

THE DEVELOPMENT OF ENTREPRENEURIAL NETWORKS: A NECESSARY CONDITION FOR INTERNATIONAL NEW VENTURES?

Abstract

A long-standing view in the literature on international new ventures (INV) was that the liabilities of smallness, newness and foreignness that adhere to INVs were offset by some sort of ownership advantage, usually in the form of a superior product or technology (Zahra, 2005). More recent empirical work has demonstrated the existence of INVs in a wide range of industries, including traditional industries where hi-tech knowledge was not a factor (Knight, Bell, & McNaughton, 2001; Moen & Servais, 2002). This had led to a greater focus on the entrepreneur rather than the product as the driver of INV activity (Madsen & Servais, 1997). In this paper, we argue that the formation of a business network of stakeholders willing to commit resources to the INV is both a necessary and sufficient condition to justify the formation of an international new venture. We propose that *international social competence* and social astuteness are characteristics that encourage the development of these entrepreneurial networks.

The emergence of international new ventures (INVs), or born globals, has been one of the defining features of 21st century global capitalism (McKinsey & Company, 1993; Oviatt & McDougall, 1994; Knight & Cavusgil, 1996). More open markets, lower communication and transport costs, and the availability of staff with more international experience have created opportunities for smaller players to enter global markets (Madsen & Servais, 1997; Karra & Phillips, 2004). As a result, more companies are now 'born global' with an explicit vision to draw a substantial portion of their sales from beyond their home market.

However, born globals face a triple threat when they enter foreign markets (Sapienza, Autio, George, & Zahra, 2005). Not only do they have to cope with the liabilities of smallness and newness common to all entrepreneurial ventures, but they also must overcome an additional liability of foreignness that adheres to all ventures entering foreign markets (Zaheer, 1995). INVs must therefore overcome three handicaps that arguably large, mature, multinational firms do not.

To date, it has been assumed that these liabilities have been overcome through the possession of a superior resource, such as a new technological innovation or highly specialized knowledge – an ownership advantage to use Dunning's (1993) OLI terminology. Born globals were thus assumed to cluster in the high tech sectors (McKinsey & Company, 1993; Oviatt & McDougall, 1994). However, recent research has revealed that international new ventures also exist in low tech industries, particularly in countries with small domestic markets or strong immigrant populations (Madsen & Servais, 1997; McAuley, 1999; Knight et al., 2001).

As a result, Madsen and Servais (1997) have proposed that strong entrepreneurs are more important for a global vision than strong products. Strong international entrepreneurs are typically characterized as having substantial international experience (whether through school, work or social contacts), cross cultural competence (including the ability to speak multiple languages), and excellent global networks (Madsen & Servais, 1997; Andersson & Victor, 2003; Karra & Phillips, 2004). To a large degree, these characteristics reduce to one underlying talent: *international social competence*. Social competence enables an entrepreneur to identify international opportunities, assemble global resources, and maintain worldwide relationships among stakeholders. It is the "social glue" that holds the international new venture together. In this paper, we develop a theoretical argument to highlight the importance of international social

competence in driving international new venture formation/success by explicitly linking social competence to value creation in an international context.

INTERNATIONAL ENTREPRENEURSHIP

Following a long line of economists, we define entrepreneurship as “the recombination of resources in the expectation of profit” (Schumpeter, 1934; Hayek, 1945; Kirzner, 1973; Casson, 1982; Shane, 2003). These new combinations may include new products, new markets, new processes, or new ways of organizing. However, unlike other views on entrepreneurship, our definition does not necessarily imply the creation of new ventures (see Gartner, 1988). In our view, speculators and corporate venturers are just as ‘entrepreneurial’ as small business owners and inventors (Vesper 1980, Casson 1982).

Entrepreneurial profit arises when the value of the resources in their new use exceeds the value of the resources in their old use (Barney, 1986). Interestingly, there is an assumption that the gains will always flow to the entrepreneur but this is only true if the entrepreneur had complete *ex ante* control of the relevant resources before the recombination occurred. Otherwise, some of this value may have to be shared with the prior owners of the resources, or strategic factor owners (Barney, 1986). In fact, entrepreneurs rarely have complete control over all of their resources. Some resources, such as human capital, cannot be owned, and thus ongoing bargaining with stakeholders is the norm (Coff, 1999). The total value of an entrepreneurial initiative *to the entrepreneur* is thus the capitalized value of the residual entrepreneurial profits after such bargaining (Lewin & Phelan, 1999). The generation and protection of superior information on the value of resources is thus critical to the realization of entrepreneurial profits (Barney, 1986; Peteraf, 1993).

It follows from our definition that an international entrepreneur is one who undertakes the recombination of global resources in the expectation of entrepreneurial profit. There is a difference between expected and realized profit because of the inevitable passage of time required to assemble and deploy resources to their new uses. Thus, entrepreneurs usually bear some risk in their activities. Entrepreneurs tolerate these risks because of their desire for profit. The desire for profit distinguishes our opportunistic entrepreneur from other types, such as Smith’s craft entrepreneur or Carland’s small business owner who pursue self-employment for personal (i.e. non-profit) motives (Smith, 1967; Carland, Hoy, Boulton, & Carland, 1984).

Our definition is consistent with previous characterizations of international entrepreneurship. For instance, McDougall and Oviatt (2000) defined “international entrepreneurship” as innovative, proactive, and risk-seeking behavior that crossed national borders and was intended to create value in organizations. Similarly, McDougall, Shane and Oviatt (1994) have argued that international entrepreneurs are more “alert” to the possibilities of combining resources from different national markets than regular entrepreneurs because of their unique experience, networks, and knowledge.

