

Changing role of knowledge in internationalization (analysis of Uppsala model)

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Abstract: The authors analyze Uppsala model of internationalization and the role of knowledge in internationalization process of companies. They conclude that globalization, ICT technologies, Internet, company networks, nature of the products and services changed dramatically the framework for internationalization, however some basic rules and principles in this domain in knowledge area have stay unchanged.

Keywords: Internationalization, Uppsala model, knowledge.

1 Introduction

Named after the University of Uppsala and developed by Johanson and Vahlne in 1977, this model is based on empirical observations of Swedish manufacturing firms. It describes firm-level internationalization as a process of incremental adjustments to changing environments, driven by experiential knowledge and learning (Johanson & Vahlne, 1977).

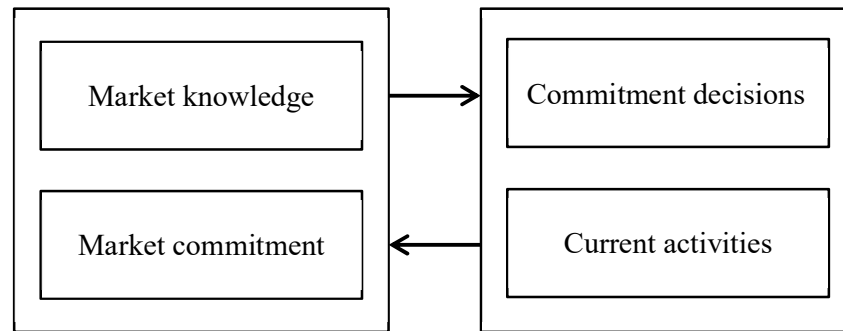
The foundation of this dynamic model dates back to 1966, when Swedish economist S. Carlson analyzed a firm's foreign decision process. The core concept of his pioneering research concludes that lack of knowledge in doing business in a foreign market represents a significant obstacle for firms which have the intention to internationalize (Carlson, 1966). Due to the recent changes in business environments and theoretical advances made in the process of firm-level internationalization, the Uppsala model was revised in 2009 offering new insights into the internationalization process. (Johanson & Vahlne, 2009).

2 Uppsala model I.

As observed in Swedish and some US manufacturing firms, the Uppsala model introduces a new dimension of internationalization - the pattern of the *establishment chain*. Johanson and Vahlne believe that internationalization should occur in multiple stages in order to successfully increase firms' commitments in foreign markets (Johanson & Wiedersheim-Paul, 1975). In most cases, firms start by exporting to foreign markets via independent representatives, develop sales subsidiaries later and eventually, begin production abroad (Johanson & Vahlne, 1977).

The model considers two aspects to explain the internationalization process of firms: state and change aspects (Johanson & Vahlne, 1977). While state aspects are represented by the market knowledge and market commitment of resources to foreign markets, change aspects are focused on the decisions to commit resources and the performance of business activities (Johanson & Vahlne, 1977). The Uppsala model mechanism is described in Figure 1.

Fig. 1 Uppsala model – Original



Source: Johanson & Vahlne, 1977

The fundamental focus is paid to the aspect of knowledge and learning, and the explanation how firms learn to gain knowledge throughout their international operations. According to Johanson & Vahlne (1977), the most efficient knowledge lies in the firm's own operations. Unlike the objective knowledge, which can be taught, the model believes in experiential knowledge, which cannot be easily acquired, and thus relies on the lifelong experiences of individuals. It is assumed that this knowledge and experience not only helps to analyze problems, influence the decisions to commit resources, and generate business opportunities, but also evaluates the market environment prior to performing business activities abroad. With this respect, the lack of experiential knowledge at specific stages of the internationalization process in a new market explains why firms pursue a gradual, step by step, process of internationalization (Johanson & Vahlne, 1977).

