IDENTIFICATION OF THE KEY RISK FACTORS OF THE INTERNATIONALIZATION PROCESS OF SMES OPERATING IN THE TEXTILE INDUSTRY

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Abstract

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The aim of this paper is to identify the key risk factors of the internationalization process of Czech SMEs operating in the textile industry. To reveal the key risk there was conducted the survey (2011–2012) among 803 Czech SMEs operating in the textile industry, 161 responses were processed. The obtained data were analyzed by statistical methods. Potential risks of entry into foreign market were rated according to their impact on businesses. The greatest influences on the process of successful internationalization have, according to obtained responces, following factors: shortage of capital, lack of the information on foreign markets and high transportation costs. Other factors that may impede the successful internationalization are language barriers, inexperience of management with the internationalization and high prices of products. Knowing the key risk it is easier for SMEs to manage it.

Keywords: internationalization, small and medium-sized enterprises, crucial key factors, internationalization process, textile industry

INTRODUCTION

In the recent days, there is seen the acceleration and deepening of the globalization, which brings the convergence and links the world economies. Globalization is closely linked to companies' internationalization, to the development of multinational companies and also to removal of barriers and increasing competition in domestic markets. The increasing competition is reflected in the effort of companies to expand into foreign markets. The process of globalization leads to stronger internationalization of the world economy; it leads to the development of international relations and economic interdependence of countries. Competition from abroad has been growing and for small and medium sized companies it is difficult to be competitive in this battle. For SMEs it is often more difficult to succeed and then to maintain the position in the foreign markets than for large companies. The advantage of small and medium-sized enterprises (SMEs) is their ability to respond quickly and flexibly to the market changes, but on the other hand, they often have to cope with the lack of capital, they often have also less experiences with foreign markets, have not as experienced management as large companies and have more difficult access to foreign resources than large firms. SMEs are very important market sector of the economy; they are the driving force of business, growth, innovation and competitiveness. Therefore it is given constant attention to small and medium-sized enterprises' development and SMEs have been increasingly subjected to the examination in an attempt to identify the factors influencing the success of their international activities. Knowing the key factors influencing the internationalization process of SMEs can effect positively other small and medium-sized enterprises in their plans to penetrate foreign markets. Like all processes in the firm also the international process is

accompanied by risks. The main aim of this paper is to identify the key risk factors of this process – knowing the risk factors it is possible to propose to SMEs the way how to reduce or eliminate possible risks in their activities on foreign markets. There are not the same conditions for all SMEs to enter the international arena in all sectors of the industry. In some sectors, there are provided some export supports for SMEs which can help to eliminate or reduce risks of the internationalization process and, of course, there are some industries, where companies can enter foreign market more easily due to nature of their production. This article is focused on the internationalization process of the Czech textile industry, which has been recently flooded with cheap products from Asian countries.

MATERIAL AND METHODS

SMEs in Czech Republic as well as in the other countries of EU play very important role in the international arena. In the last three decades we can see an increase in the number of SMEs relative to large firms and SMEs have become an important market sector of the economy and they can be considered today as the driving force behind business, growth, innovation and competitiveness. SMEs are also an important factor in providing job opportunities.

Economic and social benefits of SMEs can be characterized by several faculties. These include in particular, that mitigating the negative effects of structural change, acting as subcontractors for large firms, create conditions for the development and introduction of new technology, create jobs at low capital cost, quickly adapt to the requirements and market fluctuations are a source of innovation and technological progress, employ nearly 60% of active workers, involved more than half of GDP, completed in peripheral areas of the market that are attractive for larger businesses, decentralize business activities and help accelerate the development of regions, towns and villages. Small and medium-sized businesses have many advantages in the market, but faced with a number of negative effects. The advantages of SMEs are particularly simple organizational structure that brings lower costs for company management and reduced bureaucracy, the setting up of the company capital is usually not as demanding as it is for large enterprises. Then there is flexibility – small and medium-sized businesses can react faster and more sensitive to changes than large corporations (with it even greater flexibility and ability to improvise). Another advantage is less demand for energy and raw materials, SMEs also easier look for small niche markets and they can better apply to local markets, they can address the needs of individual customers. One positive aspect is also personal and direct contact with the company owner and other employees the possibility of maintaining personal contact with customers. SMEs are considered as vectors of a large number of innovations. The disadvantages include the fact that it is more difficult for SMEs to access foreign capital than larger companies, SMEs are unable to participate in a business where large investments are needed, often have a weaker position in the bidding for government contracts, they cannot afford to hire top professionals and scientists, have limited resources for promotion and advertising, their market share is low and often threaten the majors. SMEs also threatened, it is easier to fall into insolvency, especially in cases of insolvency of their customers. SMEs have also major problems with entry into foreign markets because they lack sufficient information on foreign legislation, potential partners, the market, the availability of counseling services at a lower level. Therefore the paper is focused on the internationalization process of SMEs.

