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## **SME Internationalization and Distant Emerging Economies: Exploring the Market Entry Role of Asian Global Cities**

**By Philippe Régnier**

Professor, School of Management (Fribourg and Genève)  
HES-SO // University of Applied Sciences Western Switzerland  
Chemin du Musée 4  
1700 Fribourg (Switzerland)  
Philippe.Regnier@hefr.ch

**and Pascal Wild (co-author)**

Assistant Professor, School of Management Fribourg  
HES-SO // University of Applied Sciences Western Switzerland  
Pascal.Wild@hefr.ch

### **Summary:**

This paper suggests a tentative conceptual framework to study the internationalization of foreign/OECD-based SMEs (Small and Medium-sized Enterprises) attracted by fast growing emerging markets, such as China and other Asian economies, and the supportive role of global cities as market gate focal points providing a wide range of financial and non-financial services facilitating emerging market entry. In other words, the hypothesis is that a number of global cities (about 75 cities are classified and ranked as such worldwide) play an important business intermediation role, including vis-à-vis distant and difficult regional emerging markets.

This proposed research is to bring up added value to the study of global cities, which has been envisaged so far exclusively in terms of their global growth as contributed by transnational corporations. The existing literature reveals that the business intermediation role of global cities has been studied in terms of services provided to transnational corporations and their affiliates, which tend to concentrate their regional offices and other business coordinating logistics and management in such cities.

The first part of this contribution aims to propose a conceptual framework that combines studies in international business management with a strong focus on SME internationalization on the one hand, together with knowledge from economic geography and urban studies with a focus on global cities on the other hand. In the second part of this contribution, an empirical study of Swiss SME internationalization vis-a-vis distant Asian emerging markets and their relative direct and indirect presence in so-called alpha-type global cities provides some first-hand scientific evidence illustrating the proposed conceptual framework. The findings derived from the empirical study tend to demonstrate the high importance of global cities for European internationalizing SMEs – as illustrated in the Swiss case - especially when it comes to far distant emerging market penetration and market development in countries with strong cultural differences from the SMEs home market.

**Key words:** International business management, SME internationalization, distant emerging markets, global business intermediation functions of global cities.

## Introduction:

Internationalization of SMEs (below 250 employees and annual turnover of maximum Eur 43 Mio. according to the EU definition) refers to non-domestic activities of SMEs, namely to various types of external ventures ranging from (i) exports of goods or services, (ii) marketing & technology partnership, and to (iii) foreign direct or indirect investment overseas.

This subject has been studied conceptually and empirically since the 1970s, but no single theory has been able to capture all the dimensions of the SME internationalization process (Che Senik, 2011 ; Coviello 1999; Gankema, 2000, Fujita 1998; Philipps 1994; Rialp et Rialp, 2001; Zahra & George, 2002 ; Zuchella 2007). Available data is mostly limited to SME exports and is systematically collected in a limited number of countries. OECD SMEs tend to expand overseas either gradually (majority of SME cases) or as globally born-SMEs (start-ups for instance) (e.g. Bell et al., 2001, 2003; Coviello & Jones, 2004; Coviello & Munro, 1995, 1997; Fujita, 1998; Johanson & Vahlne, 1977, 1990, 2009; McDougall & Oviatt, 1994, 2000). Most SMEs tend to internationalize in trans-frontier markets and in markets of proximity (i.e. European SMEs within Europe). Accessing distant and highly foreign markets is more difficult for a wide range of reasons (Baldegger, 2013 ; OECD 2013).

Due to the rapid expansion of the Asian region, a rising number of OECD SMEs has been considering this region as a new business growth destination. However, geographic distance is not the only access barrier. Local cultures and languages, reliability of economic and financial information, business and political networking, judiciary and legal environment, mobilization of human and financial capital, technology and knowledge partnerships are also perceived by most OECD SMEs as potential risks to be considered before/when moving to emerging Asia (Ojala, 2008; Reuber 1997; Ruzzier 2006, Schueffel 2008).

SMEs are the backbone of most OECD economies, esp. Europe and Japan. Similarly, Swiss SMEs are one of the two pillars of Swiss manufacturing, which still weights 22% of national GDP. As many Swiss SMEs are highly specialized, the strength of the SME sector has also contributed to the first ranking classification of Switzerland in the annual global competitiveness report for a number of years (Régnier & Wild, 2016).

Due to the small size of the domestic market, high production costs, shortage of labour and a strong currency, Swiss SMEs tend to internationalize within Europe/EU first (78%), over the Atlantic, and more recently to distant emerging markets. Emerging Asia ranks as the second destination of Swiss SME exports ahead of North America - which ranked as third export market even before the 2008 global financial crisis (Baldegger, 2013). With a total number of slightly more than 300 000, 99,7% of all Swiss firms are SMEs. They are mainly family-owned (80%, and 48% purely family-based) Source and account for 67,5% of total employment (Habersaat et al., 2001). According to the *Swiss International Entrepreneurship Survey 2013* based on a sample of about 800 Swiss SMEs, most of the surveyed SMEs were set up before 2008 (Baldegger, 2013). Even though 60% of Swiss jobs depend on exports, only 28% of those surveyed SMEs are “international“, meaning sell abroad. 93% of their exports go to Europe, and especially neighbour countries (France, Germany, Italy). In addition to geographic proximity, these markets offer business/contractual /language/standards practices close to the Swiss ones. Interestingly, 49% of the surveyed SMEs exports go to the Asia continent, ahead of North America (40%). South America, Australia and Africa weight 25%, 21% and 19% respectively. 62% of the surveyed SMEs were not born global, and have internationalized gradually, first through trading activities (Journal Swiss-Asia Chamber of Commerce 1/2012, SIES Survey, 2013).

The core research question is whether the internationalization of Swiss SMEs to non-traditional and distant emerging markets can be enabled by the business facilitation environment provided by global cities, such as in emerging Asia for example. The main

hypothesis is derived from the *Global Entrepreneurship Monitor (GEM)*, and especially from a recent series of GEM data-based scientific articles suggesting the need to study the entrepreneurial roles of global cities (Acs, 2002, 2004, 2008 ; Currid, 2006; Doel 2002; Friedmann, 1986; Sassen 2001; Taylor, 2004). This research paper identifies a possible conceptual framework and, empirically, whether Asian global cities (such as Tokyo, Hong Kong, Mumbai, Shanghai, Singapore,...) are being used as foreign SME business hubs vis-à-vis regional emerging markets.

This paper offers a review of (i) the existing knowledge related to SME internationalization, and of (ii) the various theories of global cities and their business services. A conceptual framework is then proposed and also guides an empirical study of the case of Swiss SMEs exploring Asian emerging markets and possibly use global cities of this region as business entry points.

## **1. International business management and SME internationalization**

Internationalization of firms has been studied across different research domains such as strategic management, entrepreneurship, international business, organizational theory and small business economics (Zucchella & Scabini, 2007; Ruzzier et al., 2006; Peiris et al., 2012; Bell et al., 2003).

