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The Uppsala Internationalization Model and its limitation in the new era

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Abstract: The Uppsala Model has been one of the most discussed dynamic theories in Nordic School and International Business Studies and has affected many researches in the way to explain the process of internationalization of companies. This paper highlights the limitation of The Uppsala Model in order to describe the process of internationalization of companies in the new era of globalization. First I attempt to describe the theory itself, before to emphasise the changes in international business environment and its impact on the model and its limitation.

The Uppsala Internationalization Model

Swedish researchers (Johanson and Wiedersheim-Paul, 1975; Johanson and Vahlne, 1977) from Uppsala University had vast criticisms of the theories at the time, which explained international involvement. They believed most existing theories at that time toned down the problems of cultural differences and ignored the internal foundations needed so that companies could handle international activities. As a result Swedish researchers developed their own model as a more independent model to explain the sequential steps in the direction of increased foreign dedication (Johanson & Vahlne, 1977; 1990)¹. The model was based on empirical observation from four Swedish manufacturers and influenced by the works of Penrose (1959), Cyert & March (1963), Aharoni (1966) Vernon (1966) and others. The Uppsala Internationalization Model distinguishes four different steps of entering an international market, which cannot be viewed independently of a company's situation, market and the market knowledge. (See Fig. 1:1 below)

- Step 1: No regular export activities (sporadic export).
- Step 2: Export via independent representative (export mode).
- Step 3: Establishment of a foreign sales subsidiary.
- Step 4: Foreign production/manufacturing.
(Hollensen 2007)²

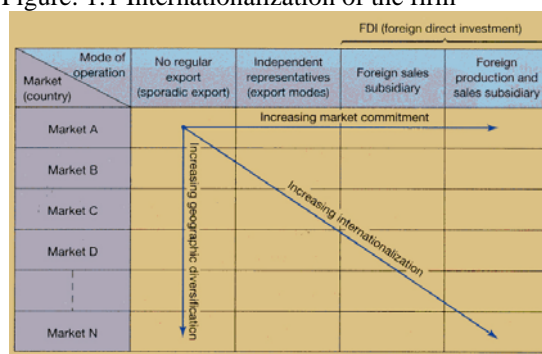
From the observation, they find out that companies normally start their expansion in a psychic nearby market. There, they have enhanced knowledge of the market and more control of resources, thereafter gradually when the companies have become more experienced and acquired better resources, they expand to the more distance market. (By distance market, they refer both to the cultural distance; as well the differences in language, politics, geographical and the difficulty to acquire knowledge and information from the market)³. Secondly, most often companies entered a new market through export before establishment of foreign sales subsidiary or foreign production.

¹ Johanson, J. & Vahlne, J.-E. (1977). The Internationalization Process of the Firm - A Model of Knowledge Development and Increasing Foreign Market Commitments. *Journal of International Business Studies*, <http://www04.sub.su.se:2065/stable/pdfplus/254397.pdf>
Johanson, J. & Vahlne, J.-E. (1990). The Mechanism of Internationalisation. *International Marketing Review*, <http://www04.sub.su.se:2131/insight/viewContentItem.do;jsessionid=3134E067D99179B71D1BF6089924F9FD?contentType=Article&contentId=855188>

² Hollensen S. *Global marketing*, 4th edition 2007, Pearson Education Limited, pp 63

³ *Ibid*, pp 64

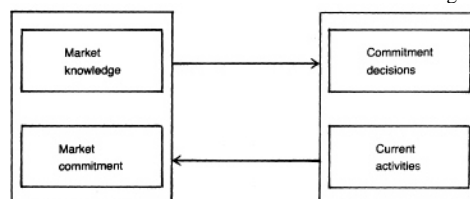
Figure: 1:1 Internationalization of the firm



Source: adapted from Forsgren and Johanson, 1975

In their study, they refer to (Aharoni, 1966) about the interdependence of market knowledge and market commitment and they develop a matrix model to illustrate the positive correlation between market knowledge and the commitment decisions, as well to emphasize the sequential development of market activities and its positive correlation to market commitment. The core explanation of the model is that increased market knowledge will lead to increased market commitment, and vice versa. (Andersen, 1993)⁴

Figure 1.2 The Basic of Internationalization-State and Change Aspects



They make a distinction between general knowledge and the specific knowledge. The former, which is more about the operation in the foreign market, can easily be transferred from one market to the other. It is important to note that the special knowledge, which is more specific to a particular market, cannot be achieved without specific activity in that market and it would be difficult to use this knowledge in other markets.

