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Initial Target Market and New Venture Performance

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Abstract

This paper explores the effects of initial selection and change of target market on the performance of new ventures. Compared to internationalization of general SMEs, Born-globals identifies and exploit business opportunities in the global market at the early stage of growth. There are little studies on the relationship between change of the initial target market and the performance of new ventures. Based on 105 Korean new ventures in high-technology industries, this paper investigated the difference between local new ventures, born-again globals, Born-globals. In terms of initial target market, new venture to compete in global market earns higher performance than domestic new ventures to exploit business opportunities in local market. Also new ventures that focus on initial target market either domestic or global earn higher performance than others to change their target market. Also Born-globals have larger founding team and internationally experienced founding team members and higher degree of internationalization. These results show that new ventures have to be more conscious to select their initial target market. Finally, this paper suggests some implications for new venture to identify and exploit business opportunities and future research directions on early internationalization of new ventures.

Key words: Initial Target Market, Born Global, New Venture Performance, and International Entrepreneurship

1. Introduction

There are increasing interests in the entrepreneurship as the sources of technological innovation and economic development. To identify and exploit promising business opportunities is one of most important factors for the survival and growth of companies. In addition, timely recognition and aggressive seeking of promising business opportunities in the global environment beyond specific geographical markets is important to compete in the turbulent environment and gain higher performances. Traditionally small and medium-sized firms (SMEs) expand their business areas by internationalization. Researchers have investigated the motivation and determinants of internationalization, internationalization processes, and the effect of internationalization on the performance of SMEs. Accelerated by rapid technological change and globalization, however, many new ventures compete in the global markets at the early stage of development beyond local or home markets where their major business operations are located. These new ventures, international new ventures (INVs), pursue business opportunities in the global market from their inceptions rather than gradual internationalization. In spite of increasing interests, there are little studies on the effects of internationalization of new ventures' performance. Most of researches on the internationalization of new ventures are drawn from the experiences of advanced countries.

This paper is purposed to investigate the effect of internationalization of new ventures on the performances and to unveil the determinant of the internationalization of new ventures in Korea. The remainder of this paper consists of four sections. First, literature review section provides the understanding the internationalization of new ventures. Research methodology is presented in the next section. This is followed by empirical results on the determinants of Korean new venture's internationalization. The implications with future research are discussed in the final section of the paper.

2. Literature Review

Early Internationalization of New Ventures

There are increasing of new ventures to commence their international business opportunities from their inceptions. Accelerated by rapid technological development and globalization, new venture would identify and pursue promising business opportunities cross-borders (Autio, Sapienza, & Almeida 2000; Knight & Cavusgil 1996; McDougall, Shane & Oviatt 1996; Oviatt & McDougall 1994). The emergence of international entrepreneurship is different internationalization patterns of traditional SMEs. Previous researches investigated that SMEs would gradually internationalize their business through accumulations of learning and commitment on foreign markets. Researchers have recommended new ventures to build competitive advantage in their home markets and then enter incrementally foreign markets to reduce the uncertainty and risks on internationalization (Johanson & Vahlne 1977).

Recently researchers have investigated the new ventures to pursue business opportunities from their inceptions under the name of 'Born-Globals,' 'International New Ventures,' or 'International Entrepreneurship' (Knight & Cavusgil 1996; Zahra & George 2002). These new type of start-ups have commenced business opportunities cross-borders regardless of competitive advantages in their home or domestic markets. These new types of firms are hardly explained under the existing theories on international business and researchers suggested comprehensive development of theories on the international entrepreneurship (McDougall et al. 1996).

