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*Te Whare Wānanga o Ōtāgo*



# **THE INTERNATIONAL ACTIVITIES OF NEW ZEALAND SERVICE PROVIDERS**

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## **ABSTRACT**

The ability of companies in the service sector to compete effectively in international markets is critical for the future growth of the New Zealand economy. This report presents the results of a study of the international activities of New Zealand service providers. Through a mail survey the study aimed to assess the extent to which New Zealand service providers offer their services in international markets, to identify the markets in which they operate and their approach to internationalisation. In addition, the study aimed to identify those service providers which have not expanded their operations overseas and to establish their reasons for not internationalising.

The results show that less than half of the New Zealand service providers participating in this study operate in international markets. Australia is the main target market for those which have internationalised, followed by Asian markets. Most service firms operating outside of New Zealand have chosen to export their services which is the lowest risk option for internationally active firms. The majority of the participating firms further reduce their risk in overseas markets by targeting a small, select number of countries.

In the case of the New Zealand service firms which have not internationalised the main reasons for not doing so are their small size and a lack of interest in expanding overseas. A large majority of these domestically-focused firms said that they were not likely to internationalise in the next two to three years.

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## **1.0 INTRODUCTION**

The service sector is an increasingly important source of job creation and wealth. The ability to compete effectively in both domestic and international markets is critical for the continued growth of the New Zealand economy. New Zealand's economy is heavily dependent of overseas trade, not just in goods but increasingly in services. Little is known, however, about the extent to which New Zealand service firms are engaged in the provision of services in an international context, which markets they are targeting, how they operate in those markets and what factors influence their performance in their chosen overseas markets.

This study aims to address these issues through a two stage process. The first stage aims to establish the level of involvement of New Zealand service providers in international markets, the form that internationalisation takes and, for those firms which have not internationalised, to assess why this is and whether they have future plans to expand overseas. The second phase of the study will focus on those firms which, on the basis of this first survey, have internationalised and will identify the marketing strategies which are associated with success in international markets.

This report presents the results of the first stage of the research programme.

## **2.0 RESEARCH METHODOLOGY**

The Kompass New Zealand database was used to generate the sample of New Zealand firms engaged in service activities. A total of 4962 service providers were identified. A one-page questionnaire was sent to the CEO or Managing Director of all of these firms requesting information on the firm's level of international activities. For those firms engaged in international activities further questions were asked about the extent of their involvement in international markets, which markets they served and the types of international activity in which they were engaged. For those firms not engaged in international operations respondents were asked to identify the reasons why they did not export their services. Finally demographic information was collected on firm size, service sector and the position of the respondent.

The questionnaire was sent out by fax except to those firms with no fax number noted in the Kompass database – these firms received the questionnaire in the mail. A total of 293 questionnaires were undeliverable and 23 questionnaires were returned unanswered. A total of 561 usable responses were received representing of response rate of 12.1%. Although this response rate is low, it is highly representative of the population of New Zealand service providers with regard to company size (see Table 1).

**Table 1: Comparison of sample with population of New Zealand service firms**

<b>Number of employees</b>	<b>% of population</b>	<b>% of sample</b>
1 - 5	32.7	32.4
6 - 10	20.0	18.4
11 - 20	16.6	16.3
21 - 50	15.5	15.5
51 - 100	5.4	4.4
100 and over	9.8	12.9
<b>Service Sector</b>		
Building and public works	5.0	14.9
Transport and communications	13.3	16.8
Medical and social	0.7	1.8
Education and training	5.9	8.3
Finance and insurance	11.1	9.2
Commercial and business services	46.7	38.5
Computer and software	17.3	10.5

As far as industry sector is concerned, Table 1 shows that there is a lower percentage of firms in the Commercial and Business Services and the Computer and Software sectors in the sample than in the population of New Zealand service providers. This is likely to result from the fact that nearly 70% of the firms in the population which employ five or fewer people are in these two sectors with many of them being sole traders. There is a stronger representation of firms in the building and public works and education and training sectors in the sample compared with the population.