The formation of organizations that are international from inception is becoming an increasingly common and important phenomenon (Oviatt & McDougall, 1994; Zahra, 2005). In this paper, we focus primarily on international joint ventures (INVs) because we believe they have the greatest challenges to overcome in creating value at the

international level and thus provide the best exemplars of the behaviors we are seeking to describe.

International New Ventures

Oviatt and McDougall (1994) defined an international new venture (INV) as “a business organization that, from inception, seeks to derive significant competitive advantage from the use of resources and the sale of outputs in multiple countries” (Oviatt & McDougall, 1994, p. 49). Previous research has identified several major catalysts underlying the emergence of international new ventures. First, the rapid development of telecommunication and Internet technologies, along with the integration of global financial markets, enabled the new ventures to be born from an international “hatcher” by utilizing resources more efficiently worldwide (Karagozoglu & Lindell, 1998). Second, the homogeneity of markets made learning about internationalization somewhat easier (Oviatt & McDougall, 1994), which accelerated the new firms’ internationalization processes. Third, the tendency for large firms to externalize certain of their non-core activities and the demand for technical expertise resulting from the rapidity of technological change and development also contributed to emergence of international new ventures (Kirby, Jones-Evans, Futo, Kwiatkowski, & Schwalbach, 1996). Finally, the presence of an increasing number of people with international business experience established another basis for the rapid rise of international entrepreneurship (Oviatt & McDougall, 1994).

Characteristics of International New Ventures

International new ventures possess several particular characteristics that differentiate them from large multinationals. First, international entrepreneurs often possess an international vision from inception (Oviatt & McDougall, 1994) while traditional multinationals have to spend time and resources to develop their internationalization motivation and accumulate their international experiences incrementally. The entrepreneurs are internationally experienced and have access to strong international business networks so that the risks of foreign operation for international new ventures are decreased dramatically.

Second, entrepreneurial orientation is an important characteristic that international new ventures possess (Oviatt and McDougall, 1994). The essence of entrepreneurship is new entry into a market or development of a market niche with new products or services (Burgelman, 1983), which is often marked in three dimensions of entrepreneurial orientation: innovativeness, risk-taking propensity and proactiveness (Miller, 1983; Lumpkin & Dess, 1996; Lee, Lee, & Pennings., 2001). Similarly, several papers have argued that international new ventures also possess a strong marketing orientation, which drives the firm to offer products and services that buyers perceive to add more value than alternative offerings (Knight, 2000; Knight & Cavusgil, 2004).

Third, advanced technological capabilities or knowledge-based assets have often been seen as important for international new ventures (Oviatt & McDougall, 1994; Bettis & Hitt, 1995; Manolova, 2001). The possession of cutting edge technological resources or knowledge enables the firm to enter valuable niches in global markets and to offer something of value to potential alliance partners. However, as we have seen international new ventures also exist in low tech industries, particularly in countries with small

domestic markets or strong immigrant populations (Madsen & Servais, 1997; McAuley, 1999; Knight et al., 2001).

Challenges for International New Ventures

In the introduction, we argued that international new ventures are subject to a higher burden than almost any other type of firm, being subject to the triple liabilities of newness, smallness, and foreignness. Note that the term ‘liability’ is just shorthand for additional costs. Thus, a liability of foreignness is the additional costs that foreign firms must incur that local firms do not (Zaheer, 1995). Similarly, a liability of newness is the additional costs a start-up must incur above established firms; and a liability of smallness is the additional costs a small firm must incur over a large firm. While the liabilities of newness and smallness are often co-terminous, researchers have been able to demonstrate that these are separate effects (Wholey & Brittain, 1986; Hannan & Freeman, 1989).

According to Stinchcombe (1965), a liability of newness is caused by the costs of establishing new structures and procedures; attracting, training and retaining new employees; and building a stable portfolio of clients (which often implies building a reputation for quality and reliability). Organizational ecologists use the term *legitimacy* to refer to the reluctance of stakeholders (customers, employees, investors, regulators) to engage with new organizations that have not established their reputations (Hannan & Freeman, 1989). The high risk of failure of new ventures makes stakeholders reluctant to bear the risk losing their own capital in the enterprise. One implication is that a new organization will find it harder to establish legitimacy if its products or processes are perceived as different or radical.

The extra costs that a small firm must bear over a large firm are also fairly well established in the literature (Aldrich & Auster, 1986). Small firms usually lack economies of scale in all aspects of their operation (including production and distribution). This puts them at an immediate cost disadvantage vis-à-vis larger players. Small firms can also not devote the same effort to complex or specialized tasks (like government regulations, tax compliance, or tendering for large contracts), which causes them to miss opportunities or incur additional costs. If it is generally known that small firms are more likely to fail then it will also become difficult to attract customers, employees, suppliers, and investors. Some stakeholders will not come at all, whereas others might only be tempted with an incentive or premium offer (i.e. investors will demand higher interest rates, customers will ask for lower prices, and employees will seek higher wages).