It has been recognized that SME growth is essential for any national economy (Coviello & Munro, 1995). SMEs perceive growth as a necessity for various reasons and decide to go international (Fujita, 1998). Internationalizing SMEs have to overcome hurdles, such as organizational change, adaption of strategy, products, marketing and distribution (Ruzzier et al. 2006; Zucchella & Scabini, 2007). They have to cope with challenges such as cultural and language differences, geographical distance, etc. (Johanson & Vahlne, 1977, 1990, 2009). SMEs active internationally are seen as more performing than non-internationalizing ones (EU-Japan Centre for Industrial Cooperation, 2012; Fujita, 1998). In fact, without good performance, lean management and quality products, survival is very difficult (OECD, 2009). SME internationalization patterns and market entry strategies have been studied (Bell et al., 2001, 2003; Coviello & Jones, 2004; Coviello & Munro, 1995, 1997; Fujita, 1998; Johanson & Vahlne, 1977, 1990, 2009; McDougall & Oviatt, 1994, 2000). However, not a single theory has been able to encapsulate the whole SME internationalization process (Bell et al., 2003; Coviello & Jones, 2004; Gankema, Snuif, & Zwart, 2000; Kraus, 2011; Ruzzier et al., 2006; Schueffel & Baldegger, 2008; Zahra & George, 2002; Zahra, 2005; Zucchella & Scabini, 2007).

### **Limitations in the use of MNC theories**

SME specialists suggest that theories, mainly derived from internationalization of MNCs, cannot be fully applied to SMEs (Ruzzier et al. 2006). Differences in terms of size, internal resources, management, and external outreach strategy make difficult to apply such theories across the board. However, they may provide a holistic understanding of internationalizing SMEs, for instance by focusing on the costs of transaction to internationalize. The Owner Location Internalization paradigm (OLI) explains the different ownership advantages for a MNC to go international through the accumulation of intangible assets, the improvement of supply chain management and the mobilization of other productive factors depending on geographical factors (Ruzzier et al. 2006). As SMEs have more limited resources than MNCs, the optimal use of their internal/external resources are crucial. This is where the business hub role of global cities can play a role, even though MNC affiliates and subsidiaries have been the major categories of firms using them widely so far.

### **SME internationalization theories: The Uppsala Model and beyond**

Different models of behaviors have been identified regarding SME internationalization. In the 1970s, SME internationalization was considered a gradual or incremental process. Two models were developed: The “I-Models” or “Innovation models”, and the “U-Models” or “Uppsala models”.

In the I-Models, each SME internationalization step is seen as an opportunity (Gankema et al., 2000), and the main focus is on the export capacity (Ruzzier et al., 2006). In general, three steps are identified: 1) Pre-export, 2) Initial Export, and 3) Advanced Export.

The U-Models suggest that a firm increases its international linkages through gradual overseas market learning (Johanson & Vahlne, 1977, 1990). New competences are acquired incrementally to enter new “psychic distant” markets as the process involves differences in language, education, and business practices.

Both models envisage internationalization as an accumulation of small steps. Stage models have been criticized as being “deterministic”. However, especially U-Models have been widely applied and have made a huge contribution to the understanding of SME internationalization.

Since the 1990s, a new type of SMEs has been identified as “born global” or “international new ventures” (Bell et al., 2003; Oviatt & McDougall, 1994; Schueffel & Baldegger, 2008). Such firms target global “lead markets” (Bell et al., 2003) and have global activities since the very early phase of their creation (i.e. some start-ups in ICTs). They have generally high and specific skills and/or proprietary technologies used as competitive advantage. These global start-ups internationalize rapidly and do not fear “psychic” distance. Definition efforts have been proposed in recent years, and have contributed to the identification of a new research domain in international entrepreneurship, whose boundaries are still being discussed (McDougall-Covin et al. 2014). Bell (2003) proposes an integrative model of SME internationalization, which explains the differences between traditional, born global and born-again global firms. It suggests a causal link between the SME internal knowledge and the chosen mode of internationalization.

### **SME network and resource-based approaches**

SMEs entering distant markets need to consider financial, marketing and organizational implications. In order to shed light on these aspects, two additional analytical models are useful.

The network approach considers any firm as a part of business networks. It looks into the linkages between its business development and the role of external actors. The analysis is derived from the U-Model, as Johanson adopts a network perspective to explain internationalization motives (Zucchella & Scabini, 2007).

The resource-based view (RBV) is derived from strategic management, and it analyses the use of resources to develop competitive advantages. Resources can be tangible (e.g. capital, facilities), intangible (e.g. patents, knowledge), or in the form of capabilities (e.g. ability to determine entrepreneurial opportunities) (Zucchella & Scabini, 2007). Both approaches consider “internal” and “external” resources as the total assets of a firm. The development of both models go “hand-in hand” (Ruzzier et al., 2006).

### **SME market entry and business development services (BDS)**

According to Fujita (1998), SMEs generally choose among several modes to enter a market: licensing, subcontracting, know-how and technology transfers, foreign direct investment (FDI), joint ventures, international partnerships and management contracts, merger and acquisitions. In order to overcome financing limitations and to mobilize other resources, SMEs can get public or private business facilitation from supportive institutions or from B2B linkages (Fujita, 1998; Bell, 2003).

Based on the existing literature on BDS, a clear distinction is made between financial services provided by various institutions (accounting and auditing firms, banks, brokers, credit guarantee funds, insurance companies, ...), and non-financial or technical institutions (coaching, training, legal counseling, technology incubation, scientific and testing services, etc.) (Fujita, 1998). This distinction is usual among academics and practitioners. Banking and other financial services are one world in itself, and all other types of services are “technical” with various sub-categories. Since post-1989 neo-liberal globalization, deregulation and privatization, this divide has been enriched by a second distinction between private and public services, later somehow reconciled by the promotion of so-called public-private partnerships (PPPs), and considered as more efficient to promote SMEs. Since 1999-2001, the concept of BDS has been introduced by leading international consulting firms, including the OECD and the World Bank. The concept of BDS covers financial and technical services contributing to a friendly entrepreneurial eco-system and a pro-SME regulatory environment facilitating business internationalization. The supply of BDS should be market-driven and with limited public intervention (White, 2001).

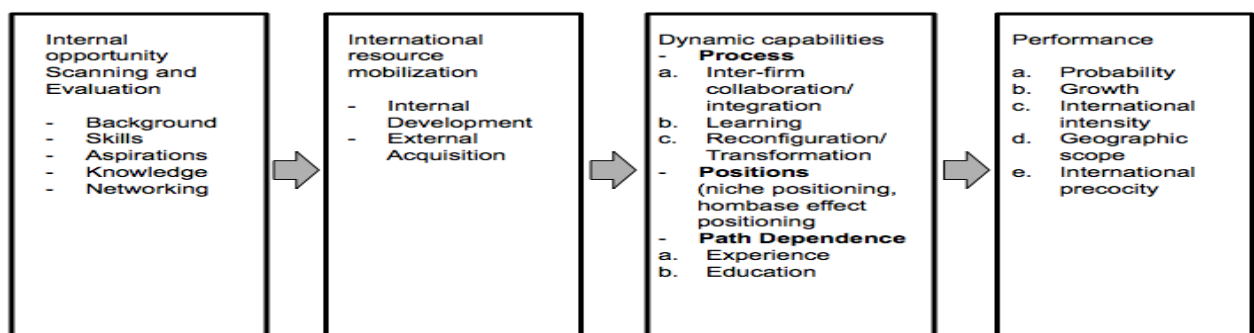
### SME internationalization integrative model

Different integrative models have been developed (Ruzzier et al., 2006; Zahra & George, 2002; Zucchella & Scabini, 2007). The graph here below includes the main SME theoretical contributions.. An SME can mobilize resources either internally, or acquire them externally. Internal development refers to investment and innovation. External acquisition refers to strategic partnerships in order to “introduce new products, services and ideas in the market” (Zucchella & Scabini, p. 126). It involves SME outreach to a wide range of financial and technical inputs provided by business linkages, supportive organizations and/or inter-personal networks.