Researches on international entrepreneurship could be categorized into three areas. The first group of studies is to investigate key factors impacting on the emergence and determinants of born-globals. A number of studies have found several general forces like technological developments and increasing globalizations. As more specific key factors, the international experience of entrepreneurs and founding team members are important to recognize business opportunities cross-borders and to access to information and knowledge on the foreign markets (Bloodgood et al. 1996; McDougall et al. 2003). Other studies found that new ventures' behavior or strategic factors are important to pursue international business opportunities (Bloodgood et al. 1996; McDougall 1989). New venture armed with entrepreneurial orientation and differentiation strategy would start their businesses for global markets from their inceptions (Knight & Cavusgil 2004). In addition, the studies explained the market structure and characteristics of industry could impact on the internationalization of new ventures. New ventures with small size of home markets would internationalize their businesses to overcome the limitations of growth. New ventures in the high-tech industries and higher level of global integration of industries would commence international businesses.

Second group of researchers have investigated the types of new ventures and structural differences among different new venture types. For example, researchers have found significant differences between international new ventures and domestic new ventures in terms of market structures, competitive

strategies, and resources and capabilities (McDougall 1989; McDougall et al. 2003). Recently researchers added another types of new ventures, 'born-again globals' that changed their target market from local markets to global markets (Bell 1995; Bell et al. 2001). These new ventures changed their target market at early stage of development driven by intended or reactive of structural transitions like the change of leaderships and/or ownership, client-followship, and development and launch of new products and services. They also investigated the performance differences among new venture types.

Third group of studies on international entrepreneurship would try to unveil the consequences of the early internationalization on the growth and development of new ventures. Born-globals could have some advantages from early internationalization rather than incrementally internationalization. Autio et al.(2000) suggested the learning advantage of early internationalization that provide new venture leaning opportunities to develop competitive capabilities on foreign markets. Accelerated internationalization could provide new ventures to access recent technological development and information on markets. These benefits could enhance new venture's technological capabilities and technological learning.

Previous studies on international entrepreneurship would stress the importance of initial target markets for new venture growth and development. The initial target market whether local markets or global markets are would have significant impacts on the initial performance and the trajectory of capability development over the new ventures' life cycles.

Initial Target Market and the Characteristics of New Ventures

There are increasing interests in the characteristics of new ventures to identify and exploit business opportunities in the global markets from their inceptions. Researchers investigated several factors for entrepreneurs to build their global start-ups. International new ventures differ from local new ventures in terms of founding teams, market structures, and networking relationships (McDougall 1989; McDougall et al. 2003). Entrepreneurs and founding team members have influenced the initial resources and key development directions of new ventures. As new ventures have little resources and experiences, the experiences of founding team members are transferred into the foundations of early days of new ventures. The experiences and capabilities are important for capability building, strategic decision-making, and organizational system developments (Reuber & Fisher 1997).

The different experiences and skills of entrepreneurial teams could impact on the identification and exploitation of their initial business opportunities. Entrepreneurs with more exposure in global market could find promising global markets. International experience of founding team could get more information and knowledge on foreign market and access to local partners through personal networking. In addition, their knowledge on foreign language and cultures could help new venture overcome diverse cultural problems encountered in foreign markets. Previous studies also found the international experiences of founders and founding team members are one of key factors of early internationalizations.

New ventures have little resources and capabilities in their early days. However, one of key aspects of entrepreneurship is to pursue business opportunities regardless of internal resource constraints. To overcome the internal lack of resources, new ventures should proactively use external resources. These external resources can be available through personal networking and formal business relationships (Coviello & Munro 1995, 1997). There would be many types of network relationships. One is the strategic alliance with other partners that could provide new ventures opportunities of technological developments and social endorsement effects. Another is external financing from private investors including venture capitalists and organizational investors. As these external investors could get only higher returns from success of new ventures, they should help invested new ventures become more successful businesses by providing invaluable advices, recruiting skillful members, and bridging other business partners.

The internationalization would be risky process for new venture with little experience and capabilities to solve numerous challenges in the internationalization processes. So researchers on international business have recommended gradual internationalization to reduce uncertainty from the foreign entry. In spite of high risk, recently increasing born-globals would identify and exploit international business opportunities through learning advantages of early internationalization. When start-ups enter foreign market, they could have more advantages to get knowledge and information on foreign markets, learn the customer preferences, and build network relationships with capable local partners.

