The Conference Board of Canada

BRIEFING JULY 2013

TOOL KIT FOR GROWTH MARKETS

SUCCESS IN FAST-GROWTH MARKETS

Strategies for Smaller Players.

At a Glance

- Canadian small and medium-sized companies (SMEs) are most likely to succeed in fast-growth markets if they have:
  - bridging arrangements that enable them to learn quickly about the market;
  - experience-building strategies that embed this learning in the company, with coherent market entries that build on previous entries;
  - technological advantages and a global reputation;
  - a realistic understanding of the challenges and a serious, long-term commitment to developing sustainable relationships in the market.

EXECUTIVE SUMMARY

While global trade was taking off over the past decade, Canada's export performance flatlined. This is bad news: With its small domestic economy, Canada depends on trade to bolster its living standards. The poor trade performance is due to Canadian companies being overexposed to slow-growth markets and underexposed to faster-growing emerging markets.

To be sure, Canadian trade with fast-growth markets has taken off. Still, on the whole, Canada's businesses are vastly underexposed to these fast-growth markets, which offer exporters much greater growth potential than do traditional markets.

Evidence suggests that, contrary to common wisdom, small and medium-sized businesses are leading the way in diversifying exports to non-U.S. markets, especially to fast-growth markets. Small companies have accounted for almost all of Canada's export growth to such markets as Thailand, India, Singapore, Hong Kong, and Vietnam. Yet, only a small number of small and medium-sized businesses account for the lion's share of this activity.

Fast-growth markets can be extremely challenging places to do business, especially for companies with limited resources. This briefing assesses the challenges that fast-growth markets present for smaller players, and examines strategies that have been shown to work in these markets. The analysis is rooted in a review of the evidence, accompanied by the experiences of a variety of Canadian and U.K. goods and services companies.

Not all small and medium-sized businesses are suited to expand into fast-growth markets. To have the greatest likelihood of success, companies should:

- be prepared to be on the ground often in a fast-growth market in order to develop relationships (even though this is difficult and time-consuming)
- be persistent
- offer a world-class, distinctive product or service
- constantly innovate in order to protect against intellectual property theft (formal IP mechanisms are less reliable than they might be in traditional trade partners)
- look for opportunities to piggyback into a fast-growth market with an existing customer
- think through sequences of market entries so that you can use what you learned in one country for the next
- take full advantage of matchmaking and mentoring services offered by governments and international trade associations, as well as municipal "twinning arrangements," to find strong local partners

Policy-makers should:

- support companies that are likeliest to succeed: those with cutting-edge technology that recognize the need to make a long-term commitment to a market
- consider twinning arrangements, especially for Canada's smaller communities
- support bridging and experience-building programs; though headlines tout free trade negotiations as the main government tool to help companies succeed in global markets, SMEs need experience-building arrangements in order to learn and develop their reputations

This analysis is part of The Conference Board of Canada's "Tool Kit for Growth Markets," which provides tools and strategies to help Canadian companies—and those who develop policies to support them—to succeed in fast-growth markets.

SCOPE

This briefing addresses two questions:

1. What important challenges face small and medium-sized enterprises (SMEs) doing business in fast-growth markets?
2. What practices enable SMEs to overcome these challenges?

We examined these questions by reviewing the most recent and relevant scholarly literature and by interviewing founders and top managers of SMEs that have successfully sustained sales in fast-growth markets. To look beyond Canada, we studied two British SMEs, as well as a British government-to-government twinning arrangement that has been integral to the success of one of the featured firms. For descriptions of the companies studied, which represent diverse industries and foreign markets, see box "Companies in the Study and Their Experience in Emerging Markets."

This briefing examines the challenges that firms doing business in fast-growing markets face, and then describes how Canadian and British SMEs are overcoming those challenges. We recognize that not all SME owners and managers will perceive these challenges in the same way. (See box "Experience Leads to a More Accurate Perception of How Significant the Challenges Are.") We therefore focus on the frequently occurring challenges that most SMEs face. We conclude by outlining the implications of these insights for business owners and policy-developers.

Why Look at Success Strategies for SMEs in Fast-Growth Markets?

While global trade was taking off in recent years, Canada's export performance flatlined. The 2012 Conference Board of Canada report *Walking the Silk Road: Understanding Canada's Changing Trade Patterns* shows that Canadian exports stagnated between 2001 and 2011, even though global goods trade expanded by almost 70 per cent during the same period. Canadian export growth continues to lag behind the global average by about 5 per cent annually.[1] This is bad news for a country like Canada that, with a small domestic economy, depends on trade opportunities to bolster its citizens' living standards.

This "lost decade" for Canadian exports largely reflects the countries that Canadian businesses trade with. The Bank of Canada's research shows that, over 2000–10, 85 per cent of Canada's exports were aimed at slow-growth markets (such as the United States, Japan, and the European Union). Only 8 per cent went to fast-growth markets (such as China, India, and Brazil).[2] This combination of overexposure to the slow-growing U.S. market and underexposure to the faster-growing emerging markets is almost entirely responsible for Canada's loss of world market share over the last several years, which has slowed Canada's export growth.[3]

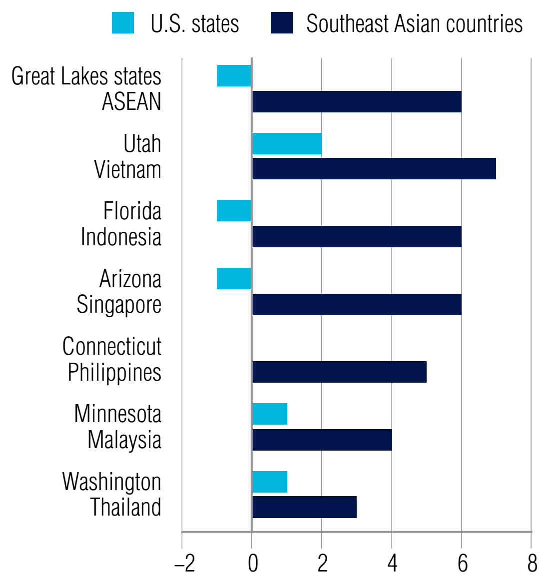
To be sure, Canadian trade with fast-growth markets has taken off. Sixteen per cent of Canada's exports went to emerging markets in 2012.[4] Still, Canada's businesses on the whole are vastly underexposed to these fast-growth markets.