### 3.0 RESPONDENT PROFILE

#### 3.1 Firm size

Of the firms responding to the survey 45.5% were engaged in the provision of services in overseas markets. This compares well with an earlier study of service sector competitiveness within New Zealand in which 46.5% of service firms were found to provide services to customers in other countries (Gray et al, 1999). Over half (54.5%) of the participating firms, however, were not involved in international operations of any form. The majority of firms with no international activities were small firms with over half (56%) having fewer than 10 employees (see Table 2). However, size is not necessarily a key issue determining whether a New Zealand service provider internationalises. Nearly 45% of the firms engaged in the provision of services in overseas markets also employed fewer than 10 employees (see Table 2). More of the larger firms were engaged in international activities which is no doubt a reflection of the higher level of resources available to them for international activities. This bears out research in other countries which had found that larger firms are more likely to have the managerial expertise to successfully internationalise (e.g. White et al, 1999).

**Table 2: Internationalisation by firm size**

<b>Number of employees</b>	<b>% of firms engaged in international activities</b>	<b>% of firm not engaged in international activities</b>
1- 5	22.8	40.1
6 - 10	21.6	15.9
11- 20	12.5	19.4
21 – 50	16.0	15.3
51 – 100	5.6	3.5
100 and over	21.5	5.9

#### 3.2 Service Sectors

Taking a look at the service sectors in which the participating firms are operating, Table 3 shows that over one third of respondents operate in the commercial and business services sector with the building and public works and transport and communications sectors representing the next largest service sectors in this study. A comparison of the firms which have internationalised with those that have not by industry sector reveals that the sector with

the highest levels of sales from overseas markets is the transport, communications industry with over one third of firms in this sector receiving over 90% of their turnover from outside of New Zealand.

**Table 3: Internationalisation by service sector**

<b>Service Sector</b>	<b>% of firms engaged in international activities</b>	<b>% of firms not engaged in international activities</b>
Building and public works	15.5	14.3
Transport and communications	17.4	15.7
Medical and social	1.2	1.7
Education and training	16.7	2.1
Finance and insurance	4.7	13.2
Commercial and business services	32.6	43.9
Computer and software	12.0	9.1

As Table 3 shows, in most industry sectors similar percentages of participating firms have internationalised compared to those which have not. In the Finance and Insurance sector, however, significantly more firms are not offering their services overseas. This is largely the result of reverse internationalisation as many of the firms which participated in this survey are subsidiaries of overseas financial and insurance organisations which themselves have expanded into the New Zealand market.

In the commercial and business services sector a higher proportion of respondents have also not internationalised. Company size appears to play a role here as over 60% of those firms which have not expanded outside of New Zealand employ fewer than five staff and are often sole traders offering consultancy services to specific customers within New Zealand. More of the respondents in the education and training sector have internationalised. This figure could be artificially high as some respondents may not be engaged in the provision of services outside of New Zealand per se, but consider themselves to have internationalised by attracting a significant level of income from students and clients who originate from overseas. Issues associated with internationalisation, however, are just as important to organisations in this sector as they seek to attract revenue from overseas customers.

## 4.0 FIRMS WHICH HAVE INTERNATIONALISED

### 4.1 Number of markets served

45.5% of the respondent firms have international operations of one form or another. In a quarter of the cases only one overseas market was served (see Table 4) with a third of firms serving between two and four markets. Nearly 20% of the firms in this study had international operations in over 20 countries which suggests a high degree of internationalisation. The most markets served by a single company was 149.

Overall the results of this study suggest that the majority of New Zealand service providers have a selective approach to international markets preferring to focus on a small number of markets, thereby minimizing the risks associated with internationalisation.

**Table 4: Number of overseas markets served**

<b>Number of markets served</b>	<b>% of firms which have internationalised</b>
1	25.7%
2 – 4	33.5%
5 – 10	16.6%
11 – 20	5.7%
More than 20	18.4%

### 4.2 Overseas markets targeted

Not surprisingly Australia was the market targeted by the most firms (see Table 5). Just over 70% of all internationally active firms in this study sold their services to Australian customers. In this respect New Zealand service providers are no different to goods exports as Australia is the number one export market for New Zealand products ([www.stats.govt.nz](http://www.stats.govt.nz)).

Interestingly, over half of all internationally active respondents are targeting Asian markets, no doubt because of their relative physical closeness to New Zealand. North America and Europe are targeted by over a third of respondents followed closely by the Pacific Islands. Latin America, The Middle East and Africa appear to be less attractive to New Zealand service providers. These results suggest a strong regional approach by New Zealand service

providers with the majority of firms targeting developed countries in which the service sector plays a major role in the economy.

