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DIFFERENTIATING THROUGH CLUSTERING: CONTRASTING SMEs WITH LARGE-SIZED FIRMS

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Abstract

This paper investigates the impact of globalisation on the international strategic management process of small to medium sized enterprises (SMEs), within the Australian wine industry (AWI). We identify the particular complexities of international strategy processes for this type of firm. Findings suggest that these complexities stem principally from fundamental variations in strategic outlook between different organisation types, particularly in relation to organisational size, geographic location and the perception that SMEs have of the phenomenon of globalisation.

We infer, through 14 case studies with both SMEs and large suppliers within the AWI, that globalisation accentuates the strategic divide between small and large organisations. In particular, the international strategic options available to smaller AWI firms are significantly fewer. SMEs are compelled to adopt almost solely 'business' strategies, as opposed to large firms, which can adopt an array of 'corporate' and 'business' strategies. We also found that AWI SMEs utilise the benefits of location (or 'clustering') namely geographic proximity and that this is different to large organisations, and they face different challenges, stemming from the industry life cycle as a whole.

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INTRODUCTION

Strategy theorists such as Porter (1980; 1985; 1991), Yip (1992; 1998) and Eisenhardt and Sull (2001) have suggested a number of strategic blueprints for firms competing in the global arena. Yet no single approach is able to provide a suitable strategy for both the large and small firm when dealing with the complexities of international strategy processes.

Industries differ in their concentrations of international competitors and the stage of the industry life cycle (Yip, 1998; Johansson and Mattsson, 1988). This paper will analyse the implications of globalisation for the development of the AWI, predominantly from an international strategic management perspective, highlighting the complexities. These complexities stem from fundamental differences in strategic outlook between organisation types, particularly in relation to *organisational size*, (Caloghirou, Protogerou, Spanos and Papagiannakis, 2004) *geographic location* (Birkinshaw & Hood, 2000) and the very *perception* taken by organisations towards of the phenomenon of 'globalisation'.

The central objective of this paper is to examine the impact of globalisation on the international strategic management methods of SMEs, and their interaction with key organisational players in the AWI. The AWI is defined as an 'industry cluster' (Porter, 1990; 1998a). This is an important concept in international business research and a key focus is the link between industry clusters and international competitiveness (Narula, 1993; Rugman, 1991; Porter, 1990). This refers to the industry cluster's ability to remain competitive overtime, and this 'sustainability', is dependent upon the four elements of the cluster's 'diamond' (Porter, 1990) (demanding customers, related and supporting industries, factor endowments, and firm structure and rivalry) (Birkinshaw & Hood, 2000).

BACKGROUND

The globalisation debate is multi-dimensional and multi-disciplinary. A universal definition of globalisation does not exist, as it would need to extend across the political, economic and social fields. This view is echoed by Held and McGrew (2000: 3), who claim that, "as with all core concepts in the social sciences, its precise meaning remains contested". Globalisation, primarily, can be regarded as an economic phenomenon, involving the increasing interaction, or integration, of national economic systems through the growth in international trade, investment and capital flows (Oman, 1999; Reinicke, 1998). However, there are those who view it as a rapid increase in cross-border social, cultural and technological exchange (Scholte 1997; Held and McGrew, 2000). On the whole, the term globalisation has been coined to incorporate a vast range of developments that encompass a worldwide economic, social, political and cultural evolution.

GLOBALISATION: IMPLICATIONS FOR INDUSTRIES

Globalisation compels both organisations and industries to shift from a domestic to a 'multi-domestic', 'transnational' or 'global' mindset (Bartlett and Ghoshal, 1986, 1987a, 1987b, 1989). Some industries have a greater need for internationalising than others. Some industries are more prone to internationalise their operations because organisations have the need to sell their products rapidly across national and regional markets (Madsen and Servais, 1997; Nummela, 2001). For organisations in these industries, competition is an important pressure for internationalisation and globalisation.

