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# Barriers to Enter into Foreign Markets: Evidence from SMEs in an Emerging Economy<sup>1</sup>

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## **Abstract**

**Purpose** –Foreign market entry is considered as a key strategy to grow and survive over longer period of time for the Small and Medium Enterprises (SMEs). The decision to enter in a foreign market is not a straight forward story. Considering the resource limitation, SMEs need to analyse the key barriers to enter in foreign markets very carefully. The purpose of this paper is to identify these barriers for the SMEs in an emerging economy.

**Design/methodology/approach** – This study has used primary data collected through the questionnaires from 212 Bangladeshi SMEs. A mixed method data analysis technique is used to analyse the firms both from micro and macro levels. Following the running example based case study approach, this study has developed and validated partial least square based structural model (PLS-SEM) to assess the key barriers to enter in foreign markets.

**Findings** –This study has identified the key socio economic barriers faced by the SMEs in an emerging economy to enter into the foreign markets. It has successfully framed the socio economic barriers to enter in foreign markets for Bangladeshi SMEs as a second order hierarchical model.

**Originality/value-** It is often believed that the foreign market entry is more affected by the social barriers as explained by the existing theories including Uppsala model. Using institutional view, this study revealed that the international market expansions of SMEs in developing countries are more sensitive to the economic barriers.

**Keywords-** Market entry, SMEs, Emerging economy, Internationalisation, Institutional theory

**Paper type-** Research paper

## **1. Introduction:**

For decades, entering foreign markets has been a topic of extensive debate, yet researchers concur that more needs to be understood (Hennart and Slangen, 2014; Arslan et al., 2015). Multinational companies (MNCs) attracted the most interest leaving SME entry mode research relatively underexplored (Brouthers and Hennart, 2007). Selecting an appropriate method for entry is therefore crucial, and inappropriate decision-making by SMEs could have serious financial and survival implications (Gatington and Anderson, 1988; Root, 1994). SMEs have a number of foreign entry mode options and exporting has been identified as one of the most important among those (Lu and Beamish, 2001). Exporting (both direct and indirect) has been identified as the most dominant, and popular due to the lower cost commitment and lower degree of risk involved in it (Katsikeas et al., 2000; Leonidou et al., 2002; Majocchi et al., 2005; Wheeler et al., 2008 and Leonidou et al., 2010).

However, despite the need for SMEs to internationalise, little is known about the barriers that hinder or slow down the process (see Laufs and Schwens, 2014). This, despite an increasing number of international SMEs failing to thrive, is regardless of the size of the economy (Hulbert et al., 2013). The failure rates are extremely high for emerging countries as mentioned by Khalique et al. (2011), Ahmed and Seet (2009) and Fatoki and Asah (2011). Based on the gap in existing research, this paper intends to explore the barriers to SME internationalisation from the context of an emerging country.

To explore the barriers of SME internationalisation, this paper has used an institutional approach as suggested by North (1990). Formal and informal institutions play vital roles as they affect transaction and coordination costs of firms engaged in internationalisation (Arslan

and Larimo, 2011). Institutional factors affect export propensity and performance, and therefore omitting institutional dynamics in exploring drivers and performance could seriously limit our understanding (Gao et al. 2010). Hessels and Parker (2013) maintained that due to their size, SMEs are vulnerable to institutional barriers, and emphasized careful consideration of such obstacles to maintaining growth. Referring to possible barriers, Laufs and Scshwens (2014) pointed to the need for additional research in the area of home country institutional factors. This paper examines home country factors that may act as barriers for SME internationalisation.

The determinants of SME internationalisation have been previously examined in international marketing literature (D'Angelo et al., 2013; Morgan et al., 2004). However, findings may not be applicable to developing economies as a majority of studies are focussed on North American or European SME sectors (Bruton et al., 2008). Socio-economic aspects of developed countries differ from developing countries (Gao et al., 2010; Peng et al., 2008), so generalising could be misleading (Milanzi, 2012).

This study collected data from SMEs operating in Bangladesh. Bangladesh was chosen due to a heavy dependence on SMEs as a major source of economic growth. In addition it had the highest number of SMEs in South Asia, including India and Pakistan (Stein et al., 2010). Ahmed et al. (2011) reported that 82% of the Bangladeshi labour force was working within SME organisations across the country, and the fourth-largest ready-made garment exporter (BBS, 2014), with potential of becoming one of the top exporters of apparel products (Ahmed et al., 2011). However, due to the lack of appropriate empirical research, potential entrepreneurs from Bangladesh could have incorrect or insufficient information about the

challenges. Therefore, identification of the international market entry barriers for SMEs is certainly timely. Moreover, the difficulties identified in previous studies might be inconsistent due to weak methodologies (Arteaga-Ortiz and Fernández-Ortiz, 2010). In this study, and building on from previous literature, a model on the factors that hinder SME international expansion has been developed and validated.

The organisation of this paper is as follows: The next section (section two) focuses on the literature and theoretical background with the development of hypotheses based on a proposed conceptual model. Section three describes the research method and data, and explains the method of data analysis. Two selected running examples have also been presented in this section to capture the macro aspect of the socio-economic barriers. Section four describes the empirical findings. Finally, in section five, a summary has been provided.

## **2. Literature Review and Hypothesis Development:**

In response to a criticism from Shaver (2013) regarding voluminous research on foreign market entry mode, Hennart and Slangen (2014) concluded that research on such strategies are still inconclusive, and a need for further research. Pan and Tse (2000) pointed out that there are a number of entry mode choices available to firms to enter foreign markets. Prominent among those are export (both direct and indirect), contractual agreements, such a licensing and franchising, joint ventures, acquisitions and wholly owned greenfield investment. The choice of entry is an important strategic decision with substantial bearing on a firm's commitment to resources, risks faced from the host market (Hill et al., 1990), and level of control (Anderson and Gatington, 1986). Moreover, Lu and Beamish (2001)

mentioned that by changing the entry mode after initial entry could have a serious negative impact on performance. Considering the critical importance of entry mode on internationalisation strategy, a number of authors have come forward to examine various entry strategies - like joint venture, greenfield and acquisition. For example, Georgopoulos and Preusse (2009), Slangen and Hennart (2008) compared the greenfield and acquisition entry from the context of MNCs from developed countries. Demirbag et al. (2008) and Arslan and Larimo (2011) explored the suitability of greenfield and acquisition from the context of emerging markets. Junni et al. (2015) studied the role of strategic agility in acquisition. Almor et al. (2014) examined different aspects of maturing born global firms. Zhang et al. (2015) observed the effect of leadership style on talent management during M&A. Uddin and Boateng (2011) examined the macroeconomic determinants of UK cross-border mergers and acquisitions. Slangen and Hennart (2007) provided a detailed literature review on entry mode choice between greenfield and acquisitions. Recently, Slangen and Dikova (2014) examined greenfield and acquisitions from the context of marketing adaption by internationalising firms.