Hypothesis 1. New ventures with different target market have different characteristics in founding team, networking, and level of internationalization.

Target Market and New Ventures Performance

The initial conditions of new venture could have imprinting effects on the developments and growth over life cycles (Stinchcombe 1965). These initial conditions include founding team characteristics, financial and non-financial resources, and strategic choices on the target (Bamford, Dean, & McDougall 1999; Cooper, Gimeno-Gascon, & Woo 1994; Eisenhardt & Schoonhoven 1990). Researchers investigated that there are positive relationships between the internationalization and new venture performances (Autio et al. 2000; Zahra et al. 2000). When new ventures could be successful, the start-ups pursuing business opportunities in the more risky and larger global market could get higher financial performance than local new ventures with relatively low risk. Previous studies found that the speed and degree of internationalization have been associated with higher financial performances. A learning advantage from early internationalization could provide new ventures initial learning opportunities and capabilities suitable for foreign markets (Autio et al. 2000).

There are little experiences and organizational inertia at the early days of new ventures. The initial target market and conditions could guide new venture to build organizational capabilities. With limited internal resources, new ventures should competitive advantages to get higher performances. The change of initial conditions would make new venture delay in building organizational capabilities and lose business opportunities in the fast-changing competitive markets. Total different organizational capabilities are required for new ventures to pursue new products and service as well as international business opportunities. This organizational inertia was one of key reasons that existing firms would hardly successful after strategic changes. After the change of target market, new ventures could at most shortly misfit between acquired capabilities within a organization and required capabilities in the competitive markets so that under-perform than other types of new venture that incrementally develop organizational capabilities.

Hypothesis 2. New ventures with different target markets will show performance differences.

3. Research Methodology

Research Samples

This paper empirically tests the effects of selection and change of initial target market on the characteristics and performance of new ventures. One of difficulties in the empirical studies on new ventures is to define and select the new ventures. In this paper, we used following criteria to select samples based on the previous empirical studies on the internationalization of new ventures and related studies. First, this paper focuses on the independent Korean new ventures. Other form of new ventures such as affiliates or spin-offs from existing corporations, joint ventures or subsidiary of multinational corporations were excluded as these new firms hardly managed independent entrepreneurs in the process of identification and exploitation of business opportunities since the early stage of development. Secondly, the sample only excluded new venture less than three years because of stabilities and reliabilities of their financial performance. Also this paper excluded the samples with more than fifteen years difficult to sustain new venture characteristics. Finally, the samples in this paper focus on the new ventures in the high-tech manufacturing industries such as electronics and telecommunication equipments and medical, precision, and Optoelectronics. These industries are characterized as promising and fast growing industries and high level of internationalization. Also there are many Korean new ventures to pursue business opportunities both local market and global market in Korea in these areas.

To conduct empirical research, research samples new ventures were screened from the database registered in Korean Small Business Administration as of July 2001. Among more than 10,432 new ventures satisfied with three criteria in this research, we initially screened 1,462 new ventures and contacted new ventures to ask this survey by sending electronic mail. Among 639 new ventures interested in this research, we send survey questionnaire and ask for founders or executive members with rich information on the development history to respond to the key measures. From 124 received data from new ventures, we finally used 105 data to analyze the different characteristics among target markets and the effect of target market on performance of new ventures.

Measurement

Types of New Ventures: In this paper, we measure two indicators to show target market, selection of initial target market and change of initial target market. Target market means the geographical market where new ventures are pursuing business opportunities and major customers are located. In this paper, we classified the target market into two geographic locations: local market and global market. Local market means the domestic and home markets of new ventures, contrast to global market where new ventures identify and exploit product and services in foreign and other geographical market. We asked each informant of new ventures to select target market, domestic market or international market, where your new ventures mainly identify and exploit business opportunities both at the inception stage and current stage. This paper has neither considered psychic distances among global markets nor the degree of internationalization along value chain processes. The types of new ventures for internationalization were classified by two indicators where the initial target market of new ventures are and whether these initial target markets of new ventures have changed or pursue in the same target market. Each of information was collected from key informants to answer their initial and current target market. Depending on the initial target market and the change of target market, this paper categorized the types of new ventures into domestic new venture, Born-again Globals, and Born-Globals. One is the domestic new venture that has selected local or home market as initial target market and has pursued business opportunities in the local or home markets. Another is Born-again Globals that identified their initial business opportunities in the local or home market but changed its target market from local to global market. The others are Born-globals that pursue their business opportunities in the global market from their inceptions. Each of new ventures was categorized as one of new venture types.