IMPLICATIONS FOR INTERNATIONAL EXPANSION STRATEGIES

Globalisation theory could essentially explain why organisations enter international markets. The theory of the growth of the firm (Penrose, 1959) – which states that effective utilisation of organisational resources is a key component of sustainable growth; the internalisation theory (Hymer, 1960) – which concerns the economic reasons for organisations entering into foreign markets, especially internalisation gains and profit opportunities; and the industry life cycle theory (Vernon, 1966) – which links trade and foreign direct investment to the stage of the life cycle; these are the three main streams in this vein.

INTERNATIONAL STRATEGIC MANAGEMENT AND SIZE

In their recent analysis, Eisenhardt and Sull (2001: 107) fashioned a set of 'simple rules' for strategy, which they believed could be universally and generically employed by "all kinds of companies – large and small, old and young". This paper challenges this notion, contending that all organisation types – referring to organisation size, geographic location and stage of development – require their own distinctive strategies, given the complexities of international strategic management processes, the fundamental differences in the strategic outlook for each, and the impact of globalisation. Caloghirou et al (2004) found that managerial capabilities have a far greater influence on firm performance than industry effects for both SMEs and large manufacturing firms. However, there is considerable variation between SMEs and large firms with respect to both managerial capabilities and strategic direction. They also acknowledged how little research has been done on SMEs in the area of industry versus firm specific effects. Their results, at the firm level, indicate that financial and marketing competencies, together with transformation capability are the factors significantly affecting the performance of SMEs. Large firms, by contrast, rely heavily on financial assets and on developing technological assets but these approaches do not appear to enhance their profitability (Caloghirou et al, 2004).

ORGANISATION SIZE – SMALL vs. LARGE

The broad differences between large and small organisations support the claim that strategy cannot be universally embraced, given their size-related constraints, and that these firm specific limitations are more of a concern for the financially constrained SMEs (Caloghirou et al, 2004). International strategic management processes within organisations can differ markedly according to organisational size. As Shuman and Seegar (1986: 8) argue:

> Smaller businesses are not smaller versions of big businesses… Smaller businesses deal with unique size-related issues as well, and they behave differently in their analysis of, and interaction with, their environment.

From an international strategic management perspective, it is noteworthy that small businesses cannot adopt the same strategies and structures as their larger counterparts (Jennings and Beaver, 1997). According to Penrose (1980: 19), "the differences in the structure of the very small and the very large firms are so great that in many ways it is hard to see that the two species are of the same genus... We cannot define a caterpillar and then use the same definition for a butterfly".

Hamel and Prahalad (1989) argue that there are two types of strategies that an organisation should embark on. The first is a 'corporate' strategy. This relates to those strategic activities which impact on the operations of the whole of the organisation. The second type of strategy is referred to as 'business' strategy. This relates to how an organisation operates or competes within each of its broad areas of activity.

Porter (1980) argues that for organisations to sustain a competitive advantage, they need to adopt either a 'cost leadership', 'differentiation' or 'focus' strategy (Porter, 1980). Yet, where a plethora of small organisations are competing for a small share of the market – as is the case in the AWI – these strategy positions become increasingly unattainable.

Recent studies have confirmed that conclusions reached in the context of large organisations may be inappropriate for small companies as each have their own unique characteristics (Caloghirou et al, 2004; Hill and Stewart, 2000; Vinten, Lane and Hayes, 1997). Typical differences between the different size organisations can be seen in Table 1.

Table 1 about here

GEOGRAPHIC LOCATION – CLUSTER THEORY

Strategies can be shaped by the geographic location of the organisation. In turn, organisational capabilities have a strong bearing on location within 'clusters'. Porter (1998a, p.78) defines 'clusters' as geographic concentrations of interconnected companies and institutions located in a particular field or industry. 'Clusters' comprise an array of linked industries and other entities important to the various participants competing in the industry. 'Clusters' can also be extended 'downstream' to channel members and customers and laterally to manufacturers along the supply chain of complementary products and similarly to companies in industries related by skills, technologies, or other related inputs. 'Clusters' may also include a range of stakeholders, such as governmental and other institutions – for example, universities, standards-setting agencies, think tanks, vocational training providers, and trade associations. They provide a range of related services including specialized training, education, information, research, and technical support (Porter, 1998a).

