

25 the effect of international entrepreneurship orientation

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2 The Effect of International Entrepreneurship Orientation and Network Capability on SMEs International Performance; The Important Role of Government Support

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Abstract This research aims to analyze the effect of the international entrepreneurship orientation and the SMEs' network capability on the SMEs' international performance. Furthermore, it also analyze the moderation effect of the government's supports on the causal relationship between international entrepreneurship orientation and SMEs' network capability on SMEs' international performance. The sample of this research is 160 SMEs producing furniture and handicrafts that have engaged in international marketing for at least 3 years. The analytical tool used in this study is moderating regression analysis using interaction method. The results show that international entrepreneurship orientation positively affects the SMEs' international performance, network capability has a positive effect on international performance, the government's supports strengthen the effect of international entrepreneurship orientation, and that the government's supports weaken the effect of network capability on SMEs' international performance.

Keywords: international entrepreneurship orientation, network capability, government's support, international performance, SMEs

1 Introduction

The massive growth of globalization, advanced communication technology, and transportation have lessened trade barriers among countries. This encourages business practitioners to expand their business activities into the international market [1]. This changes affect companies, not only the big one, but also seen as an advantageous opportunity for the Small Medium Enterprises (SMEs) to widen their businesses in the international level.

SMEs' internationalization can be concluded as SMEs' efforts in entering the international market. However, the process is not simple and has many challenges. It is because SMEs have limited resources, limited knowledge on the foreign market, and low capability to capture business opportunities or develop international business [2]. A research conducted by [3] on internationalization in Southeast Asia SMEs shows that the biggest obstacle in their internationalization is due to the lack of resources, especially the financial, technological, and trained workforce resources, as well as access to the market and information. Besides, SMEs are also limited in economic scale, high transaction cost, and the international market tight competition, especially when competing with large companies.

A similar condition happens in Indonesia. The number of internationalizing SMEs is very limited, that is less than 5% of the overall SMEs. Indonesian SMEs' contribution to national export is also low, only around 17%. This contribution is lower than that of the other countries, for example, Philippine's SMEs is 25% and Thailand's is 30% of their total export. Only a few SMEs in Indonesia that has conducted export, as most of them have low understanding in export schemes and procedures, export certification terms and conditions, and export standard setting. SMEs' entrepreneurship orientation and capability are also poor, while the government support has been not optimal. [4] conducted a study revealing that government's supports are insufficient in encouraging Indonesia SMEs' internationalization [20]

This research aims to analyze the effect of SMEs' international entrepreneurship orientation and network capability towards SMEs' internationalization performance in Indonesia. Furthermore, it also analyzes the moderation effect of government's role in the effect of international entrepreneurship orientation and network capability on SMEs' international performance. It is expected that government support can strengthen the effect of SMEs' international entrepreneurship orientation and network capability for better international performance.

2 Literature Review and Hypothesis Development

1) SMEs Internationalization

Internationalization can be defined as a gradual mechanism in a company to join, to do and to add business transactions in the international market. A company's internationalization is encouraged by several things, among others are the desire to expand the market abroad, respond to the unfulfilled market demands, cutthroat competition in the domestic market, and to lower production cost abroad [5].

Globalization without barriers and technological advances have stimulated SMEs to internationalize. However, this process has its challenges, especially the ones related to the lack of business network and internationalization experience [5]. [6] grouped internationalization obstacles into two categories, internal obstacles, and external obstacles. Internal obstacles such as holistic information, functional, and marketing obstacles. External obstacles such as procedural, governmental regulation, and environmental obstacles.

2) International Performance

International performance is the result gained from internationalization activity. This can be measured in several indicators, such as *Return on Assets (ROA)*, *Return on Sales (ROS)* and *Growth of Sales and Assets* [7]. International performance also can be assessed by subjective measurement. [8] stated that international performance is a construct reflecting the result of internationalization activity, which consists of two dimensions which the satisfaction level of the internationalization activity result compared to the company's goals, and performance comparison between a company's international activity and its competitor's. [9] used 3 measurements to assess international performance, namely: the company's satisfaction level of the internationalization activity related to 1) the goal realization and internationalization activity target, 2) the profit level gained from internationalization activity, and 3) sales level of the internationalization activity. In many studies, the subjective measurements are often chosen since many SMEs are incapable of making proper financial reports while secondary data of SMEs' financial reports are unavailable.