It is notable from these studies that the main focus of those entry mode studies is on MNCs around the world. The conclusions are not generalizable for SMEs as they are different to MNCs with respect to resource commitment (Erramilli and D'Souza, 1995), sensitivity to external challenges (Lu 2002), and ownership (Kotey, 2005). Therefore, authors like Laufs and Schwens (2014) concluded there is a huge potential for further research on SME entry mode.

Lu and Beamish (2001) stated that entering into foreign markets is one of the most important decisions for any SME in order to increase customer base and maintain organisational growth. Firms enter foreign markets in a number of ways including exporting, licensing, joint venture, acquisitions or greenfield investment (Pan and Tse, 2000). However, exports have been identified as the most dominant and popular entry mode choice for SMEs because of the lower cost commitment and degree of risk involved (Katsikeas et al., 2000; Leonidou et al., 2002; Wheeler et al., 2008). Similarly, Leonidou et al. (2010) and Majocchi et al. (2005) pointed out that SMEs tended to move into foreign markets mainly as exporters because it was the cheapest, simplest and quickest way to achieve internationalization. D'Angelo et al. (2013) stated that export performance, along with its main determinants, is one of the most intensively researched topics in international marketing. Morgan et al. (2004) and Zou et al. (2003) further support this. However, despite the critical role of export for SMEs to internationalise, little is known about the barriers that hinder or slow the process (see Laufs and Schwens, 2014).

A number of scholars have attempted to explore the prominent export barriers including Cavusgil and Nevin (1981), Cavusgil (1984), Gripsrud (1990), Cavusgil and Zou (1994), Cavusgil and Yeoh (1994) and Tesfom and Lutz (2006). However, Uner et al. (2013) pointed out that despite the plethora of studies, little consensus exists due to differences in method and content. They also pointed out, rightly, about the dearth of theoretical framework in explaining export barriers. Although there is scant evidence, suggested by Laufs and Schwens (2014), institutional assessment in expounding export barriers is rare. Exploring export barriers from the context of institutional setting is very important since there is a defined difference between developed and emerging countries (Peng et al., 2008).



Due to differences in institutional settings, export barriers for developed countries could be very different from export barriers in emerging countries. Building on institutional theory developed by North (1990), Scott (1995) and Peng et al. (2008) it was stated that strategic choices, such as export decision, is not just driven by industry conditions and firm capabilities, but also by formal and informal institutional constraints faced by the managers. Formal and informal institutions play a vital role in internationalisation decisions as they affect transaction and coordination costs that engage in internationalisation (Arslan and Larimo, 2011). Institutional factors affect export propensity and performance, and therefore omitting such factors could seriously limit our understanding about exporting (Gao et al., 2010). Hessels and Parker (2013) maintained that due to smaller size, SMEs are vulnerable to institutional barriers, and emphasized careful considerations of such obstacles to maintain expected growth. Laufs and Schwens (2014) pointed out that foreign market entry mode is likely to be dependent on home country institutional factors. However, linking home country factors with the entry mode decision of SMEs is very rare in cases of emerging markets. For example, in a recent comprehensive survey, Laufs and Schwens (2014) stated that most studies in this area focus on developed markets, and there is a scarcity of detailed analysis for the impact of home country factors on SME entry mode decisions.

## **2.1 Selected Home Country Barriers to Enter into Foreign Markets:**

### ***2.1.1 Economic Barriers***

North (1990) defined 'institution' as humanly devised constraints that structure political, economic and social interactions. There are formal institutions that include government system, legal procedures etc. and informal institutions that include social and cultural

components. Political and legal institutional constraints are part of formal institutions and work as economic barriers for SME internationalisation. Politics is the combination of efforts by government, and other bodies and groups, to give future direction to the country - considering the value and interest that people hold - in addition to maintaining governmental and state affairs (Daunton, 2011). Generally, government develops the rules and procedures for day-to-day life through a political and legal framework. Business is considered as the integral part of this daily life, therefore, cannot be conducted against the tide of the political and legal system (Sethi et al., 2012).

How might a political and legal framework influence the business environment? Firstly, the political and legal system of each country directly influences the business environment by amending (or introducing) policies, regulations and laws. Secondly, government determines a fiscal and monetary policy that directly influences the way of doing business. Finally, political stability has a huge and contributing impact on the way business is conducted. Political forces might assist the internationalisation of firms, such as, removing international trade barricades and embargoes, or by setting up export processing zones (EPZ) where the firms can produce and trade under favourable condition. Similarly, certain political and legal factors might become barriers to entering foreign markets, such as, political instability, legal procedural barriers, corruptions and inadequate legal supports (Bhatti and Awais, 2012). Therefore, the decision to go for international trade expansion should only be taken after understanding the nature of political and legal environment of the target country.

### ***2.1.2 Social Barriers***

The social and cultural environment, which form part of informal institutional dimensions as suggested by North (1990), include the attitudes, tastes, beliefs, behaviours, lifestyle and relationships among the population. Business activities objectively meet the demands of the people, whereas, the demands of the people are based on social needs, functional requirements and cultural aspects. In cases of international business activities, the role of the social and cultural environment is more predominant. By crossing the national boundary through the internationalisation process, firms involve themselves with a different culture and society (Gomes et al., 2011, p.238). Although most theories raised these cultural aspects as dominant factor for internationalisation (Ellis, 2011), the Uppsala model shed light on the term ‘psychic distance’. According to Johanson and Vahlne (1977), psychic distance is “the sum of factors preventing the flow of information from and to the market.” Furthermore, they have given such examples as, language, education, culture, political factors, business practices and industrial development as related distances. For Uppsala’s model of internationalisation, culture is the part of psychic distance. Previous studies collectively identify social and cultural factors as barriers of internationalisation including socio-cultural traits, verbal and nonverbal language differences, habits, and attitudinal components of foreign customers and clients (OECD, 2006). Similarly, Barkema and Vermeulen (1997) reported cultural distance as one of the most influential barriers of internationalisation. Rothaermel et al. (2006) similarly identified a strong connection between cultural dimension and internationalisation.

