

# International Business Strategy for Overseas Expansion of Local Small and Medium-sized Enterprises

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## Abstract

It is pointed out that the overseas expansion of local small and medium-sized enterprises (hereinafter referred to as “SME”) has positive effects, such as introducing products that match customer needs, improving quality and employee capacity and strengthening sales structure. However, SMEs strongly tend to have a lack of planning of international business strategy before expanding overseas and after starting overseas trading, because their management resources, such as human resource, goods and capital are limited.

I regarded the framework of the international business strategy of SMEs’ overseas expansion as six stages of vision – feasibility study (hereinafter referred to as “F/S”), target, sales strategy, tactics and business plan, categorized the strategies that SMEs were developing independently and clarified the success factors.

I could verify how SMEs gathered and analyzed information about customer needs and developed market without international business strategy of large enterprises, as well as how they gained their competitive advantage and differentiation. I believe that this research would lead to further sustained growth of SMEs.

Keyword : *International business strategy, Vision, Target, F/S, Sales strategy, Tactics, Business plan*

## **1. Introduction**

### **1.1 Background**

Considering the prospect of a decrease in domestic demand due to the decline of population of Japan and efforts towards overseas demand of emerging countries, SMEs should not rely solely on orders and production from large companies, but it is important to actively expand overseas and advance into growing overseas markets.

As for the overseas business development of SMEs mainly in the manufacturing industry, there are certain management activities, such as export type to create buyers of products and services with developing new markets, import type to create suppliers of raw materials and products and business management type to create overseas production bases/sales bases through direct investment.

Although there is an opinion that overseas business development of SMEs causes an industrial hollowing out, it does not always bring about an industrial hollowing out, but it leads to economic revitalization with an increase in production volume and employment rate due to an increase in sales and profits by import and export transaction.

In general, among the backgrounds for SMEs to expand overseas, there are “development of new markets by shrinking of the domestic market”, “cost reduction of procurement of management resources”, “risk diversification”, etc. However, if thinking positively about overseas expansion of SMEs, gathering information, and developing products and markets, it is expected that SMEs’ overseas expansion will lead to regional revitalization strengthening the bases of the companies’ existences, and economic growth.

### **1.2 Significance and Purpose of this Research**

There are two types of export trade with overseas : direct export to deal directly

with overseas and indirect export to trade via trading company etc. According to Organization for SMEs and Regional Innovation (2017), among 3,121 export companies, 33.0% deal with only “direct export”, 30.6% – with only “indirect export” and 32.0% – with “direct export and indirect export”; so each accounted for about 30%.

Major tasks of SMEs dealing with export are : (1) securing human resource speaking foreign languages and capable of trade affairs, (2) developing local customers, (3) developing and strengthening relationship with local sales partners, (4) developing products that meet local customer needs (function/specification/design, etc.<sup>(1)</sup>).

Besides, according to “Survey results on overseas expansion of SMEs” of Research Institute of Japan Finance Corporation (2012), 72.4% of SMEs are not expanding overseas, 11.5% are dealing with only indirect export, 9.2% are dealing with only direct export, and 2.3% have business/technical alliance, etc. The result shows that many SMEs do not expand overseas, but they make about 28% in total (1 in 3-4 companies), whereas, nearly 40% in the manufacturing industry and nearly 20% in the non-manufacturing industry are conducting overseas trading<sup>(2)</sup> (Chart 1).

In the era when SMEs actively expand overseas, the purpose of this research is to verify (1) what kind of issues exist in SMEs that hamper the expansion of the business due to poor performance in overseas, and (2) whether it is possible to classify the issues and present success factors.

In this paper, I believe that it is meaningful to share the issues among SMEs that are facing sluggish growth of developing in overseas markets, find solutions to the issues and clarify the success factors. I would like to support regional revitalization by clarifying whether local SMEs can achieve the success factors by themselves or they need cooperation with municipalities etc., and giving concrete suggestions.

Chart 1 : Types of overseas expansion of SMEs (Unit : %)

	All industries	Manufacturing industry	Non-manufacturing industry
To have bases for expatriate workers and gathering information	2.0	2.7	1.4
To have permanent relationship with foreign companies other than capital relationship, such as business/technology collaboration, dispatch of executive officers (Overseas development without production base)	2.3	3.6	1.3
<b>To export directly to overseas</b>	<b>9.2</b>	<b>14.9</b>	<b>4.5</b>
<b>To export indirectly to overseas (exporting via trading company or domestic buyer company)</b>	<b>11.5</b>	<b>20.0</b>	<b>4.4</b>
To import directly from overseas	13.0	18.1	8.7
Other	1.2	1.5	1.0
<b>No overseas expansion</b>	<b>72.4</b>	<b>59.5</b>	<b>83.1</b>

Source : Created by the author based on "Survey results on overseas expansion of SMEs" of Research Institute of Japan Finance Corporation

In addition, I focused on indirect export, direct export, and consignment sales among SMEs' overseas expansion, and excluded business and technical alliances, consignment production, foreign direct investment, etc. from this research.