International new ventures also need to overcome a ‘liability of foreignness’ in host markets (Hymer, 1976; Zaheer, 1995). Zaheer (1995) identifies four cost categories, including: 1) spatial costs – the costs of travel, transportation, and coordination over distance; 2) firm-specific costs, related to the firm’s unfamiliarity with the host environment; 3) host country costs – related to the lack of legitimacy of foreign firms and economic nationalism; and 4) home country constraints – for instance, barriers to the export of a given technology to certain countries. According to Zaheer (1995), firms with a liability of foreignness will have lower profits and a higher probability of failure everything else being equal. This insight can be expanded into a more general proposition:

P1: Due to liabilities of newness, smallness, and foreignness, international new ventures will have lower profits and a higher failure rate than domestic firms, *ceteris paribus*

DRIVERS FOR INTERNATIONAL NEW VENTURES

The preceding analysis suggests that international new ventures should never be founded (at least by rational investors seeking a normal rate of return on capital) because they would operate at a permanent cost disadvantage to older, larger, domestic firms. The fact that INV phenomenon appears to be becoming more common suggests that there must be one or more compensating factors, or drivers, that offset the triple liabilities outlined above. In this section, we review and critique a range of compensating factors that may account for this observation, including changes in the global context, industry characteristics, firm characteristics, and founder characteristics.

The Global Context

Several authors have commented on the changes in the global environment that have encouraged the development of international new ventures (Oviatt & McDougall, 1994; Knight & Cavusgil, 1996; McDougall & Oviatt, 1996; Andersson & Wictor, 2003). These changes include the lowering of tariff barriers and other regulatory obstacles to international commerce; the decline in transport and communication costs; the greater international experience of professionals and managers; and the hollowing out of large multinational corporations, which has increased strategic alliances and outsourcing activities.

Of course, to reduce the triple liabilities, these trends must *differentially* affect international new ventures. That is, international new ventures must gain more from these changes than multinationals. For instance, the reduction in regulatory barriers affects all international firms but the reduced compliance efforts may be more beneficial to small firms that cannot afford to hire specialized resources to negotiate complex regulatory hurdles in global markets. Similarly, the decline in transport and communication costs benefits all international ventures. In theory, those with (relatively) limited resources might be able to differentially discover and develop international market opportunities they might have foregone in the past because of the prohibitive cost. Likewise, while the hollowing out of multinationals seems to provide clear benefits for small ventures, it is not clear that international ventures would have an implicit advantage over small domestic players that would also be bidding for outsourced business. We conclude, therefore, that changes in the global context are certainly likely to positively affect the development of international new ventures, but that such developments will occur at the margin. Global factors alone are not sufficient to explain the formation, or success, of an international new venture.

Industry Characteristics

Another line of inquiry has focused on the industry characteristics of international new ventures by arguing that certain industries are more disposed to the development of international new ventures than others (Andersson, 2004). Initial attention focused on hi tech and knowledge intensive industries. An early Australian study by McKinsey found that firms classified as born-globals tended to export leading-edge technology to global

niche markets (Rennie, 1993). The ease of transferring valuable knowledge across national borders and combining it with local (immobile) factors was seen as an important way of achieving a competitive advantage over local players (Oviatt & McDougall, 1994). It has also been argued that growing industries that provide more opportunities for small players to find a competitive niche are more likely to attract INVs (Andersson & Victor, 2003).

A number of industry-based factors that ‘push’ companies to form INVs have also been identified. For instance, narrow specialized niches, high up front R&D costs, short product life cycles, and shrinking domestic markets force firms to quickly go international to achieve sales growth and return on investment (Preece, Miles, & Baetz, 1999; Nummela, Saarenketo, & Puumalainen, 2004). Similarly, a high degree of internationalization by customers and competitors may also ‘push’ firms into establishing a born-global orientation (Madsen & Servais, 1997).

The industry-based argument is somewhat weakened by the fact that international new ventures have been identified in a wide variety of industries. Although a definitive study of the distribution of INVs across industries has yet to be undertaken, we know that mature industries, such as rubber and industrial cranes, and low tech industries, such as wine and seafood, also seem to have produced their share of international new ventures (Madsen & Servais, 1997; Knight et al., 2001). In fact, Moen (2002) has reported that up to one-third of new firms in a European sample were exporting within two years. A majority of firms in the sample were exporting within ten years (Moen & Servais, 2002). Echoing research in strategic management (e.g. Rumelt, 1991), this suggests that industry characteristics are not the sole determinant, nor perhaps even the major determinant, of the decision to become global from inception. This has prompted some researchers to explore variations in firm and founder characteristics to explain how *particular* firms or founders overcome the triple liabilities of newness, smallness, and foreignness.

Firm Characteristics

The resource-based view of the firm has been used to explain the central question of INV theory, namely why one firm is global from inception while another is not (McDougall et al., 1994; Bloodgood, Sapienza, & Almeida, 1996; Knight & Cavusgil, 2004). Strategic management theory asks “Why does one firm perform better than another?” In the INV sphere, the same question is asked to understand the factors that enable superior performers to clear the triple liability hurdle and (profitably) enter the global marketplace. Of course, the simple answer is that superior performers (or born globals) have resources that other firms (in either the home or host country) do not possess. Following Dunning (1993), we will refer to these resources as the INV’s ownership advantage. Thus, a firm with a large ownership advantage will be able to overcome the triple liabilities of international new ventures.