In order to “integrate, build and reconfigure internal and external competencies [...] the SME depends on managerial processes, position and path dependence” (Zucchella & Scabini, p.128). The SME managerial process commands the coordination and integration of resources to enter a market and its local environment. Path dependence concerns SME entrepreneurial learning characterized by its educational and practical experience (SME entrepreneur and senior management). It involves aspects of organizational learning.

Measuring international performance is complex “as it may be measured in terms of profitability, growth, export intensity, geographic scope and international precocity” (Zucchella, 2007, p.134).

Figure 1: An Integrative Model for International Entrepreneurial Organizations



Source: Zucchella & Scabini, 2007, p.126

### ***SME internationalization to distant markets***

SMEs are understood as foreign to a given distant market. The notion of distance can be geographical but also cultural and even psychological. SMEs generally choose among several modes to enter distant markets: licensing, subcontracting, know-how and technology transfers, foreign direct investment (FDI), joint ventures, international partnerships and management contracts, merger and acquisitions. Each mode can be conceived in a consecutive and gradual manner, and it has various types of internal financial and organizational implications (Fujita, 1998). A number of studies have been conducted using either the network and/or the resource-based approaches.

### ***Network approach***

Based on the revisited U-Model of Johanson & Vahlne (2009), recent studies analyze “ the process of how an SME actively enters its internationalization-relevant network ” (Schweizer, 2013, p. 81). They focus on OECD high innovative SMEs developing new international networks to distant markets, in particular to Japan and South Korea. The process contains four phases:

Phase 1: Recognition of the existence and liability of outsidership (not being part of the relevant networks)

Phase 2: Identification of the relevant network

Phase 3: Re-bundling of the firm’s resources and capabilities

Phase 4: Accessing, managing, and leveraging opportunities identified in the new network

(Schweizer, 2013, pp. 97–98)

Based on the study of internationalizing Malaysian SMEs, the relevant network approach can be explained in more details (Che Senik and al., 2011). According to this model, an SME network is constituted of supportive institutions (government agencies), business associations and personal relations. Such linkages can initiate awareness, as well as trigger, strengthen, and sustain SME internationalization (Che Senik, p. 273).

### ***Resource-based approach***

Some authors have investigated the changes in terms of actors, activities and mobilized resources during the SME internationalization process (Nummela, 2002), often combined with the network approach (Smiler and Gil, 1986). Numela for instance has studied the internationalization of Finnish manufacturing SMEs and their interaction with external and supportive institutions (business associations, professional consultants, public services, subcontractors, universities). Ojala also underlines the importance of supportive networks in the internationalization process of knowledge-based Scandinavian firms interested to enter the Japanese market (Ojala, 2009). Most available studies tend to focus on software SMEs and the development of linkages with larger clients without taking into account a holistic approach as indicated on figure 2 (Moen, Gavlen, & Endresen, 2004; Reuber & Fischer, 1997; Zain & Ng, 2006).

### ***Knowledge management approach***

As part of the resource-based approach, recent studies underline the role of internal/external knowledge mobilization and management, introducing a clear distinction between gradually internationalizing SMEs and globally-born SMEs. In the first category, SMEs do mobilize their internal knowledge of proximity markets, where they have started to internationalize during the first 5-10 years of the process. Globally-born SMEs are for instance young start-ups in high tech, which perform in very specific segments of high tech markets in manufacturing or services, and can (but not always) expand overseas rapidly, including to distant markets.

### ***Vicarious learning***

SMEs may capitalize on internal knowledge accumulated during their initial phases of internationalization, especially vis-à-vis markets of proximity, and then expand gradually to more distant ones, in order to connect in particular to difficult emerging markets such as in East Asia.

They may also source external knowledge from other SMEs and business networks having already established such connections and accumulated experience locally. Vicarious learning is one of the concepts developed by social cognitive theories developed since the 1960s (Bandura, 1952, 1977).

Internationalizing SMEs tend to learn from other SMEs, which are not necessarily direct competitors or may be even active in different sectors. What matters is that these SMEs have already penetrated distant emerging markets, and they may share both their difficulties and success stories.

### **SME internationalization theory: tentative conclusion**

No theory has so far captured the whole SME internationalization process. The Uppsala model developed in 1977 and revised in 2009 has remained dominant and serves our research project along two key concepts as follows:

- SMEs tend to internationalize gradually and incrementally, and seldom to distant markets before having accumulated first hand experiences in foreign markets of proximity. For instance, recent surveys show that since the last decade, Asian markets represent Swiss SMEs' second export destination behind EU markets of proximity (*SIES, 2013*).
- SMEs have to cope with high risks and transaction costs to reduce the “distance“ between overseas markets. SME network economics shows that SMEs need to identify both functional and social networks to access reliable business information and access distant markets. Such networks are even more crucial to penetrate new emerging and unknown markets, where incomplete and unstable market institutions still prevail.
- Identification and use of functional and social networks by SMEs imply access to territorial and institutional actors providing business intermediation services to approach distant and risky markets such as in emerging East Asia.

## **2. Global cities: Interdisciplinary approach and theories**

It is generally accepted that a global city is a major urban center that represents an important node in the world economic and financial system. The emphasis is put on the regional, international and global linkages of some cities. They are an object of research interest in various disciplines such as geography and urban studies, history, economics, sociology, politics, and more recently entrepreneurship and management (*Global Entrepreneurship Monitor reports since 2007-08*).

### **Definitions**

Considering the importance of past cities (e.g. Rome in the Roman Empire, cities in the Hanseatic network) (Abu-Lughod, 1989; Braudel, 1984; Dollinger, 1970), social sciences have studied the role of cities as economic, historical, geographic, political, and socio-cultural centers (Currid, 2006; Friedmann, 1986; Jacobs, 1969, 1984). Cities are viewed in a global city network (Castells, 1996, 2011; Sassen, 1991, 2001; Peter J. Taylor, 2004). A global city is an important node in the global economic system (Beaverstock, Smith, & Taylor, 1999; Castells, 1996, 2011; Doel & Hubbard, 2002; Friedmann, 1986; Jacobs, 1969, 1984; Sassen, 1991, 2001; Peter J. Taylor, Derudder, Faulconbridge, Hoyler, & Ni, 2014; Peter J. Taylor, 2011, 2004).

The *GEM data* has inspired scientific articles (Acs, Bosma, & Sternberg, 2008), and a new research avenue has emerged aiming at the integration of entrepreneurship combined with the entrepreneurial eco-systems of global cities. Such eco-systems offer high spatial concentrations of services that may not only facilitate entrepreneurship but also act as business hubs for MNCs and SMEs venturing to distant markets. For instance, Tokyo is ranked in third position by *Foreign Policy* behind New York and London (2012 *Global Cities Index*).