## **2.2 Conceptual Model and Hypotheses Development**

Based on the extant literature on socio-economic barriers to entering foreign markets, this paper proposes the following research model (see Figure 1).

Please insert figure 1 here

In the figure 1, there are 7 hypotheses based on the factors found in literature of the internationalisation of SMEs. Socio-economic barriers for Bangladeshi SMEs are classified into 2 major categories: Social and Economic. Out of 7 hypotheses, 3 are related to social and 4 to economic barriers.

Language is the medium of communication between two or more individuals by using arbitrary signals (speech, script, signs etc.). The failure to communicate, and interpretation, would hinder overseas business prospects. By crossing national boundaries, SMEs have to be active in an alien economic, political and cultural climate (OECD, 2006; Kiss et al., 2012). In addition to language, a common socio-cultural barrier faced by SMEs is the varying social approaches (Barkema and Vermeulen, 1997; Child and Hsieh, 2014). There is no denying social approaches differ from one country to the next. Although it is generally agreed that different social attitudes have impacts on business, the nature of impact (positive or negative) is ambiguous. While past studies suggest negative impacts of different socio-cultural approaches, others (Hsu et al., 2013; Krishnan et al., 1997; Morosini et al., 1998) have claimed the diversity may be a source of value creation. Some research pays little or no attention to different social approaches as the key barriers of internationalisation of SMEs (Okpara and Kabongo, 2010). Considering the important link between language and social approach with social (and cultural) barriers of internationalisation, this study proposes that these components act as functions of social barriers to entering foreign markets in the context of developing countries' SMEs. On the basis of the above observations, the following hypotheses are proposed:

H1: Language difference between home and host country would work as a barrier for SMEs to enter into foreign market.

H2: Difference in social approaches between home and host country would work as a barrier for SMEs to enter into foreign market.

Research and Development (R&D) is the initiative of discovering a new understanding about products, services or process. While the ability to increase technological development is considered as an important dimension of competitive advantages (Junni et al., 2013), R&D is viewed as the key source of such ability (Yam et al., 2011). SMEs from developing countries (such as Bangladesh) may find it difficult to face the global challenges due to a lack of R&D spending and facilities. With limited R&D resources, organizations then find it difficult to compete internationally (Tseng et al., 2009). In contrast, other studies overlook deficient R&D facilities as the key barriers of SME internationalisation (Al-Hyari et al., 2012; Gunaratne, 2009; Okpara and Kabongo, 2010).

Considering the important link of R&D facilities with social (and cultural) barriers of internationalisation, then this study proposes a lack of R&D facilities as a function of technological and infrastructural barriers of internationalisation in the context of developing countries. In the light of above, the following hypothesis is proposed:

H3: Insufficient R&D investments would work as a barrier for SMEs to enter into foreign markets.

Impacts of political instability are a major concern for business activity particularly in emerging economies. According to Luo and Tung (2007), political instability is the common feature of developing countries. Due to these constraints, a majority of business organisations, particularly the SMEs from the developing countries, are not achieving adequate opportunities from foreign markets (Zeng et al., 2008). Al-Hyari et al., (2012) found negative relationships between political instability and international business performance. Political instability may also increase the cost of business and create competitive disadvantages both for local and international firms. Due to the negative outcomes (for example, higher risk, additional cost, market fluctuation and competitive disadvantage) some investors may become demotivated to invest in regions of political instability (Al-Hyari et al., 2012; Lu and Beamish, 2001). In contrast, other studies ignore political instability as the key barriers to internationalisation of SMEs (Okpara and Kabongo, 2010). Therefore, the influence of political instability as a barrier is still an unresolved argument. Considering the important link between political instability and political (and legal) barriers of internationalisation, this study posits political instability as a function of economic barriers in the context of developing countries' SMEs. In the light of above discussion, it has been hypothesized that:

H4: Political instability in the home country would work as a barrier for SMEs to enter into foreign market.

All nations have legal systems for individuals and organisations – it is a fabric of constitutional society. Guidelines are adopted to ensure justice, equality, objectivity and impartiality and procedures, such as, property ownership, tax liability, business enterprise should conform to legal obligations. Administration based on size, duration and procedural requirements, all have a bearing on business and the ease at which it can operate. This ease of doing business varies from country to country due to the legal processes (Al-Hyari et al., 2012). In Bangladesh, it takes a minimum of six working days to obtain a trade licence from local government authorities, whereas it might take less in some developed countries. In cases of international business, firms may face additional legal restrictions than domestic firms, such as, currency restrictions, quotas, or tariffs. Based on the country of origin of the foreign partners, additional formalities may be in place, for example, product standards, compliance procedures, health and safety requirements, and patent and trademark issues (OECD, 2006).

Despite its importance, legal procedural complexity has not been considered as a key barrier to SME internationalisation (Okpara and Kabongo, 2010). Thus, the impact of procedural complexity is still an underexplored issue. Considering the important association between legal procedural complexity and political (and legal) barriers of internationalisation, this study proposes legal procedural complexity as a function of economic barriers in the context of developing countries' SMEs. On the basis of the above discussions, it has been hypothesized that:

H5: Legal procedural complexity in the home country would work as a barrier for SMEs to enter into foreign country.

Express service is an accelerated service where customers or clients receive the delivery of goods or services faster than the normal time. Considering the value of time, express service is becoming increasingly popular, and larger firms use express service facilities in their day-to-day operations. However, resource constraint may limit SME ability to use this service and subsequently hinders the process of internationalisation. OECD (2006) has reported that duration for developing countries to complete the process of either exporting or importing is three times higher than developed countries. Despite the critical role of express service to facilitate internationalisation of SMEs, earlier studies failed to identify this as a key barrier for SME internationalisation process (Al-Hyari et al., 2012; Okpara and Kabongo, 2010). In the light of above, it has been hypothesized that:

H6: Lack of express service within the home economy would work as a barrier for SMEs to enter into foreign market.

Corruption is the abuse of public power for private and personal gain. Common forms of corruptions are bribery, extortion, fraud, embezzlement, nepotism, cronyism, appropriation of public assets and property for private use, and influence peddling (Myint, 2000). These corruptions can occur at any time, and at any level, in any sector effectively being ubiquitous. Corruption is not only costly for business but can be arbitrary and unpredictable. Morrissey and Udomkerdmongkol (2012) argue that corruption discourages both domestic and foreign investments. In cases of SMEs, corruption is considered as a significant political and legal barrier in a number of countries (Al-Hyari et al., 2012; Okpara and Kabongo, 2010). Though



the negative relation between corruption and growth of SMEs are identified both from developed and developing countries, the latter are mostly affected by the presence of corruption (Okpara and Kabongo, 2010). On the basis of the above discussions, it has been hypothesized that:

H7: Corruption in the home economy would work as a barrier for SMEs to enter into foreign markets.