3) International Entrepreneurship Orientation

Small Medium Enterprises' (SMEs') internationalization shows SMEs' international-oriented entrepreneurship behavior, which is an effort made by SMEs to identify and explore new business opportunities in a new business environment in the international market. International entrepreneurship orientation is a reflection of behavior characteristics in international entrepreneurship. It can be defined as innovative, proactive, and risk-taking characteristics to seize opportunities in the international market [10]. It has 3 dimensions, namely 1) Innovative (the company's behavior to get involved and to support new ideas, to experiment in creative process to generate new product, new service, and new process in business activity), 2) Proactive (the company's active and mindful behavior to seek new opportunities in the international market), and 3) Risk-taking (the company's willingness level to take risk out of the decision to enter the international market).

SMEs with international entrepreneurship orientation possess high innovative and proactive behavior as well as the courage to take failure risk to seize opportunities in a highly competitive international market [10]. Empirical evidences show the positive effects of international entrepreneurship orientation on SMEs' international performance. This means, the higher the international entrepreneurship orientation of an SME is, the higher its international performance is [11],[12] This confirms [11] finding, which proved that international entrepreneurship orientation positively affects the company's readiness to have an international marketing, associated with an indicator of subjective international performance. Moreover, a study conducted by [13] also confirmed that there is a positive effect of international entrepreneurship orientation on the entrepreneurship satisfaction in their activity in the international market. International entrepreneurship orientation positively affects the international performance of exporting companies.

Therefore, the first hypothesis is proposed as follows:

H1 : International entrepreneurship orientation positively affects the SMEs' international performance

4) Network Capability

There is no business without network [14]; this statement emphasizes the importance of networks in a business process. In a business' internationalization, networks also play an important role in identifying new market opportunities in internationalization process [15]. Literatures in SMEs' network development reiterate the importance of business networks to overcome various constraints faced by SMEs in entering the international market [16].

A network capability is a company's ability to develop and utilize cooperative relationships with other companies to access various resources owned by its partners. Partners in a network can take place as consumers, distributors, suppliers, competitors, and government. In this sense, a network also includes interconnected relationship among the partners, for example, between a customer and a customer, a customer and a supplier, a

customer and a competitor, and so forth. Network capability is integrated with several dimensions representing different capabilities required to cooperate with business partners, namely coordination, relational skill, business-partner knowledge, and internal communication [17] and [18].

SMEs ability to start and maintain relationships with their business partners is crucial in internationalization process since SMEs have conditions that which make it hard for them to penetrate the complicated and intricate international market [19] and [20] Internationalization process is complicated and intricate because it involves many factors, among others are different business characteristics, different institutions, different rules, different policies, and different laws in the involved countries.

Some empirical studies confirm that network capability significantly influences SMEs' international performance [9] and [12]. Those validate the research conducted by Chetty and Wilson [21], which verified that network capability has crucial roles in SMEs' internationalization process. By means of the network it builds, an SME can learn the internationalization, choose the right mode to join in the international market, and obtain opportunities to share resources with its partners in their relationship. Furthermore, [16] and [18] also confirm that network capability has positive effects to SMEs' international performance. Therefore, the second hypothesis is proposed as follows:

H2 : Network capability positively affects the SMEs' international performance

5) Government Support

Government support is the supports and aids given by the government to SMEs to help their efforts in entering the international market. These take forms as various policies and incentives.

H3 : Government's supports strengthen the effect of international entrepreneurship orientation on SMEs' international performance

H4 : Government's supports strengthen the effect of network capability on SMEs' international performance

3 Methodology

1) Sample and data collection

The population of this research is all Small Medium Enterprises (SMEs) in Indonesia that have conducted international marketing. The samples are 160 furniture and handicrafts SMEs, that have been conducting international marketing for at least 3 years. Data are collected through interviews and questionnaires. The technique for the interviews is the *depth interview*. Meanwhile, the questionnaires are devised systematically with close and open questions to obtain the MSEs' perceptions on international entrepreneurship orientation, network capability, government's supports, and international performance.