### **International classification of global cities**

The concept of 'global city' was first promoted at Princeton University by sociologist Saskia Sassen in her book *The Global City: New York, London, Tokyo* (Sassen, 1991). The term 'world city' goes back to the 19th c. describing the control of a disproportionate amount of global business as suggested by the *Illustrated London News* related to the port of Liverpool in 1886. Patrick Geddes also used this term later in 1915 (Doel, 2002). The role of global cities is compared to other categories of cities (Jacobs, 1969; Friedmann, 1986; Jacobs, 1984), to their relation in networks of cities (Taylor, 2004), or in terms of high concentrations of services (Acs et al., 2008; Castells, 1996). The first attempt to better categorize and rank global cities was made in 1998 by British academics (Beaverstock and al., 1999). They established the *Globalization and World Cities Research Network* (GaWC) as a kind of roster ranking cities based on their connectivity through four "advanced producer services": accountancy, advertising, banking/finance, and law. The GaWC inventory identifies three levels of global cities and several sub-ranks. Since 2004, it has included some new indicators while continuing to rank city economics more heavily than political or cultural factors. It has contributed since 2008 to the following categorization:

**Alpha++** cities are London and New York City, which are vastly more integrated with the global economy than all other cities.

**Alpha+** cities complement London and New York City by filling advanced service niches for the global economy.

**Alpha** and **Alpha-** cities are cities that link major economic regions to the world economy.

**Beta** cities are cities that link moderate economic regions to the world economy.

**Gamma** cities are cities that link smaller economic regions to the world economy.

**Sufficiency** cities are cities, which concentrate a sufficient degree of services so as not to be dependent on world cities.

In 2008, *Foreign Policy*, in conjunction with the Chicago-based consulting firm A.T. Kearney and the Chicago Council on Global Affairs, published a ranking of global cities, based on consultation with S. Sassen and others (2012 *Global Cities Index* and *Emerging Cities Outlook*). It was noted that world's largest and most interconnected cities help the setting of global agendas, weather transnational dangers, and serve as hubs of global integration. They are engines of global growth and gateways to regional resources. The main parameters are: "Business activity" (30%), "Human capital" (30%), "Information exchange" (15%), "Cultural experience" (15%) and "Political engagement" (10%) (*Foreign Policy*, 2008). This index has been updated every two years until 2014. In all rankings, New York, London and Tokyo rank first. Looking at East Asia, Beijing, Hong Kong, Singapore and Tokyo are among the top ten global cities, whereas Seoul (12th), Shanghai (18th) Kuala Lumpur (39th) and Bangkok (42nd) lag behind.

### **Command and control center**

In history, there have been command centers, where important decisions influenced a nation, a region or even a continent. For example, in the Roman Empire, Rome was the control center of a whole empire. Most of the time, cities are capital cities, but in the ancient Northern European Hanseatic system, a sea-based city would gain importance mainly from trade (Taylor, 2004). This was reproduced later in East Asia by Hong Kong and Singapore as trading city-states.



Friedman (1986) analyzes the “spatial organization of the new international division of labor” and the inter-linkages among cities. He suggests a hierarchical categorization of cities between core/primary and peripheral/secondary cities. Later in the 1990s, he focused on their “economic articulations” (Taylor, 2004).

### **Concentration of services**

Jacobs (1984) defines dynamic and static cities. Dynamic cities project economic activities as centers of innovation and trade, and concentrate human skills. In contrast, peripheral or static cities do not contribute to overall economic wealth. They are trading houses where goods are only conveyed but with little added value. They tend to remain the “hinterlands” of dynamic cities (Taylor 2004).

Due to globalization, Sassen has brought up the concept of inter-connected cities. She identifies global cities as world servicing centers concentrating manufacturing activities and services, with a high propensity for innovation (Sassen, 1991). If we refer to the post-1990s concept of business development services (BDS), it can be argued that global cities offer a high density of BDS, and play crucial functions in corporate internationalization modes.

### **Networks of cities**

Another focus is to envisage global cities in terms of their linkages to other cities (global and not). Jacobs (1984), Sassen (1991), Castells (1996) and Taylor (2004) adopt a geographic and spatial approach. There is space for cities and transaction flows in the world system. Thanks to ICTs, products and services can be interconnected across borders, independently from their spatial location, and global cities take leadership in this transnational process. Such interconnectivity stimulates within and among global cities a highly entrepreneurial environment based on information, knowledge, creativity and innovation (Taylor, 2004). These concepts are quite distant from the more traditional notions of global cities envisaged as control or command centers.

### **Entrepreneurship and globalization**

Global cities can be analyzed through various lenses (hierarchical functions, servicing concentration, networking integration), and different typologies can coexist. For example, in the case of Europe, besides London and Paris, several other types of strategic cities coexist in a relatively small spatial geography, Geneva or Zurich are far more global than many others despite their small population.

Recent conceptual research tries to link urban and geographic studies to other scientific domains such as entrepreneurship: New York can maintain its first class position as a global city thanks to a special concentration of brain and creativity (Currid, 2006). Based on previous authors (Fritsch & Falck, 2007), leading scholars have started to use *the Global Entrepreneurship Monitor* combining national data surveys for over 70 countries to study the global status of world cities (Acs et al. 2008). The focus is centered on their role as facilitators of corporate internationalization, mainly MNCs but also increasingly SMEs. Global cities offer a top quality entrepreneurial milieu, which facilitates MNCs and even SMEs to venture into domestic, regional and intercontinental markets. Micro processes interconnect different spaces, time zones, and both real and virtual flows. Using global cities as entry points, interconnections with more ‘static cities’ in the ‘hinterland’ seek resource optimization and entry simplification to psychic distant markets. As indicated by Zucchella & Scabini (2006), a firm may benefit from ‘strategic enhancement’ as follows:

- Easy access to reliable information by means of B2B associations, service centers and corporate consortia, reduce search costs;
- Knowledge and technological spillovers are possible thanks to high numbers of Schumpeterian imitative processes and high rates of business spin-offs;

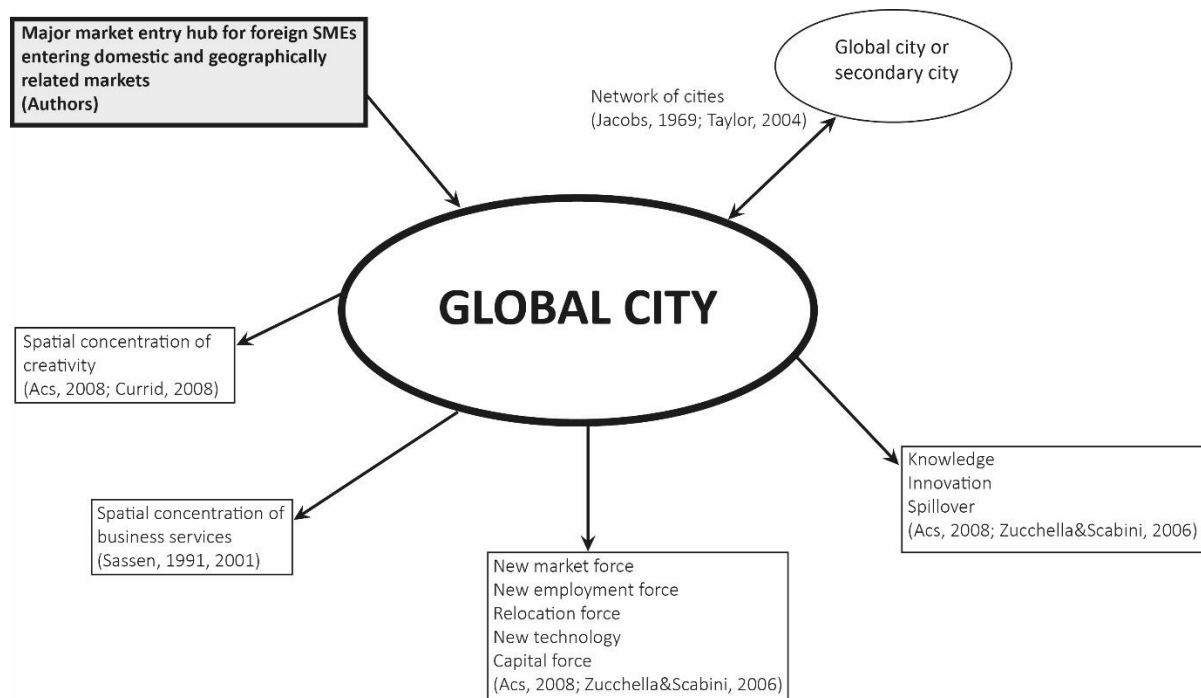
- Access to human resources are facilitated, in particular to highly specialized professionals;
- Rapid connections are made available to backward and forward linkages associated to international value chains and large domestic or regional markets;
- Variety of options are offered to share infrastructure, logistics and networks among firms and subsidiaries located close to each other. (Zucchella & Scabini, 2007, p. 95).