### **3. Research Methodology**

This study has proposed a hierarchical reflective model on the barriers to entering foreign markets for Bangladeshi SMEs and it formulates a theory that is empirically testable. An empirical survey was carried out because this study also attempts to measure a casual network relationship as proposed by Jenkins (Jenkins, 1985) on the barriers to enter foreign markets for Bangladeshi SMEs. To carry on the empirical investigation, a cross-sectional survey technique was applied to extract views from the respondents only once (Malhotra, 2008). To achieve the maximum response rate, a postal survey was applied rather than telephone, email or online survey (Malhotra, 2008).

#### **3.1 Questionnaire Survey**

Data was collected from four major divisions of Bangladesh – Dhaka, Khulna, Chittagong and Rajshahi from July 2011 to September 2011. 250 questionnaires were distributed to each

division following cluster sampling technique. From each division, districts were selected and from each district, villages or wards of the four major city corporations were selected. Finally, international SMEs were selected from each villages and wards, and systematic random sampling technique was applied. The population for the survey was defined as the SMEs doing international business. Out of 1000 questionnaires, 219 responses were received. Among the 219, 7 were unsuitable due to missing data. Ultimately, 212 questionnaires were analysed.

Please insert table 1 here

From table 1, it can be understood that the data was collected from a diverse cross sectional population. Out of 212 respondents, 68.1% were male and 32.9% were female. As a business sector breakdown, 13.9% came from primary, 51.4% from manufacturing and 34.7% from service sector. 28.5% from Dhaka, 25.8% from Chittagong, 22.1% from Rajshahi and 23.6% from Khulna. From business type, 28.9% were sole traders, 21.4% partnerships, 9.1% family businesses, 6.9% co-operatives and 33.7% private limited companies.

Items of the questionnaire were identified from a systematic review of literature. The questionnaires were measured using a 5-point Likert-scale. To avoid any misunderstanding, the survey used questionnaires written both in English and Bengali. Where answers were given in English, no measure was taken, as there was no risk of information loss. However, where questionnaires were completed in Bengali, a professional translator was used, as suggested by Churchill (1979), with knowledge in business vocabulary so there was no information breakdown. Prior to the final data collection, a pre-test was carried out among 20 sample firms and 5 academics to ensure the appropriateness of wording, contents, scales,

sequence and format. Minor amendments were made on the basis of pre-test. This study has been assessed for content validity by undertaking a literature survey (systematic review) targeting similar studies where similar measures were used. The pilot study conducted, and gathered information, based on consultation with leading academics in relevant and non-relevant field. Insight was acquired from top officials of acquiring firms who helped to gauge the content validity of the instruments used. Based on these explorative findings two latent variables and seven manifest variables were identified. Seven hypotheses' of this study are based on these seven MVs. Each hypothesis is addressed through individual questionnaire items.

Following Ahammad et al. (2014), this paper examined common method bias (CMB), nonresponse bias and retrospective bias, widespread for survey-based studies. CMB was initially a concern as the variables were latent and measured through a cross-sectional survey (Cheng et al., 2010). To address this issue, both ex-ante (research design stage) and ex-post (post research stage) approaches were applied. Firstly, this study used data from two different sources (case study and questionnaire survey) and this should control CMB as suggested by Cheng et al. (2010). Secondly, on the first order latent variables, Harman's single factor test was applied as suggested by Podsakoff and Organ (1986) and Podsakoff et al. (2003). The un-rotated factor analysis with both dependent and independent variables produced four factors where the largest factor explains little over 35% of variance. This indicates the absence of common method bias. In addition to the CMB, there exists a nonresponse bias in the mail survey (Wickramasekera and Oczkowski, 2006). Several methods were applied to overcome this response bias, such as minimising the number of nonresponse through pre-notification and reminder; using cluster sampling technique and t-tests on the average of early and late respondents. As the test found no significant differences, nonresponse bias may not

be problematic as suggested by Armstrong and Overton (1977). Insignificant values for t-tests conducted for exports in two different timeframes, (between 2008 and 2010), confirms the absence of retrospective bias (Ahammad et al., 2012; Ahammad et al., 2014).

### **3.2 Running Example Based on Case Study**

In addition to macro level quantitative analysis, this study also used qualitative case study at the piloting stage as the context can play crucial role to understand the socio-economic phenomenon. This approach has facilitated both contextual understanding and causal explanation, which is not otherwise offered by the SEM. Two firms were selected based on the definition of SMEs in Bangladesh and their engagement in international market.

Please insert table 2 here

Imperial Collection is one of the leading, oldest and reputed buying agents in knit items exporting in Bangladesh. Utilizing ICT facilities, the firm was very innovative in its early stages but the lack of an R&D culture is apparent. The firm positioned itself as an experienced trading agent as reflected in the quote below:

“We have the pleasure to introduce ourselves as a leading, oldest and reputed buying house of Bangladesh, established in the year 1990.” (Imperial Collections, 2014)

RM Associates is one of the leading Bangladeshi garment accessories manufacturers in Bangladesh. Strong networks within leading local and international garments manufactures is the key strength of the firm as highlighted in the website:

“We have supplied garment accessories in most of the leading garments in Bangladesh and for the international buyers.” (RM Associates 2015)

Political instability and legal procedural barriers delay the process of production and shipments of goods. The firm keep multi-site production plants to carry on production in one place while there is apolitical unrest in the factory area of another. It confirms to provide additional monitoring to ensure timely shipment of products to foreign markets as expressed below:

“We monitors to our buyers regarding production status from starting to end (sic). We have sister concern of T-shirt factory as well as good contacts and control over many factories in Dhaka, Naryanganj and Chittagong.” (Imperial Collections, 2014)

“We are committed to timely delivery of any orders.” (RM Associates 2015)

Lack of express service as an economic barrier to enter in foreign market was also reflected by the firm’s ability to maintain timely shipments with foreign buyers. The firm and the industry are always concerned about this as expressed by the owner/manager:

“Although we are bringing huge foreign earnings from abroad, government seem non cooperative in need of express service as it is available in other countries.” (Owner/Imperial Collections)

“By having express service from relevant government organisation we can develop a strong base of satisfied customers for garments accessories of Bangladesh.” (Manager/ RM Associates)

Language variations and different social approaches are considered as the key barriers to foreign markets in many theories including the Uppsala model. The firm used middlemen or negotiators to overcome this problem. As the owner put it:

“We employ commission agents to overcome language issues and social problems in foreign countries particularly in some EU countries except UK.” (Owner/Imperial Collections)

“We maintain strong relationship with our local and international clients and foreign agents to avoid social and cultural constraints.” (Manager/ RM Associates)

Political instability is viewed as a cause for concern among the SMEs in Bangladesh.