Internationalization of the companies is generally defined as the involvement in the international environment. The concept of internationalization in the literature varies widely by various authors, such as Beamish (Beamish, 1990) understands internationalization as a process by which firms increase their awareness of the direct and indirect effects of internationalization transactions on their future and create and manage transactions with other countries. Accordigd to Majerová (Majerová, 2007) the internationalization process of continuous and progressive interconnection of economies in the world economy runs through an expanding network of international relations. The process of internationalization can be also defined as "the increasing process involved in international operations (Welch, Luostarinen, 1988). The process essentially involves the adaptation of firm operations like strategy, structure, resources etc., to perfectly fit the international environment. The degree of internationalization can be measured as foreign sales relative to total sales (Welch, Luostarinen, 1988). According to Kunešová and Cihelková internationalization is one of the most persistent trends shaping the world economy. Its content is the establishment and deepening of economic relations between different countries, based on the gradual elimination of various barriers and converting some old national events on the international effects (Kunešová, Cihelková, 2006). The internationalization process can be described also as a gradual development taking place in distinct stages (Melin, 1992) and it can be clearly identified under two major school: the models initially developed by Johanson and Wiedersheim-Paul (1975) and Johansona and Vahlne (1977), refered to as UppsalaModels (U-models) and the Inovattion-Realated internationalization models (I-models) conceptualized by Cavusgil (1980). Both I-models as well as the U-models emphasize on firms involvement in foreign market segments, both of the models view internationalization as a gradual incremental process. U-model is more often featured

in international business literature. The entering of new markets by the company is usually perceived as a psychically near. Many companies do not follow incremental stage approach but is often reported that they start their international activities immediately from their birth (Anderson *et al.*, 2004). Literature defines them as "born globals" (e.g. Oviatt, McDougall, 1997). Although the "born global" phenomenon is relatively new phenomenon in International Business, it is described in many international literature, e.g. Knight and Cavugsil (1996) define "born globals" as "small technology oriented companies that operate in international markets from the earliest days of establishment". It is possible to find out various classifications of internationalization models in the literature, for example Li, Li and Dalgic (2004) divide theoretical approaches to internationalization processes into 3 main groups: the first is called "Experiential Learnig", where theories of Johanson and Vahlne, or Lam and White or Cavusgil can be involved. The second group can be called "Systematic planning" (Root, 1987; Miller, 1993; Yip, Biscarri, Monti, 2000) and the third group involves theories from e.g. Welch, Boter and Holmquist or Coviello and Munro. This group of theoretical perspectives can be called "Contingency perspective".

In last few years there are many other authors who criticize all of these theoretical models of international process and they try to put together all known approaches and develop some hybrid models of internationalization process (e.g. Li, Li and Dalgic, 2004) which reconciles different theoretical perspectives and bears normative implications for managers. In their opinion this hybrid models can help specially to SMEs for examining the internationalization process, because the process of internationalization of small and medium – sized enterprises is different than the international process of MNEs. SMEs usually have limited resources; have less internationally experience than multinational MNEs and they often have to respond to international market opportunities in a very timely manner. In connection with the internationalization theories the issue of key success factors in the internationalization process of SMEs is often asked question. Many surveys and researches were carried out to sum up the key factors of internationalization process success. And not only identification of the key success factors but also evaluation of the international process is often discussed problem.