Birkinshaw and Hood (2000) summarize the established logic for MNEs "to tap into" industry clusters in foreign countries in order to gain access to leading-edge ideas and specialized talents. There are also 'leading-edge' industry clusters, (Porter, 1990; 1998a), and that, typically, firms can take on one of two roles. First, there are 'scanning units' (firms) which have R&D capabilities but with limited capacity to develop because of financial constraints. This typically describes the smaller firms in the cluster (Caloghirou et al, 2004). Second, are the main manufacturing firms in the industry, that have the capacity to develop R&D. These manufacturing 'scanning unit' are seeking to participate in R&D in the clusters and are typically large, with considerable financial assets (Caloghirou et al, 2004).

The existence of 'clusters' adds weight to the argument that strategy cannot be based on 'simple rules'. The conception of industry clusters dates back to the 19th century. Marshall (1890) focused on clusters in his study of industries in the United Kingdom. More recent literature (Birkinshaw and Hood, 2000; Navdi and Schmitz, 1994; Dunning, 1995; Fountain, 1997; Porter 1998a, 1998b) has suggested that the essence of 'clusters' rests in the ability to develop strategic relationships between companies, customers, suppliers, research and education institutions and the wider business community. In order to improve competitiveness, organisations can combine their skills and resources through collaborative arrangements, common technologies, shared procurement sources, distribution channels, or common labour pools (Porter, 1998b: 149).

AUSTRALIAN WINE INDUSTRY (AWI) OVERVIEW

In recent years, the AWI has enhanced both its product quality and its international reputation. This success has been manifested in the high degree of penetration of Australian wine in the domestic market and its dramatic growth in international markets. *Strategy 2025*, the AWIs strategic and developmental vision, assumes that the industry is at the 'mature' stage of development. However, a number of factors suggest that the AWI may in fact be in the 'growth' phase where strategy is highly complex, particularly in light of the increased market opportunities presented by globalisation for SMEs (Caloghirou et al, 2004).

INDUSTRY STRUCTURE, INDUSTRY PLAYERS AND MARKET SHARE

The number of Australian wine producers listed in the Wine Industry Directory stood at 1,465, up from 1,318 at the end of 2000 (Australian Wine Online, 2002a). Accounting for closures and mergers, the AWI showed a net gain of 147 wine producers in the year 2001, an increase of 11 percent on the previous year (Australian Wine Online, 2002a). Despite the plethora of competitors, however, the AWI is oligopolistic in structure. An industry can be an oligopoly, even if it has many players. According to McConnell and Brue (1993), an industry is oligopolistic when it yields a concentration ratio – the percentage of market share owned by the largest four organisations in an industry – of greater than 40 percent. The four main AWI competitors – Southcorp Ltd., Foster's Group Ltd., BRL Hardy Ltd. and Orlando Wyndham Group Pty. Ltd. – account for 72.4 percent (IBIS Industry Report, 2002, p.24). Broadly, the industry can be defined as oligopolistic. This industry specific factor makes it difficult for small firms to enter (Caloghirou et al, 2004).

Below the top level of the industry which is very concentrated, the AWI is also a highly fragmented, with the lower end of the industry sharing 1 to 2 percent market share. An industry is fragmented when it contains a large number of small and medium-sized organisations, which compete for a small share of the total market (Porter, 1980, p.21). As stated by the Australian and New Zealand Wine Industry Directory editor, Michael Major (2002, in Australian Wine Online, 2002a):

> Australia's top 20 wine companies accounted for about 94 percent of total branded wine sales in fiscal year 2000-01… the other 1,445 producers are competing for the remaining 6 percent of sales.

As a result, there has been much discussion of an oversupply of wine grapes. However, this problem could also be attributed to an oversupply of small boutique producers (niche-differentiation) who are competing in an industry "that is becoming more dominated by the huge global wine companies" (Major, 2002, in Australian Wine Online, 2002a). In short, the AWI is becoming more fragmented, with a new Australian wine producer opening for business every 73 hours (Australian Wine Online, 2002a). This notion masks the fact that many small organisations actually go out of business within a year (Australian Wine Online, 2002a), which highlights the competitive pressures facing small organisational players. This places particular pressure on SMEs to have a clear, international strategic management approach.