“We are very disturbed by the continued political instability in our country. This has been giving a negative image to the foreign partners and we are struggling to keep our regular orders due to this uncertainty.” (Owner/Imperial Collections)

“Political instability is number one enemy for our business. Frequent strikes for day after day, week after week is virtually breaking our export system. We cannot produce on time, we cannot even deliver goods on time.” (Manager/ RM Associates)

Legal procedures are also viewed with concern for both start-ups and established SMEs in Bangladesh:

“How can you do business if you have to wait months to get a trade license to start a business, and then pay bribes to corrupt government officials who stops you every time you

export a consignment by showing you various legal restrictions?” (Owner/Imperial Collections)

“Legal procedures in this country are not at all supportive to do business. Bureaucratic procedure linger every things that you do. Frequent payments of bribes hugely increase the cost of doing business.” (Manager/ RM Associates)

The above illustrates the concerns regarding the socio-economic barriers for the SMEs in Bangladesh to entering foreign markets. These micro-level observations are further analysed along with macro-level findings later in this paper.

### **3.3 Specifying Socio-economic Barriers to Enter in Foreign Markets for Bangladeshi SMEs as a Hierarchical Reflective Model**

Hierarchical construct (also known as multidimensional construct) is defined as a construct with multiple dimensions at several hierarchies to capture an overall latent variable (Jarvis et al., 2003).

For the advantages of reducing the model complexity and increasing theoretical discretion, these constructs (hierarchical constructs) have proven to be successful in many studies (Akter et al., 2010). Besides, the ‘level of abstraction for predictor and criterion variables’ are considered as one of the most important advantages of using the hierarchical constructs in the research studies (Chin and Gopal, 1995). Considering this exploration, this study stipulates the barriers of internationalisation for Bangladeshi SMEs as a hierarchical, reflective model

with two reflective constructs (see Figure 1) – social and economic barriers to enter in foreign markets for Bangladeshi SMEs. Besides, all of these constructs of this model share the common theme that is the overall socio-economic barriers faced by the Bangladeshi SMEs to enter in foreign markets. According to Bollen and Lennox (1991), the correlation between two measures is supposed to be highly positive for a reflective construct. The most important element of reflective constructs is internal consistency as supported by Akter et al. (2010). Besides, the un-dimensional nature of the reflective measures assist to get rid of individual measures for the purpose of improving the construct validity with no effect on the content validity (Petter et al., 2007).

Insert figure 2 here

In figure 2, there are two orders - first and second. In the first order, there are two latent variables of socio-economic barriers to enter in foreign markets for Bangladeshi SMEs – social and economic barriers that are related to the respective indicators (manifest variables (MVs)). In the second order, barriers to enter in foreign markets for Bangladeshi SMEs are shown in a hierarchical, reflective model that is constructed by 7 MVs (3+4) of two first order constructs.

Please insert table 3 here.

In table 3, presented, the equation for estimating hierarchical reflective models on the socio-economic barriers to enter in foreign markets for Bangladeshi SMEs. There are two order models – first-order model and second-order model. The equation for the first order model specifies first-order manifest variables ( $y_i$ ), latent variable ( $\eta_j$ ), loadings ( $\Delta y$ ) and an error term ( $\epsilon_i$ ). The equation of the second order model specifies the first-order factors ( $\eta_j$ ) in terms



of the second-order latent variables ( $\xi_k$ ) and error ( $\zeta_j$ ) for the first-order factor and second-order latent variable loadings ( $\Gamma$ ).

### **3.4 Using PLS to Assess the Socio-economic Barriers to Enter in Foreign Markets for Bangladeshi SMEs**

PLS path modelling, also known as the component based structural equation modelling, is used for ensuring more theoretical parsimony and less complexity (Akter et al., 2010). In the above section, it has been discussed that higher order, reflective models, will be used to encompass the constructs of having more than one dimensions and indicators. By using the higher order reflective model, this study will avoid the limitations of co-variance based Structural Equation Modelling (SEM). Therefore, this study will be free from the common drawbacks of SEM including measurement level, sample size, distributional properties, and lack of identification (Wetzels et al., 2009). Besides, “it can give more accurate estimates of mediating and moderating effects by accounting for the measurement error that attenuates the estimated relationships and improves the validation of theories” (Akter et al., 2010, p.293). Furthermore, it is suitable where the objective is prediction and the research context is new or changing (Chin and Gopal, 1995). Therefore, a higher order reflective model will be suitable for this study because it aims to assess the Socio-economic Barriers to Enter in Foreign Markets for Bangladeshi SMEs.

## **4. Findings**

### **4.1 Analysis of Measurement Model**

This study has used PLS Graph 3.0 (Wetzels et al., 2009) to investigate the Socio-economic Barriers to Enter in Foreign Markets for Bangladeshi SMEs by using the hierarchical model with PLS path modelling with a path weighting scheme for inside approximation (Akter et al., 2010). Following the path weighting scheme, this study used nonparametric bootstrapping (Wetzels et al., 2009) where the standard error of the estimates are obtained by using 500 replications. Following suggestions made by Akter et al. (2010) this study has used the approach of repeated indicators to estimate the higher order latent variables. Therefore, the second-order factor (Socio-economic Barriers to Enter in Foreign Markets for Bangladeshi SMEs) is measured directly by indicators (manifest variables) of the first-order factors (Social and Economic).

Please insert table 4 here.

As proposed in Wetzels et al. (2009) a confirmatory factor analysis (CFA) is conducted to test the model and analyse the reliability and validity. Table 4 shows individual item loading is higher than 0.70, which is also significant at 0.01. Further, reliability of the scale is assessed through the Composite Reliability (CR), Cronbachs Alpha (CA) and Average Variance Extracted (AVE) as recommended in Akter et al. (2010). The results (Table 4) find that the values for CR and CA on the social and economic barriers are well above to the threshold point of 0.70 (Hulland, 1999), which indicates the scale consistency for each item. On the other hand, AVE for economic and social barriers (Table 4) is also higher than the modest threshold 0.50 (Fornell and Bookstein, 1982). Again this indicates that each construct captures adequate variance from its items and all the constructs are conceptually distinct. Therefore, the convergent validity of all the scales is ensured. Finally, the result of square

root of AVE finds in Table 5 ensures discriminant validity. The square root value of AVE confirms that they are higher than the corresponding correlation coefficients in the correlation matrix (Fornell and Bookstein, 1982). Therefore, it can be concluded that all the empirical results related to the analysis of the measurement model are satisfactory with respect to adequate reliability, convergent validity and discriminant validity.