The international process is, like all processes in the firm, accompanied by risks. Small and medium sized companies often don't have enough experiences with the internationalization process, as it was mentioned above, therefore they often deal with the problem how to identify the key risk factors of this process. The idea is that knowing the risk factors it is possible to propose to SMEs the way how to reduce or eliminate possible risks in their activities on foreign markets. Risks of the internationalization process can be divided in various ways, e.g. according to Stremtan *et al.* (2009) risks of the international process can be divided into two categories: the risks caused by underestimating the costs and risks arising from uncontrollable international environment. Risks due to underestimating the costs usually result from a bad estimate of the cost to enter the foreign market, an unrealistic assessment of their own competitive advantage in foreign markets, miscalculations of both the physical distances that influence the cost of transportation, communication, etc., but also cultural distance, which is reflected by differences in language, culture, economic development, etc. Risks caused by uncontrollable international environment are unexpected and unpredictable, it can be e.g. the changes in legislation, regulation of import and customs duties, changing course, changes in fiscal policy target countries, political instability the country of destination, or may even be a major political crisis or war in the country, etc. For this reason, most companies selected for their international business in particular countries that appear to be stable. In addition to these two aforementioned categories of risks there may be other risks. According to Stremtan (2009) the other risks can be e.g. limited target market potential, inadequate infrastructure of target market or the risks caused by climatic events. Another criterion of risk dividing into groups is, according to the Babiš, (Babiš, 2007) distributing risks according to subjects, who bears the risks. Risks are then divided into sales risks, arising from the supply of goods or services and shopping risks (connected with the delivery of goods or services). Risk management process can be described in different ways, for example Palojarvi (2009) defines the risk management process as five consecutive stages, the first should identify risks, to further evaluate their consequences and evaluate the likelihood of risks. In these three phases is possible to evaluate the significance of the risk. In the fourth stage it is necessary, according to Palojarvi, clearly define what is the risk aversion and what are the possibilities of its mitigation. The final stage is to calculate the consequences of defined risks. These last two phases of the defined process are important in determining responsibility for the risk accepted by a regulated process.

The factor of the attitudes to risk is involved into the description of the risk management process by Flanagan and Norman (Flanagan, Norman, 1993), who are taking into account the approach of management of the company to risk. This approach has the direct effect on the last stage of the risk management process – responsibility for risk. Although risk management in relation to companies internationalization is widely discussed issue, studies that would focus on risk internationalization process are currently very little available and only few studies are dealing with the risks of the internationalization

process of small and medium enterprises. To find some studies dealing only with risk factors of internationalization process in the textile industry is very difficult. Therefore author of this article decided to focus on the detection of risk factors of the internationalization process of SMEs in the textile industry. To be able to identify the key risk factors of the internationalization of small and medium sized textile companies, there was conducted a survey of 803 Czech textile SMEs in 2011 and 2012. To collect primary data there was chosen the form of written inquiries. The data were collected electronically through the "Umbrela" system, 161 responses were obtained – total return rate was 20.05%. The obtained data were converted to the MS Excel format, which was modified and then exported to the Statistica format, where further processing took place. The obtained data were analyzed; it was possible to identify the characteristics of the common features of exporting textile SMEs – e.g. the size of the company, respective the number of employees, the management proficiency and the length of business operation in the domestic market before entering the international market, the territorial status. It was also possible to identify the dominant form of internationalization and the reasons for entering the foreign market as well as to define the target market of export, the number of countries of export and their nominal destination. Finally it was also identified what are the most important barriers to entry to foreign market and what are the most important strengths of companies products.

RESULTS AND DISCUSSION

The main objective of the research was to identify possible risks and limits of the internationalization process. The first task was to learn the potential risks to prevent the entry of SMEs into the foreign market. The attention was separately paid to barriers (obstacles) to the entry into foreign markets and separately to factors that can cause the failure when company is operating abroad. Interestingly, it was found that according to respondents are not barriers of entry to the foreign market expected factors as e.g. the age of the enterprise, stereotypes, lack of public support or failure of competition in target markets. The main barriers of entry of SMEs into foreign markets are summarized in Tab. I.