The resource-based view actually describes two paths to competitive advantage – resource picking and capability building (Makadok, 2001). Resource picking involves acquiring and using superior resources with commonplace routines (Barney, 1986) whereas capability building involves deploying widely available resources in novel ways (Dierickx & Cool, 1989). The distinction might be compared to the old sports adage that a champion team will always beat a team of champions. A champion team results from capability building, whereas a team of champions is the result of a resource-picking

process. The processes can also be complementary (i.e. creating a champion team of champions). Central to the concept of resource picking is the notion that the entrepreneur must maintain some sort of information asymmetry with the resource holder that enables them to obtain the resource on favorable terms (Barney, 1986). If the resource holder, or to use Barney's terminology, the strategic factor holder, were to become aware of the future value of the resource they would adjust their price upwards thus reducing or perhaps even eliminating any residual entrepreneurial profits.

The INV literature makes reference to both resource-based processes to explain the ownership advantage of born-globals. An ownership advantage based on leading-edge technology or specialized knowledge implies skill at resource-picking (McKinsey & Company, 1993; Rennie, 1993; Oviatt & McDougall, 1994). However, there has been little discussion in the literature on how the firm was able to acquire the resources on favorable terms without the strategic factor owners appropriating the gains. Of course, if we assume that the founder personally developed the technology or specialized knowledge then the problem is solved.

Recently, there has been much more focus in the literature on the competences or capabilities of international new ventures (Zahra, Ireland, & Hitt, 2000; Knight & Cavusgil, 2004). According to Zahra, Ireland and Hitt (2000, p. 925), "Even when it has a technologically superior product, a new venture firm must learn other skills to position its product successfully and develop the competencies that are necessary for superior performance...international expansion can promote organizational, especially technological, learning facilitating the development of skills and competencies that help the firm achieve a competitive advantage." Thus, an international new venture learns faster than its domestic counterpart and this learning enables the firm to leverage its unique (technological) resources for greater competitive advantage. This sentiment is echoed by Knight and Cavusgil (2004) who find that a global technological competence is a key element of successful INVs.

Other researchers have argued that born globals have a unique entrepreneurial orientation and a distinctive marketing orientation/competence that sets them apart from domestic rivals (Knight, Madsen, & Servais, 2004; Knight & Cavusgil, 2004). The entrepreneurial orientation creates a firm that is more innovative, risk-taking and proactive in relation to its peers (McDougall & Oviatt, 2000), while a marketing oriented firm seeks "...to offer products and services whose value buyers perceive to exceed the expected value of alternative offerings" (Knight and Cavusgil, 2004, p. 130). Successful INVs have an urge to continuously provide value to foreign buyers and this orientation becomes embedded into the business culture and routines of the firm creating an international marketing competence. The relatively small size of an INV also creates greater flexibility and an ability to promptly adapt to changes with less structural inertia (Autio, Sapienza, & Almeida, 2000).

The firm-level explanations of INV behavior suffer from a number of limitations. First, an ownership advantage based on resource-picking to overcome the triple liabilities problem places an enormous burden on the value creation potential of those resources (Madsen & Servais, 1997). While it is possible to think of examples of firms that have developed blockbuster products and technologies on the basis of their unique specialized knowledge, a strong product will usually not be sufficient to overcome the liabilities facing INVs, particularly outside the high tech sector. The development of secondary

competences (in marketing and entrepreneurial orientation for example) enables the firm to create more value by leveraging its product advantage. This extra leverage increases the probability that a firm will pass the triple liability hurdle. It may also be possible that some firms survive in the global marketplace simply by means of their entrepreneurial and marketing competences without ever having a unique product offering or specialized asset base (Madsen & Servais, 1997).

A 'firm-level competence' also represents an abstraction that obscures the role of individuals in the INV process. A firm does not act; it is the people within the firm that act (von Mises, 1949; Fligstein, 1997). A marketing or entrepreneurial competence is nothing more than a form of shorthand that purports to summarize the way that a firm acts (or reports that it acts). Not everyone in the company will experience the same risk-taking propensity or customer serving zeal. At best, a competence reflects a general tendency among individuals in the firm to act in a given way. It is certainly possible to speak about an 'entrepreneurial competence' or 'marketing culture' being created in a company, but once again a culture is the product of the action of individuals.

In fact, the INV literature has tended to assume that the founder (or founders) of an INV has more influence on the culture and competences of the firm than any other persons (Kuemmerle, 2002; McDougall, Oviatt, & Shrader, 2003). It is the founder (or founders) of the INV that typically makes the decision to become global from inception, not the 'firm' In fact, in the smallest firms, the founder *is* the firm. Thus, Madsen and Servais (1997) are led to argue that a strong entrepreneur is more important than a strong product in the 'born global' decision, particularly in a small firm where founders are likely to have more influence on decisions than 'professional' managers.

Founder Characteristics

A number of studies have focused on the founder characteristics of born globals (Oviatt & McDougall, 1994; Madsen & Servais, 1997; Andersson & Wictor, 2003; Karra & Phillips, 2004). These studies have reported that founders of international new ventures typically possess a global vision, international experience, and strong networks. A global vision implies a vision of the organization that is global from inception rather than a domestic firm internationalizing (McDougall et al., 1994; Karra & Phillips, 2004). The founder makes no distinction between customers in global and domestic markets and tends to perceive national market boundaries as irrelevant (Johanson & Vahlne, 2003).

Founders of international new ventures also tend to have extensive international experience (McDougall et al., 1994; Madsen & Servais, 1997; Andersson & Wictor, 2003). This experience often takes the form of several years living, working, or studying in foreign countries. Karra and Phillips (2004) reported that international entrepreneurs were often immigrants or people who had spent long periods abroad. They brought their intimate knowledge of another country's language and culture back to their home country. As such, they often perceived starting an international new venture dealing with their former place of residence as less risky than starting a domestic business.

