

DECLARATION

'I hereby declare that have read this thesis and in our research is sufficient in terms of scope and quality. This project is submitted to Universiti Teknikal Malaysia Melaka as a requirement for completion and reward Bachelor Degree of Technopreneurship'

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INTERNATIONALIZATION IMPACT ON THE BUSINESS PERFORMANCE OF
MALAYSIAN SMEs

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A project paper submitted

In fulfilment of the requirements for the Bachelor Degree of
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STUDENT'S DECLARATION

I declare that this project entitled **“Internationalization Impact on the Business Performance of Malaysian SMEs”** is the result of my own research except as cited in the references. The project paper has not been accepted for any degree and is not concurrently submitted in candidature of any other degree.

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DEDICATION

*Specially dedicated to my father, mother, and stepmother, Abang Abdul Rahman bin
Abang Drashid, Dayang Mordiah binti Abang Narudin, and Rosmina binti Ismuni
thank you for your prayers and to the love and care for all this while
To all of my brothers and sisters, thank you for your concerns
For all the encouragement, big thanks to all my dear friends*

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ABSTRACT

Internationalization is usually one of the main objectives in an entrepreneurial journey. Internationalization offers many benefits and one of them is the dependent variable in this research, which is the enhancement of business performance. In this study there are two research objectives and it is (1) to investigate the relationship between internationalization criteria (motivational factors, firm characteristics, industrial issues, political economy, and networking) and business performance, and (2) to determine the most significant criteria that impact on business performance. Questionnaire are used in this research because it provides an efficient way of collecting responses from a large sample prior to quantitative analysis. Respondents are SME managers and SME employees in Melaka. Questionnaire are consisted of scale questions of collecting opinions from the target respondents. SPSS (Statistical Package for Social Sciences) version 20 is used to analyze the data set. Data is collected through questionnaire and keyed into the software and the results generated are used by the researcher. The results of this study shows that internationalization positively affects business performance. There is a high contribution of internationalization criteria toward business performance. In the findings, internationalization criteria contributed 75.7% (R square = . 757) to the business performance of SMEs. This study highlighted the need to enter global market in order to increase business performance. The most significant criteria that impact on business performance is motivational factors with P value of 0.009 which is $P < 0.05$. All the result of the findings proved that there are significant relationships between the variables.

Keywords: Internationalization, Business Performance

ABSTRAK

Pengantarabangsaan biasanya salah satu objektif utama dalam perjalanan keusahawanan. Pengantarabangsaan menawarkan banyak manfaat dan salah satunya adalah pembolehubah bersandar dalam kajian ini, yang merupakan peningkatan prestasi perniagaan. Dalam kajian ini terdapat dua objektif kajian dan ia adalah (1) untuk menyiasat hubungan antara kriteria pengantarabangsaan (faktor-faktor motivasi, ciri-ciri firma, isu-isu industri, ekonomi politik, dan rangkaian) dan prestasi perniagaan, dan (2) untuk menentukan kriteria yang paling penting yang memberi kesan kepada prestasi perniagaan. Soal selidik telah digunakan dalam kajian ini kerana ia menyediakan satu cara yang berkesan untuk mengumpul jawapan daripada sampel yang besar sebelum membuat analisis kuantitatif. Para responden adalah pengurus PKS dan pekerja PKS di Melaka. Soal selidik merupakan soalan skala untuk mengumpul pendapat dari responden sasaran. SPSS (Statistical Package for Social Sciences) versi 20 digunakan untuk menganalisis set data. Data dikumpul melalui soal selidik dan dimasukkan ke dalam perisian dan keputusan yang dihasilkan digunakan oleh pengkaji. Keputusan kajian ini menunjukkan bahawa pengantarabangsaan secara positif memberi kesan kepada prestasi perniagaan. Terdapat sumbangan yang tinggi oleh kriteria pengantarabangsaan ke arah prestasi perniagaan. Dalam penemuan, kriteria pengantarabangsaan menyumbang 75.7% (R persegi = .757) kepada prestasi perniagaan PKS. Kajian ini menekankan keperluan untuk memasuki pasaran global untuk meningkatkan prestasi perniagaan. Kriteria paling penting yang memberi kesan kepada prestasi perniagaan adalah faktor-faktor motivasi dengan nilai P 0.009 yang $P < 0.05$. Semua hasil daripada penemuan membuktikan bahawa terdapat hubungan yang signifikan di antara pembolehubah.