The second task, as it was mentioned above, was to learn what factors influence the success/failure of SMEs that have been operating abroad. As the main causes of failure abroad, most often were mentioned incompetent and unreliable management, ineffective form of promotion and lack of contacts in foreign markets. Respondents mentioned also some factors that can affect the success or failure sometimes, these factors are not as important as previous, but it is also necessary to take them out – most often were mentioned miscalculation of consumer preferences and bad choice of pricing strategy. These factors are summarized in Tab. II together with the factors that according to textile SMEs don't affect the success on the foreign market. Surprisingly, among the main factors which, according to SMEs, do not affect success belong expected factors, as e.g. wrong choice of target market, bad "timing" of foreign market entrance as well as low quality of offered product.

To sum it up, based on the survey we can generalize that according to the respondents the most important risks are:
- lack of capital to enter foreign markets,
- lack of information about foreign markets,
- high transport costs.

I: *Possible barriers of internationalization process of SMEs operating in textile industry*

Barriers of entry into foreign market	Factors what can be sometimes considered as barriers of entry into foreign market	Factors that don't limit SMEs in the internationalization process
Lack of capital to enter foreign market	Language barriers	Age of the company
Lack of information about foreign markets	Lack of management experience with internationalization process	Stereotypes
High transport costs	High price of the products	Lack of public support
		Failure of competitors in target markets
		Fear of failure

II: *Factors that affect the success or failure of SMEs on the foreign market*

Main cause of failure abroad	Factors that sometimes may affect the success or failure on foreign market	Factors that don't affect the success on foreign markets
Incompetent and unreliable management	Miscalculation of consumer preferences	Wrong choice of target market
Ineffective form of promotion	Wrong pricing strategy	Bad "timing" of foreign market entrance
Lack of contacts in foreign markets		Low quality of offered product
		Wrong choice of exported product

And other barriers are then language barriers, lack of management experience with internationalization process and high price of the products.

The main causes of failure abroad are:
- incompetent and unreliable management,
- ineffective form of promotion,
- lack of contacts in foreign markets.

Another objective that was achieved by processing the data of the research was to identify the predominant form of internationalization of SMEs as well as to define the target market of export, the number of countries of export and their nominal destination. Finally it was also identified what are the most important barriers to entry to foreign market and what are the most important strengths of companies products. The vast majority (79%) of textile small and middle sized companies operating in the domestic market for more than 11 years. Companies that operate in foreign markets mostly exported to at least 5 countries and they exported most often to Germany (71% of respondents), Slovakia (63%), Austria (36%) and Poland (24%). The most often mentioned reason of internationalization is the lack of the demand and considerable competition on the domestic market and the possibility of extending the portfolio of products. The dominant form of internationalization is the direct export (76%). The most often reported advantage of the direct export is the ability to control implementation of own marketing strategy. The second most often mentioned form of internationalization was the indirect export (19% of responds). The most important barriers to entry to foreign market proved to be financial capabilities of the company (37%), language deficiencies (25%) and the differences in legislation in the other countries (17%). As the most important strengths of textile SMEs in the international process have been listed: the quality of the products (81% respondents), price (60%) and the accuracy and the reliability of supply (55%).

To be able to describe the situation of SMEs from the complex point of view there were also established three hypotheses which can help us to understand the situation of SMEs in the textile industry properly by examining dependence of different characters. For each of these hypotheses it was necessary to formulate a null hypotheses and the alternative hypothesis. The null hypothesis (H_0) indicates the independence of characters and alternative hypothesis (H_1) shows the relation of characters.

First hypothesis: The number of the years the company operates on foreign market affects the number of the foreign markets on which the company operates.

H_0: Operation on more than one foreign market is independent on number of years of firms operating on foreign markets.

H_1: Operation on more than one foreign market depends on number of years of firms operating on foreign markets.