Fast-growth markets offer tremendous opportunities to Canadian companies. The first chart shows how dramatically Southeast Asian countries grew, on average, over the 2006–11 period relative to the equivalent-sized U.S. state economies that are some of Canada's traditional trade partners.

To make a practical contribution to boosting Canadian company exposure to fast-growth markets, this briefing examines strategies that have been shown to work in fast-growth markets. The focus is on small and medium-sized companies (SMEs).

Evidence suggests that, contrary to common wisdom, SMEs are leading the way in diversifying exports to non-U.S. markets, especially to fast-growth markets. The second chart shows that small companies have accounted for almost all the export growth to markets such as Thailand, India, Singapore, Hong Kong, and Vietnam.

Southeast Asian Economic Growth, Compared With Equivalent-Sized U.S. Economies
(2006–11 compound annual average real growth, per cent)



Sources: World Bank; U.S. Bureau of Economic Analysis; The Conference Board of Canada.

Despite growth in SME activity in fast-growth markets, actual levels of activity remain low. While SMEs account for the vast majority of Canada's exporters, only one-tenth of all SMEs export goods and services. And those SMEs that do export account for less than one-third (in dollar value) of Canada's overall exports.[5]

Moreover, only a tiny group of SME exporters accounts for most of these exports: Less than 550 businesses account for more than 70 per cent of SME goods exports.[6] Canadian SME exports to the largest emerging economies (Brazil, Russia, India, and China) represented only $5.5 billion in 2009.[7] And most Canadian SME export revenue still comes from the U.S. market: 74 per cent in 2011, compared with only 7 per cent from Asia and 2 per cent from Latin America.[8]

1 Carney, "Exporting in a Post-Crisis World."

2 Ibid.

3 Ibid.

4 Office of the Chief Economist, Department of Foreign Affairs and International Trade, "Slides."

5 Sydor, "Internationalization of SMEs."

6 Ibid.

7 Industry Canada, "Canadian Small Business Exporters."

8 Sydor, "Internationalization of SMEs."

(continued …)

Why Look at Success Strategies for SMEs in Fast-Growth Markets? (cont'd)

Economic evidence shows that exporting companies are consistently larger, pay higher wages, and are more innovative and productive than non-exporters.[9] Moreover, entering new markets has been shown to improve company productivity.[10]

To boost Canadian business success in fast-growth markets (which are often very different from Canada's traditional markets), this briefing highlights the on-the-ground challenges that SMEs face in fast-growth markets and shares the strategies they use to overcome those challenges. We looked at lessons from successful Canadian and British companies.

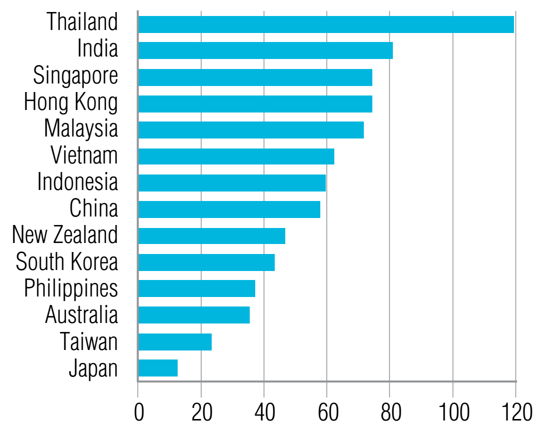
This is part of The Conference Board of Canada's "Tool Kit for Growth Markets," which provides tools and strategies to help Canadian companies—and those who develop policies to support them—to succeed in fast-growth markets.

9 Ibid.

10 Ibid.

Source: The Conference Board of Canada.

Share of Canada's Export Growth to Asia Accounted For by Companies With Fewer Than 200 Employees
(percentage)



Sources: Department of Foreign Affairs and International Trade; Statistics Canada.

Companies in the Study and Their Experience in Emerging Markets

CANADIAN COMPANIES

FORREC (www.forrec.com)
FORREC is a planning and design firm that creates entertainment and leisure environments worldwide. The company has done business in emerging markets in Asia since the 1980s, and since then has expanded into emerging markets in South America and the Middle East.

Intelysis Corp. (www.intelysis.com)
Intelysis is an investigative firm specializing in fraud and corruption investigations, partnership disputes, due diligence, and forensic accounting. The company started doing business in the Caribbean in 2004.

NOVO Plastics Inc. (www.novoplas.com)
NOVO Plastics offers a variety of engineered plastic components and assemblies for the automotive and consumer/commercial industries, including its innovative ECO2 line of products. The company started doing business in India in 2009.

Sandvine (www.sandvine.com)
Sandvine provides intelligent networking equipment and end-to-end network policy control solutions to broadband and wireless service providers. The company has done business in fast-growth markets in Europe, the Middle East, and Africa since 2003 and since then has expanded into 85 countries.