CONTENTS

CHAPTER	TITLE	PAGE
	DECLARATION	li
	DEDICATION	lii
	ACKNOWLEDGEMENT	Iv
	ABSTRACT	V
	ABSTRAK	Vi
	CONTENTS	vii
	LIST OF TABLES	Xi
	LIST FIGURES	xii
	LIST OF ABBREVIATIONS	xiii
	LIST OF APPENDICES	xiv
CHAPTER 1	INTRODUCTION	
	1.1 Background of the Study	1
	1.2 Problem Statement	2
	1.3 Research Question	3
	1.4 Research Objectives	3

CHAPTER 2 LITERATURE REVIEW

2.1	Introduction	4
2.2	Internationalization	4
2.3	Motivational Factors for Internationalization	6
2.4	Firm Characteristics	8
	2.4.1 Important of Resources	9
	2.4.2 Financial	11
	2.4.3 Capabilities	12
2.5	Industrial Issues	15
	2.5.1 Intensity of Competition	15
	2.5.2 Attractive Markets Outside Malaysia	16
	2.5.3 Improved Economy	17
2.6	Political Economy	18
	2.6.1 Economic Factors	19
	2.6.2 Political Forces	21
2.7	Networking	21
2.8	Business Performances	22
	2.8.1 Cash Flow Management	23
	2.8.2 Pro Forma Profit and Loss	24
	2.8.3 Peer Analysis	25
2.9	Relationship Between Internationalization and Business Performance	25
2.10	Theoretical Framework	27
	2.10.1 Dependent Variable	27
	2.10.2 Independent Variable	27

CHAPTER 3 RESEARCH METHODOLOGY

3.1	Research Design	28
3.2	Purpose of Study	28

3.3	Quantitative Research	29
3.4	Study Setting	29
3.5	Research Strategies	29
3.6	Unit of Analysis	29
3.7	Time Horizon	30
3.8	Primary and Secondary Data Sources	30
3.9	Data Collection Method	30
3.10	Measurement of Variables	31
	3.10.1 Operational Definition	31
	3.10.2 Scaling	32
	3.10.3 Statistical Tools	32
	3.10.4 Statistics Associated with Multiple Regression Analysis	32
3.11	Location of Research	33
3.12	Sampling Method	33
3.13	Scientific Cannons	34
3.14	Summary	34

CHAPTER 4 DATA ANALYSIS AND DISCUSSION

4.1	Introduction	35
4.2	Descriptive Statistics on Demographic	36
	4.2.1 Gender	36
	4.2.2 Age	37
	4.2.3 Race	38
	4.2.4 Highest Educational Attainment	38
4.3	Respondent Profile of Variables	39
	4.3.1 Motivational Factors	39
	4.3.2 Firm Characteristics	42
	4.3.3 Industrial Issues	44

4.3.4	Political Economy	46
4.3.5	Networking	48
4.3.6	Business Performance	50
4.4	Scientific Cannons	52
4.4.1	Reliability	52
4.4.2	Validity	53
4.5	Multiple Regression Analysis	54
4.6	Objectives and Hypotheses Test	56
4.7	Summary	59

CHAPTER 5 CONCLUSION AND RECOMMENDATION

5.1	Introduction	60
5.2	Conclusion	60
5.3	Limitation and Recommendation for Future Research	61

REFERENCES	63
-------------------	----

APPENDIX	66
-----------------	----

LIST OF TABLES

TABLE	TITLE	PAGE
4.1	Gender of Respondents	36
4.2	Age of Respondents	37
4.3	Race of Respondents	38
4.4	Highest Educational Attainment of Respondents	38
4.5	Questions for Motivational Factors	39
4.6	Questions for Firm Characteristics	42
4.7	Questions for Industrial Issues	44
4.8	Questions for Political Economy	46
4.9	Questions for Networking	48
4.10	Questions for Business Performance	50
4.11	Reliability Test	52
4.12	Item Statistics	52
4.13	Validity Test	54
4.14	Multiple Regression Analysis	56
4.15	Coefficient	57