Firm Age and Firm Size: In this paper, we measured two variables on the characteristics of new ventures including firm age and number of employees. The firm age was calculated how many years new ventures operated after its inception. The number of employees was measured by total number of full-time employees in the new ventures. These variables are transformed natural log calculation.

Founding Team characteristics: To measure the characteristics of founding team, we measured the number of founding team member(s) and ratio of internationally experienced founding team members of all founding team members.

Networking: To measure the networking characteristics, this paper measured by the number of R&D networking separated by domestic R&D networking and international R&D networking. Another networking indicator is the financing networking whether new ventures are financed from external investors such as angel investors, venture capital and other organizational investors.

Internationalization of new ventures: To measure the characteristics of internationalization of new ventures, this paper used two variables whether new ventures get revenues from foreign markets and level of internationalization measured by ratio of foreign market revenues of all sales volume. These intensity of internationalization are calculated by using sales volumes in recent three years.

New Venture Performance: The new venture performances can show eclectic characteristics because the each indicator shows different aspects of new venture performance. This paper used multiple measures to explain the effects of selection and change of initial target market on the diverse performance of new ventures. In this paper the new venture performances were measured as average sales volume, sale growth rate, average return on asset (ROA) and average sales volumes per employee. All of new venture performance were calculated by the performance in last three years.

4. Results

Characteristics between different target market change of new ventures

The difference among new ventures depending on their initial and current target market are analyzed by conducting ANOVA analysis shown in Table 1. The result shows that there are significant differences among new ventures with different target market in terms of networking and level of internationalization.

Born-globals have more external networking relationship than other types of new ventures. These new ventures targeting global market since their founding need more information and resources to develop competitive capabilities and compete in foreign markets. These needs make born-globals build diverse network relationships. Among the networking, Born-globals have more business relationship with external financing providers like venture capitals and organizational investors. These private investors seek higher returns by identifying more prospectus new ventures among a set of alternative new ventures, by providing helpful information on foreign market, and by bridging new ventures to business partners in

the foreign market. Born-globals also build more foreign R&D cooperation relationships than local new ventures, though the size of domestic R&D collaborations is insignificant among new ventures.

In terms of internationalization, there are significant differences among new venture types. Born-globals get average 43% of revenues from foreign market, comparing to local new venture with 8% and born-again-globals with 13% of sales from foreign market. In addition, 42% of local venture have any volumes of export experiences in their life cycle and 82 % of born-globals have any kinds of export experiences.

The differences in the characteristics of founding team are statistically significant among new ventures. Both of the size of founding team nor the ratio of internally experienced founding team does statistically different among new ventures. The born-globals were founded by more founding members than local new ventures and born-again-globals. Also born-globals have more members with international business experiences that revealed as one of key factors to accelerate new venture internationalization and emergence of born-globals in the previous studies.