U-Model's limitation in the new global era

Even though the Uppsala Model has contribute greatly to broader understanding of internationalization process of companies but the model itself suffer in some fundamental bases to describe the Total Internationalization Process as it meant to be its original unit of analysis, even before we consider the changes in business environmental during the last 20 years and its impact on the theory's development. For example the model dose not shows much consideration to management incentive and its effect on decision making, or when they introduce the sequential four steps of market entry they ignored some other forms of market entries which are difficult to place on the model's scale, such as franchising which is considered to be a relatively less risky market entry and have the opportunity to build great market coverage and control (Doole, I & Lowe, R, 2008)⁵, or licensing which requires low levels of investment and provide

⁴ Andersen, O. 1993. On the Internationalization Process of Firms: A Critical Analysis, Journal of International Business Studies, Vol. 24, No. 2, pp. 209-231

⁵ Doole, I & Lowe, R, International Marketing Strategy, 5th Edition (2008), pp 243-244

considerable control over the market (Doole, I & Lowe, R, 2008)⁶ or strategic alliance and some other market operation. Other shortfall in the model is that it does not discuss the reason behind foreign direct investment and why should it be a desire as the ultimate market operation, or why should/would companies follow that step development. For example, why the export mode could not be the final step of internationalization?

However in the last 20 years the advancement in telecommunication, transportation and production technology has been enormous. The technology development has been probably the most influenced factor in the process of globalization and has both changed the contemporary business environment and provided means for the firms to responding to this change faster and better than before.⁷ As the same time we have witnessed tremendous changes in international trading environment, while the emerging economies such as China, India, Brazil and Russia are becoming major players in the international trade as well reduction of barriers to world trade through WTO, IMF and various trading groups and agreements,⁸ and in the other hand increasing cultural de-territorialisation as each culture is penetrated by the influences of other cultures⁹ has major influence on consumer behavior and market situation.

Rapid technology development and globalization has brought opportunity as well challenges to field of international businesses. Looking at the u-model in the contemporary business environment it highlights even more deficit in the original model which needs to be looked over and evolved in order to describe the internationalization process of modern companies. For example the original model has look at internationalization process purely as an internal capability and has ignored external factors such as market potential and competitive forces which has become more important in the global world and in some case even override the psychic distance factor in the management decision making.¹⁰

Johanson and Vahlne (1990)¹¹ presented no limits on the units of analysis for their model and have applied a broad generalization in their interpretation. It brings up the question whose behavior were they describing? SMEs, LSEs or MNCs..., however they mentioned, that large firms can be expected to take larger internationalization steps than small firms. But how would this imply to firms from emerging economies such as China and India? For example there is much evidence that Indian IT and pharmaceuticals companies primarily targeting USA and European market¹².

Service industries accounted for approximately 70% of total economic activity in the United States in 2006,¹³ and approximately 60% for EU-27¹⁴ and it has been one of the fastest growing industries sector in the industrial world. Even though considering the importance of service sector, most international business researches had had product orientated focus including U-model. Reihlen & Apel (2005)¹⁵ described the service

⁶ Doole, I & Lowe, R, International Marketing Strategy, 5th Edition (2008), pp 248-249

⁷ Doole, I & Lowe, R, International Marketing Strategy, 5th Edition (2008), pp 419

⁸ Doole, I & Lowe, R, International Marketing Strategy, 5th Edition (2008), pp 38-65

⁹ Doole, I & Lowe, R, International Marketing Strategy, 5th Edition (2008), pp 85

¹⁰ Hollensen S. Global marketing, 4th edition 2007, Pearson Education Limited, pp 64-65

¹¹ Johanson, J. & Vahlne J.E. 1990. The mechanism of internationalization. International Marketing Review, 7(4): 11-24

¹² Kundu, S.L., India Inc goes global, http://www.atimes.com/atimes/South_Asia/GK29Df01.html, 22 October 2008

¹³ Service Annual Survey, 2006, U.S. Department of Commerce, http://www.census.gov/svsd/www/services/sas/sas_data/historical/sas-06.pdf 22 October 2008

¹⁴ Pekka ALAJÄÄSKÖ, Industry, trade and services, European Communities, 2008
http://epp.eurostat.ec.europa.eu/cache/ITY_OFFPUB/KS-SF-08-078/EN/KS-SF-08-078-EN.PDF 22 October 2008

¹⁵ Reihlen, M. & Apel, B.A., (2005) Internationalization of professional service firms as learning – a constructivist approach, Department of General Management, Business Policy & Logistics, University of Cologne, Köln, Germany

sector as highly knowledge-intensive, provided by highly educated people, involve a high degree of customization, interaction, discretionary effort and personal judgment by the professional(s) delivering the service. However as the product manufacturing has been the primary focus of U-Model, a drawback for it is the failure to predict or describe the service industries behaviour in their internationalization process. For instance Reihlen & Apel (2005)¹⁶ find out that unlike more traditional firms that move gradually into international markets, Born Global firms internationalize quickly and contradictory to U-Model which believe market knowledge can only be acquired through activities on the market (experimental knowledge) (Forsgren & Johanson, 1992)¹⁷ Born Global Firms combine the experimental learning with other modes of knowledge creation such as learning through grafting, imitating or searching (Saarenketo et al., 2004)¹⁸. Like when the Swedish & Danish engineers Niklas Zennström and Janus Friis started their VOIP company's "Skype" in 2003, from very early beginning the company started to use international resources as they registered the company in Luxembourg, using American Bank finance and a team of software developer based in Tallinn and Estonia and within few months they expanded their services to the global market simultaneously.