2) Measures

A five-point Likert scale is used to measure the respondents' perceptions on the research variables. The variables are international entrepreneurship orientation, network capability, government support, and SMEs' international performance. The conceptual definitions and indicators for each variable are as follows:

International Entrepreneurship Orientation is an entrepreneurship behavior that is internationally oriented. It is an effort to identify and explore new business opportunities in a new business environment in the international market. According to [10], international entrepreneurship orientation is measured in three dimensions, 1) Innovative (a company's behavior to get involved and support new ideas, to experiment in creative processes to generate new product, new service, and new process in business activity), 2) Proactive (the company's active and mindful behavior to seek new opportunities in the international market), and 3) Risk-taking (the company's willingness level to take risk out of the decision to enter the international market).

Network Capability is a company's ability to develop and utilize cooperative relationships with other companies to access various resources owned by its partners. Network capability is measured in 4 dimensions, namely: a) coordination, b) relational skill, c) knowledge on partner, and d) international communication [16].

Government Support is the supports and aids given by the government to SMEs to help their efforts in entering the international market. These take forms as various policies and incentives, which include: a) marketing support (production and promotion), b) financial support, c) international trade incentive, and d) capacity building for internationalizing SMEs through trainings, workshops, and seminars.

International Performance is measured by SMEs' perception to: a) increase in profit obtained from international commerce, b) increase in trade volume of international commerce, and c) increase in international market share [10] and [22]

4 Data Analysis and Discussion of Finding

To test the moderating effect of the government support to the effect of international entrepreneurship orientation and network capability, a moderated regression analysis using interaction method was conducted. There are 3 steps in this method. The first one is regressing independent variable (X_1 and X_2), to analyze the effect of the independent variables to the dependent variable (Y). The first equation is:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \epsilon \dots\dots\dots (1)$$

The second step is regressing the independent variables (X_1 and X_2), the hypothesized moderating variable (Z) and interacting variables (X_1Z dan X_2Z) to the dependent variable (Y). If the multiplication variable resulted from the independent variables and hypothesized moderating variable is significant, it can be concluded that the hypothesized moderating variable does moderate the effect of the independent variable to its dependent variable. The second equation is:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 Z + \beta_4 X_1Z + \beta_5 X_2Z + \epsilon \dots\dots\dots (2)$$

The third step is regressing the independent variables (X_1 and X_2) and the hypothesized moderating variable (Z) to the dependent variable (Y) to determine the type of moderating effect. The third equation is:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \epsilon \dots\dots\dots (3)$$

The analysis result of the 160 SME samples are as follows:

- a) The result of the first regression equation is $Y = 5,205 + 0,401 \text{ IEO} + 0,238 \text{ NC} + \epsilon$. Based on the output, it can be seen that regression coefficient of international entrepreneurship orientation is 0,401, with t-count 5,960 and sig. (0,000) and regression coefficient for network capability is 0,238 with t-count 4,060 and sig. (0,000). The results show that the international entrepreneurship orientation and network capability positively influence the SMEs' international performance. Thus, hypothesis 1, which states that international entrepreneurship orientation positively affects the SMEs' international performance, is accepted. Hypothesis 2, which states that network capability positively affects the SMEs' international performance, is accepted.
- b) The result of the second regression equation is $\text{IP} = -2,784 - 0,442 \text{ IEO} + 1,115 \text{ NC} + 0,063Z + 0,064 \text{ IEO.Z} - 0,069 \text{ NC.Z} + \epsilon$. Based on the output of the second equation, it can be seen that the interacting variable regression coefficient 1 (multiplication of international entrepreneurship and government support) is 0,064, with t-count 1,986 and sig. (0,049). Interacting variable regression coefficient 2 (multiplication of network capability and government support) is -0,069, with t-count -2,277 and sig. (0,024). The results showed that government's supports positively moderate the effect of international entrepreneurship orientation on SMEs' international performance. On the other hand, the government's supports negatively moderate the effect of network capability on SMEs' international performance. Therefore, the third hypothesis stated that government's supports strengthen the effect of international entrepreneurship orientation to SMEs' international performance is accepted. Meanwhile, the fourth hypothesis that stated the government's supports strengthen the influence of network capability to SMEs' international performance is rejected.
- c) Based on the output of the third equation, the value of regression coefficient obtained is 0,057, with t-count value is 1,500, sig. (0,136). The effect of the government's supports in the third equation is insignificant, showing that the type of moderating effect is pure moderator.