LIST OF FIGURES

FIGURES	TITLE	PAGE
2.1	Theoretical Framework	27

LIST OF ABBREVIATIONS**ABBREVIATIONS****MEANS**

MRA

Multiple Regression Analysis

SME

Small Medium Enterprise

LIST OF APPENDICES

APPENDIX	TITLE	PAGE
A	Questionnaire	66

CHAPTER 1

INTRODUCTION

1.1 Background of the Study

International business comprises all commercial transactions (private and governmental, sales, investments, logistics, and transportation) that take position between two or more areas, rural areas and nations beyond their political limits. In political economy, internationalization has been seen as a procedure of increasing participation of enterprises in international markets, although there is no agreed definition of internationalization or international entrepreneurship. Situated in Southeast Asia, Malaysia is one developing nation that is assisting SME to become international players. Malaysia has advantages such as political stability, a first-class physical infrastructure, and a skilled, multicultural and multilingual workforce (The NST, 2006). Nevertheless, the upcoming ASEAN Economic Community (AEC) in 2015 will somehow be a primary reason for Malaysian SMEs to step up their game. This is because AEC will introduce a single marketplace and the production base concept in the ASEAN trade, so showing a very dynamic and competitive environment for firms within the ASEAN area. AEC is no doubt the proof that Asian nations are inflating their status in the worldwide marketplace. This site will then make Malaysian SMEs enter the world-wide market and challenge their capabilities. Internationalisation is a phenomenon researched intensively over the final few decades from a diversity of vantage points, including: organization theory, marketing, strategic management, international management, and small business management (Ruzzier et al., 2006). Business performance relates to the business' independent criteria to measure its overall results, in relation to its own ends.

Geographic expansion is one of the most important parts of firm growth. It is a particularly significant growth strategy for SMEs whose business scope has been geographically confined (Barringer and Greening, 1998). Born global companies have drawn a great deal of attention in the literature on the internationalization of SMEs. This type of company contradicts the theory of the gradual, incremental internationalization of the company. Born global companies are created specifically with the aim of taking over an international opportunity (Rodriguez, 2007).

1.2 Problem Statement

For many years, people have argued about the internationalization of Malaysian SMEs. It is often questioned whether by adopting internationalization criteria SMEs can improve their business operation. Many people believe that by dominating and keeping local market is enough to improve business and yield high profit. This initial perception fails to increase the reputation of local firms in the world marketplace. If we continue to believe that internationalization is as not as important in exploring the local market, our economic growth will never show significant improvements. All the same, in this research I am straining to indicate that SMEs do need to adopt internationalization factors or criteria in society to increase job operation.

1.3 Research Questions

In order to adopt internationalization criteria, SMEs need to interpret the components included in the term itself. Therefore, this research will try to solve these questions:

- i. What are the determinants of SME going international?
- ii. If the company wishes to go international, what is the effect on the company's performance?

1.4 Research Objectives

In this research, the objectives are:

- i. To identify the relationship between motivational factors to business performance when company decides to enter international market.
- ii. To analyze the relationship between firm characteristics to business performance when company decides to enter international market.
- iii. To investigate the relationship between industrial issues to business performance when company decides to enter international market.
- iv. To study the relationship between political economy to business performance when company decides to enter international market.
- v. To determine the relationship between networking to business performance when company decides to enter international market.
- vi. To determine the most significant criteria that impact the business performance.

CHAPTER 2

LITERATURE REVIEW

2.1 Introduction

The theory used in this research is derived from Senik, Zizah Che, et al. "Influential factors for SME internationalization: Evidence from Malaysia.". Influential Factors Twenty-four key topics were identified as reasons Malaysian SME internationalize and these can be categorised into five different components or aspects. The first factors relate to the reasons or motives for internationalizing; the second relates to firm characteristics, such as the firm itself and the top managers; the third relates to Industrial issues; the fourth relates to external influences (political economy) and the fifth relates to factors of networking. (Che Senik et al., 2010).