Many SMEs appear to be using multiple linkages through a cluster structure of various entities within the wine and food industry. Using the Victorian wine cluster to explain cluster theory, Figure 1 shows the relationships between the agricultural, tourism and food and restaurant clusters. The Victorian wine cluster incorporates an extensive complement of industries that support both winemaking and grape growing. On the growing side, there are strong connections to the Victorian agricultural cluster, whilst on the winemaking side, there are strong links to both the food and restaurant cluster and tourism cluster. Additionally, the wineries interact with a cluster of 708 industry suppliers, 167 wine organisations and 154 industry distributors (ANZWD 2000; VWTC 2000).

Figure 1 about here

STAGE OF INDUSTRY DEVELOPMENT

The implications of globalisation for industries in a local sense, are significant, with many industries now absorbing more international players than ever before. This places increasing pressure on existing local players, especially for the SME. In addition, many firms are facing declining demand as the industry cycle progresses or are located in small domestic markets facing saturation. This has meant that organisations must increasingly seek international markets in order to survive, either for reasons of saturation or competition. This implies strategic challenges as not all markets are at the same stage of development and different international markets will require different strategies. Using the concept of lagged life cycles as a theoretical base, an organisation competing in international markets will find that not all markets are at the same stage of development (Keegan, 1989: 50). This can be seen through differences that exist in economic and market development levels between countries, and some products may be at different stages of their life cycle in different countries (Buzzell, 1968; Birkinshaw and Hood, 2000). This phenomenon can be explained through the life cycle concept for an industry competing simultaneously in different countries and the effect that globalisation has had on the industry life cycle by representing each individual country as a new curve and a new market.

METHODOLOGY

Sample Selection

The overarching research design was determined largely by the central objective of the paper; which was to examine the impact of globalisation on the international strategic management methods of SMEs, and their interaction with key organisational players in the AWI. This involved embracing a qualitative research method and using a single industry context (AWI) and a multiple-case study approach (Eisenhardt, 1989; Yin, 1994) to examine the AWI and the fundamental differences in the strategic outlook between organisation types within the industry. In-depth, semi-structured interviews were utilized as the primary research instrument for fieldwork and data collection.

Analyses of primary and secondary source documents (company memos and reports) were included to assist in the development of information in the cases and support knowledge of past events. The interviews and documentary evidence were analyzed using methods inspired by grounded theory (Glaser and Strauss, 1967; Glaser, 1992; Strauss and Corbin, 1998). Each case was treated as a comprehensive unit in and of itself, and the data analyzed and triangulated within the integrity of that case. Eisenhardt (1989) emphasizes that an exploratory approach to data analysis is guided by a process of understanding field data, resulting in some order, structure and meaning to the mass of collected data. The analysis of data was undertaken at a number of levels: Open coding and content analysis of in-depth interviews, identifying areas that relate to the influence of globalisation on international management strategies of each type of organisation; Axial coding to establish relationships between categories and across sub-categories; and Selective coding to develop the descriptive narrative about the central phenomenon (Strauss and Corbin, 1998).

In total, eighteen in-depth, semi-structured interviews were conducted, across 14 cases (organisations). Each interview was conducted by telephone and generally lasted between 30 and 45 minutes. The eighteen participanting organisations were chosen from a range of organisation types (particularly in relation to organisation size and geographic location) and the choice of respondent was based on their position within their respective organisation. The choice of organisation type was important, given that this paper seeks to highlight the complexities of international strategy processes according to variation in organisational circumstances and strategic positioning within the industry. The participants included: one industry patron, three industry analysts, eight senior managers (three from large corporations, two from medium-sized organisations and three from small organisations) and six middle managers (three from large corporations, one from a medium-sized organisation and two from small organisations).