As seen, in the original model (Johanson & Vahlne, 1977) the knowledge is particularly important in the internationalisation process. To sum up, this knowledge has following characteristics (Pedersen, Pedersen & Sharma, 2000):

- The knowledge of crucial importance to firms' internationalisation process is market-specific, i.e. the knowledge is about how to do business in the targeted foreign country. Considering that all foreign markets differ from each other, this kind of knowledge acquired in one foreign market can be used only in a limited extent in another one. (On the other hand, we have to admit that the experience from one market definitely helps while penetrating another ones – see personal experience).
- The knowledge is experience-based. It originates from the current foreign business activities, and as such the knowledge acquisition is a learning-by-doing process. (The longer and broader the experience is, the better is entry situation while entering new markets).
- The knowledge is embedded in individuals, i.e. the market-specific knowledge is acquired through personal experience. (These individuals could be in-company resources, however the company can also hire new individuals with a lot of international experience from their former employer.)
- The individually embedded experiential knowledge does not mean that it is automatically and easily disseminated throughout the organisation. The transfer of essential knowledge from one employee to another, and from one organisational unit to another, may be very difficult.

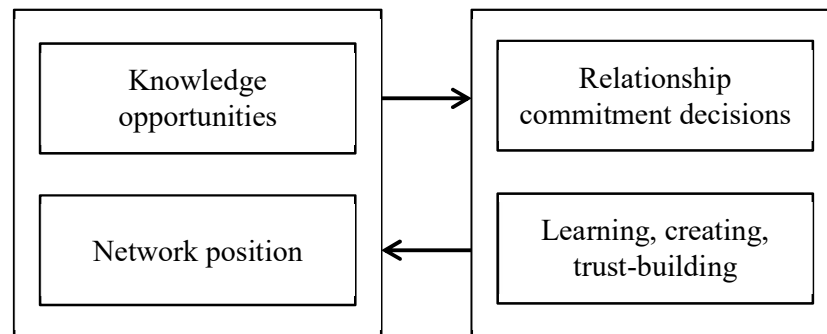
- The international involvement, including commitment of irrevocable resources to foreign markets, increases proportionately with knowledge acquisition (and vice versa).

Besides the aspect of knowledge and learning, special attention is paid to the aspect of psychic distance as well. Typically, the stronger the language, cultural or environmental differences are, the greater the psychic distance is. Johanson & Vahlne (1977) believe that firms choose psychically close markets for expanding first in order to reduce possible risks and market uncertainty.

3 Uppsala model II

Due to the recent changes in business environments and theoretical advances made in the process of firm-level internationalization, the Uppsala model was revised in 2009 offering new insights into the internationalization process. Firstly, it claims that firms operate in markets defined by networks of relationships, rather than being parts of independent webs of suppliers and customers (Johanson & Vahlne, 2009). With this respect, “insidership” in close networks is necessary for firm’s successful internationalization, while “outsidership” from such networks represents a significant obstacle in the process. Outsidership from a particular network can additionally cause a greater uncertainty than the psychic distance alone (Cassia & Baronchelli, 2008). Secondly, such networks of relationships foster knowledge creation, trust and commitment building for firms. Johanson & Vahlne (2009) therefore, emphasize the importance of networks as the key influencing factor for the firm-level internationalization.

Fig. 2 Uppsala model – Revised



Source : Johanson & Vahlne, 2009

The revised model, as presented in Figure 2, puts more emphasis on opportunities. They are assumed to be the most important element linked to knowledge that drives the process of internationalization (Johanson & Vahlne, 2009). The authors also believe that the business network concept along with great opportunities can explain why some firms deviate from the originally proposed establishment chain and why some firms, mainly small new ventures, internationalize very rapidly (Johanson & Vahlne, 2009).

Even though the model is still considered up-to-date and used as theoretical base for related research, it is still criticized for the following reasons: Firstly, the conclusions are based on observations of only four Swedish manufacturing firms and therefore, do not have the sufficient explanatory power. Secondly, the pre-described internationalization process does not fully explain the rapid internationalization of some firms, or why some firms result in skipping the

intermediate stages of the establishment chain (Pignatti, 2009). Lastly, the psychic distance proposed in the model does not take legal and competitive environments into consideration and thus, is not the only significant factor that influences firm's selection of foreign markets. Size, value and opportunities of the potential markets are also being considered (Pignatti, 2009).