Trojan Technologies (www.trojanuv.com)
Trojan Technologies provides diverse water treatment solutions using environmentally friendly ultraviolet (UV) light in markets such as municipal wastewater, drinking water, and industrial processing. The company started doing business in emerging markets in Asia in 1999 and since then has expanded into emerging markets in South America and the Middle East.

BRITISH COMPANIES

J&D Wilkie (www.jdwilkie.co.uk)
J&D Wilkie is a global textile manufacturing company that provides products for commercial, defence, and medical markets. The company started doing business in China in 2004.

Mylnefield Research Services Ltd. (www.mrsltd.com)
Mylnefield Research Services Ltd. undertakes contract research, especially plant breeding, and licenses plant varieties internationally. The company started doing business in China in 2006.

Source: The Conference Board of Canada.

Experience Leads to a More Accurate Perception of How Significant the Challenges Are

Both over- and underestimating a challenge can hinder success. Overestimating a challenge that's easily solvable can result in a decision not to enter a fast-growth market and a lost opportunity for growth. Conversely, underestimating a challenge can result in a naive market entry with little chance of survival.

Perceptions of challenges vary due to differences across firms,[1] such as the level of international experience,[2] marketing capabilities,[3] and the fit between the SME and a particular fast-growth market. For example, entry into a fast-growth market will be perceived as easier—and is likely to be easier—when top managers have ancestry, family, or work experience in that market;[4] when foreign customers are actively soliciting a company's business; or when the company enters the market by piggybacking, such as supplying the foreign subsidiary of an existing domestic customer.[5] As a company's experience in fast-growth markets increases, its perceptions of the challenges become more accurate. (See exhibit.) This implies that owners and managers who are inexperienced with fast-growth markets should seek out ways to increase their experience using the experience-building tactics highlighted in this briefing.

1 Arranz and De Arroyabe, "Internationalization Process."

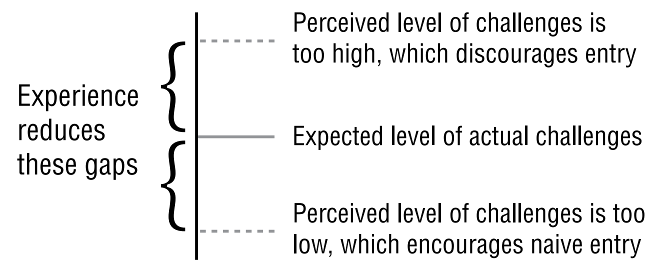
2 Baum, Schwens, and Kabst, "International as Opposed to Domestic"; Reuber and Fischer, "Targeting Export Support."

3 Baum, Schwens and Kabst, "International as Opposed to Domestic."

4 Riddle, Hrivnak, and Nielsen, "Transnational Entrepreneurship."

5 Erramilli and Rao, "Choice of Foreign Market Entry Modes."

With Experience, People's Perceptions of Challenges Become More Accurate



Source: The Conference Board of Canada.

CHALLENGES FOR CANADIAN SMEs IN FAST-GROWING MARKETS

This section outlines challenges that SMEs face when doing business in fast-growing markets, based on our review of the academic literature and interviews with owners and managers of SMEs. These challenges fall into two groups:[1] those related to the politico-economic environment of countries, such as laws, regulations, politics, and financing;[2] and those related to the sociocultural environment of countries, such as communication and the business practices associated with economic exchange. (See Table 1.)

POLITICO-ECONOMIC CHALLENGES

Cost of doing business: The cost of doing business, including the paperwork burden, can be higher in fast-growth markets than in developed markets. For example, the tax system in Thailand can result in double taxation for FORREC, which results in the need for expensive international tax expertise to navigate the double taxation treaty between Canada and Thailand.

Protection of people, assets, and intellectual property: In regions with a high crime rate, owners and managers need to be more vigilant about personal safety than they do in Canada. For example, the CEO of Intelysis always uses the same car and driver in Trinidad.

As well, companies that might have relied on patents for leading-edge technology to gain early advantage and sustain their sales in a developed foreign market may not be able to do so to the same extent in a developing market where there is a more serious threat of IP violations.[3] Weak IP regimes can make it hard to protect IP, and language barriers can make it difficult even to monitor whether IP is being violated. Even if a company finds a product bearing a counterfeit version of its label, it may not be cost-effective to find and accuse the violators. This means that SME owners and managers

1 Banalieva and Dhanaraj, "Home-Region Orientation."

2 Peng, Wang, and Jiang, "An Institution-Based View."

3 Levesque and Shepherd, "Entrepreneurs' Choice of Entry Strategy."

Lessons

Lessons for Canadian SME owners and managers:

- Your company should maximize its ability to learn from others and from experience, through ways such as these:
  - Think through sequences of market entries in culturally similar countries so you can use what you learned from one country for the next entry, and the reputation you built in one country is recognized in the next entry.
  - Look for opportunities to piggyback into a fast-growth market with an existing customer, while paying attention to developing your own opportunities when there.
  - Look for matchmaking and mentoring services offered by governments and international trade associations, as well as municipal "twinning" arrangements, to find strong local partners. Be prepared to commit to developing personal relationships in local markets (even though this can be difficult and time-consuming because of geographic distance and socio-cultural differences).
- Because customers in fast-growth markets have many companies vying for their attention, the quality and distinctiveness of your technology, products, and services will greatly influence interest in your company.
- Strong relationships, constant innovation, and leading-edge technology may offer some intellectual property (IP) protection in markets where formal IP protection is weak.
- Not all SMEs are suited to expand in fast-growth markets.