**Table 5: Regions in which New Zealand service providers operate internationally**

<b>Region</b>	<b>% firms operating internationally</b>
Australia	70.6
Asia	54.9
North America	35.3
Europe	34.9
South Pacific	32.9
Latin America	15.7
Africa	9.4
Middle East	5.9

Note: many firms operate in more than one region.

### 4.3 Mode of Internationalisation

The predominant mode of operation adopted by New Zealand service providers in international markets is exporting, with over half of the firms in the sample choosing this mode of internationalisation (see Table 6). International Strategic Alliances were the next most popular form of internationalisation, but used by less than 20% of the internationally active firms. Only about 10% of respondents had offices in overseas markets with a similar number having distribution arrangements in other countries.

**Table 6: Mode of operation in international markets**

<b>Mode of operation</b>	<b>% of firms operating internationally</b>
Exporting	54.5
International Strategic Alliances	19.5
Foreign Sales Office	11.0
Distribution arrangement	10.2
Licensing or franchising	8.6
Foreign Direct Investment or acquisition	2.8

The numbers of firms involved in Foreign Direct Investment, franchising and acquisitions was very small which is likely to be a reflection of the small size of many of the participating firms. Given the small size of many of the firms in this study, it is interesting to note that so few service firms are entering into strategic alliances with overseas partners. Small firms in other countries have often found an international strategic alliances to be an effective means

of entering new overseas markets as they can gain access to much needed overseas capital and valuable local market knowledge. The strong bias towards exporting of services suggests that most New Zealand service firms adopt a risk averse approach to international markets.

#### 4.5 Extent of international activities

Just over one third of New Zealand service providers are only involved to a small degree in international markets (see Table 7). It is encouraging, however, that a quarter of the internationally active service providers in this sample obtain over half of their sales from overseas markets. It is important to find out how these companies achieve this level of internationalisation and to identify key lessons for those service providers looking to extend their international activities. Firm size does not appear to be an issue here as 45% of those firms achieving more than 50% of their turnover from overseas markets employed fewer than 10 people.

**Table 7: Percentage of annual sales turnover generated from overseas business**

<b>Sales turnover</b>	<b>% of firms operating internationally</b>
less than 10%	38.2
11 – 20%	12.2
21 – 30%	10.9
31 – 50%	13.0
51% and over	26.5

## 5.0 FIRMS WHICH HAVE NOT INTERNATIONALISED

### 5.1 Reasons for not internationalizing

Those companies not engaged in international operations were asked to assess the extent to which a set of 20 factors had influenced their decision not to internationalise. As Table 8 shows, size appears to be the key barrier to internationalisation by New Zealand service providers. However, given that nearly 45% of those engaged in international operations had less than 10 employees (see Table 2) size alone cannot be the only determining factor so other issues are likely to come into play. Given that the respondents consider size to be an issue it is interesting to look at the barriers to internationalisation according to the number of people employed by New Zealand service providers (see Table 8).

**Table 8: Factors influencing firms' choice not to internationalise**

Factor	Company size (no. employees)			
	1 – 5	6 – 10	11 – 50	50+
Restrictions imposed by foreign rules/regulations	6.1%	10.5%	2.4%	8.7%
Uncertainties in foreign domestic markets	8.3%	13.2%	14.6%	9.1%
Inability to be competitive in foreign markets	18.8%	15.8%	14.6%	18.2%
Lack of New Zealand government assistance/incentives	14.6%	10.5%	8.5%	18.2%
Lack of access to foreign distribution channels	18.9%	15.5%	14.6%	22.7%
Limited information to locate/analyze foreign markets	23.2%	18.4%	15.7%	9.1%
Inadequate/inexperienced management/staff	21.9%	28.2%	17.9%	17.4%
Different consumer habits/attitudes in overseas countries	10.8%	15.8%	8.6%	4.5%
Not interested/not willing to expand	39.8%	36.6%	21.4%	26.1%
Lack of foreign market government support/incentives				
Unfavorable exchange rates	9.6%	10.5%	14.6%	4.5%
High risks/costs involved in selling abroad	31.6%	36.8%	25.0%	18.2%
Difficult to understand business practices in overseas countries	17.0%	13.2%	13.8%	0
Existence of language/communications problems	12.8%	7.9%	7.4%	4.5%
Concern over getting paid by international customers	19.8%	26.3%	19.8%	9.1%
Overseas customers are too demanding	3.2%	7.9%	5.1%	0
Lack of understanding of how to access foreign markets	25.3%	34.2%	18.3%	19.0%
Lack access to potential foreign partners	19.4%	18.4%	15.2%	18.2%
Our company is too small to operate in overseas markets	58.3%	40.9%	34.8%	28.6%
High cost of adapting existing services to meet overseas customer needs	19.4%	13.2%	25.0%	22.7%