The reason for choosing senior and middle managers is that they are commonly responsible for dealing with international strategy processes (Langfield-Smith, 1997: 208; Ohmae, 1982) and as such would be in a position to discuss the intricacies of these processes for their respective organisations. As for the industry patron, given his longstanding involvement in the industry, it was believed that he would be in a position to provide an authoritative account of the issues facing the industry. Finally, industry analysts were selected, as it was thought that they would be in a position to provide an unbiased, unemotional version of the industry.

RESULTS

Analysis and Findings

In combination with the literature on globalisation and international strategic management, fieldwork interviews led to the perception that globalisation greatly accentuates the strategic divide between small and large organisations. This is demonstrated in the AWI, with variations existing according to organisational circumstances, strategic positioning and geographic location. Aggregating these factors reveals a great deal of international strategic management complexity. Evidence gathered from the AWI bears this out as various ‘themes’ are explored below in the analysis.

THE IMPACT OF GLOBALISATION ON INDUSTRY PLAYERS: PESSIMISM AND OPTIMISM

The multi-faceted nature of globalisation highlights the strategic complexities implied for international strategic management processes (Held and McGrew, 2000). Bartlett and Ghoshal (1986, 1987a, 1987b, 1989) argue that globalisation compels organisations to shift from a domestic to a ‘multi-domestic’, ‘transnational’ or ‘global’ mindset. Fieldwork interviews suggested that this strategic choice framework did not provide a helpful prediction of internationalisation options for the vast majority of AWI participants. Apart from the large organisations, who themselves acknowledged the shift in mindset from ‘domestic’ to ‘transnational’ strategies, no other organisations were able to compete on this scale.

Characteristic of the responses of all the participants from large organisations, a middle manager of a large organisation based in South Australia asserted:

> People are now, within the organisation, taking a whole new lease on life. They are more upbeat about the future because they are seeing no end in sight to the potential of Australian wine and the strong brands that we have established.

In contrast, most participants from small organisations were pessimistic about the impacts of globalisation. A statement by a senior manager of a small organisation based in New South Wales reflects this shared sentiment:

> In my mind, there is no doubt that the opening up of markets facilitates the larger companies, as they are the ones who are in the best position to take advantage of it. And we, by definition chase niche markets. But, the niche markets – with globalisation – tend to break down… So, for us, globalisation has had a detrimental effect… and is only likely to get worse.

COMPLEXITIES OF INTERNATIONAL STRATEGIC MANAGEMENT WITHIN THE AWI ORGANISATION: SIZE – SMALL vs. LARGE

Fieldwork interviews found that small organisations cannot follow the same strategies and structures as their larger counterparts. Specifically, large organisations embark on 'corporate' strategies while small organisations are confined to 'business' strategy. It was found that all of the large organisations embarked on 'corporate' strategies. These strategies are generally in the form of strategic alliances, joint ventures and mergers and acquisitions. An industry analyst of an industry body based in South Australia asserted:

> Our major companies are very visibly setting up arrangements in the US, in terms of alliances, mergers, acquisitions with companies on side over there, to set up the distribution networks that are necessary.

In contrast, small organisations were found to adopt 'business' strategies, in particular through niche marketing. A senior manager of a small organisation based in New South Wales affirmed:

> The boutique wineries are always sought after, but again that's very much a niche market and it's certainly not the volume end of the market. And, because of its very nature it is in some ways a lot harder, because you often have to search a lot harder to find the niche, and then the setting up and the servicing of that niche can be a lot more problematic.

GEOGRAPHIC REGION – CLUSTER THEORY

The most prominent regions in Australia are: Barossa Valley in South Australia, Hunter Valley in New South Wales, Yarra Valley in Victoria and Margaret River in Western Australia (Australian Wine Online, 2002b). As fieldwork interviews revealed, organisations based in these regions share a different international strategic outlook to those based in the smaller, less recognised regions.
According to a middle manager of a large organisation based in South Australia, a noted wine-producing cluster:

> Being in the Barossa helps tremendously when entering new markets… it [Barossa Valley] is well recognised all around the world… It opens many avenues with suppliers… I think we export to 76 or 86 countries, and we're probably in every market that has some sort of wine culture.