It has also been observed that founders often have strong personal networks of family and business contacts, including customers, distributors, investors, and suppliers (Jack, Dodd, & Anderson, 2004). McDougall, Shane and Oviatt (1994) argue that

founders are pushed to build networks to counter their liabilities of newness and smallness. Karra and Phillips (2004), on the other hand, find that founders of INVs are 'promiscuous collaborators' who thrive on building networks.

In a major revision to the Uppsala model, Johanson and Vahlne (2003) acknowledge that perceived psychic or cultural distance between countries is irrelevant in the internationalization process. Rather, it is the network of relationships between the founder and others that determines the evolutionary trajectory of a business. "There is nothing outside the relationships. Internationalization is, in this network world, nothing but a general expansion of the business firm which is in no way affected by country borders. All barriers are associated with relationship establishment and development" (Johanson & Vahlne, 2003, p. 93).

This network model is also be used to predict the emergence of international new ventures:

"Since relationship building is time and resource demanding we have reason to suspect that successful entrepreneurship is based on the entrepreneur's existing network. Her/his experience and earlier commitments will influence where the first market entry will occur. Whether this will be a foreign market entry or not depends on the relationships of the entrepreneur" (Johanson & Vahlne, 2003, p. 95).

Thus, the establishment of an international new venture is a special case where the entrepreneur's business network extended across one or more national boundaries at the time of inception. Past experience, then, is a proxy for network relationships.

Johanson and Vahlne (2003) also recognize that networks are bilateral devices and that international expansion can be triggered by others. For instance, knowledge of a firm's products (perhaps from the internet or trade publications) may spur international agents to attempt to establish a relationship that firm. Thus, not all relationship building has to be initiated by members of the firm but as relationships take time to mature, prior relationships will be more important on early market entry choices than subsequent contacts. Similarly, as the firm grows, the business acquires the networks of new employees which may trigger further international or domestic expansion that is not related to the founders' initial thrusts.

Although Johanson and Vahlne (2003) describe their network thesis as a 'process theory' it is still a very macro-level description of the process. Prior experience in a foreign country does not automatically build business networks. Many business people have lived and worked in foreign countries but have not managed to start a new venture nor even establish a strong social network. In the next section, we argue that *social competence* is the 'glue' that creates and holds social networks together and that *social astuteness* is the force that transforms social networks into business networks. The relationship of these abilities to international entrepreneurship and the foundation/success of international new ventures is then considered.

THE CASE FOR INTERNATIONAL SOCIAL COMPETENCE

Social competence is the ability to form and maintain relationships (i.e. to create a social network). Past studies on social competence have conceptualized it as a bundle of skills and capabilities, including impression management, social perceptiveness ("I usually read others well"), social adaptability ("I can adjust to any situation"), and

persuasiveness (Fligstein, 1997; Baron & Markman, 2000; Baron & Markman, 2003). Social competence has been contrasted with social capital, the latter being conceived as a way of gaining access to people critical to the venture's success, while the former plays a key role in the determining the outcome of that experience (Baron & Markman, 2000). As such, social competence has been positively related to entrepreneurial success (Baron & Markman, 2003).

The mechanism underlying the development of a social network has been a relatively understudied area in entrepreneurship (Hoang & Antoncic, 2003). In our formulation, the possession of social competence produces better quality relationships (both with close friends and acquaintances) which strengthens social networks and thus builds social capital.

International social competence is the ability to form and maintain relationships (and build social networks) across national boundaries. International social competence includes the skill set of social competence (impression management, social perceptiveness and adaptability, and persuasiveness) but also includes a cross-cultural ingredient based on language skills and cultural empathy (Karra & Phillips, 2004). These cross-cultural skills are most likely to develop when a socially competent individual has the opportunity to spend significant periods of time in other cultures.

The first benefit of an extensive international social network is the ability to gather more information and identify more opportunities. While a nascent entrepreneur may stumble upon a profit opportunity in the course of a casual visit to another country, we believe that an entrepreneur with a wider network of contacts in the international community will be better informed about profit opportunities because both the quantity and quality of information will be greater. Hence, simply spending a great deal of time in a country will not have the same effect as actively creating (and maintaining) a strong network. In fact, there is already some evidence in entrepreneurship research that entrepreneurs with larger networks identify more opportunities (Hills, Lumpkin, & Singh, 1997). A number of propositions flow from this argument:

P2: International social competence will increase the strength of an entrepreneur's international social network.

P3: Stronger international social networks will create better profit opportunities.

P4: Firms with good international profit opportunities from inception are more likely to be 'born global'.

Social competence may also improve the founder's ability at resource-picking and capability building, which are essential to a resource-based competitive advantage (Makadok, 2001). A broad circle of friends and acquaintances can introduce the international entrepreneur to a wider circle of resource holders, including suppliers, investors, employees, distributors, customers, and regulators (Davidsson & Honig, 2003). This will tend to give the entrepreneur a greater choice of resources to pick from. Members of an entrepreneur's social network can also provide knowledge about best practice and provide emotional support during the startup process (Greve & Salaff, 2003). Socially competent entrepreneurs may also be more adept at capability building, because of their ability to form non-pecuniary (friendship) ties with various stakeholders, customers, employees, suppliers, distributors, and even competitors (Ingram & Roberts, 2000). These friendship ties may increase the organization's ability to overcome complex

coordination and cooperation challenges during its development (Kogut & Zander, 1996; Phelan & Lewin, 2000). This leads us to propose that:

P5: Socially competent individuals will be more adept at resource-picking and capability building.