### Theory of global cities: tentative conclusion

Existing theories have established that global cities are territorial nodes essential to the sustainable development of world trade and financial flows along global value chains. Furthermore, due to their high concentration of foreign MNCs and affiliates, they provide an exceptional density of specialized services and project various types of entrepreneurship capacities linking their hinterland to regional and world markets.

As global cities offer a wide range of functional and social networks used but also reinforced overtime by global MNCs, a small number of transnational SMEs (mainly from the OECD economies) are making a similar utilization of global cities. It remains to be seen, through SME sample surveys and best practice case studies, how and how far foreign SMEs access global cities as providers of BDS needed to facilitate and secure their access to distant and risky emerging markets. The high costs for SMEs to access global city services may be compensated by an equivalent reduction of business risks and of downstream market transaction costs. Thanks to global cities' BDS, SMEs may increase confidence and securitization when initiating business deals locally with emerging markets. Otherwise, SMEs may fail and loose much by going direct.

**Figure 2: Design of proposed conceptual framework**



Source: designed by the authors

### 3. Methodology:

This paper has an interdisciplinary ambition to cross-fertilize two areas of knowledge, namely:

- entrepreneurship and international business, with a focus on SME internationalization,
- economic geography and urban studies, with a focus on global cities.

The central research objective is to produce conceptual and practical insights to guide SME internationalizing processes in the use of business development and networking services provided by a number of global cities. The proposition is that such services mainly available in global cities may prove to be crucial for foreign SMEs to minimize risk and increase operational efficiency to enter attractive but distant/difficult emerging markets such as in East Asia.

A global city is generally considered as an important node in the global system. This concept is derived from world economic history, development economics and urban geography, but more specifically by sociology since the early 1990s. Inspired by the masterpieces of S. Sassen (1991, 2001), it suggests that globalization is facilitated by strategic hubs according to a hierarchical organization of the global trade and finance system. The study of global cities has been produced by geographers, historians, and sociologists, but its integration in international business studies, and SME internationalization in particular, is a recent proposal. It was initiated by the *Global Entrepreneurship Monitor*, and derived from a highly ranked paper by Acs, Bosma and Sternberg (2008) titled *The Entrepreneurial Advantage of World Cities: Evidence from GEM Data*. The paper suggests that global cities provide specific entrepreneurial climate, which has much to do “with cultural richness, economic diversity, international connectivity and infrastructure excellence that is not available in any city “ (Acs, 2008, p 5). Other authors such as Taylor (2004) or Fritsch and Falck (2007) underline that qualitative entrepreneurship features are still lacking in most metropolitan studies. They refer to quality of professional life, mobilization capacity of needed resources, availability of technical supportive services and venture capital, spatial proximity to both customers and suppliers, concentration of industrial knowledge and business regional networks.

Empirical data and evidence have been collected since the late 1990s in the case of multinational corporations and their various modes of presence in global cities, but so far not in the case of internationalizing foreign SMEs.

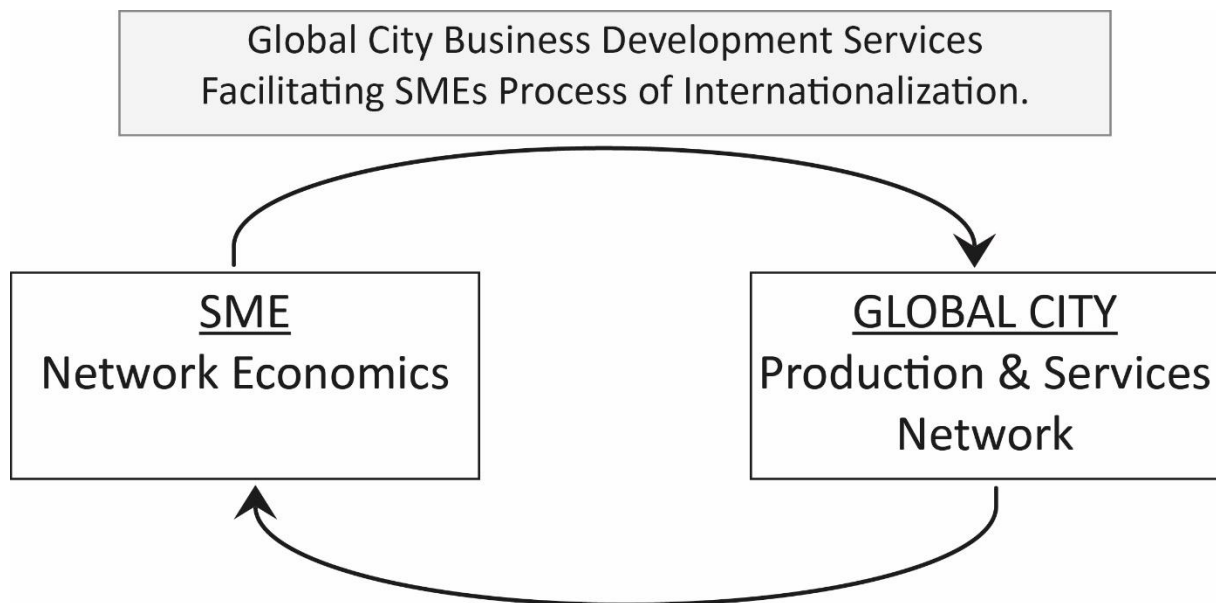
The empirical part of this contribution delivers an empirical study of Swiss internationalizing SMEs to distant markets and their utilization of global cities. This study is derived from the *Swiss International Entrepreneurship Survey 2016* conducted by the School of Management-Fribourg, and which is the largest SME internationalization survey conducted in Switzerland every 3 years.

### 4. Conceptual framework proposal

This paper aims to propose the construction of a conceptual framework, which combines two sources of knowledge, namely SME internationalization theories and global city theories. SME quantitative and qualitative surveys exist in a number of global cities, but they concentrate mainly on the study of domestic SMEs, and consider both domestic and foreign SMEs as only one SME category. In addition, national SME surveys available do not concentrate on major cities exclusively, and not on the specific category of global cities. Theories and classifications of global cities have been built so far and exclusively based on MNC data. This is due to the magnitude and visibility of MNC presence in global cities, and by available access to their data (also electronically) in each global city. A similar exercise to

be extended to internationalizing SMEs present (directly or indirectly) in global cities is much more difficult and remains to be conducted locally and on a comparable global scale.