## 2. Literature Review

### 2.1 International Business Theory of SMEs

In order to explain the internationalization of enterprises, stages, such as indirect export, direct export, establishment of overseas sales subsidiary, overseas production, transfer of research and development activity are shown in Uppsala model which is a classic model of internationalization (Johanson and Vahlne (1977)).

Yoshihara (2011) mentioned that international business strategy is a strategy on

the international aspects of corporate strategy and business strategy. This theory is based on multinational corporation as the corporate strategy is the company's overall management strategy and the business strategy is the management strategy of the individual business.<sup>(3)</sup>

However, Touhara (2012) pointed out that, considering the medium scale of SMEs, the internationalization process is not necessary and, depending on the situation, staying at each stage is considered to be appropriate internationalization for each SME. Based on the abovementioned, he states that the internationalization process of SMEs in Japan cannot be grasped correctly by just applying the Uppsala model as many SMEs in Japan are not internationalized or they are in the early stages of the internationalization process, and they show a strong tendency of preferring production consignment.<sup>(4)</sup>

## 2.2 International Business Strategy of SMEs

The importance of international business strategies, such as F/S, sales strategy, competitive advantage, differentiation strategy, etc. is pointed out for overseas expansion of SMEs, but compared with large companies the strategies are hardly implemented due to the limitation of their management resources.

Among the preparations before expanding overseas, the implementation of F/S is closely tied to the outcomes of overseas bases. Since the purpose of overseas expansion of SMEs is changing to market development, how to work on the local market development after expanding overseas is important<sup>(5)</sup> (Tange, 2017).

Takahashi (2016) pointed out that risk management, such as considering risk countermeasures in advance with assuming future wage increases, labor supply capacity, and market growth potential from the F/S stage of overseas expansion is particularly important as a condition for successful overseas business. Actually, the less employees, the less F/S is implemented as the management resources are limited.

Zhang (2012) stated that the roles of local distributors/importers are also important for SMEs to increase overseas sales steadily.<sup>(6)</sup> The roles include (1) development of new products with using the external resources, such as public technical institutions and universities, etc., (2) securement and development of sales channels, (3) Sales promotion activities at stores to convey product information to consumers.

Masuyama (2008) specified that product development technology, production technology, marketing ability, management ability, etc. are sources of competitive advantage, and product development ability is the combination of technical ability and marketing ability. He also stated that SMEs are building a sustainable competitive advantage by intensively investing the management resources in their strong and specific areas as their management resources are limited.

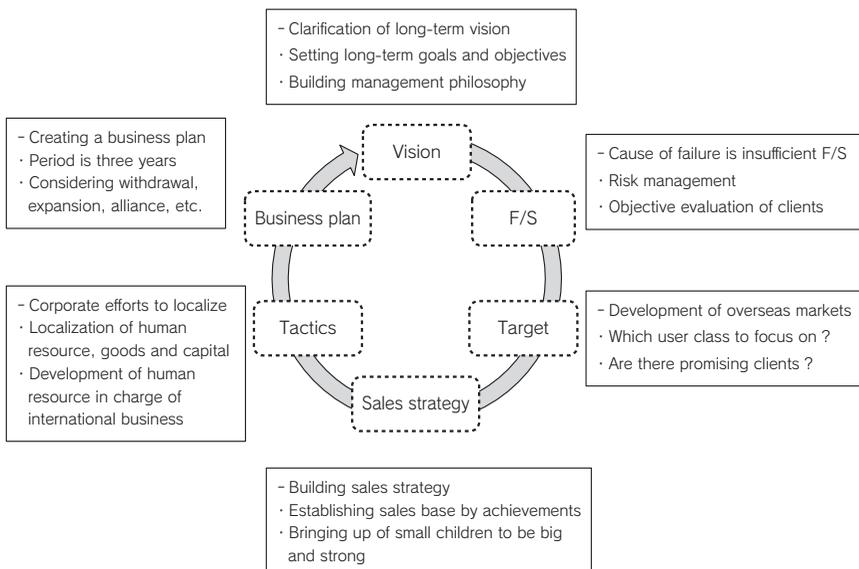
### **3. Framework of International Business Strategy of SMEs**

Based on the previous researches, I regard the framework of international business strategy of SMEs' overseas expansion as six stages of vision, F/S, target, sales/marketing strategy, tactics, business plan, and believe that successful overseas expansion can be achieved by timely and accurate execution of all stages from vision to business plan.