<Table 1 > Comparison of Characteristics and Performance among Different type of new ventures

	New Venture Types			ANOVA F-value
	Local New Ventures (n=33)	Born- again Globals (n=42)	Born- Globals (n=29)	
Target Market				
Initial target market	Local	Local	Global	
Current target market	Local	Global	Global	
General Characteristics				
Firm age (years)	6.39	7.62	7.10	1.255
Number of employees	41.29	44.36	45.36	.106
Founding Team Members (FTM)				
Number of FTM	5.06	4.69	8.20	2.640*
Rate of internationally experienced FTM (%)	2.71	7.95	15.64	2.869*
Networking				
External Financing (%)	27.27	35.71	58.62	3.509**
Local R&D cooperation	3.30	2.62	3.21	.493
Foreign R&D cooperation	0.15	0.19	0.66	4.025**
Internationalization				
Export experience (%)	42.42	69.05	82.76	6.348***
Ratio of export to sales (%)	7.30	13.31	43.33	13.644***
Performance				
Average sales volumes (KRW)	6984.88	4522.07	9225.97	2.501*
Sale growth rate (%)	52.79	66.89	58.96	.254
ROA (%)	10.73	2.93	8.04	3.476**
Sales per employee (KRW)	184.05	100.06	178.20	3.514 **

* p<0.1, ** p<0.05, *** p<0.01

Effect of selection and change of initial target market on the New Venture Performance

The performances of new ventures were affected by the initial selection and subsequent change of target market at their early days of development. Among of performance indicators as shown in Table 2, sales volume and profitability, return on assets (ROA), either local new venture or born-globals is higher than new ventures changed their target market from local to global market. Also productivity measured by the average sales per employees was similar differences. This performance differences shows that new ventures persist initial target market, either local new ventures or global new ventures outperform the new ventures that re-selected their target market. However, the differences of sales growth rate were insignificant among new ventures with different target market. The selection and change of initial target market, either local or global, was little impacted on the sales growth rate.

These results explain that the importance of initial target market for new ventures. The new ventures

persisting their initial target market outperform new ventures that changed their initial target market. The change of target market needs new capabilities for new venture to serve new customers and compete in the new market. One of interesting findings in this analysis is that born-globals insignificantly outperform the other types of new ventures, especially new ventures targeting local market. Although the initial target market is important for new venture performance, it does not mean that all of new venture select and pursue international market as their initial target market. Local new venture can earn sufficiently good performance in their local market depending on the competitive capability of new venture and market characteristics like market prospectus and competitive environment.

5. Discussions and Conclusion

The initial conditions of new ventures are important to identify prospectus business opportunities and to grow their new business with limited internal resources and capabilities. The rapid technological development and advanced transportations make new venture pursue business opportunities across national borders from their inception. With high hazard rate of success, new ventures should identify and select their promising initial target market where their products and services can attract key customers around the world.

This paper enforced the importance of initial target market for the growth and performance of new ventures. One of the key findings is that new ventures persisting their initial target markets outperform new ventures that changed their target markets. Either of new ventures with local market or new ventures with global market could get higher performance than new ventures have reset their target market. The initial conditions, as known as imprinting effects, have deeply impacts on the capability development and business relationships. New venture persisting their initial target markets develop competitive capabilities suitable at the initial target markets. These evolutionary interactions between initial markets and capability development make new ventures get higher performances.

New ventures resetting their target market could be affected by a number of factors like unfavorable initial market conditions, the occurrence of incidental or critical events, the change of leadership and ownership, and development and launch of another new products and services. Whatever the factors are, the change of target market could lead new ventures with resources constraints hazardous in the competitive environment and could delay the development of capabilities for new target market where would be fundamentally different market conditions and customer preferences on the products and services. The changes of target market require new venture rebuild and reconfigure their products and services for new customers.

Another interesting finding is that born-globals are not significantly outperforming other types of new ventures. There are insignificant performance differences between Born-globals and other new ventures. It means that the global market is hardly necessary conditions of the growth and higher performance of new ventures. In the selection and pursuit of initial target markets, what the matters are not to pursue global business from its inceptions but to find and pursue promising business opportunities with competitive initial conditions. Born-globals should develop different capabilities from the local new ventures, serve different customer preferences, and challenge numerous issues like liability of foreignness.

These results indicate that the initial target is the matter of strategic choice for new ventures depending on the initial conditions including founding team characteristics and initial products and capabilities. New venture targeting local market have sufficient capabilities for local markets required different capabilities for global markets. Local new ventures could get higher performance and growth comparable to the born-globals. When new ventures are pursuing business opportunities in the global market, they should accelerate their internationalization and develop global capabilities by entering early global market, learning international market and customers, and building sufficient capabilities and business network relationships.