**Figure 3: Proposed conceptual framework**



Source: designed by the authors

The cross-fertilization of the two sources of scientific knowledge enables to propose a conceptual framework in order to conduct research on the use of functions and services of global cities by foreign internationalizing SMEs to distant emerging markets.

First, SME internationalization theories as a sub-component of SME economics and management are embedded in small business network economics. This means that such internationalization relies on both functional and social networks to be identified and mobilized through global cities in order to reduce market entry risks and transaction costs.

Second, theories of global cities have established that they represent major hubs of global production and service networks. Parts of these networks are also constituted by dense business interlinkages among global cities within continents and across continents.

The combination of these two sources of knowledge lead to the proposal that global cities can and do provide services to foreign SMEs, which are integrated in their core functional and social networking capacities to link their hinterland (regional markets) and the global origins of foreign internationalizing SMEs.

Empirically, research work cannot be carried on a random basis like it has been done to measure quantitatively and qualitatively MNC presence in global cities through their affiliates, subsidiaries and representative offices. It has to rely on two sources of SME internationalization data, which can be collected (i) in the country of SME origin, and (ii) in the global city of BDS intermediation, depending on the location of the final distant market targeted by that specific SME.

In the country of origin, such as Switzerland for instance, it requires a fairly large quantitative and qualitative research apparatus to be able to document the numbers and profiles of local SMEs already in the internationalizing process, and using for instance Hong Kong and/or Singapore as global trading cities to reach China and Southeast Asian markets.

In the global city of BDS intermediation (i.e. HK or Singapore), it requires the selection of a sample of foreign SMEs, for instance Swiss SMEs, using in one form or another the functional services and social networks concentrated there as enablers to access neighbor emerging markets.

As a word of caution, the authors do not suggest that all foreign SMEs make an exclusive use of global cities to internationalize. Some SMEs may find other routes to access distant markets by themselves, and sometimes more directly. However, preliminary trial interviews indicate that such cases are seldom (esp. in B2B transactions), and face high risks and business hazards in difficult markets such as China or Indonesia. Hong Kong or Singapore are perceived as costly, but do provide reliable and often unique financial, marketing and technical expertise enabling foreign SMEs to internationalize on most solid and sustainable ground.

## **5. Empirical Study**

In order to gather first empirical evidence to operationalize the proposed conceptual framework and to validate or not the proposed hypothesis, an empirical study was conducted during the first semester of 2016, and focused on Swiss internationalizing SMEs (SIES Survey 2016).

The Swiss economy is rated as the world's most competitive (Schwab, Sala-i-Martin, Samans, & Blanke, 2016) since many years in a row. This is partly due to its rather high population of SMEs, representing 99.6% of all existing firms (Swiss Statistics, 2009). A number of Swiss SMEs are global leaders in their respective niche markets. Due to the limited size of the domestic market, many have to explore international markets in a very early stage of their lifecycle.

### **Sample**

Between April and July 2016, an empirical survey focused on the profile of Swiss internationalizing SMEs was conducted by the School of Management – Fribourg together with a Swiss public bank.

Swiss Statistics provides very general SME databases classifying them according to their location, industrial branch and size (number of employees). However, it is not possible to extract a selection of internationalizing SMEs due to rather limited information available. Therefore, a major Swiss private business information vendor was mandated to generate a sample of relevant SMEs. A sample of 18'000 SMEs was randomly selected, each firm generating at least 10% of its annual turnover from foreign markets. The number of employees for each selected SME would not exceed 249 full-time-equivalents in order to correspond to the largely accepted SME definition by the European Union.

The SME sample represents eight different industrial sectors and SMEs can be subdivided into micro-enterprises (0 to 9 employees), small enterprises (10 to 49), and medium-sized ones (50 to 249).

According to Jaeger & Toni (Jaeger & Thöni, 2008), about 14% of all Swiss SMEs export and 13% have even invested overseas. Based on such evidence, the number of Swiss internationalizing SMEs is estimated to approximately 43'000. Finally, almost half of this population has been randomly selected and 17'097 personalized letters and structured questionnaires have been disseminated all over Switzerland.

### **Measures**

Each SME was asked to indicate its world business destinations and its turnover percentage by world region. Furthermore, each SME was invited to specify in which global city it has a direct representation (such as its own branch or a purchasing office), or an indirect representation such as a business partner, a distributor, etc. The selected global cities belong to the three highest ranking categories, namely alpha ++, alpha + and alpha.

**Table 1: Classification of world regions and global cities**

World Region	Alpha Global Cities
North America	Chicago, Los Angeles, New York
Central America (incl. the Caribbean)	Mexico City
South America	Sao Paulo
Western Europe	Amsterdam, Brussels, Frankfurt, London, Madrid, Milano, Paris
Eastern Europe (excl. Russia)	<i>No alpha global cities in this region</i>
Russia and Central Asia	Moscow
Near and Middle East	Dubai
North East Asia (China, South Korea, Taiwan, excl. Japan)	Beijing, Hong Kong, Shanghai
South Asia (incl. India, Sri Lanka, Nepal)	Mumbai
South East Asia (ASEAN)	Singapore
Japan	Tokyo
Australia / New Zealand/Oceania	Sydney
North, East, West and Central Africa	<i>No alpha global cities in this region</i>
Southern Africa	<i>No alpha global cities in this region</i>

Source: Classification by the authors with data from GAWC 2012

Most of the alpha global cities can be assigned to Western Europe, followed by North America and North East Asia. Many world regions have one major global city. In Eastern Europe and Africa global cities can be only ranked under the “alpha – “ category. The first three are Johannesburg, Prague, and Warsaw.

In addition to this, each surveyed SME was asked to indicate the date of its foundation, the year of its first export, and specific strengths and weaknesses related to its international business activities.

## Findings and Results

### *Respondents and sample bias*

With a total of 609 validated questionnaires, the return rate of this survey was around 3,5%. In order to assess any possible non-response bias, a comparison was carried out between respondents and non-respondents with regard to their normal attributes (i) industry affiliation and (ii) SME size-category.

Most of the responding SMEs can be allocated to the electrical, mechanical, electrical or metal work sectors, followed by others active in manufacturing (such as agro- food, automotive, clock and watch) and by services (such as banking, insurance, real-estate, IT and other types of consulting).

**Table 2: Responding SMEs by sector**

Industry type	Respondents		Non-respondents		Difference
Mechanical engineering, electrical - and metal industry	164	27.5%	2512	15.2%	-12.3%
Chemical industry, medical engineering, pharmaceutical industry and cosmetics	61	10.2%	515	3.1%	-7.1%
Other manufacturing industry (food, car, watches etc.)	119	20.0%	5391	32.7%	12.7%
Trade	84	14.1%	1688	10.2%	-3.9%
Building industry	16	2.7%	852	5.2%	2.5%
Transport	24	4.0%	1223	7.4%	3.4%
Banks, insurances, real estate, IT, consulting	111	18.6%	3655	22.2%	3.5%
Nurse, medical health, welfare etc.	17	2.9%	652	4.0%	1.1%
<b>Total</b>	<b>596</b>	<b>100.0%</b>	<b>16488</b>	<b>100.0%</b>	

Source: Analysis by the authors with SIES 2016 data.

Note: A total sample of 596 SMEs was validated in terms of sectoral categorization. Differences among sectoral representation may produce misleading results but only when comparing various SME manufacturing sectors. For the more generic analysis of SMEs across sectors, the sample represents rather well the total population of Swiss internationalizing SMEs.