The outline of the framework of international business strategy is as follows (Chart 2).

- 1) Vision is a common management philosophy, both domestic and overseas.
- 2) F/S is for investigating and considering the possibility of realizing a project in advance. This includes investigating and examining market size, clients, agencies, sales partners, etc. in advance.
- 3) Target is for focusing on promising users in overseas markets.
- 4) Strategy is a comprehensive and long-term planning means to achieve goal.

Chart 2 : Framework of SMEs' International Business Strategy



Source : Created by the author

It is important to accumulate know-how of sales and marketing strategies by making achievements first.

- 5) Tactics is a practical means of planning to pursue a strategy, such as localization of human resource, goods and capital, and development of human resource in charge of international business.
- 6) Business plan is for making a review within three years after expanding overseas and considering withdrawal, expansion and alliance, etc.

## 4. Setting and Verification of Hypothesis

### 4.1 Setting Hypothesis

I conducted a hearing survey and a factory survey for five companies. The hypothesis was set based on the previous researches. I verified the hypothesis by

analyzing the two companies with high sales in the framework of international business strategy I created.

Hypothesis : SMEs are expanding overseas without sufficient planning of international business strategy and lacking the process of strategic planning even after starting overseas trading due to shortage of the management resources, such as human resource, goods and capital.

## 4.2 Research Method

I conducted a hearing survey and a factory survey for five manufacturing SMEs in Kagawa prefecture. I verified the hypothesis by analyzing the two companies that are expanding overseas actively in the framework of international business strategy I created.

## 4.3 Research Object

The outline of company S and company K that are manufacturing SMEs in Kagawa prefecture is as follows.

### [Case 1 : Outline of Company S]

Company S was founded in 1910 and established in May of 1971. The annual sales amounts to 1.25 billion yen, the number of employees is 38 and the capital is 10 million yen. It is a manufacturer of noodle making machines selling compact handmade noodle-making machines for shops, handmade noodle mass-production machines, and full automatic noodle making systems. In addition, it also focuses on intangible aspects of business, such as holding seminars on technique of making noodle and management know-how at 11 venues nationwide, including “Sanuki Noodle Technical Training Center”.

The major export destinations are South Korea, China, US, Taiwan, Southeast Asian countries and others : in total 30 countries. The overseas sales amounts to 250 million yen per year (about 20% of annual sales) and the export type is direct export and consignment sales.

### **[Case 2 : Outline of Company K]**

Company S was founded in 1910 and established in April of 1990. The annual sales amounts to 250 million yen, the number of employees is 18 and the capital is 3 million yen. It manufactures and sells apparel products, such as original T-shirts, polo shirts, hoodies, etc. based on group orders and personal orders.

In 2009, it launched the brand “Curly” as men’s fashion. They are developing business of T-shirts, jackets, blousons, pants, etc. of “Curly” for overseas markets. It also opened “Welt” as a local specialty shop in Minami Aoyama, Tokyo in 2013.

The major export destinations are China, South Korea, Canada, US, UK : in total 5 countries. The overseas sales amounts to 6 million yen per year (about 2.4% of annual sales) and the export type is direct export.

I visited both companies and conducted a hearing survey and a factory survey. I applied the framework of international business strategy to them and verified. The results are as follows.

## **4.4 Verification of Hypothesis**

### **[Case 1 : Company S]**

- 1) Vision is “to evolve, i. e. to cope with the changes of the time, master the latest noodle making techniques and make the best quality noodles using the noodle machine technology”.
- 2) F/S is to investigate the growth potential of the market. Ramen now expands all over the world and is already a trend as it has developed

to overseas earlier than udon. They get business inquiries directly from companies that collect information from the exhibition held twice a year or internet. In case if products are imported by individuals, it is sometimes impossible to purchase as the tax is around 50%.

- 3) Target is the whole world, but, actually, many Chinese and Koreans purchase noodle making machines. There are cases when people start noodle business individually after eating Japanese noodles in Europe and liking it, and, then, feeling the real taste of ramen, udon and soup in Japan.
- 4) Sales strategy is to add value by combining tangible and intangible aspects, such as noodle making machine (50%) + guidance on how to make soup with delicious noodles using local raw materials (50%) = sales (100%).
- 5) Tactics is to use the local materials (such as wheat flour) which are cheap and can be purchased quickly for making ramen. They are guiding how to make delicious noodles by making soup with local raw materials and devising how to boil and texture.
- 6) Sales by business plans are stabilized as they have established a certain market share.