Lessons for policy-makers:

- Focus on supporting firms with the biggest likelihood of success: those with cutting-edge technology that recognize the need to make a long-term commitment to a market.
- Investigate the success factors of twinning arrangements, especially for Canada's smaller communities.
- Support the establishment of bridging and experience-building programs. Though headlines tout free trade negotiations as the main government tool to help companies succeed in global markets, SMEs need experience-building arrangements in order to learn and develop their reputations.

Table 1
Politico-Economic and Socio-Cultural Challenges that SMEs Face in Fast-Growth Markets

Politico-Economic Challenges	Socio-Cultural Challenges
Higher or unexpected costs of doing business, related to paperwork, tariffs, taxes, regulatory burden, and transportation	Differences in language and culture, which can hinder the building and maintenance of relationships
Need to protect people, physical assets, and intellectual property	Differences in business practices
Need to deal with political interference, corruption, and government interactions	Difficulty in obtaining information about market opportunities and conditions
Impediments to financing (access to capital for riskier activities, foreign exchange risk, payment delays)	Initial lack of credibility and reputation in the new market

Source: The Conference Board of Canada.

need to rely on informal control mechanisms to guard against opportunism and imitation, such as placing a premium on continuously nurtured relationships and continuous innovation,[4] to mitigate the risk of violation of formal control mechanisms such as patents.

4 Banalieva and Dhanaraj, "Home-Region Orientation."

Political interference, corruption, and working with governments: SMEs can be unprepared for political interference and outright corruption, which can result in lost bids as well as project delays. Also, working with government clients can be slow, and a slow pace can crimp cash flow. For example, while Intelysis receives payment from foreign companies within three to four weeks, it can take three to four months to receive payment from a foreign government.

If the Challenges Are So Great, Why Bother?

Why should SME owners and managers want to do business in challenging fast-growth markets? The reason is that more challenging markets can often yield a higher return. They may be more in need of expertise and products and technologies from elsewhere, and they may have greater growth potential. Indeed, FORREC thinks of fast-growing Asian markets in three groups: Singapore, Hong Kong, and Korea as the most advanced in terms of politico-economic infrastructure and doing business in ways that Canadians recognize; Thailand, Malaysia, and the Philippines in the next group; and China, Vietnam, and Indonesia in a third group that is less developed but offers the largest market growth potential.

Access to financing: Many young and small firms have trouble accessing financing for any foreign market expansion,[5] especially when they are entering fast-growth markets. Banks and investors perceive activities in fast-growth markets as risky, because it can be difficult to predict costs and revenues due to foreign exchange fluctuations and obstacles to receiving payments promptly.

SOCIO-CULTURAL CHALLENGES

Socio-cultural challenges are those that relate to an SME's ability to learn about, adapt to, and participate with market players in a fast-growth market. Formal trade initiatives such as free trade agreements, which focus on politico-economic challenges, tend not to address the socio-cultural challenges inherent in interpersonal relationships.

These challenges can significantly discourage entry into fast-growth markets. For example, among Internet-based companies, where politico-economic differences are less salient, a greater socio-cultural difference between a firm's domestic market and a foreign market is associated with a lower likelihood of entry into that foreign market.[6] However, this effect is dampened in large foreign markets, supporting the expectation that companies are likely to enter more challenging markets when there is a greater anticipated return.

Though socio-cultural challenges are reduced through foreign market experience, experience in one foreign market may not yield useful experientially based learning for a different foreign market. Companies that acquire experience in one context may draw erroneous conclusions about a new, very different context. This means that experience in developed foreign markets may not translate to knowledge of how to succeed in an emerging foreign market. Research has shown that this "incorrect learning" is exacerbated during fast-paced foreign expansion, because managers do not have enough time to thoroughly understand how particular actions lead to particular outcomes.[7] Thus, SME owners and managers need to find ways of gaining knowledge of the particular fast-growing market they are interested in entering, rather than assuming that it will be similar to foreign markets they are familiar with.

SMEs can be unprepared for political interference and outright corruption, which can result in lost bids as well as project delays.

With these comments in mind, we outline four groups of socio-cultural challenges:

Differences in language and culture, which can hinder the development of relationships. Language barriers should not be minimized. Relatively straightforward, but often costly, is the need to communicate in two or more languages. For example, Trojan Technologies needs to translate its written material and website content into many languages, and it is costly and time-consuming to keep them up to date.

More fundamentally, language barriers inhibit the establishment of personal relationships. The most effective network ties exist between individual people rather than at the company level, and even without language differences, the establishment of trusting personal ties between people in different markets is rare due to the distance.[8] When there are language barriers and both parties need

5 Riding and others, "Financing New Venture Exporters."

6 Rothaermel, Kotha, and Steensma, "International Market Entry."

7 Zeng and others, "Cultural Differences."

8 Rangan, "Search and Deliberation."

to rely on interpreters, the development of personal rapport is even more difficult. For example, Mylnefield Research Services Ltd. experienced few problems in day-to-day communications in China because the interpreters they relied on were effective; however, the Mylnefield people's inability to communicate directly in Chinese (and understand the nuances of what was being said) sometimes hindered their capacity to develop close business relationships.

Differences in business practices. Business practices, and cultural practices more generally, often differ substantially. This increases the learning curve for a Canadian SME entering an emerging market. The differences in business practices can affect the ongoing management of business partnerships, as well as their formation.[9] For example, NOVO Plastics has had to become accustomed to a much more personal way of doing business in India. Staff can't merely send a prototype in a courier package and rely on e-mail and phone follow-ups; they have to personally visit their clients' site quarterly to present the prototypes and discuss them with their engineering teams. In South America, Trojan Technologies had to adapt to working in a culture where time is often not of the essence.