Business Networks

An entrepreneur's business (or instrumental) network can be distinguished from his or her social network by the nature of their ties. Whereas social networks are based on friendship ties, business networks are based on *instrumental* ties (Lincoln & Miller, 1979; Larson & Starr, 1993). Instrumental (or exchange) relationships are concerned with pecuniary or financial gain. Although business and social networks can (and do) overlap, every relationship that is used for value creation must necessarily have an instrumental component. Instrumental relationships can be created from social networks or from arm's length transactions, where the parties have no prior social relationship.

If a social relationship exists, an entrepreneur may be able to elicit a resource commitment on the basis of a strong affective tie or obligation. These ties are most likely to occur in family or kinship networks where close relatives feel motivated or obligated to assist each other although there is an expectation such favors will be reciprocated in the long-term (Chen & Glen, 2004). A family network will always have fewer members than a fully functioning capital market and, as a result, even the wealthiest families will find it difficult to raise the large sums of capital required to enter into large-scale, capital intensive businesses (Chandler, 1990; Haber, 1991). Despite this limitation, family firms have been found to earn similar returns on equity to non-family firms even with a smaller capital base (Gorritz & Fumas, 1996). This leads us to propose that:

P6: Entrepreneurs with strong social networks will find it easier to start an INV

P7: Entrepreneurs with strong ties will cluster in industries with low capital intensity

However, in the absence of strong social ties, a stakeholder will only enter into an instrumental relationship if the expected net present value from the relationship exceeds the expected value of other opportunities (i.e. the opportunity cost). This means that an employee will only come to work for an entrepreneur if the expected wages exceed the wages he or she could earn in other pursuits. Similarly, an investor will only invest in an international new venture if the expected returns exceed those of other investment opportunities and a customer will only buy a product if the expected value exceeds the value of other product offerings.

In a competitive spot market, such as the market for office furniture, an international new venture is unlikely to be at a cost disadvantage with an established firm because payment is received immediately and the next best opportunity (i.e. another customer) would typically fetch the same price. (In fact, a customer with cash in hand may be preferred to a future customer that may not appear anytime soon.) Complications only ensue when the relationship extends over time. For instance, if an international new venture wanted to buy their office furniture on credit they would face a steeper finance charge than an established business because of the risk that a new business will fail and default on its payments. In these situations, the firm's reputation becomes an important factor in determining the price of resources.

Unfortunately, almost all business relationships have a temporal component, including customer relationships, supplier relationships, employee relationships, and

financial relationships. A customer that purchases a durable good or service is typically concerned about reliability and after-sales service. Firms without an established reputation will find their value proposition discounted. Similarly, an employee who is trying to maximize the value of his or her human capital will be concerned about future wage growth, promotion opportunities, and skill development. Everything being equal, an employee will demand a higher wage to work at a startup than an established firm because their future cash flow is more uncertain. Similar arguments can be used to explain why investors expect higher returns and why suppliers and distributors will be harder to find.

This situation has serious ramifications for the born global firm because, as we have seen, the triple liabilities of smallness, newness, and foreignness imply that stakeholders will impose additional costs or burdens on international new ventures (if they choose to do business with them at all). More sophisticated stakeholders, such as venture capitalists, will demand evidence of an entrepreneur's reputation or track record before committing to a venture (Amit, Glosten, & Muller, 1990). Perhaps this is why fewer than 1 in a 1,000 startups in the US are financed using venture capital (Bhide, 1992).

In financial terms, this means that the expected value calculations of potential stakeholders will be biased downwards for international new ventures. If the expected value of a relationship with an INV falls below the opportunity cost then a transaction will not be entered into. As we have argued, an international entrepreneur will need a major ownership advantage or some other compensating factor to overcome this issue.

Social Astuteness

Social astuteness is the ability to influence the expectations of potential and existing stakeholders so they will commit resources to a business network on favorable terms. A socially astute person is likely to be an effective negotiator, aware of other's motives, and diplomatic in presenting issues to others. Such a person will tend to get his or her way with people without their necessarily becoming aware of the subtle means used to achieve that purpose. A person high in social astuteness may sometimes be considered manipulative or opportunistic but is usually perceived as charming and a natural leader. Socially astute individuals tend to see social interactions as opportunities not threats. While social astuteness can be considered an aspect of social competence, not all socially competent people have developed the ability to manage expectations. However, social astuteness is a difficult skill to delegate or hire as socially astute individuals are likely to appropriate gains for themselves. Thus, founders often need to be more socially astute than their employees.

As we have seen, the triple liability problem ensures that the expected value of an international new venture will typically be lower than that of other opportunities. However, an expectation is merely a perception about the future and perceptions can be changed. There are several ways to do this: by improving the perceived ownership advantage of the INV, by downplaying the perceived liabilities of newness, smallness, or foreignness, or by altering the perception of the value of other opportunities. Research has shown that socially astute people perform significantly better on resource picking tasks making higher profits in mixed bargaining tasks (Phelan & Alder, 2005). Social astuteness was also highly correlated with other traditional entrepreneurial variables, such as risk taking, openness to experience, and propensity for innovation.

