. India, South Africa, Mexico etc.) innovative actions are fundamental for the long-term success of the firm. Due to the increasing diversity of products and production processes (Coombs & Metcalfe, 1998) intangible assets and knowledge has become more important. Additionally, operating in foreign markets would allow small firms to become stronger players in their home market (Lages & Montgomery, 2004), and achieve growth (Kuuluvainen, 2012).

Internationalisation in general and exporting in particular; the first stage of internationalisation (Jones, 2001), can enhance a firm's capability, and make it much more flexible for taking business risks (Young et al., 1989). After the topical review of the theories of internationalisation e.g. stage model, knowledge based view (KBV) and resource based view (RBV) etc., it was observed that resource based view and subsequently resource capabilities take precedence for this study. Hence, in the following paragraphs, a brief review of the streams of resource based view, competence approach, and dynamic capabilities approach, is presented as the three theoretical frameworks to describe the resource capability of a firm, and its importance to perform in dynamic environments. The study concludes with an agenda for future research.

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Literature review

Extant international business theory suggests that internationalising firms possess certain ownership advantages such as size, superior technology, unique products, or special managerial/marketing know-how (Chen & Chen, 1998). However, many firms with international activities are small and seemingly with few resources and capabilities, and conventional theory does not provide an

adequate explanation for either their motivation or the mechanism of their internationalisation (Wright et al., 2007). Previous research suggests that born global firms create sustainable competitive advantages based on unique technologies and innovation, which they leverage worldwide (Oviatt & McDougall, 1994; Bell, 1995; Keeble, Lawson, Lawton, Moore, & Wilkinson, 1998; Rugman & Wright, 1999; Jones, 2001; Stray, Bridgewater & Murray, 2001; Hashai & Almor, 2004; Knight & Cavusgil, 2004). The ability to create proprietary technologies and transform product and process innovations into business activities allows small firms to create competitive advantages that may support their internationalisation strategy. Studies show that born global companies frequently have a superior capability to perform R&D activities (Manalova, 2003; Knight & Cavusgil, 2004). The resource based and dynamic capabilities perspectives also suggest that network partnerships are important to many small firms as they provide important social capital (Davidson & Honig, 2003). These partnerships may be especially important in the emerging markets as they enable firms with relatively weak internal resources to access complementary resources and capabilities within the wider network (Bruton et al., 2003). Redding (1996) portrays these firms as weak organisations linked by strong networks, suggesting that network-related factors should play an important role within the context of their internationalisation decisions and performance.

The resource based view of the firm focuses on the internal organisation of firms and factor market imperfections. Clark (2000) emphasises that this focus of resource based view toward a firm highlights the heterogeneity of firms, their varying degrees of specialisation, and the limited transferability of corporate resources. The strategy process then revolves around identification and exploitation of idiosyncratic resources and distinctive competencies. Resource based view also conceptualises firms as unique collections of resources and routines from which competitive advantages can be drawn when those are valuable, rare, inimitable and non-substitutable (e.g. Penrose, 1959; Wernerfelt, 1984; Barney, 1991). The logic of the resource based view has been taken further in the (core)

competence approach to formulate strategies. This view, developed by Prahalad and Hamel (1990), argues that unlike the physical assets of a firm, which diminish over time, the core competencies of a firm are enhanced as they are applied and used, and are the source of sustainable competitive advantage. These core competencies in turn lie behind the firm's ability to bring together intangible resources (such as skills and technologies) enabling it to provide unique value to the customers.

More recently, the resource based view has been extended to the dynamic markets by the scholars. The logic is that the resource based view does not satisfactorily explain how and why certain firms sustain their competitive advantage in dynamic business environments. Teece, Pisano and Shuen (1997) expanded the resource based view of the firm to explore the possibility of a theory of dynamic capabilities, which they define as 'the firm's ability to appropriately adapt, integrate, and reconfigure internal and external organisational skills, resources and functional competences' or in other words, intangible assets like knowledge, expertise, skills, and processes of learning take a precedence. Zollo and Winter (2002) on the other hand, have suggested that dynamic capability should be defined more specifically in terms of the generation and modification of a firm's operational routines. Although dynamic capabilities as such are idiosyncratic to each firm due to path dependencies and firm-specific resource configurations as well as related to specific industrial settings, it is emphasised in the literature that their formation and articulation also depends on external relations (Peteraf, 1993; Coombs & Metcalfe, 1998). Furthermore, it is possible to identify fundamental capability patterns across a range of firms, which allows for drawing general conclusions (Eisenhardt & Martin, 2000).