Difficulty in obtaining information about market opportunities and conditions. Differences in language, culture, and business practices can hinder an SME's ability to obtain market information, because rich sources of information are inherently interpersonal and therefore difficult for outsiders to access.[10] When standards, conditions, tastes, and preferences are different in a fast-growth market from those in an SME's other markets, the SME will need to adapt its product or service. For example, NOVO Plastics needs to adapt its products to the climate and road conditions in India. Trojan Technologies needs to adapt its products because electrical, safety, and environmental standards and conditions vary widely among regions. In such situations, the firm's managers need to be plugged into the market enough to know that adaptation is needed, and they need to know how to get the information required to do the adaptation.

Lack of credibility and reputation in the new market. The importance of establishing credibility and reputation becomes evident when one realizes that while a new, unfamiliar market is risky to an SME, this SME is also new, unfamiliar, and risky to potential representatives, partners, and customers in the new market. These organizations may have many companies from all over the world vying for their business, and it can be difficult to get them to pay attention to an unknown player from Canada. SMEs need to be able to signal that they're a credible, trustworthy player in their industry and offer high-quality products and services.[11] A better reputation enables an SME to price higher and to attract higher-quality local representatives, partners, and customers.

EFFECTIVE PRACTICES TO OVERCOME THE CHALLENGES

The practices that SMEs use to overcome the challenges of fast-growth markets represent five goals. As Exhibit 1 shows, there is a hierarchical relationship among them, with the two goals on the bottom—maintaining technological advantage and focusing selectively—providing a foundation for others. A simultaneous emphasis on the two goals at the top—establishing a strong global reputation and developing internal knowledge about local markets—is important to success in fast-growth markets. However, given the socio-cultural barriers of doing business in emerging markets, a technological advantage and sound entry decisions alone rarely yield sufficient reputation and knowledge. Therefore, a fifth type of practice—the use of bridging arrangements—is necessary. All five practices are described below.

9 Zhou, Wu, and Luo, "Internationalization and the Performance of Born-Global SMEs"; Arranz and De Arroyabe, "Internationalization Process."

10 Johanson and Vahlne, "The Uppsala Internationalization Process Model."

11 For a discussion of signalling reputation to foreign markets online, see Reuber and Fischer, *Building International Sales in a Digitized Economy*.

MAINTAIN A TECHNOLOGICAL ADVANTAGE

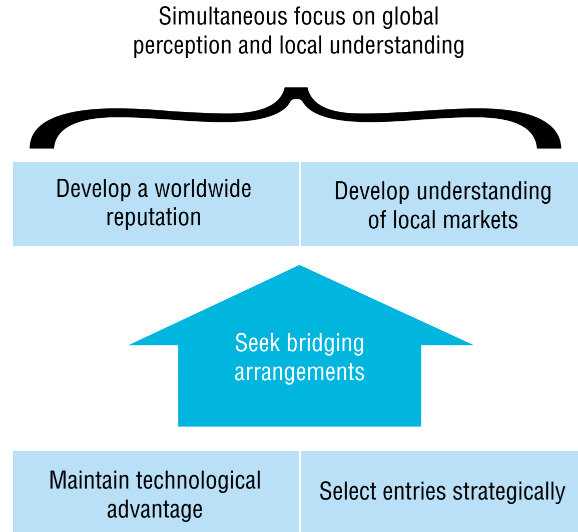
The SMEs that fare best in fast-growing foreign markets are those that maintain their innovativeness and a technological advantage over their competition. Where IP protection can be weak, ongoing technological capabilities provide advantages.[12] It is harder and costlier to imitate SMEs that are trailblazers offering something unique in the market. For example, Trojan Technologies' state-of-the-art knowledge of North American regulatory standards and regulations is attractive to regulators in emerging markets. The company has worked with governments and academics to develop water-related regulations where none existed or those in place were unclear, which bolsters their reputation. Moreover, Trojan honours its equipment warranty only if the equipment contains genuine Trojan parts. This warranty practice helps to combat IP violations.

A technological advantage also enables companies to charge high prices, and it enhances their reputation. For example, FORREC's innovativeness gives the company an edge in the lucrative front-end stages of development, where there are fewer competitors, and therefore lower cost pressures, than in the later construction stage. As well, clients are willing to pay extra to have FORREC on a project, since the company's reputation can make it easier for clients to obtain land, approval, and financing requirements.

Sandvine has found that providing innovative technology can be a way to gain access to a new market through small players in that market. Many fast-growth markets are characterized by a few giants and many smaller, newer competitors. While the large companies may be unwilling to make quick decisions and initiate market innovation, the newer firms, which are looking for ways to differentiate themselves and penetrate the market, are more likely to move quickly and transform the market. Once the smaller customers demonstrate the value of Sandvine's products, the larger, established companies are more likely to follow their lead.

12 Banalieva and Dhanaraj, "Home-Region Orientation."

Exhibit 1
Five Goal-Based Practices to Overcome the Challenges of Fast-Growth Markets



Source: The Conference Board of Canada.

How Do These Five Success Practices Address the Two Types of Challenges?

Politico-economic challenges can be mitigated by these practices, but are unlikely to be removed. Owners and managers of SMEs might be able to change the politico-economic infrastructure in which they do business by lobbying, but the process will be time-consuming, as the experience of Mylnefield Research Services Ltd. shows. Until 2004, the lack of an intergovernmental trade agreement between the United Kingdom and China prohibited trade in seed potatoes between the two countries. The managing director of Mylnefield Research Services Ltd. started lobbying in 2000 for his government to sign a trade protocol with China. The protocol was not signed until 2004, which delayed the company's market entry and took up much of his attention during this process.

Socio-cultural challenges can be mitigated in the short term by these practices, but ideally those challenges will be reduced or even removed in the longer term once an SME has gained experience in a given market.