As for the knowledge opportunities, the model could be enlarged and deepened by introducing several layers that influence it:

- **ICT technologies** that help to transform tacit knowledge into explicit knowledge. However this may be easier for big companies and very difficult for SMEs. Explicit knowledge cannot replace personal knowledge and managerial capabilities of experienced managers.
- **Internet** – Internet dramatically lowers cost of acquiring new knowledge, marketing, logistics, communication etc. However the filtering of all the information and the choice of the relevant knowledge related to the internationalization could be a problem. What is however undeniable, is the access of the companies, including SMEs to the new distribution channels via Internet what lowers the necessity of that type of information that is related to the direct form of internationalization, especially creation of subsidiaries abroad.
- **Globalization** – Due to lowering obstacles for internationalization, the companies internationalise much faster than in the past. There is a widespread belief that the companies in global industries internationalize much faster than the companies in classical industries (see for example Petersen and Pedersen (1999)). It is still a remaining question whether the role of knowledge has changed in relation to the globalisation effect. Faster internationalisation of firms may be explained by increased competitive pressure as a result of the globalisation. But it may also mean that many companies are pushed to internationalize without the relevant knowledge.

4 Uppsala model and its implications on CEE countries

The situations of the CEE firms have changed significantly after the fall of communism and the transition to market economy at the beginning of the 1990's. Before 1989, the firms had very limited knowledge and exporting was possible only through very few foreign-trade institutions. If some of the biggest local players had access to the foreign markets, they usually focused on the Eastern Block, hence the COMECON countries. However, the beginning of the 90's meant several unexpected challenges for local CEE firms. Lack of foreign-market knowledge, know-how in operations and inadequate foreign language capabilities forced local firms to concentrate their foreign activities on neighboring countries, primarily. The political history of the CEE region supports the idea of psychic distance as well. The division of Czechoslovakia and Yugoslavia for example, initiated a big trade concentration among the succession states (Ferencikova & Schuh, 2012). After all, close historical ties, cultural, language and economic similarities of the countries must not be neglected. Aside from the aspect of psychic distance, the pattern of the establishment chain of the Uppsala model was typically used by the local firms; mostly by the classical industries, such as agriculture, which entered neighboring markets first, established manufacturing facilities later and eventually, started manufacturing products and services abroad (Ferencikova & Schuh, 2012).

Multiple studies on firm-level internationalization with the focus on the CEE region confirm the patterns of the *establishment chain* and *psychic distance* introduced in the Uppsala model:

for example the study of Jaklič and Svetličič (2003) examines recent growth of multinational firms emerging from Czech Republic, Estonia, Hungary, Poland and Slovenia. The main findings of this research show that firms internationalize primarily to neighboring countries (Jaklič & Svetličič, 2003). Additionally, the study underlines the significance of both, firms' past experience and ambitious plans, as they experienced positive effects from the outward foreign direct investment. Another paper: the study of Mockaitis, Vaiginiene, & Giedraitis (2006) examines the internationalization patterns of Lithuanian manufacturing firms. The main objective is to examine the foreign market entry decisions of firms through the analysis of their size, age, knowledge base, risk aversion and commitment toward the internationalization process (Mockaitis, Vaiginiene, & Giedraitis, 2006). The study states that the degree of internationalization is positively related to a firm's age and size (Mockaitis, Vaiginiene, & Giedraitis, 2006). According to the authors, young firms usually suffer from insufficient experience, network connections and knowledge, which relates to the Uppsala model and the incremental process of internationalization, gradual knowledge and experience acquisition (Johanson & Vahlne, 1977). The study of Ferencikova and Hluskova on internationalization of ICT companies from Slovakia concludes that its internationalization is the result of specific resources (specific knowledge), network relationships and globalization trends that allow them to internationalize rapidly via internet. (Ferencikova & Hluskova, 2015).

5 Future avenues of the research

The authors believe that globalization, ICT development and Internet change the ways of acquiring, and implementing knowledge in internationalization process. However, they believe that the personal factor remains the most important in this process. His role may decrease in bigger companies given the potential of the change of the tacit knowledge to explicit one in them, however it has remained unchanged in smaller companies. These are the assumptions that require further research in this area. The authors believe that the case study method would be the best method for the relevant study in the Slovak conditions.

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