Please insert table 5 here

Please insert table 6 here

Please insert figure 3 here

#### **4.2 Summary of Findings:**

This study has estimated the relationship between the overall socio-economic institutional barriers (and its sub-dimensions, i.e., economic and social barriers) with foreign market entry mode of Bangladeshi SMEs with an objective to measure the structural validity of the model (see Figure 3). The respective standardized beta reported in table 6 for social and economic barriers are 0.900 and 0.936 respectively. This result refers to a strong association between selected entry mode and economic and social barriers. Further, all these path coefficients are significant at  $p < 0.01$  (please see table 6). Therefore, overall findings support the hypotheses reported in table 7. The running examples presented in section 3.2 also support these findings. For example, both the CEO and the manager from the two selected SMEs clearly indicated language, political instability, legal procedures and corruption are possible hindrances to SME internationalisation.

Please insert table 7 here

The paper has found language barriers, differences in social approach, lack of R&D facilities, political instability, legal procedures, lack of express service and corruption have a significant bearing on internationalisation of Bangladeshi SMEs. The path coefficients for all those factors representing barriers are well above the threshold level of path coefficient value and are statistically significant. This is a clear indication of our prediction based on literature that these home country institutional factors act as possible barriers for internationalisation. For example, the results in our paper are in line with previous findings on language barriers (OECD, 2006) that indicate lower language ability of home firm personnel disturbs the communication flow between the home organisation and its foreign counterpart. As a result, internationalisation would become more complex and costly (Uner et al., 2013; Gripsrud, 1990; Pinho and Martins, 2010). Differences in social approaches (Barkema and Vermeulen, 1997) have been found to strongly associate with SME internationalisation propensity. Social approaches are shaped by culture and influence the way firms deal with customers and other stakeholders. Differences in social approach between participating firms also increase complexity in the exporting process and hence affect internationalisation activity (Bauerschmidth et al., 1985; Cavusgil, 1984a,b; Gripsrud, 1990; Pinho and Martins, 2010). The paper has also found that R&D investments (Yam et al., 2011), political instability (Zeng et al., 2008), legal system and express service as government support (OECD, 2006) and corruption (Okpara and Kabongo, 2010) also work as impediment to SME internationalisation.

This paper has significantly contributed to the theory by developing a foreign market entry barriers based model, which provides an holistic view of socio-economic barriers for the internationalisation of SMEs from the context of an emerging market. Since previous studies have often not adequately addressed foreign market entry barriers for the SMEs in the context of emerging economies, this study provides perhaps the most comprehensive understanding within this area of research. Two types of foreign market entry barriers (social and economic) are evaluated in this study. Although both types of obstacle are significant for the foreign market expansion, the economic barriers are seen as more influential as evident from higher factor loading reported in figure 3. This is in line with results found in Uner et al. (2013) who explored the export barriers within emerging markets. Altintas et al. (2007), Shaw and Darroch (2004) and Pinho and Martins (2010) found similar results. At individual institutional barrier level, the paper has found that government support as represented by lack of express service is the most important barrier for SMEs in Bangladesh. Other more important barriers include social approach and language difficulty. This is in contrast to the results found in Uner et al. (2013) who found procedural barrier as the most important barrier for Turkish SMEs. The result is also in variance with Shaw and Darroch (2004) who found financial barrier as most important for SMEs in New Zealand. Other studies like Pinho and Martins (2010) and Suarez-Ortega (2003) have found informational barrier as most prominent for Spanish SMEs and Portuguese SMEs respectively. The differences in results are clear indications of the impact of different institutional settings on export barriers. Developed countries like New Zealand and Spain have a different institutional setting compared to Bangladesh. Moreover, Turkey and Portugal are also relatively different to Bangladesh. Therefore, differences in relative importance of export barriers are not surprising. At the micro level, the running examples complement the macro level findings of social and economic barriers. For example, both Imperial Collection and RM Associates

confirmed that legal procedures and political unrest work as barriers to SME internationalisation as suggested by Uner et al. (2013), Kaynak et al. (1987), Barker and Kaynak (1992), Bodur (1986) and Karafakioglu (1986). These firms normally keep multi production sites to cope with political uncertainty, and also try to circumvent procedural complications to ensure timely production of their goods and services. These statements compliment the findings in our macro analysis that support hypothesis four and five. In their second statements both the companies emphasised the role of government through express services for SMEs. The lack of express services contributes to increased dissatisfaction, as the customer would have to bear the burden of any delay (Uner et al. (2013). This complements the findings of our macro analysis that supports hypothesis six. In another statement, both firms confirmed they engaged professional services to maintain proper communication, and also maintain close relations with local community and customers to overcome language barriers and social approach issues (Gripsrud, 1990; Pinho and Martins, 2010 and Uner et al., 2013). This complements our macro findings that support hypothesis one and two.

Another objective of this paper was to demonstrate the complex relationship among the social and economic barriers to enter in foreign markets for SMEs empirically through PLS path modelling. To support this objective, a second order reflective hierarchical model is developed using the data collected from SMEs in Bangladesh. This model should be able to better explain the complex relationship as suggested by Fornell and Bookstein (1982). Following the suggestion made by Wold (1985), this study used repeated indicators from first-order model to the second-order model. All results confirmed the validity of measurement and structural models. Therefore, it has successfully shifted individual barriers of internationalisation to overall barriers of internationalisation as stated by Wold, "PLS

comes to the fore in larger models, when the importance shifts from individual variables and parameters to packages of variables and aggregate parameters." (Wold, 1985: 589).