Not All SMEs Are Suited To Expand into Fast-Growth Markets

Frequently, an SME's resources and capabilities just may not be sufficient for success in a fast-growth market. For example, if its products and services are of middling quality and the company is competing on the basis of low cost in developed markets, it may not be able to reach the level of technological sophistication required to succeed in a fast-growth market where it is unlikely to be able to compete on the basis of low cost.

If SME owners and managers are unwilling or unable to devote the necessary time and determination, they are unlikely to sustain sales in a fast-growth market. Both persistence and patience are required. All the people we interviewed emphasized the need to take a long-term perspective on doing business in emerging markets. It took NOVO Plastics a year or two to find the right local partner. Even after market entry, the president and the engineering managers spend two weeks in India every quarter. It can take Trojan Technologies two to four years to develop a new market. Trojan views a market entry as more than just a sale: It constitutes a presence in that market. For FORREC, repeat customers are the key to success. That requires trust, which takes time to develop.

On the other hand, innovative, technologically advanced SMEs can attract the interest of the highest quality customers that conduct their activities according to the familiar norms of multinational corporations. For example, NOVO Plastics' technology attracted the attention of India's larger automotive four- and two-wheeler manufacturers, many of which are sophisticated, savvy multinational companies that respect IP rights and have a history of forming partnerships with foreign companies. And these executives in the fast-growth markets are looking for the same attributes in their suppliers as would their counterparts in Canada and the United States, which reduces the socio-cultural challenges for the suppliers. Furthermore, having large Indian original equipment manufacturers (OEMs) as first customers in India also endorsed NOVO Plastics to other Indian and global automakers, thereby enhancing its worldwide reputation.

Finally, technological advancement also involves the ability to estimate demand. In a fast-growth market, demand is growing at a rapid, but unpredictable pace. Customers in those markets are wary of committing to a variable (per unit) pricing scheme, because, given the unpredictability of demand, it is hard for them to predict their total costs. Canadian companies have found benefits in offering an upfront fixed cost and a two- to three-year contract, which allows their customers to better predict the cost of serving their own customers. However, the Canadian SME needs to be able to estimate demand relatively accurately for this pricing scheme to be profitable.

SELECT ENTRIES STRATEGICALLY

A key decision for SMEs entering emerging markets is what to do, and where and when to do it. Selectivity is particularly important in the initial stages of doing business in fast-growth markets, because a broader scope of activity and geography is difficult to manage for an inexperienced firm.

In a fast-growth market, demand is growing at a rapid, but unpredictable pace, so Canadian companies have found benefits in offering an upfront fixed cost.

One aspect of being selective in entry is deciding what to keep in Canada and what to move offshore. Both FORREC and NOVO Plastics keep their head office and design activities (and, in the case of NOVO Plastics, manufacturing) in Canada, because a centralized location provides a cluster for high-quality work and is more cost-effective. This also helps to protect IP.

Another aspect of selective entry is deciding where to locate within a particular country. Because many countries with fast-growth economies are large and transportation is slow, a wrong choice can be constraining. NOVO Plastics' Indian customers are spread out in Delhi, Bangalore, Mumbai, and Chennai, and since travel times in India are very long, there have been no advantages so far in setting up a specific physical location in India. In this case, deciding where to locate has ended up being a decision to not set up in any one location.

An additional consideration in deciding where to locate in a particular country is the quality and responsiveness of local governments. They can have a significant impact on transparency and the ease of doing business, for better or worse. For example, Vietnam is troubled by severe and growing corruption, which favours state-owned enterprises over private firms. But that corruption varies greatly across Vietnam's provinces, and provincial governance policies, such as regulatory enforcement, influence its extensiveness.[13] This variation illustrates the importance of investigating which other foreign companies are doing business in a locale before committing to it: Lots of foreign activity in a region can suggest that other companies are able to operate there satisfactorily.

Selectivity is especially important early on. A broader scope of activity and locations is difficult to manage for a firm inexperienced in fast-growth markets.

A fourth aspect of selective entry is timing. Conditions will be more attractive to entry at particular times. India is a suitable locale for NOVO Plastics because of its favourable regulations for environmentally friendly products. Because Trojan Technologies looks for infrastructure spending when assessing a market's potential. For example, Brazil is attractive with its growing economy and infrastructure under construction for the 2014 FIFA World Cup and the 2016 Summer Olympics. Intelysis looks for markets with the need and desire to improve practice and the money to spend on it. Sandvine looks for markets where local firms are already looking for outside solutions to meet regulatory requirements; for example, in some countries, network operators need to adhere to new roaming charges regulations and are looking for technology to make that possible.

With respect to timing, owners and managers of SMEs also need to pay attention to the sequencing of market entries. Although an entry can be slow and involve setbacks, learning how to do business in one fast-growing market—such as finding an effective local representative, dealing with issues related to contract enforcement, and managing liquidity risks due to customer payment delays—can then be applied to subsequent fast-growth markets that are similar. This implies that SME managers need to be attuned to opportunities in similar countries in a region. They should plan subsequent entries coherently, to take advantage of this learning, rather than selecting markets haphazardly.[14] An additional advantage of a coherent entry strategy is that the reputational signal of success in one market will mean more to a subsequent entry in a similar region, because it indicates that the SME is able to do business in that particular politico-economic and socio-cultural environment.