According to the target markets, new ventures have different characteristics including founding team experiences, level of internationalization, and network relationships. In this paper, we categorized new ventures into three types of new ventures. Domestic New Ventures, Born-again Globals, and Born-Globals. New ventures with different target markets have commenced their business with different initial conditions and current capabilities.

Domestic new ventures have little internationally experienced founding team members similar to the previous researches. Also these firms have few business network relationships including R&D and

financing. In spite of less level of internationalization, the performances of domestic new ventures are similar to those of Born-globals and better than those of Born-again globals. These results indicate that new ventures pursuing domestic markets could get good performance when they develop competitive capabilities for the promising domestic business opportunities.

The characteristics of Born-globals are similar to the previous researches on international new ventures and international entrepreneurship. Born-globals have more international experienced founding team members with knowledge and personal networks on foreign markets. These new ventures build more business network relationships in R&D and financing. Born-globals could marshal more resources from these external resource holders and access to information on foreign market through business partners. As private investor should search more prospectus new venture to get higher returns, born-globals with higher risk and higher return could be attractive for investors who could formally and informally help these startups grow promising business. International R&D collaborations help new ventures develop competitive products and services, build internal technological capabilities, and access to recent technological information and another business partners. These network relationships could make born-globals overcome numerous constraints to encounter when they pursue cross-border business opportunities.

In this paper, born-again globals have changed their target market and get underperformance than other types of new ventures persisting their initial target markets. These firms hardly have characteristics of gradual internationalized firms that initially build competitive advantage in home market and then incrementally globalize their target markets through learning by commitment. Rather than the gradual internationalization, these new ventures reset their target markets by incidental events like change of leadership or ownership. Although these new ventures initially targeted local new ventures, they have pursued business opportunities in the global markets. These changes of target market make new ventures rebuild and reconfigure their capabilities, business systems, and networks relationships. The redirections of organizations can delay new ventures learn their customers and markets and can lessen the learning advantage of foreignness generated from early internationalization.

6. Research limitations and future researches

This paper explores the effects of initial target market on the new venture characteristics and new venture performance. The results investigate the importance of initial target market for new ventures to build competitive capabilities and get financial performances. In spite of these implications, there are several limitations. First, this study is based on the small survival new ventures with selection bias in high-tech industries. Future researches based on larger samples and diverse industries could help the generalization problems of this paper's key findings.

Second, the measurement on the target market should be robustly developed to trace the initial and current target market. This paper depends on the retrospective and subjective response from new ventures informants rather than more objective and comparable measurement. Future researches should adopt more robust measures for target market and the change of target market.

Third, this paper could hardly suggest the dynamic performance between new venture types. In this paper, there are little samples on the target market transition from global to local market. This result could be that born-globals have higher risks so that only survivals could be included in the analysis. Longitudinal studies could provide more dynamic performance, especially survival rate and profitability, between new venture types because each type of new venture has different risk-return relationships.

Fourth, the paper is lack of investigations on the key factors on the determinants of initial target markets and transitions of target market. New ventures could identify promising business opportunities affected by numerous factors. Also there are little studies on the dynamic transition patterns and factors to alter their target markets.

Finally, the international comparison studies on the international entrepreneurship are needed. Increasing interests on accelerated internationalization of new ventures, there are little studies on the cross-border comparison on the key factors, patterns of born-globals, and performance of international entrepreneurship.

The growth and performance of new ventures are determined by numerous factors including dynamic capabilities in competitive market conditions. The selection of initial target market would be a first step to initiate business opportunities. The competitive results from these initial target markets could lead new ventures to change their target market or to build more competitive capabilities in the initial

market. Future researches on the identification and exploitation of business opportunities including initial target markets would help entrepreneurs and new venture to identify new businesses and build dynamic capabilities for success.

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