## **5. Conclusion:**

Building on the research gap regarding the home country institutional factors on the SME entry mode choices, as identified by a recent review by Laufs and Schwens (2014), this study has identified key institutional factors as suggested by Scott (1995), which hinders the growth of SME entry into a foreign market. According to Laufs and Schwens (2014), there is a lack of research on SME entry mode from the context of an emerging market. This paper used a set of Bangladeshi SMEs to examine how certain home country institutional variables, both social and economic, may affect the foreign market entry mode choices. The study has found that selected institutional factors like political instability, corruption, government support, R&D investments, legal procedures, language difference and social approach have significant impact on firm's entry mode decision. All seven hypotheses are supported (table 7), and from the theoretical context, theory suggests that institutional settings in an emerging market are very different than developed market (Peng et al., 2008). This study has found that the relative importance of individual institutional barriers for Bangladeshi SMEs is different than that of say New Zealand or Spain as suggested by Uner et al. (2013). This supports the theoretical prediction that differences in institutional setting among countries will have an impact on entry mode barriers. As an emerging country, Bangladesh has to keep pace of economic growth to move to the next level of development. The Bangladesh government has already unveiled its vision to become a middle income country by the year 2030. To achieve this goal, investing and supporting SMEs more actively is the most realistic strategy as the country, as many other emerging countries, suffer from an inadequate supply of capital to

support growth of larger industries. Furthermore, Javalgi et al. (2011) mentioned that owners and managers needed to be responsive about the different entry modes available to firms in the context of the operating environment. Therefore, the findings from this paper are of immense importance to practitioners and policymakers as it points clearly that SMEs in Bangladesh suffer from economic and social barriers while they plan to internationalise into foreign markets. Furthermore, identification of socio-economic barriers to enter into a foreign market is important but the SMEs cannot undertake independent research considering resource limitation (Ghauri et al., 2003). Study findings have significant practical contributions from this context alone. The policymakers along with other stakeholders should address and support SMEs in Bangladesh to overcome those economic and social barriers, as suggested in the paper, and facilitate a smooth internationalisation process to ensure the expected pace of national development. Another key contribution is the development of a hierarchical reflective model using PLS to assess the socio-economic barriers to enter in foreign markets for the SMEs in a developing country.



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Table 1: Demographic Profiles of Respondents

Particulars	Category	%	Particulars	Category	%
Gender	Male	68.10	Sector of business	Primary	13.90
	Female	32.90		Manufacturing	51.40
Area	Dhaka	28.50	Business Type	Service	34.70
	Chittagong	25.80		Sole trader	28.90
	Rajshahi	22.10		Partnership	21.40
	Khulna	23.60		Family	09.10
			Co-operative	06.90	
			Private Ltd	33.70	

Table 2: Basic Information of the case firms

Particulars	Imperial Collection	RM Associates
Year founded	1990	2002
Owner/CEO	Hemayet Uddin	Shaheen Bagh
Number of employees	5-10	50-70
Business type	Trading Company, Buying office, Agent	Manufacturer
Foreign market activity	Exporter of knit items	Exporter of Garments Accessories
Main market/source	North America and EU	Emerging markets mainly

Table 3: Estimation of the Socio-economic Barriers to Enter in Foreign Markets for Bangladeshi SMEs as a reflective hierarchical model

First Order	Second Order
$y_i = \Delta_y \cdot \eta_j + \varepsilon_i$	$\eta_j = \Gamma \cdot \xi_k + \zeta_j$
$y_i$ = manifest variables	$\eta_j$ = first order factors (e.g. political)
$\Delta_y$ = loadings of first order latent variables	$\Gamma$ = loadings of second order latent variables
$\eta_j$ = first order latent variables (political, economic, technological and social)	$\xi_k$ = second order latent variables (procedural barrier)
$\varepsilon_i$ = measurement error of manifest variables	$\zeta_j$ = measurement error of first order factors

Table 4: Psychometric properties for first order constructs

Constructs	Items summary	Loadings	CR	CA	AVE
Social Barriers	Language differences	0.971	0.967	0.948	0.907
	Different social approaches	0.974			
	Lack of R&D facilities	0.911			
Economic Barriers	Political instability	0.937	0.953	0.934	0.837
	Legal procedural barrier	0.897			
	Lack of express service	0.962			
	Corruption	0.861			

Table 5: Latent Variable Correlations

	Social	Economic
Social	0.952*	
Economic	0.689831	0.915*

Note: square root of AVE on the diagonal\*

Table 6: Analysis of Structural Model Path Coefficients (Mean, STDEV, T-Values)

	Original Sample coefficient	Sample Mean coefficient	Standard Deviation (STDEV)	Standard Error (STERR)	T Statistics
Overall Barriers -> Economic	0.936195	0.932717	0.021119	0.021119	44.32955
Overall Barriers -> Social	0.900278	0.896526	0.028672	0.028672	31.39871

Table 7: Results on Hypotheses

Hypothesis	Path coefficient	t-value	Conclusion
H1: Language difference as a factor of social barriers and foreign market entry of SMEs will not be independent from each other.	0.971	123.988	Supported
H2: Different social approach as a factor of social barriers and foreign market entry of SMEs will not be independent from each other.	0.974	124.100	Supported
H3: Lack of R&D as a factor of social barriers and foreign market entry of SMEs will not be independent from each other.	0.911	25.022	Supported
H4: Political instability as a factor of economic barriers and foreign market entry of SMEs will not be independent from each other.	0.937	47.427	Supported
H5: Legal procedural complexity as a factor of economic barriers and foreign market entry of SMEs will not be independent from each other.	0.897	21.329	Supported
H6: Lack of express service as a factor of economic barriers and foreign market entry of SMEs will not be independent from each other.	0.962	74.254	Supported
H7: Corruption as a factor of economic barriers and foreign market entry of SMEs will not be independent from each other.	0.861	21.263	Supported

# Barriers to Enter in Foreign Markets for the SMEs in a Developing Country

Figure 1 Hypothesis on the socio-economic barriers to enter in foreign markets for Bangladeshi SMEs