DEVELOP A WORLDWIDE REPUTATION

A technological advantage and well-sequenced entries can help an SME develop a reputation for being able to do business successfully in emerging markets. SMEs can take additional steps to develop a global reputation. For example, Trojan Technologies perceives the water industry as global, and it has become a recognized player at that level. The company gives presentations at the major water conferences around the world. These are technical presentations based around case studies of projects, rather than sales pitches, and they are targeted at technical decision-makers, such as plant operators, consulting engineers, and regulators. This involvement in global events provides the side benefit of creating opportunities to network with local water industry experts.

Participation in such events can be costly, but even very new and small firms can communicate their foreign-market experience online. Intelysis, for example, obtained its first customer in the Caribbean through a story posted on the company website. When working on a fraud case for a Canadian company, Intelysis sent a team to Costa Rica to investigate gambling houses. There was news coverage of a raid, and Intelysis posted this on its website, together with a case study on the project. Soon afterwards, the Integrity Commission of Trinidad and Tobago was searching for a forensic accounting firm that had Caribbean experience, found Intelysis online, and then invited the company to bid on the job.

13 Nguyen and van Dijk, "Corruption, Growth and Governance."

14 Bingham, "Oscillating Improvisation."

Similarly, participation in high-level trade missions can enhance an SME's reputation abroad. NOVO Plastics gained credibility when its CEO joined a trade delegation to India with the Canadian Prime Minister and participated in business roundtable discussions with Indian counterparts.

DEVELOP UNDERSTANDING OF LOCAL MARKETS

A technological advantage and well-sequenced entries can help an SME understand local markets. As well, specialized trade agencies can provide valuable information. Both NOVO Plastics and FORREC see Export Development Canada and Foreign Affairs and International Trade Canada as having knowledgeable people on the ground who provide connections, market intelligence, reputational transfer, and information. NOVO Plastics was introduced to companies in India after meeting with Export Development Canada and then the Trade Commission Office in India. In Scotland, Mylnefield Research Services Ltd. gained initial knowledge of China through the China-Britain Business Council (CBBC), a private trade organization. Unlike government agencies, the Council specializes in China and has many offices there. It is inexpensive for an SME to join (membership costs roughly £870 annually for companies with annual sales under £7 million), and its services can be subsidized by government trade promotion organizations. With more than 800 members, CBBC is able to derive and share a wealth of information from and with its members. Due to its high-level connections in both the U.K. and the Chinese governments, the CBBC can help SMEs improve their government-related networks.

SEEK BRIDGING ARRANGEMENTS

Developing leading-edge technology and making sound market-entry decisions can help reduce socio-cultural barriers. Novel technology can bring a firm to the attention of blue-chip buyers who are similar to buyers in developed markets, and entering a market where the timing is right can attract buyers who are ready and able to purchase. However, in most cases, great technology and well-chosen market entries alone aren't enough to adequately reduce socio-cultural barriers and provide the needed reputational and learning benefits. It is therefore common for SMEs that are successful in fast-growth markets to develop arrangements that bridge the gap between themselves and a local market.

Bridging arrangements can help an SME learn about, and navigate within, a local market. As well, they can help a local market learn about the SME, making the SME seem less risky. The CEO of Intelysis points out a paradox: It is important not to be seen as a foreigner, even though it is often foreign expertise that is valued. Bridging arrangements can reduce perceptions of foreignness.

Bridging arrangements can take various forms. The most common is the establishment of a relationship with a trusted local representative or partner. Not only does a local partner provide a face for the SME, its in-depth knowledge of how things are done in that market can be invaluable. For example, NOVO Plastics noticed an expedited time frame after it started working with a local host that was familiar with the business landscape.

Having a local representative tells the market that the Canadian SME is committed to doing business there. Sandvine has noticed that representatives from many foreign companies are showing up in fast-growth markets hoping to make a quick and easy profit. They often arrive unprepared: shocked at the cost of hotels and support services, and knowing little about the local government, history and geography, and even the currency. They may enter into discussions with a local customer, and then never return. This makes companies in the fast-growth market wary of investing time in talking with foreign SMEs. Sandvine has found that taking the time to build relationships is an effective way to win back the trust that previous companies may have squandered.

Local representatives are particularly important for selling capital equipment projects such as Trojan Technologies has, and for design-based businesses such as FORREC, which have no tangible product to show clients. Accordingly, both of these companies need dedicated, full-time representatives in each market. In the past they have found representatives through word of mouth and conferences, but now that it has more experience with local reps and a better idea of what they are looking for, FORREC has had success through international recruiting agencies.

Mylnefield Research Services Ltd. uses its relationship with local partners to guard IP. The company educates local partners about the value of IP (in this case, plant variety rights) and transfers to them the responsibility to protect and exploit the IP by granting them exclusive licences in return for equity in a cooperative joint venture.

A second type of bridging arrangement is to enter an emerging market with a current customer or other relationship that the SME has in a developed market. For example, when deciding where to develop relationships in China, Mylnefield Research Services Ltd. followed both existing customers and academic relationships with U.K. and Chinese research organizations at Scottish universities. As well, Mylnefield gained knowledge of the Chinese market from its large domestic customers, which were already doing business in China. Piggybacking on an existing customer can expedite entry into an emerging market, and it can allow an SME to test the waters without making a big commitment. However, SME managers need to be cautious of over-reliance on a customer-following strategy because it may inhibit their own learning. They need to find their own opportunities as well.

A third type of bridging mechanism is a formal government-to-government agreement that promotes trade between two countries. J&D Wilkie leveraged its local government's close relationship with a sister city in China (see box "The Twinning Arrangement of Angus Council and Yantai") to negotiate a long-term, advantageous supply agreement with a Chinese manufacturer in China. This enabled them to win a large European order.

IMPLICATIONS FOR BUSINESS OWNERS AND POLICY DEVELOPMENT

Our study suggests a number of implications for SME owners and managers.

