

International expansion, custom tailored for smaller businesses

Inditex, owner of Zara, is the tip of the iceberg of Spanish expansion overseas. Smaller businesses already make a third of their sales in foreign markets.

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Between 2000 and 2014, the absolute value of Spain's exports doubled to nearly 250 billion euros. At the same time, exports' importance in the Spanish economy also grew — moving up 4 percentage points to represent more than 23 percent of GDP in 2014.

This jump wasn't just due to business giants like Zara's parent company, Inditex: smaller Spanish businesses have also taken to international expansion like ducks to water. So much so, that small and medium-sized enterprises (SMEs) reported that foreign sales accounted for 32 percent of their revenues in 2011 — up 6 percentage points from 2006.

Although in most cases foreign sales are made via distributors, licensees or franchisees, Spanish companies are increasingly looking to grow by making direct investments abroad — with varying levels of risk and participation.

Research by [Adrián Caldart](#) and Niccolò Pisani shows [where Spanish SMEs are investing and which tactics they use for international expansion](#).

Identifying attractive markets

A survey of business strategies by Spain's state-run SEPI Foundation shows that, from 2006-2011, most Spanish SMEs realized foreign sales via contracts. More specifically, 87 percent of exporting Spanish SMEs made deals with local distributors, licensees or franchisees to reach target markets.

Meanwhile, the remaining 13 percent made direct investments abroad — usually by acquiring full or partial ownership of a local company or by creating a joint venture or subsidiary.

The primary destination for direct investment was the European Union, which received 56 percent of these transactions. Portugal and France were the top two destination countries — with 19 percent and 11 percent, respectively — thanks to their geographic, economic, administrative and cultural proximity to Spain.

However, Spanish SMEs didn't hesitate to venture further from home, also choosing to invest in China (8 percent), the United States (7 percent), Mexico (6 percent) and Brazil (5 percent).

Drilling down to look industry by industry, those SMEs working in computer, electronic and optical equipment production are the most likely to directly invest abroad: 24 percent of these invest internationally. Producers of agricultural and industrial machinery follow, with 21 percent. In all other industries, less than 20 percent of companies directly invest abroad.

Finding the right formula

Caldart and Pisani stress that a company's best bet for international expansion depends on its specific situation and priorities. Specifically, business leaders must answer the following questions:

- **In terms of resources, how much are you willing to commit?**

Taking a stake in a local company or founding a new subsidiary requires a significant investment. That said, direct-investment strategies may help businesses overcome regulatory or economic hurdles when entering new markets.

On the other hand, having a licensing agreement or exporting via local distributors may be more efficient for products with low shipping costs, for example.

- **How much control do you require?**

A company's control over its foreign investments is determined by the operation's governance structure in the target market.

In the case of joint ventures and third-party agreements for exports, the clarity of the contract governing the relationships is key. Along with the degree of efficiency and transparency of the investment country's judicial system, the clarity of the contract determines how well a company will be able to enforce it.

A company's own organizational model also plays a role: many SMEs are family businesses and, thus, may shy away from sharing control with other partners, research suggests.

- **What risks are you willing to take?**

How much is at stake depends on the volume of resources committed and the level of unfamiliarity with the local environment. Partnering with local companies can help mitigate these risks — to a degree that depends on the terms of the partnership.

On the other hand, a strategy based on contracts with local distributors significantly reduces the financial risk. However, in reducing a company's control over the process, the risk of reputational damage or of intellectual property rights being violated tends to increase.

Let go, reel in

Caldart and Pisani find that most of the Spanish SMEs that invest directly abroad prefer governance structures that grant them a high degree of control. Few accept minority stakes and almost none are interested in entering a 50-50 joint-venture.

However, if executives' training and experience allowed them to feel more comfortable sharing the reins in uncharted territories, they could also reduce their resource requirements and mitigate risk. This, in turn, could greatly increase the opportunities to invest in new international ventures. While increased trust and confidence may be the final keys to successful investment abroad, it seems that Spanish SMEs are already well on their way to getting their sea legs.

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