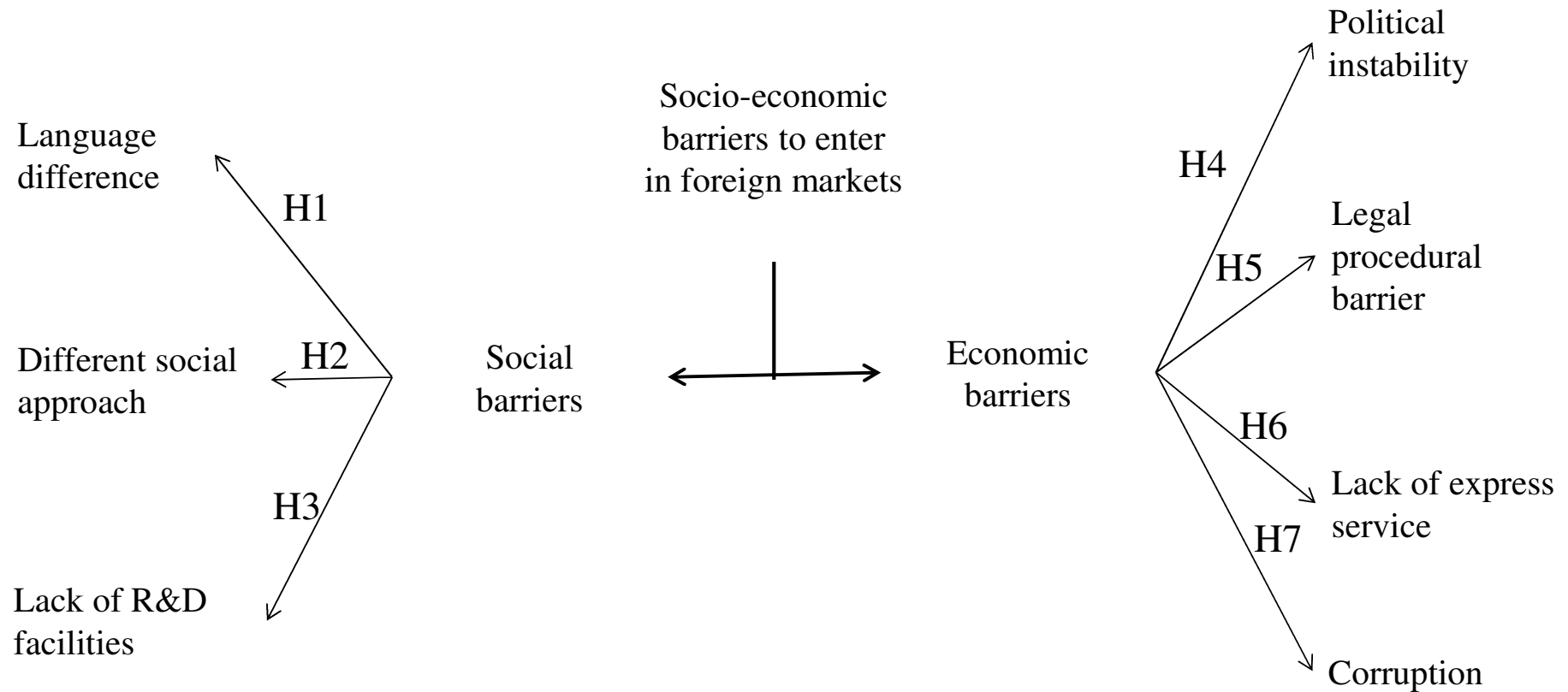




Figure 2: Socio-economic Barriers to Enter in Foreign Markets for Bangladeshi SMEs as a Hierarchical Reflective Model

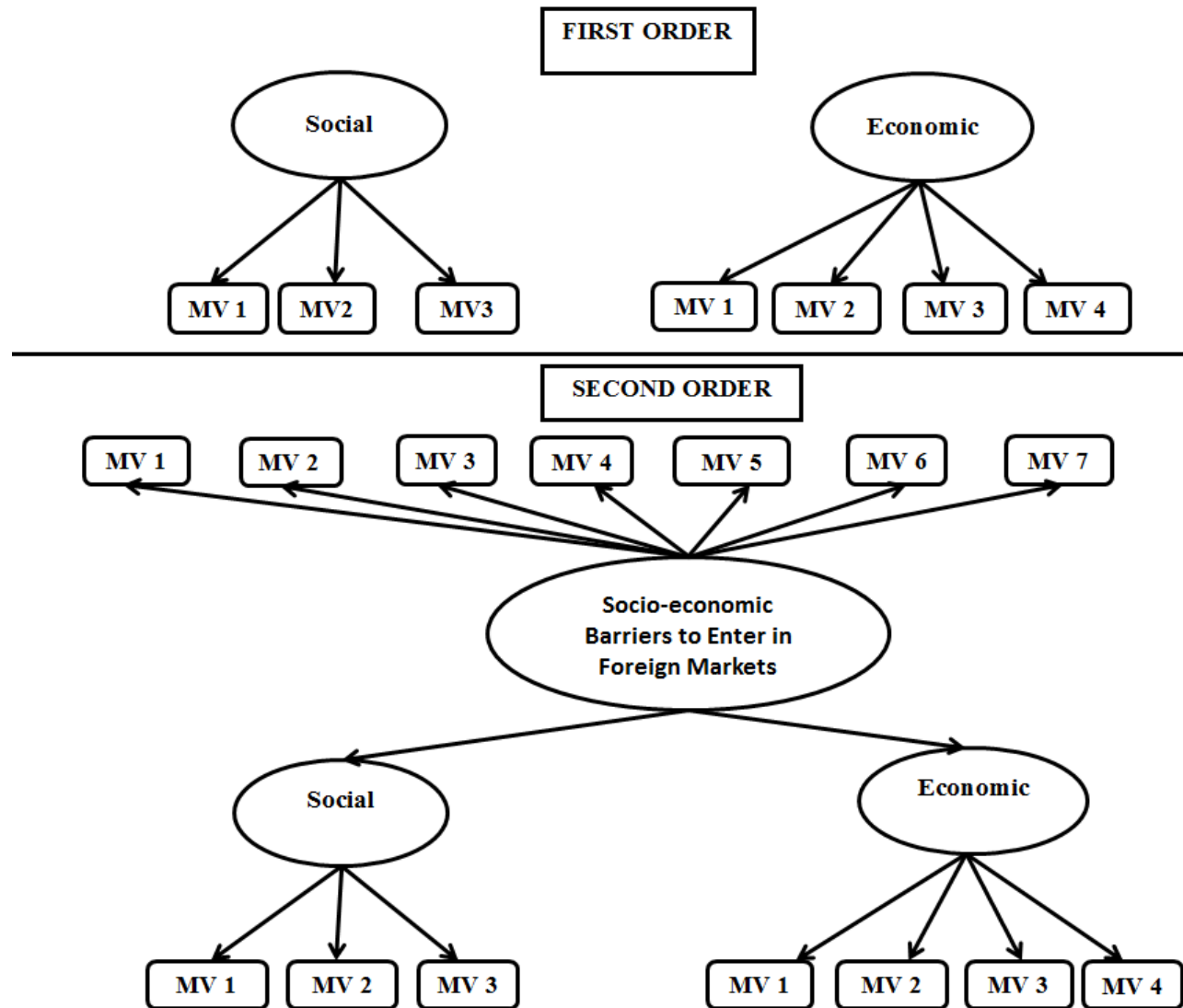


Figure 3: Main Loadings of the Model