Socially astute entrepreneurs tend to use impression management and influence tactics to accomplish their goals (Stuart, Hoang, & Hybels, 1999; Baron & Markman, 2000; Cialdini, 2001; Greene, 2001). For instance, Stuart et al (1999) reported that biotech firms with prominent alliance partners and equity investors were quicker to go public and earned greater valuations than a matched sample of firms without endorsements. This type of association strategy serves to build legitimacy, even among sophisticated investors. A socially astute entrepreneur will therefore be adept at cultivating real (or apparent) high-level associations and leveraging those connections to build legitimacy and reputation among other stakeholders. Additional impression management tactics include: acting in a way others expect, power dressing, projecting self-confidence, adopting a caring attitude, and telling others what they want to hear (Drummond, 1993; Rosenfeld, Giacalone, & Riordan, 1995).

Story telling can also be used to legitimize or enhance the firm's prospects. Lounsbury and Glynn (2001) define cultural entrepreneurship as the process of storytelling that can mediate "between extant stocks of entrepreneurial resources and subsequent capital acquisition and wealth creation (p.545)." Stories often provide a convincing rationale for the new venture and reduce uncertainty (Aldrich & Fiol, 1994). The goal of the story is to provide a coherent account of how the entrepreneur will create wealth for stakeholders in the venture. In essence, it is the 'elevator story' that is used to sell the business model. These stories may be directed at any stakeholder, including potential investors, employees, or even customers. However, in order to elicit a favorable interpretation from a story, the entrepreneur must modify the story to conform to the normative beliefs of each audience (Lounsbury and Glynn, 2001). In the international context, the story must be sensitive to the traditions and aspirations of the host country.

Once resources have been committed to the venture, the entrepreneur still faces the ongoing challenge of retaining mobile resources within the organization (Peteraf, 1993) and resisting attempts by stakeholders to renegotiate arrangements and appropriate entrepreneurial profits (Coff, 1999). For instance, an employee may be offered a higher salary outside the firm or argues that they should be paid more for their contribution they are making to the firm. Almost all entrepreneurs face these problems from time to time. By definition, a socially astute entrepreneur will be better at leadership, diplomacy, and negotiation. This places them in strong position to assure resource-owners (primarily the owners of human and financial capital) that it still makes sense to link their prospects to those of the firm and not seek greener pastures. He or she will also be better-placed to bargain with opportunists to preserve a profit share.

On the basis of these arguments, we propose that:

- P8: A socially astute entrepreneur will be able to build (and maintain) a stronger international business network.
- P9: A stronger international business network will make an international new venture more competitive.
- P10: A socially astute entrepreneur will be better placed to retain resources and resist appropriation attempts.