Teece et al. (1997) argue that dynamic capabilities are in fact organisational and strategic routines by which managers alter a firm's resource base and renew competencies in order to generate new sources of competitive advantage. Furthermore, organisational processes have three roles: coordination/integration, learning, and reconfiguration. First, effective coordination and integration of activities is important both inside the firm and with

external sources. Second, learning has been conceptualised as an individual and organisational process, by which repetition and experimentation enables tasks to be performed better and quickly to identify new production opportunities. Accordingly, improvements in organisational processes also lead to the creation of new strategic capabilities (Argote, 1999). Third, the ability to sense the need to reconfigure a firm's asset structure is particularly valuable in volatile environments (Augier & Teece, 2009). In order for an organisation to exhibit dynamic capabilities, however, it must properly adjust responsive actions and move to implement a new system effectively and efficiently. During this process the organisation receives and interprets messages about new markets, new technologies, and competitive threats (Teece, 1998).

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Theory development

In spite of a significant number of theoretical and conceptual contributions, empirical evidence of the nature of dynamic capabilities and their influence on firm performance is still relatively inadequate. Previous researchers have suggested the following problems: lack of consensus on a common definition (Henderson & Cockburn, 1994), potential tautology (Priem & Butler, 2001), difficulty to measure (Wernerfelt, 1984) and operational limitations (Williamson, 1999). On the other hand, Eisenhardt and Martin (2000), suggest that dynamic capabilities consist of many well-known processes that create, integrate, reconfigure and release resources and competences. In the following paragraphs a brief review of studies that have addressed those aspects of dynamic capabilities is presented.

Dynamic capabilities related to the integrating of dynamic capabilities are described as routines to develop products and make strategic decisions. Product development routines are considered as dynamic capabilities as managers combine their diverse skills and functional backgrounds to create new products and services (Helfat & Raubitschek, 2000). Brown and Eisenhardt (1997) examined continuous change in organisations in the context of multiple product innovation and found that firms successful in multiple product

innovation exhibit the following characteristics:

- blending limited structure around responsibilities;
- prioritising with extensive communication;
- providing design freedom to create improvisation;
- relying on a wide variety of low cost measures to develop new products; and,
- linking present and future technologies together through step by step, time bound transition processes.

Strategic decision making is an integrating dynamic capability since it involves the pooling of business, functional, and personal expertise (e.g. Eisenhardt 1989; Olejnik & Swoboda, 2012; Welter, Bosse & Alvarez, 2013). Researchers also suggest that integrative knowledge underlying dynamic capabilities can be a source of strategic advantage (Brusoni, Prencipe & Pavitt, 2001; Henderson & Cockburn, 1994).

Another type of dynamic capability identified in the literature is creation of new resources, which includes knowledge creation routines as well as alliance and acquisition routines that bring new resources into the firm from external sources (Powell, Koput & Smith-Doerr, 1996). McGrath, Ming-Hone, Venkataraman and Macmillan (1996) developed a framework that explains the creation and evolution of competences that are necessary for innovation. They point out that process counts, stressing the fact that team processes of learning and of developing proficiency shapes the economic outcome of an innovation attempt. Pisano (1994) observed significant differences in environments of firms, and concluded that approaches to learning are different in different environments. In yet another study, by Katzy, Dissel and Blindow (2001) two streams of dynamic capabilities were identified, e.g. incubating and grafting. These were instituted to coordinate processes of creation of internal ventures and their integration in the existing set up.

Some other examples of dynamic capabilities that focus on reconfiguration are resource allocation routines (Burgelman 1994) and transfer processes, including routines for reproduction and brokering (Hargadon Sutton, 1997; Hansen, 1999). Sull (1999) suggests that there are dynamic capabilities that release resources

i.e. giving up a resource combination that no longer provides competitive advantage to the firm, which might prove to be crucial in firm's ability to remain competitive.

Researchers have made significant efforts to deal with the problem of measurement difficulties as well by constructing measures of dynamic capabilities. Zott (2003) explored how the dynamic capabilities of firms may be linked to differential firm performance within an industry. Zott (2003) proposed three performance-relevant attributes of dynamic capabilities (timing, cost and learning of resource deployment) and developed appropriate measures. The study concluded that effects of timing, cost and learning significantly contribute to intra-industry differences in performance. In another study, Macher and Mowery (2009) examined the role of the R&D based organisation and information technology practices for problem solving and learning-based improvement in innovation in semiconductor manufacturing firms. Their results indicated that allocation of human resources to problem-solving activities and the use of information technology in the manufacturing facility determine (semiconductor) manufacturers' problem-solving abilities and subsequently their performance.