Slightly more than half of total respondents belong to the category of micro-enterprises (below 9 employees). In contrast, every third respondent (10%) belongs to the small category, and a minority (2%) to the medium-size one (between 50 and 249) belonged to the smallest group of respondents.

**Table 3: Responding SMEs by size**

Size	Respondents		Non-respondents		Difference
MICRO ENTERPRISES (0-9 EMPL.)	319	52.47%	10858	65.85%	13.39%
SMALL ENTERPRISES (10-49 EMPL.)	207	34.05%	4527	27.46%	-6.59%
MIDDLE ENTERPRISES (50-249 EMPL.)	82	13.49%	1103	6.69%	-6.8%
TOTAL	608	100%	16488	100%	

Source: Analysis by the authors with SIES 2016 data.

### ***Results on SME internationalization***

As shown in table 4 below, Swiss SMEs tend to internationalize mainly in developed markets with little physical and psychical distance from the home market. Western European markets are the nearest and rank as the most popular foreign markets. Western Europe is then followed by more distant and some emerging markets such as Eastern Europe, North America and North East Asia. Near and Middle East, Russia and Central Asia as well as South East Asia and Latin America rank in the middle class. Other markets are small due to their underdeveloped status such as Africa and South Asia, or due to their physical distance such as Oceania. Japan combines the complexity of geographical and cultural distance.

**Table 4: Responding SMEs by size and regional destination**

<b>World Region</b>	<b>Percent SME (0-249 empl., n609)</b>	<b>Percent Micro (0-9 empl., n320)</b>	<b>Percent Small ( 10-49 empl., n207)</b>	<b>Percent Middle (50- 249 empl., n82)</b>
<b>Western Europe</b>	81.0%	75.6%	84.5%	92.7%
<b>North America</b>	35.5%	27.8%	39.6%	54.9%
<b>Eastern Europe (excl. Russia)</b>	30.7%	25.6%	31.4%	48.8%
<b>North East Asia</b>	27.4%	17.2%	32.9%	53.7%
<b>Near and Middle East</b>	22.8%	18.4%	25.6%	32.9%
<b>Russia and Central Asia</b>	19.5%	15.9%	18.8%	35.4%
<b>South East Asia (ASEAN)</b>	19.5%	13.4%	22.7%	35.4%
<b>South America</b>	16.7%	12.5%	19.8%	25.6%
<b>Japan</b>	16.1%	11.9%	16.9%	30.5%
<b>Australia / New Zealand / Oceania</b>	15.4%	13.1%	16.4%	22.0%
<b>South Asia (incl. China, South Korea, Taiwan, excl. Japan)</b>	15.1%	12.8%	12.6%	30.5%
<b>Central America (incl. The Caribbean)</b>	9.5%	7.5%	10.6%	14.6%
<b>North, East, West and Central Africa</b>	9.5%	8.1%	8.7%	17.1%
<b>Southern Africa</b>	9.0%	6.6%	10.6%	14.6%

Source: Analysis by the authors with SIES 2016 data.

### ***The intermediation role of global cities***

251 out of 540 SMEs had either an indirect or a direct representation in a global city. Due to the limited internal resources of SMEs, it comes as no surprise that indirect business representation modes, such as contracting a partner or a distributor are much more popular than direct representation ones, e.g. own branches of production or distribution and sales, overseas.

Responding SMEs tend to use distant global cities such as Hong Kong, Tokyo, Shanghai or Singapore almost equally as compared to well established ones in Europe such as Frankfurt,



London and Paris. When comparing the direct versus indirect presence of Swiss SMEs in alpha-type global cities vis-a-vis their respective world region of location, Tokyo ranks first, ahead of Mexico City, Singapore and Moscow.

In world regions having one major business hub, such as Tokyo for Japan, Mexico City for Mexico or Moscow for Russia and Central Asia, the relative importance of such global cities for Swiss internationalizing SMEs is tremendously high. In emerging regions with more than one alpha-ranked global city such as North East Asia and South East Asia, between one third and one half of Swiss SMEs active in such emerging regions do cultivate important links with such global cities.

**Table 5: Swiss SME direct/indirect use of global cities**

<b>Total</b>	<b>Indirect</b>	<b>Direct</b>	<b>City</b>
<b>69</b>	59	10	Hong Kong
<b>69</b>	64	5	Tokyo
<b>68</b>	49	19	Frankfurt
<b>64</b>	48	16	London
<b>62</b>	45	17	Shanghai
<b>61</b>	48	13	Paris
<b>59</b>	52	7	Milano
<b>58</b>	48	10	Singapur
<b>56</b>	50	6	Dubai
<b>52</b>	41	11	Peking
<b>52</b>	45	7	Moskau
<b>50</b>	45	5	Amsterdam
<b>46</b>	43	3	Brüssel
<b>46</b>	41	5	New York
<b>44</b>	38	6	Madrid
<b>41</b>	36	5	Sao Paolo
<b>37</b>	31	6	Mumbai
<b>35</b>	32	3	Toronto
<b>34</b>	30	4	Chicago
<b>31</b>	26	5	Los Angeles
<b>30</b>	27	3	Mexico
<b>29</b>	28	1	Kuala Lumpur
<b>29</b>	25	4	Sydney

Source: Analysis by the authors with SIES 2016 data.

**Table 6: World regions and SME business use of respective global cities**

<b>World Region</b>	<b>Number of SME in this Region</b>	<b>Alpha (++, +) Global City</b>	<b>Percentage share of SME with a link to the global city / world region</b>
<b>Japan</b>	98	Tokyo (1)	70.41%
<b>Central America (incl. the caribbean)</b>	58	Mexiko City (2)	51.72%
<b>South East Asia (ASEAN)</b>	119	Singapur (3)	48.74%
		Kuala Lumpur (12)	24.37%
<b>Russia and Central Asia</b>	119	Moscow (4)	43.70%
<b>North East Asia (incl. China, South Korea, Taiwan, excl. Japan)</b>	167	Hong Kong (5)	41.32%
		Shanghai (9)	37.13%
		Beijing (10)	31.14%
<b>Near and Middle East</b>	139	Dubai (6)	40.29%
<b>South Asia (incl. India, Sri Lanka, Nepal)</b>	92	Mumbai (7)	40.22%
<b>South America</b>	102	Sao Paolo (8)	40.20%
<b>Australia / New Zealand / Oceania</b>	94	Sydney (11)	30.85%
<b>North America</b>	216	New York (13)	21.30%
		Toronto (14)	16.20%
		Chicago (15)	15.74%
		Los Angeles (16)	14.35%
<b>Western Europe</b>	493	Frankfurt (17)	13.79%
		London (18)	12.98%
		Paris (19)	12.37%
		Milan (20)	11.97%
		Amsterdam (21)	10.14%
		Brüssel (22)	9.33%
		Madrid (23)	8.92%

Source: Analysis by the authors with SIES 2016 data.

### ***Market entry intermediation role of Asian global cities***

A more in-depth analysis was conducted regarding the sub-sample of Swiss SMEs having business activities through global cities localized in East and South East Asia. Surprisingly, not all of these SMEs seem to generate a significant turnover from these two Asian world regions. Some of them seem more active elsewhere (Japan, Western Asia), and some have even business links with these global cities without generating any significant turnover from within these two world regions.