Discussion

Interesting findings present in this research. The result of the moderated regression analysis using interaction method shows that the government's supports strengthen the effect of international entrepreneurship orientation on the SMEs' international performance. Nevertheless, the supports weaken the effect of network capability on SMEs' international performance.

It has been elaborated that SMEs possess limited resources, especially the ones of financial, technological, market labors, access to the market and information, to expand their market to the international one. Those obstacles have forced the government to aid and facilitate the SMEs in their internationalization process. In Indonesia, the government's supports are realized in various aspects, among others are marketing, finance, and taxes. In the marketing aspect, the government has founded *Small and Medium Enterprises and Cooperative (SMESCO)*, an institution that aims to facilitate SMEs in creating world-class featured products, promoting Indonesian SMEs to local and international business partners. The Indonesian government has also supported SMEs' finance, through the Ministry of Cooperatives and Small and Medium Enterprises together with Indonesia

Export Finance Institution (LPEI), to help and encourage cooperatives and SMEs to have export-oriented activities. In the tax aspect, the Indonesian government has given SMEs Income Tax incentives, in which the tax for SMEs with 4.8 billion business revenue is only 1% out of it (Indra Cahyadi, 2015). Those aids are provided by the government to boost Indonesian SMEs to compete in the international market. ²

The results of this research show that the government's supports strengthen the effect of international entrepreneurship orientation on the SMEs' internationalization performance. To escalate their performance, SMEs need to be innovative, proactive and dare to take risks. Government's supports, especially marketing support (production and promotion), have encouraged SMEs to take the experimental and creative process in producing new products or services. Besides, the supports also boost SMEs' awareness of seeking new opportunities in the international market. The supports are given in the forms of various training, workshops, and seminars aiming at increasing SMEs' capabilities as well as self-confidence to internationalize. They also take form as tax incentives to encourage SMEs entering the international market. A strong entrepreneurship orientation, together with the government's supports, is proven to increase SMEs' international performance in Indonesia. ⁴

On the other hand, the results also reveal that the government's supports weaken the effect of network capability on the SMEs' international performance. The international performance will increase provided that the SMEs are capable of developing and utilizing their network cooperation for various purposes, such as sharing resources and risks, when entering the international market. This research shows that the government's supports weaken the coordinating and relational skills, partner knowledge, and internal communication that are built to improve the SMEs' international performance. This indicates that government's supports have led to SMEs' reluctance to develop their own networks. SMEs prefer to rely on the government help in connecting them to the third parties, which aid them in entering the international market. This is the opposite of the objective set by the government. The government provides helps in marketing, finance, and tax to support MSEs in improving their international performance.

5 Conclusion

² The results of this research provide empirical evidence that international entrepreneurship orientation positively affects the SMEs' international performance. This confirms the studies conducted by [10], [11], [12], as well as [13]. Besides, it also proves that the network capability has a positive effect on the MSEs' international performance. It reinforces the results of studies by [9], [12], [18], and [21] ²³

Furthermore, this research contributes to the new theoretical aspect that is testing the moderating effect of the government's supports to the causal relationship between international entrepreneurship orientation and network capability to SMEs' international performance. The results show that the government's supports strengthen the effect of international entrepreneurship orientation on the SMEs' international performance. However, they weaken the effect of network capability to SMEs' international performance.

6 Reseach Limitation

²⁵ The main limitation of this study is the limited value of the coefficient of determination obtained, which is only 50.8%. This indicates that there are still many other variables that are thought to affect the internationalization performance of SMEs in addition to the variables examined in this study. Therefore, in future studies antecedent variables of internationalization performance can be added, such as innovation capabilities and foreign market knowledge

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