### **[Case 2 : Company K]**

- 1) Vision is “We want to deliver the most comfortable clothes to the world”.
- 2) F/S is to investigate the size of the market. They get business inquiries directly from companies (in Southeast Asia, Canada, etc.) that collect information from the exhibition held twice a year or internet. They sometimes receive orders in exhibition, but usually they receive orders through negotiations after the exhibition.
- 3) Target is men of around thirty in Europe, US, China, etc.
- 4) Sales strategy is to make products with flashy colors, as overseas customers are not interested in modest designs. In the exhibitions, it is important for

them that the participants touch the products to understand the comfort and texture.

- 5) Tactics is the product development with high technology such as water repellent pants despite of using Japanese traditional dyeing method called “Chusen” .
- 6) Sales by business plans are expanding in US, UK and mainly China.

## **5. Success Factors, Issues and Discussion**

### **5.1 Success Factors**

In this paper, I will summarize the success factors found in the cases of two SMEs working on overseas expansion, based on the viewpoints of the previous researches and the international business strategy of SMEs’ overseas expansion.

#### **1. Company S**

- 1) It is the only manufacturer in Japan that has the “Japanese traditional handmade method” mechanized and produces high-quality noodles based on excellent performance of noodle machines and abundant noodle making technology, such as product development technology and production technology.
- 2) They offer cheap noodle machines made in China and South Korea. However, they are not caught in low price competition with other companies after starting overseas trading, since their noodle machines can make unique handmade texture, and the customers, who know the real taste, prefer it.
- 3) They opened a ramen school in Los Angeles and let a local consignment sales base manage it. They have succeeded in developing new customers by teaching how to make delicious ramen, udon and soup.
- 4) The business model of company S that provides both tangible and intangible

aspects to customers is matched with differentiation strategy such as dealing with each customer carefully.

For example, investors often fail to succeed even if they purchase a noodle machine and hire employees to manage. The reason of it is that if they leave the management to the employees, the latter cannot meet customers' needs, e. g. due to overlooking the pursuing of the delicious taste.

## 2. Company K

- 1) The products are accepted in overseas markets due to the success of differentiation strategy, such as the design and functionality of the brand "Curly" launched with designers hired in 2010.
- 2) Since it was a glove manufacturer at the time of establishment, it can produce high quality apparel products by making use of its product development technology and production technology.
- 3) Although most apparel products target women, they have the high marketing ability to target men's apparel products market that other companies hardly enter.
- 4) They have a product development technology such as collaboration with designers to always deliver new products, and a strong production system such as alliance with four factories.

## 5.2 Issues

As a result of this survey and analysis, I extracted the success factors of the international business strategy for overseas expansion, but on the other hand, several issues were revealed. I believe that these two companies can further expand their business by overcoming the issues.

### **1. Company S**

- 1) For the European market, it must acquire safety measures standards such as “CE marking”, but it has acquired for only one model at present, as the acquisition cost is high. With subsidies etc., it can acquire for other models and develop markets.
- 2) It cannot advertise to the whole world due to the high cost of advertisement. The current advertisement tools are limited, such as Facebook and overseas exhibitions.

### **2. Company K**

- 1) In the European market, the functionality of products is highly appreciated, but the design gets a poor evaluation.
- 2) It is necessary to cooperate with agencies to develop markets.
- 3) Foreign users do not often come to the exhibitions held in Japan.

## **5.3 Discussion**

Both company S and company K have good evaluation as they acquired 6 or more in 10 grade scale in all items of comprehensive evaluation on overseas expansion (Chart 3).

As for mainly the excellent feature of each company, company S has the sales strategy such as offering customers a noodle machine (tangible aspect) together with the production method (intangible aspect), and company K is targeting the men’s apparel products market that is a niche market. In addition, both companies have succeeded in differentiating themselves from the competitors thanks to their excellent production system and technology.

Chart 3 : International Business Strategy Analysis



Source : Created by the author

## 6. Conclusion

I believe that this verification of the hypothesis by applying the framework of international business strategy and consideration of the success factors of SME's overseas expansion is of certain theoretical significance.

It is not easy for SMEs to succeed in overseas expansion with the limited management resources, such as human resource, goods and capital. Without the capacity of decision-making and action based on top management's international business strategy and management method they will not succeed it.

In the future, the collaboration with industry, government and academia will be indispensable and it will become more and more important to revitalize SMEs. For

example, SMEs can acquire the safety measures standards with subsidies etc. and develop the markets. Regarding information gathering, marketing, etc., universities that are specialized research institutes in the regions can play the role of the think tank. I expect that the universities can complement the shortage of management resources for SMEs by summarizing, analyzing professionally and providing information from overseas.

In this paper, the discussion was focused on the cases of the two companies that expanded overseas. I conducted detailed hearing, factory survey and data analysis, but in order to generalize the research, I will conduct more surveys and continue to verify the measures against the issues revealed this time.

#### Notes

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