Whether we reject or not the hypothesis depends on the p-value. In case of this hypothesis, p-value = 0.0000 and α = 0.005 (five per cent level of significance) – we reject the null hypothesis because $p < \alpha$ (Tab. III). We can say that operation on more than one foreign market depends on number of years the company operates on the foreign markets.

Second hypothesis: The region where the company operates affects the exploitation level of the state support to internationalization of SMEs.

The calculated is again p-value = 0.0000, and α = 0.005 (five per cent level of significance) – we reject the null hypothesis because $p < \alpha$ (Tab. IV). It can be stated that the region where company operates affects the level of exploitation of the state support.

Third hypothesis: The annual company turnover affects anticipated market entry abroad.

III: *Dependence testing H_1*

Statistics	Chi square	Degree of freedom	p-value
Pearsonś chi square	663.7449	df = 143	p = 0.0000
M-V chi square	99.17371	df = 143	p = 0.99799
Fí	2.589304		
Contingency coefficient	0.9328482		
Cramerś coefficient V	0.7807045		

IV: *Dependence testing H2*

Statistics	Chi square	Degree of freedom	p-value
Pearsonś chi square	94.43850	df = 4	p = 0.0000
M-V chi square	11.56468	df = 4	p = 0.02090
Fí	1.002330		
Contingency coefficient	0.7079290		
Cramerś coefficient V	0.7087542		

V: *Dependence testing H$_3$*

Statistics	Chi square	Degree of freedom	p-value
Pearsonś chi square	28.51421	df = 35	p = 0.77275
M-V chi square	20.15845	df = 35	p = 0.97887
Fí	0.6572925		
Contingency coefficient	0.5492652		
Cramerś coefficient V	0.2939501		

H$_0$: Anticipated market entry abroad is independent on the annual company turnover.

H$_1$: Anticipated market entry abroad depends on the annual company turnover.

The calculated is again p-value = 0.77275 and α = 0.005 (five per cent level of significance) – we do not reject the null hypothesis because p > α (Tab. V). We can say that the annual company turnover affects anticipated market entry abroad.

It follows that the number of foreign markets in which small and medium sized companies operating in the textile industry operates, increases in the case of companies that are active in international trade for longer time. It is also clear that entry into foreign markets is positively influenced by the height of the annual turnover of SMEs. In addition, the survey showed that in the textile industry do not take state aid relating to export business in all regions in the same way; the exploitation level of the support programs and general knowledge of these programs is greatly influenced by the region, where the company's seat is based. In some regions, companies don't have enough information about the potential state aid programs and they often even don't know about their existence and therefore they don't used them.

CONCLUSION

Currently, the textile industry can be, currently, characterized by a significant aggravation of competition particularly in European markets. Therefore, also in the Czech Republic, all companies operating in this area have to face great competitive fight; of course, this problem also applies to SMEs. One of the ways to cope with increased competition is to enter the foreign markets. The internationalization process involves but plenty of risks and barriers. The main aim of the research was to identify the key risk factors of the internationalization process of SMEs operating in the textile industry. There was conducted a survey of 803 Czech textile SMEs in 2011 and 2012. To collect primary data there was chosen the form of written inquiries. The data were collected electronically through the "Umbrela" system, 161 responses were obtained and processed. To describe the situation of SMEs from the complex point of view there were also established three hypotheses which can help us to understand the situation of internationalizing textile SMEs properly by examining dependence of different characters. The main risks internationalization process and the possible causes of failure were assessed: High price of products/bad price strategy, lack of capital to enter the foreign market, lack of information on foreign markets, language barriers, high transport costs, ignorance and inexperience with the internationalization of the management company, incompetent and unreliable management, ineffective forms of promotion, lack of contacts in foreign markets and miscalculation of consumer preferences. Textile companies should realize that if they know the risks, it is easier for them to deal with them. Selecting an appropriate strategy to eliminate the risk always depends on the type of risk. Therefore, it is good for SMEs when notice previously which risks can endanger their internationalization process so they can plan strategies how to avoid the risks or how to reduce them in advance.

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