The change in trend of internationalization process for Born Global firms could be due to that world has become much more homogeneous and that consequently psychic distance has decreased, as Nordström argued in 1990,¹⁹ however in the last few years we have been witnessing a complete reverse of internationalization process in entertainment and music industry such as many European and American artists looking for the successes in Tokyo and Japanese market even before the home market. Those artists after had released their work successfully in Japanese market and has acquired the resources and experiment then launch their work for the home market.

The same pattern of attitude has dominated the Fashion industry for many years, as artists and designer look at Paris, London and New York as the first market despite of their background. For example The Iranian designer Bijan after some unsuccessful attempt in the home and French market entered the American market and managed to become one of the most successful designer in US and international luxury fashion and jewelry market.

An important point here is to realize that the development of Information and Communications Technology (ICT) not only has transformed the business environment but had also had serious consequences for knowledge framework and generated fundamental different methodologies. This change is probably more tangible in the emerging and developing economies. Due to advancement in ICT access to information has become much more efficient and as a result more and more people become educated. (Approximately about 3 millions university graduate each year only in China)

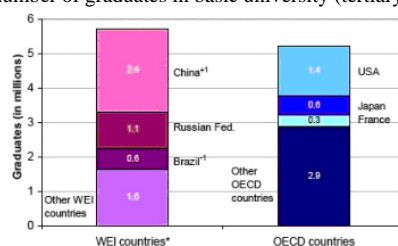
¹⁶ Ibid

¹⁷ Forsgren, M. and Johanson, J. (eds.), 1992, *Managing Networks in International Business*. Philadelphia: Gordon & Breach. P10

¹⁸ Saarenketo, S., Puimalainen, K., Kuivalainen, O. and Kylaheiko, K. (2004), "Dynamic knowledge-related learning processes in internationalizing high-tech SMEs", *International Journal of Production Economics*, Vol. 89 No. 3, pp. 363-78.

¹⁹ Nordström, K.A. (1990), *The Internationalization Process of the Firm in a New Perspective*, Institute of International Business, Stockholm

Figure 1.3 The number of graduates in basic university (tertiary type A education) 2005



Notes: * The total for WEI countries excludes India, Jamaica, Sri Lanka and Zimbabwe.
† Data refer to 2006; ‡ Data refer to 2004.
Source: UNESCO-UIS/WEI Education Counts, 2007, p.18.

With this information in our mind and basic understanding of supply and demand, we can predict the decrease of the value of knowledge.

As well as others, decrease of psychic distance and decrease of value of knowledge are probably the most contributing factors that U-model can not completely predict the process of internationalization of modern firms as those has been the foundation of the model. In the other hand I have to highlight that due to change of customer tastes in recent years which they have become more sophisticated and their purchase decisions are made less frequently on the basis of price or quality consideration but more influenced by perception of value.²⁰ This has influenced the commitment decisions in many firms as for many of them internationalization is not the matter of sales expansion any more but it has become the matter of survivor in the market. This would be natural that the management would accept higher risk in this circumstance.

Conclusion

The evidence indicated not only the external factors in the business environment has changed but it has also major impact on internal factors, such as management attitude, motivation and behavior, knowledge creation and transfer. All those changes have significant implications for theory reconstruction and development as it dose appear that the U-model despite significant contribution can not accommodate the new realities completely. As Sir Ken Robinson²¹ (2006) pointed out, in a highly competitive and rapidly changing environment in the field of knowledge, the factor of creativity and innovation become as importance as literacy in order to prepare ourselves for a uncertain future. As globalization has completely changed the basic parameters in business environment, the riskiest thing a company can do is to play safe (Godin S. 2003)²² and striving to minimize risk-taking, as radical innovation has often a great deal of uncertainty and risk. As the matter of fact many industries has understood this and changed and adopted their behavior in order to achieve competitive advantage. The challenge for researchers is not just to understand those changes but also in order to enrich our understanding of internationalization process and develop a dynamic model to explain this multidimensional phenomenon. The new researchers should focus not only on internationalization process but also focus on all surrounding processes and influenced factors such as culture, market, technology, social, political, behavior... and environmental changes. There is a need for more multidiscipline creative researches from various scientific fields in this phenomenon to be able to describe internationalization process in the contemporary world.

²⁰ Doole, I & Lowe, R. International Marketing Strategy, 5th Edition (2008), pp 382

²¹ Sir Ken Robinson: Do schools kill creativity? <http://www.ted.com> 30 October 2008

²² Seth Godin: Sliced bread and other marketing delights (2003) <http://www.ted.com> 30 October 2008