2.2 Internationalization

In economics, internationalization has been viewed as a process of increasing involvement of enterprises in international markets. (Susman, 2007). The literature defines internationalization as a process through which a firm increases its level of involvement in foreign markets over time (Welch and Luostarinen 1988). The Uppsala model has two fundamental premises. First, the firms became interested in overseas markets to continue growth because the home market had become unprofitable. They usually put down new markets through exports and only years later put up manufacturing operations in the target country (Johanson and Vahlne, 1990). In previous international business literature, mature multinational

corporations played a command role, whereas SMEs (and especially their internationalization) have only recently attracted broader interest (Miesenbock, 1988). Internationalization is a synonym for the geographical expansion of economic activities over a national country's border. The term started to be used when the phenomenon gradually replaced imperialism as the dominant organizing principle framing cross-border interaction between market economies starting in the 1920s. The economic internationalization process accelerated in the post-second-world-war era and appeared unrivalled until the early 1970s, when a new phenomenon of globalization began to emerge (Gjellerup, 2000). Internationalization also means a changing nation. The development of the firm provides a background to internationalization and to some degree the concepts of internationalization and development are intertwined (Buckley and Ghauri, 1993). In a network context, Johanson and Mattsson (1993) described internationalization as a "cumulative process, in which relationships are continually made, sustained, built up, broken and dissolved in order to accomplish the aims of the firm". In their definition, Lehtinen and Penttinen (1999) attempt to summarize the central features of the internationalization process based on the Nordic research findings. Their definition also covers two concepts occasionally applied in the context of internationalization, namely international orientation and international commitment. International orientation refers to a firm's general attitude towards internationalization, thus standing for an evaluative dimension. Reid (1981) defined it as a touchstone of the perceived conflict between foreign markets and the home market space along economic, ethnic, political, and market-strategic dimensions. International commitment is essentially associated with the demands of the operation modes chosen and the size of international concern. The latter tries to position firms somewhere between the extremes of no involvement (domestic firm) and full allegiance (a firm with a realized foreign direct investment). Ahokangas (1998) proposed a definition of SME internationalization in terms of resources inside the natural setting (e.g. within a firm's network). An internationalizing firm can be viewed as mobilizing unique and interdependent resource stocks that enable and contribute to the firm's internationalization activities within its natural setting. This definition thus implies that internationalization is "the process of mobilizing, accumulating, and developing resource stocks for international activities", irrespective of the factual substance of the international activities themselves.

2.3 Motivational Factors for Internationalization.

The factors influencing why SME go into international markets can be considered through the motivational factors for internationalization. They can be due to proactive and reactive reasons (Czinkota, Johanson, And Ronkainen, 2002). These include energy and pull factors that include positive situational and business opportunities (Littunen and Tohmo, 2003). In some instances, the pushing or the pulling factors have more influence, whereas in others it is the interaction between pushing-pulling factors (Etemad, 2004). Internal and external change agents can also drive the internationalization (Crick And Chaudhry, 1997). Understanding why SME operate in the foreign markets will facilitate the internationalization process preparation required by SME; therefore, it is important for both researchers and managers understand the factors affecting SMEs internationalization. These motives can be classified into six sub- categories: there are domestic conditions, market issues, resource seeking, globalization, the need to follow a supplier, and for survival. (Che Senik et al., 2010).

Dunning (1993) introduced a model of internationalization motives, including four different categories of motives. These categories are market seeking, resource seeking, efficiency seeking and strategic resource seeking motives. We then tallied a fifth category: network seeking motives for recognizing networks as a substantial part of internationalization corresponding to recent research. Proactive motivations represent stimuli to attempt strategic change. Reactive motivations influence firms that are reactive to environmental changes and adjust to them by changing their actions over time. In other words, proactive firms go international because they want to, while reactive ones go international because they have to. (Czinkota, 2004).

The motivations can be either proactive or reactive. Proactive motivations are initiated by the firm's management and can consist of a perceived profit advantage,

technical advantage, product advantage, exclusive market information, or managerial urge. Reactive motivations are the responses of management to environmental changes and pressures. Typical are competitive pressures, overproduction, declining domestic sales, or redundant capacity. Firms that are primarily stimulated by proactive motivations are more likely to enter international markets aggressively and successfully. (Czinkota, 2004).

Dunning (2000) explains how market and resource seeking motives have been the two most recognized categories of motives before. These two categories still correspond to most first time internationalizations by firms. Overall, efficiency seeking and strategic asset seeking motives increase in significance and are more common as motives for companies already engaged in multinational activity. He also shows that closer relations with customers and durable relations with suppliers were important motives. Furthermore, he suggests that internationalization was more driven by opportunities rather than threats.