In a similar vein, a senior manager of another large organisation based in the Barossa Valley in South Australia commented:

> Our global expansion has been paved by our competitors… the international markets are already aware of the quality of wines emanating from our region… Naturally, we do our own marketing, but for markets like the US and UK, they are already very aware of the quality of Australian wines, and more to the point, wines from the Barossa…

In stark contrast, a middle manager of a small organisation based in Victoria stated:

> We can't compete… We don't have the resources or the relationships with suppliers to leverage into international markets… we find it difficult enough as it is just to get consensus with other wineries in our region to enable us to develop any semblance of economies of scale and synergistic benefits… The larger companies don't have these problems because there is no requirement for consensus, because they basically control region… This makes exporting difficult as well, because there are so many stumbling blocks put in our way.

STAGE OF INDUSTRY DEVELOPMENT

Strategy 2025 assumes that the industry is at the 'mature' stage of development (Australian Wine Foundation, 1996). While this assertion is made by the Australian Wine Foundation, fieldwork for this paper revealed that the industry as a whole is squarely in the 'growth' phase, particularly in light of the increased market opportunities presented by globalisation. As outlined below, fieldwork interviews, together with secondary data from industry reports and websites, support this claim.

The *domestic* wine market conforms to the 'maturity' stage of the industry life cycle, as it is relatively saturated (IBIS Industry Report, 2002) and has limited growth prospects (Australian Wine Foundation, 1996). The story is very different when international markets are in focus. Fieldwork interviews, together with secondary data from industry reports and websites, supported the concept of 'lagged life cycles' by revealing that *"you have to look at it market-by-market"* (senior manager, medium-sized organisation, South Australia) and that "*in each market, a different strategy is necessary"* (middle manager, large organisation, South Australia).

A senior manager of a small organisation based in South Australia gave the best account:

> You have to adapt to the requirements of each different marketplace. And they are different. Because of your lack of support mechanisms within a boutique winery, while you try and keep your portfolio, your pricing, your packaging, everything very similar to meet every markets demand, you can't do it because every marketplace is different.

DISCUSSION AND CONCLUSION

It is generally assumed within international business and strategic management research that globalisation is a positive force, and that its benefits flow – in the long run, albeit at different rates of speed – to all people and all countries (Eden & Lenway, 2001). Yet, as Eden and Lenway (2001) argue, the international business research community is now conceding that globalisation is 'Janus-faced'; that is, it may not be universally beneficial. Laying aside its social benefits and costs and adhering to international management strategy options, we argue that globalisation does not benefit all organisations equally. Within the AWI, the range of international strategy choices is significantly greater for larger organisations than for smaller ones.

The central argument of this paper is that globalisation accentuates the strategic divide between small and large organisations in the same industry (Caloghirou et al, 2004). In particular, the international strategic options available to smaller AWI firms are significantly fewer, and the perception of globalisation is different to their larger counterparts. While there are considerable opportunities, there are also particular constraints facing SMEs in the growth stage of the industry. This presents different opportunities for large and smaller firms (Birkinshaw & Hood, 2000). This applies directly to the AWI, which illustrates the very different strategies and environments faced by small and large wine producers.

Smaller organisations are compelled to adopt almost solely 'business' strategies, as opposed to large firms, which can adopt an array of 'corporate' and 'business' strategies. Finally, it was also found that the way small AWI firms seek to take advantage of the benefits of location (or 'clustering') is different to large organisations, and they face different challenges, stemming from the industry life cycle, and we infer they rely on product differentiation (niche boutique). Despite the bold efforts of strategy theorists such as Porter (1980, 1985, 1991), Yip (1992, 1998) and Eisenhardt and Sull (2001) in looking for a strategic blueprint, this paper illustrated that no universal formula is functional (Caloghirou et al, 2004).

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Figures and Tables

Table 1: Typical Differences Between Large and Small Organisations

Large Organisations	Small Organisations
Economies of scale	Responsive, flexible
Vertical hierarchy	Flat structure
Mechanistic	Organic
Standardisation	Customisation
Quantity	Quality
Capturing market share	Creating new markets
Mass marketing	Niche marketing

(Source: Adapted from Byrne, 1989: 85)

Figure 1: Victorian Wine Cluster