In South East Asia, 119 SMEs (19,5% of the sample) generate at least 5% of their annual turnover from this world region. 46 have a link with Singapore and/or Kuala Lumpur, and 18 among them with one or both cities, but without generating any business from South East

Asia. 13 out of these 18 SMEs are using either or both cities to reach another Asian world region, mostly North East Asia (11 SMEs). Five of the 18 SMEs generate their whole turnover outside Asia, but use Singapore and/or Kuala Lumpur to connect with global markets through the Pacific and beyond.

**Table 6: Swiss SMEs and global cities in North East and South East Asia**

		Does the company have a direct or indirect link in a South East Asian global city?		Total
		No	Yes	
Does the company have a turnover from the South East Asian world region?	No	472	18	490
	Yes	73	46	119
Total		545	64	609

Source: Analysis by the authors with SIES 2016 data.

		Does the company have a direct or indirect link in a North East Asian Global City?		Total
		No	Yes	
Does the company have a turnover from the North East Asian world region?	No	413	29	442
	Yes	83	84	167
Total		496	113	609

Source: Analysis by the authors with SIES 2016 data.

The same analysis has been conducted for North East Asia, where 50% of the Swiss SMEs generating some business from this world region have a link to one of the major global cities of the region: Beijing, Hong Kong, Shanghai. Here again, 29 of the 113 SMEs with direct or indirect links to these global cities do not generate any turnover from North East Asia. 17 make profit in other Asian world regions, and 12 do not in any.

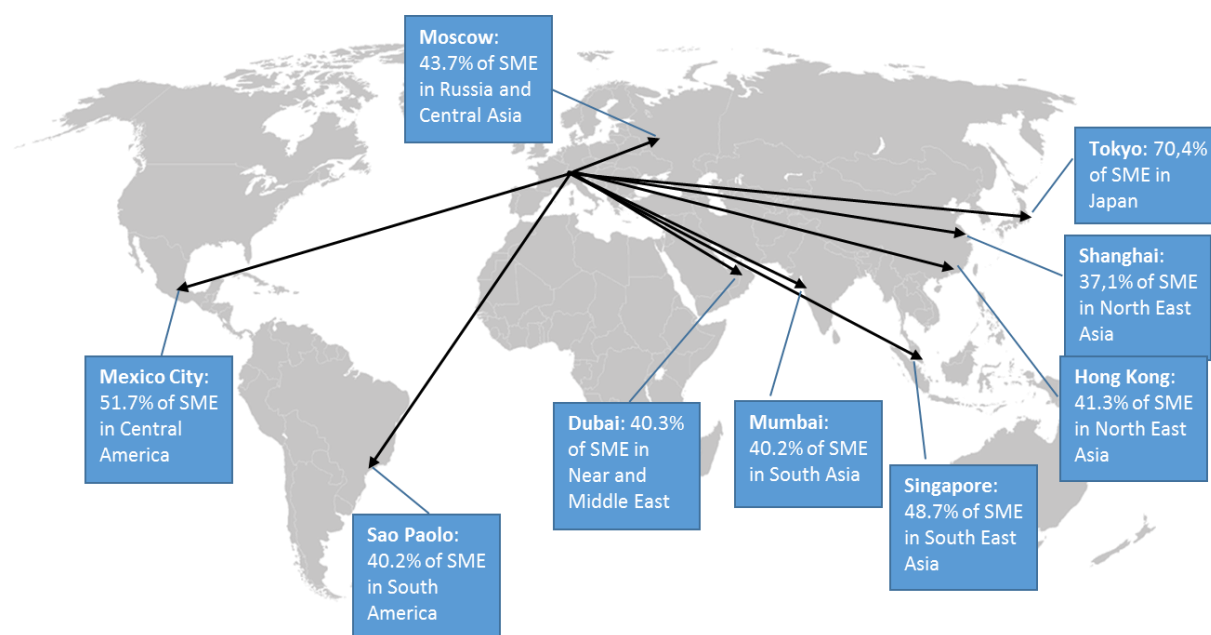
Within this sample no significant difference was found when considering the age, sector and size for each surveyed SME. Chi-squared test results resulted as non-significant for these three variables.

## 6. Final analysis

The hypothesis proposed at the beginning of this paper seems to be validated. At least, our Swiss SME empirical survey suggests that the higher the level of physical and psychical distance between the domestic and emerging markets, the more the strategic importance of global cities rises. Almost 70% of Swiss SMEs operating in distant Japan do have a (mainly indirect) representation in an alpha global city such as Tokyo to reach both the Japanese market and neighbor ones like Korea and Taiwan. Similar correlations were found for Mexico

City and both Central American and Caribbean markets, for Moscow and both Russia and Central Asia, or for Singapore and South East Asia. Such cities are major global cities in their respective world region.

**Figure 5: Swiss SMEs use of global cities by major world region**



Source: Analysis by the authors with SIES 2016 data.

The profile of SMEs with linkages to global cities do not seem to differ significantly from other SMEs in terms of age, size, and timing of internationalization. What is rather surprising is to observe that some SMEs may use directly or indirectly Asian global cities even without developing business activities in the world region corresponding to the localization of the global city concerned, and sometimes without any operation in Asia at all. This may indicate that such cities have become fully global and are primarily used as global business intermediation hubs, including for some SMEs. This should not be a too big surprise as East Asia in particular has become the third pillar of the global economy since a few decades. Through their business linkages with Asian global cities, Swiss like other OECD SMEs want to benefit from the strong business networks and services concentrated in these cities in order to penetrate world markets, and especially specialized segments and niches along global value chains. In some cases, it can go as far as developing in depth partnerships and even R & D for SME product development or marketing innovation.

### ***Implications for theory***

This conceptual paper and its first hand empirical survey suggest that other similar SME internationalization and global city studies should be conducted in various OECD countries to enlarge and deepen the collection of data.

Yet, the pertinence of the proposed conceptual framework seems to be empirically verified in the case of Swiss SMEs based on a 2016 SME internationalization survey, the largest one ever conducted in Switzerland, and the only one focused on the possible SME business intermediation role of global cities.

The two implications for theory are:

- Global cities tend to play important functions for foreign SME internationalization vis-à-vis physically and psychically distant markets, as formerly suggested by a few authors utilizing *Global Entrepreneurship Monitor* data ;
- However, the importance of such functions cannot be well documented and measured as in the case of multinational corporations and their affiliates participating to world classification and rankings of global cities, because internationalizing SMEs tend to use less directly and more indirectly global cities as business networking and servicing hub providers. Furthermore, the number, profiles, and internationalization behaviors of SMEs are highly differentiated compared to large firms.

### ***Implications for practice***

The search of implications for practice is just starting and can be several.

First and above all, it may differ among OECD economies, large or small (in terms of domestic market for local SMEs), and especially regarding their respective concentration of less or more specialized SMEs in absolute need to venture abroad, including to distant emerging markets.

Second, it may also differ from one global city to another, with different networking and servicing functions, depending on their regional and global strategic location. For instance, some can be major economic capital cities of vast countries with large domestic markets, whereas some others can be city-states with no domestic hinterland.

Thirdly, this contribution may suggest that both private and public business development services for SMEs should investigate more systematically the variety of functions and services offered by global cities, which can facilitate SME internationalization. Local costs are quite high, but direct/indirect benefits can be equally high in terms of finding reliable business information, reducing market search, diminishing risks, maximizing resource allocation in final markets of destination.

Fourthly, this contribution may invite both academics and practitioners to explore various existing and other potential SME business linkages among global cities serving and inter-connecting various world regions, which is not a new feature of world economic history.

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