1. **Maximize your ability to learn**. The challenges—the socio-cultural challenges in particular—are enormous for SMEs that lack experience in fast-growth markets. Owners and managers should look for ways to maximize their ability to learn. At the start, they will have little experience to learn from, and so they should learn from others. Managers of Canadian SMEs that are more experienced in fast-growth markets can provide advice, and specialized trade organizations can provide knowledge about new markets. Bridging arrangements, such as having local representatives, piggybacking on current customers, and leveraging twinning arrangements can reduce the amount of direct market knowledge the SME needs at the outset. Planning the sequence of market entries coherently can make the learning from one entry relevant to the next one.

2. **Spend a lot of time building relationships**. In high-growth emerging markets, personal relationships play a more critical role than in developed markets. They can:
   - provide market-related information and accelerate learning;
   - provide credibility to an SME that lacks a track record in that market;
   - help develop relationships with foreign governments;
   - provide personal endorsements and referrals for further business opportunities;
   - help protect and monitor IP;
   - reduce financial and commercial risk through the trust that comes from repeated ties;
   - support the establishment, monitoring, and enforcement of legal contracts.

   However, although personal relationships may be more crucial than in developed markets, they are harder and costlier to develop because of geographic distance and socio-cultural differences. SME owners and managers need to be prepared to spend a lot of time in fast-growth markets and to develop personal rapport with key stakeholders while they're there.

3. **Innovate and develop a worldwide reputation to protect against IP risks**. Being innovative, and being seen to be innovative, helps to mitigate many of the challenges of fast-growth markets. Innovativeness can reduce the importance of formal IP protection, and can attract high-quality exchange partners and exchange

The Twinning Arrangement of Angus Council and Yantai

"Twinning" arrangements, or "sister cities," are not new. Vancouver established a twinning relationship with Odessa, Ukraine, in 1944 and currently has five such arrangements.[1] However, the Angus Council in Scotland is notable for the extent to which its municipality of 110,000 people was able to capitalize on a twinning relationship with Yantai, a Chinese city of 6.5 million people.

Not knowing where to start, the Council took the advice of the People's Republic of China Consulate-General in Scotland regarding an appropriate match. Yantai was chosen because its location in the northeast of China mirrored Angus's northeast location in Scotland. As well, Yantai's growing interest in golf and tourism, along with its vast agricultural lands and activities in offshore oil and gas, fit well with the Angus economy, which is based on SMEs and focused on golf, tourism, agriculture, and the oil and gas industry.

Initial contacts with Yantai were arranged in 1996, and a first mission to the city, in conjunction with a number of Angus SMEs, took place in 1998. The mission was led by Angus Council leaders, because government-to-government relations are key to the development of economic and cultural links with China. A Sister Twinning agreement was signed in January 1999. The agreement provides for reciprocal visits by representatives of the respective governments from each area, accompanied by business leaders, in order to foster business, economic, and cultural links.

The benefits of this twinning arrangement for Angus SMEs have been considerable. Going to China with Angus Council can give SMEs a gentle introduction to the market. Their credibility is immediately established, and the business contacts they meet will have already been vetted to some degree. The Council believes that this saves time and money, reduces risk, and builds confidence. The high-level ties inhibit dysfunctional opportunistic behaviour on the part of individual firms. Furthermore, the close relationship of Angus and Yantai has also provided a halo effect for Angus SMEs in other parts of China, giving them access to companies in larger cities, particularly Shanghai and Beijing.

However, reaping benefits from twinning is not a short-term activity. Officials estimate that they began to see benefits four years after signing the twinning agreement. The first notable benefit was a relationship between a golf course near Yantai and a golf course in Angus, which gave Angus much publicity in Yantai for golf tourism and a marketing platform for other economic activities. The Angus budget is small: roughly £10,000 a year for a biennial visit and hosting activities in the alternate year, plus half of a full-time-equivalent staff position on the Council's economic development team.

However, the Council clearly understood that this was a long-term initiative. Not only were the positive outcomes a result of having a highly committed champion at a senior level in both localities, it was also important to build and maintain good relationships with lower-level civil servants in the Yantai government. This is because while high-level government officials tend to move around, people at lower levels stay in place longer. They can "grease the wheel" when new officials get appointed, to provide continuity as well as access to information that a newcomer official might perceive as too sensitive to share.

1 Smith and Stewart, "Beavers and Cats Revisited."

terms. Moreover, an SME that plans to do business in emerging markets should think tactically about how to increase its visibility and reputation as a credible global player, both online and in globally oriented venues.

The study also has implications for policy-makers:

4. **Focus on innovative companies**. SMEs with a technological advantage are more likely to succeed in fast-growth markets. Therefore, government services should focus on companies with a cutting-edge technology and a willingness to commit to a market and learn.
5. **Further evaluate how formal bridging arrangements, such as twinning, can be effective**. Given the experience of Angus Council's relationship with China, twinning arrangements can be advantageous. They may be an advantage to smaller communities in Canada more than larger communities, because smaller communities are likely to have fewer links with foreign markets. They may also be more suitable to more hierarchical markets, such as China, where government intervention in economic activities is widespread. It appears that to succeed, such programs need to be structured and manned to provide continuity over a 5- to 10-year period. Despite

their ubiquity, little is known about the success factors associated with twinning initiatives, so this could be a fruitful area for further study.

6. **Facilitate bridging or "experience-building" arrangements.** Though headlines tout free trade negotiations as the main government tool to help companies succeed in global markets, experience-building arrangements are crucial for SMEs to learn and develop their reputations. Policy organizations need to facilitate networking and the development of bridging arrangements, both at home and abroad, and they must support existing networking programs.

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