Karagozoglu and Lindell (1998) show that opportunities in foreign markets and inquiries from foreign buyers were the top two motives for internationalization. Insufficient domestic sales compared to R&D costs were also a significant motive. Francis and Collins-Dodd (2000) claim that for high-tech SMEs relationships and sales contacts in foreign markets are the best means for improving sales abroad. They also stress the importance of strategic alliance partners in order to improve foreign market performance. In other words, networking is vital.

Freeman et al. (2006) identify several variables that increase the rate of internationalization of SMEs. Such variables are a small domestic market, unique knowledge or technology, and different forms of relationships and alliances. The four single motives that received the highest scores are found in the market seeking and network seeking. Entering new markets and a limited market in the home country are perceived by the companies as two primary drivers when internationalizing. Instead of adapting products, make a first mover's advantage, and encouragements by host countries, etc. it is new markets that the companies focus on. For younger and smaller companies, gaining access to markets and generating revenues may be crucial when funds are scarce. One means of doing so is to look at foreign markets,

especially when the home market brings small chances for success. (Hansson and Hedin, 2007).

A domestic market is a financial market within a given country for products and services. Also known as an internal market, it has a more limited scope than international markets, usually with reduced competition. Some companies choose to focus on doing business domestically, while others may expand to external markets in order to capture more market sectors and access additional trading opportunities. Most nations keep statistics on their domestic markets for the use of tracking economic health. (McMahon, 2013).

2.4 Firm Characteristics

Within the second factor which is the firm factors, two important drivers were identified. The first is the firm itself, for example, the firm's human, financial and other resources, products, capabilities and reputation. The second is the key features of top managers. The characteristics of the firm items can be grouped into four categories; the importance of resources, and products; capability and reputation. The top managers' characteristics, three categories were identified; predominant characteristics that are interpersonal skill and ability, attitude and the manager's background. These findings suggest strong agreement among the experts that top management characteristics, such as interpersonal skills, attitude and background have an important influence on the firm's choice to become international. (Che Senik et al., 2010).

Apart from networking, to be capable to successfully internationalize, the experts also emphasized the importance of firms having strengths in terms of unique resources, sound finances, skilled and experienced employees, R&D capability, and ICT. This matches previous study that identified firm-specific ingredient as being resources such as unique assets, R&D spending, network and a beneficial reputation, advances in ICT (Barney, 1991 and 2001; Madsen, Ramussen and Servais, 1999). In summation, the experts also mentioned that SME owners-top managers should

receive international exposure. This finding supports Etemad (1999) who found in his study that in order to internationalize, the key actors must have international exposure, an international global vision, foreign education and experience. This subject area also found that to go international, it must be wanted and triggered by an SME entrepreneur which supports Andersson's (2000) findings. This contributes to resource-based view which emphasises the importance of internal capability such as a firm's unique and internally-owned resources as significant drivers in achieving competitive advantage (Alvarez and Busenitz, 2001; Barney, 1991; 2001) which also bears out the POM model on the 'organizational capacity' dimension (Welch and Luostarinen, 1988).

2.4.1 Importance of Resources

The resource advantage theory provides a perspective on the importance of the resources to potentially reach a sustained competitive advantage. Hunt (1997b, 1997c, 2000b), and Hunt and Morgan (1995, 1996) advance an evolutionary theory of competition coined as "resource-advantage" (herein R-A) in opposition to the well-known neoclassical assumptions of pure competition (see HUNT; MORGAN, 1995, p. 2; HUNT, 2000). In the R-A, competition is disequilibrium- provoking, innovation and organizational learning are endogenous, the market does not convey perfect and free information, and institutions influence performance (HUNT, 1997b).

The firm's aim is to obtain superior financial performance, broken that the resources are heterogeneous across firms and imperfectly mobile, and the behaviours are self-interest seeking to constrain (HUNT, 1997A, B, C, 2000A, B; HUNT; MORGAN, 1995, 1996; BARNEY, 1986, 1991) - that is, the behaviours are socially bounded. The heterogeneous resources and demands across and within industries result in diversity of firms' size, performance and scopes (HUNT, 1997b, 2000b). The R-A theory argues that the firms' resources are the primary determinant of competitive advantage and firm profitability (WERNERFELT, 1984; BARNEY, 1986, 1991; MAHONEY; PANDIAN, 1992).