Measured on a 5-point scale (1= no influence at all, 5 = a great deal of influence)  
 % thinking this was an influencing factor (4 or 5 on 5 pt scale)

Following firm size the second barrier to internationalisation by New Zealand service providers appears to be an unwillingness to operate internationally or a lack of interest in doing so (see Table 8). Given that nearly 80% of non-exporters in this sample consider it unlikely or very unlikely that they will engage in international business activities in the next

two to three years this lack of interest is not surprising. The high risks and costs involved in selling abroad does influence some firms' decision not to internationalise as does an acknowledgment of a lack of understanding of how to access foreign markets. Because size and a lack of interest are the dominant reasons for New Zealand service providers not expanding overseas many of the other barriers to internationalisation identified through research in other countries are not seen to be major concerns by many of the respondents in this study.

It is interesting to note that some of the larger organisations were also not interested or willing to expand which is a worrying sign. Only 20% of those firms which do not currently operate internationally said that they were very likely or likely to seek opportunities overseas in the next two to three years.

## **5.2 Barriers for service firms planning to internationalise**

For those firms showing an interest in expanding their services outside of New Zealand it is useful to understand what they perceive the barriers to internationalisation to be. As Table 9 shows the main barrier to internationalisation facing these firms is the high risks and costs associated with selling abroad. Further concerns relate to market-based factors such as limited information on foreign markets, lack of access to potential partners and distribution channels and on how to access foreign markets. Additional concerns are issues relating to cost, concerns about getting paid and lack of support from both the New Zealand and host country governments. These barriers have also been found to inhibit internationalisation in studies of non-exporters in other countries (e.g. Leonidou, 1994; Barrett and Wilkinson, 1985). Size of company also appears to be an issue for these companies reflecting the fact that 55% of those likely to operate internationally in the future have fewer than five employees. However, as other companies in this study have shown size does not need to be a barrier to internationalisation. Over 42% of the respondents wanting to expand overseas operate in the Commercial and Business services sector where there are a large number of firms with fewer than five employees. For the larger firms the main barrier to internationalisation appears to be the high cost of adapting their services to meet the needs of overseas customers.

**Table 9: Barriers to internationalisation for those firms planning to expand overseas in the future**

High risks/costs involved in selling abroad Limited information to locate/analyze foreign markets Lack of understanding of how to access foreign markets Lack of access to foreign distribution channels Lack of access to potential foreign partners Our company is too small to operate in overseas markets High cost of adapting existing services to meet overseas customer needs Concern over getting paid by international customers Lack of New Zealand government assistance/incentives Inadequate/inexperienced management/staff Lack of foreign market government support/incentives Difficult to understand business practices in overseas countries
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## 6.0 CONCLUSIONS

This study has shown that less than half (45.5%) of New Zealand service providers participating in this study are engaged in international operations. Those that are operating in overseas markets are principally targeting Australia followed by Asian markets then North America and Europe. The findings of this study suggest that the majority of New Zealand service providers which have internationalised are adopting a risk minimisation strategy by focusing on a small number of overseas markets, by not being heavily reliant on overseas trade for their turnover and by adopting the lowest risk form of internationalisation - exporting. Attention needs to be focused on existing exporters of services to encourage them to increase the number of markets they serve and the level of sales that come from overseas customers.

For those firms which have not internationalised the main reason for not expanding outside of New Zealand is company size and a lack of interest in international market opportunities. There is, however, a small group of non-exporters (20%) which, given some encouragement, could be exporters of services in the future.

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