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Resource capabilities approach

It has been observed that in the light of the definition put forth by Teece et al. (1997) of dynamic capabilities, the research has put more emphasis on a firm's ability to integrate, build and reconfigure its internal competencies. However, there is not enough evidence in the literature on the dynamic capabilities employed to integrate, build and reconfigure external competencies. Extant strategic management theory highlights that firms use alliances as a medium for acquiring external competencies, technology innovation and enhancing core business activities (e.g. Mitchell & Canel, 2013). However, so far only few studies have been conducted that analyse practices and processes that firms employ to codify and disseminate knowledge of managing alliances. A study by Kale, Dyer and Singh (2002), discussed the concept of 'alliance capability'

that would rest upon 'how effectively the firm is able to capture, share and disseminate the alliance management know-how associated with prior experience'. They reported that firms that create a dedicated alliance capability realise greater success with alliances. Their research explicitly addresses managerial practices strategically employed to build the capability of a firm to enter and manage alliances, and, suggests that deploying dynamic capabilities to manage strategic alliances is beneficial for overall firm performance. This study theorises the potential of acquisition and integration of external competencies in emerging markets' small and medium-sized enterprises (SMEs) that are involved in exporting or are in the process of internationalisation. A topical review of the relevant literature on alliances and networks suggests that there is a growing number of research on networks. The research addresses the concept of social networks and considers embeddedness an important factor in defining the alliance opportunities and other forms of inter-firm partnerships a firm might build (Gulati, 1998). Furthermore, developing such partnerships can provide the firms with opportunities to acquire new skills and improve existing ones (Terziovski, 2010; Thorgren, Wincent & Örtqvist, 2012). This necessary intelligence may lead to internationalisation (Senik, Scott-Ladd, Entekin & Adham, 2011), and achieve different organisational goals, and overcome inherent challenges such as lack of resources (O'Dwyer, Gilmore & Carson, 2011). However, emerging markets' SMEs typically lack relevant embeddedness in international social networks of firms. They rely on social contacts of their owners/managers, which may not always be sufficient for the establishment of appropriate partnerships with other firms and may prove to be an impediment to their competitiveness. Similarly, Boeker (1989) argues that SMEs lack status in the international arena, which is especially true for SMEs from the developing countries (Podolny, 1994). All of these factors gathered together may further affect the chances of potential partnerships with more established firms, who have already built competencies relevant for acquiring and integration, needed by SMEs in the emerging markets.

One of the alternate ways for smaller firms

to gain access to external competencies was put forth by Iansiti and Levien (2004a, 2004b). They drew on analogies from the field of biology, and innovatively treated business networks as ecosystems, and suggested that there are three types of firms in a business ecosystem: keystones, dominators and niche players. According to the authors, the bulk of an ecosystem is composed of niche players, and since, on average, SMEs account for approximately 50 per cent of GDP and 60 per cent of employment in national economies (OECD, 2004), and 25 per cent to 35 per cent of world manufactured exports (Schreyer, 1996; Hall, 2002; Sakai, 2002), it would be proper to term SMEs as niche players. On the other hand, a keystone player would be a firm that occupies the centre of asset-sharing relationships, employs keystone strategy and by doing so improves the performance of an ecosystem, which is assessed by measuring ecosystem's health on three dimensions: productivity, robustness and niche creation. Keystone strategy is aimed at enabling other firms in the ecosystem to create value, and sharing that value with the ecosystem.

For Example, The Tirupur Exporter's Association, in Tirupur, one of the SME clusters in the southern state of Tamil Nadu in India, through the setting up of a special purpose vehicle called G-Tech Info Solutions, adopted Wipro's next generation enterprise resource planning (ERP) solution for all manufacturing units in the clusters. Exporters in Tirupur's \$2-billion plus knitwear industry now share a common software platform on pay-as-you-go basis, as they seek to bring down operational costs and compete effectively with rivals from countries like Bangladesh and China. Among India's industrial hubs, this was the first time that small exporters joined hands to create a common technology platform. The cloud solution, based on Microsoft Dynamics ERP platform helped to improve the efficiency of over 4,000 small units in Tirupur (Tirupur partners, Microsoft & Wipro for cloud connect, 2011). By integrating such a set of solutions in their own organisational processes, SMEs can gain access to external competencies that would otherwise be hard to attain.

Drawing on an analogy with a notion of alliance capability (Kale et al. 2002) which

suggests that a firm's critical resources may be embedded in inter-firm resources and routines, this study; has examined managerial practices and processes employed to integrate competencies external to the firm by application of platforms in the context of emerging markets' SMEs.

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Concluding remarks

Small firms in emerging economies and developing countries have difficulty competing successfully in the international environment. The review presented in this study, intends to demonstrate the importance of resource capabilities as the central capability for SMEs in a growing economy, like India or, South Africa etc., that can facilitate SMEs in better

managing their resources and capabilities in order to streamline their international activities. This is an issue of great significance in the internationalisation process of smaller firms. Furthermore this study proposes that the development of resource capabilities in SMEs needs to be adapted according to their area of expertise. Their specific strengths should be aligned with their expertise to increase their alliance capability. On the other hand the SMEs should also identify the bottlenecks in the process of increasing their resource capability and should amend them. The review presented in this study represents the theoretical framework for the further development of theory. It is expected that the extension of this study combined with perhaps a field study or a case study will help to gain further insights in this field of research.

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