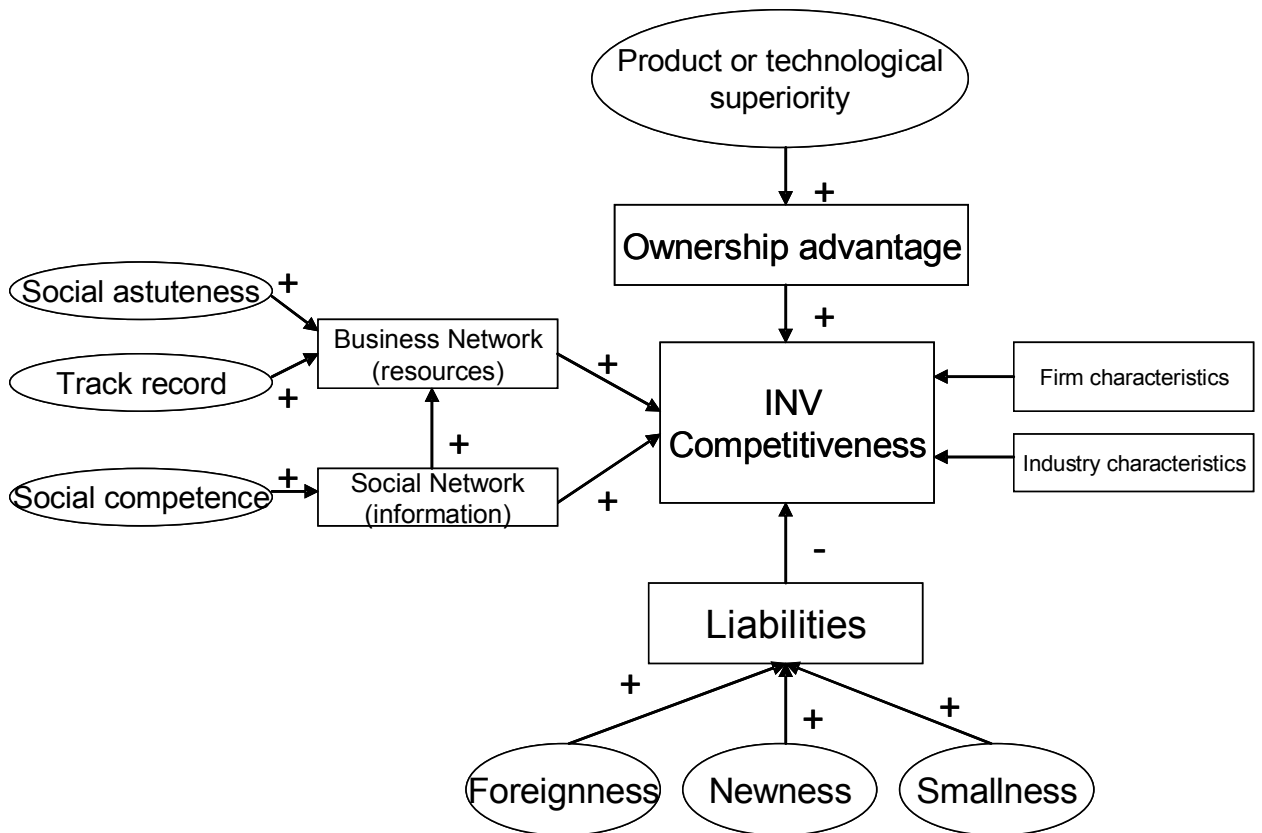


Figure 1. Conceptual Model

DISCUSSION

A conceptual model of our argument is presented in Figure 1. We conceive that ownership advantage and entrepreneurial networks (social and business) are the two major forces that balance the triple liabilities of newness, smallness, and foreignness to create INV competitiveness. Industry and firm characteristics are also acknowledged but for reasons outlined earlier are seen as less relevant to INV competitiveness. According to our arguments, a more competitive firm will be founded sooner, grow faster and produce higher entrepreneurial profits for its founders. Conversely, a firm with poor competitiveness will have trouble being established at all.

We believe that the ability to extract resource commitments from instrumental business relationships is virtually essential to the establishment of an international new venture for the simple reason that, to paraphrase John Donne, no entrepreneur is an island. Admittedly, it is still possible for an introverted self-employed entrepreneur to write a software program, post it to an internet bulletin board as shareware, create a payment system using PayPal, and sit back and watch the money roll in. However, once an ongoing relationship is required with a customer, supplier, employee, or distributor then social skills become an important part of the mix. At the other end of the spectrum, Madsen and Servais (1997) have argued that an ownership advantage is not required to create a competitive INV. An entrepreneur could profit by trading completely undifferentiated commodities across national borders simply by buying low in one region and selling high in another. Price information could be collected from the entrepreneur's social network and the level of profits would be based on the entrepreneur's ability to

bargain effectively with buyers and suppliers (i.e. on social astuteness). Network development is thus both necessary and sufficient for the development of an international new venture.

The conceptual model is also applicable to domestic entrepreneurs once the liability of foreignness is dropped from the model. This is consistent with Johanson and Vahlne's (2003) argument that new ventures become international simply because entrepreneurial networks extend across national borders. In fact, immigrants have reported feeling just as comfortable doing business in their country of birth than in their adoptive country (if not more comfortable) thus neutralizing much of the liability of foreignness anyway. Nevertheless, cross-cultural aspect of international social competence (which is required to facilitate international network development) may be one skill that remains unique to international entrepreneurs.

Over time, the liabilities of smallness, newness, and foreignness should diminish as the firm establishes a reputation and legitimacy in international markets. A successful track record will also make it easier to bargain for resources and attract instrumental relationships. The challenge then shifts to one of maintaining social capital and ownership advantages. Given that impression management and other influence tactics will be most critical at the startup phase, there may be a tendency for enthusiasm for an opportunity to turn to deception. Some business ethicists argue that it is wrong to lie about material facts but reasonable to bluff about reservation prices, which presumably would include opportunity costs, as long as the opportunity for mutual gain exists (Strudler, 1995). Another school of thought argues that any form of deception (including deliberate misrepresentation or omitting of pertinent facts) is morally regrettable in that it wastes society's resources on protracted negotiations and inefficient deals. However, an individual is not morally wrong in using deceptive tactics if not doing so would expose them to significant risks or costs (Dees & Cramton, 1991, 1995). Using this line of thought, it is morally regrettable that international entrepreneurs must use social influence to overcome the triple liabilities of smallness, newness, and foreignness but not doing so would expose them to significant costs or a significant risk of failure. Putting the two arguments together would suggest all influence tactics are morally regrettable but that as long as both sides stand to gain from the exchange it is not morally wrong. This is sometimes referred to as the 'self-defense' theory of business ethics (Strudler, 1995). There is also evidence of cultural differences in the acceptability of bargaining tactics with high power-distance and high uncertainty avoidance countries eschewing traditional bargaining tactics (Volkema, 2004). As mentioned earlier, socially astute entrepreneurs would have to learn to adjust their style in different national cultures.

A related issue is whether socially astute individuals crowd out entrepreneurs with a superior ownership advantage but poor social skills. One answer is that INV competitiveness cannot be assessed on one factor alone but rather is the sum of what an entrepreneur can bring to the table. Another answer is that HR practitioners believe that social skills can be learned in short-term training and those deficient in the area would be well advised to improve their skills (Markman & Baron, 2003).

Conclusion

This paper proposes some new ways of thinking about international new ventures. First, it seeks to create a process view of INV competitiveness by explicitly linking

individual founder capabilities (namely international social competence and social astuteness) to the development of viable entrepreneurial networks. Following Johanson and Vahlne (2003), we argue that strong entrepreneurial networks are at the heart of new venture competitiveness and see international new ventures arising from networks that happen to cross national borders. Cross border ties allow international entrepreneurs to bypass normal barriers to entry. Networks are thus both necessary and sufficient for INV competitiveness.

Previous network studies have tended to focus on the structure of the network rather than the process underlying the development of relationships (Hoang & Antoncic, 2003). Other studies have seen networks as a type of social capital that some entrepreneurs can access and others cannot. In this view, the network has a life of its own, independent of the entrepreneur (Andersson & Wictor, 2003). This paper firmly places the spotlight on the founder (or founders) of the INV as the creator/director of network relationships. International entrepreneurs are 'promiscuous collaborators' that actively seek out relationships and see opportunities instead of obstacles (Karra & Phillips, 2004). We want to avoid a privileging of firm-level (or network-level) characteristics over individual actions because individuals are the key drivers of entrepreneurial action.

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