

# A Dynamic Entrepreneurial Process Approach of Industrial Linkage Creation in Developing Countries: A Theoretical Framework

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## 1. Introduction

There is no disagreement that the creation of industrial linkages between transnational corporations (TNCs, hereafter) and local firms is of great importance for host developing countries (Halbach 1989, Altenburg 2000, UNCTAD 2001). Linkages can increase employment, output and value-added among firms linked with TNCs. Linkages are also expected to function as a vehicle for generating considerable positive spillovers from TNCs' presence; namely, the enhancement of local capabilities and the provision of technological upgrading opportunities that could help the host economy better exploit its existing endowments, improve productivity and develop new competitive advantages (Dunning 1992, Caves 1996). Thus, a successful creation of linkages increases the benefit from the inflows of FDI.

Because of its importance, there is a growing literature focused on this issue. A large number of studies concentrate on examining the *function* of TNC linkages already established with firms in the host economy (Lall 1980, Altenburg 2000, UNCTAD 2001, Giroud 2003). On the other hand, only a few studies have focused on the *process* and development of linkage creation (Driffield and Noor 1999, Castellani and Zanfei 2002). This paper aims to contribute to the latter issue. The process study of linkages is important because the establishment of linkages is inevitably the antecedent of their functions expected. Moreover, the process can never be started and developed automatically, particularly in developing countries where a number of economic, social, cultural, and political obstacles disturb it. Therefore, to overcome such structural difficulties, it is understandable that various sorts of purposeful interventions have been widely advocated and used to stimulate this process. When formulating policies, however, the role of public sector (Watanabe 1983, UNCTAD 2001) and TNCs' outsourcing strategies, including TNCs' supplier development policies (Giroud and Mirza 2006) have received most of the emphasis from both researchers and policy makers. On the other hand, the role of local firms and their entrepreneurship in this process has received disproportionately little attention (UNIDO 1974). For a proper understanding of linkage formation, however, the present research strongly proposes that equally significant attention should be paid to the role of local entrepreneurship. This study mainly focuses on this issue.

In this research, "entrepreneurship" is defined as personal traits highly alert to market disequilibrium as a profit opportunity and unusually venturesome, rather than rational, in taking risks

to run his/her own organisation. Entrepreneurs appear as a “prime mover” for economic development (Sautet 2000). However, the role of entrepreneurship has been largely dismissed not only in linkage studies but also in economics in general (Barreto 1990). This is because mainstream economics implicitly assumes that new firm generation and its subsequent development is highly elastic to the availability of an emerging profit opportunity. Under these assumptions, the process of linkage formation is automatic, spontaneous and instantaneous upon TNCs’ outsourcing demand if effectuated. The government role is appreciated so far as it can compensate ‘market failures’ related to the process. After all, the traditional linkage study sees the creation of linkages as endogenously determined largely by TNC and government-related variables. Local firms are downplayed in this process. This study provides a theoretical framework using dynamic entrepreneurial approach to explain the emergence of local suppliers to TNCs.

## **2. The Role of Entrepreneurship in Linkage Formation**

Despite an important role of government in supporting linkage formation, industrial backward linkages are a tangible form of the product created by close interaction between TNCs and local suppliers. It is quite natural to consider local suppliers as one of the essential players in determining the performance of linkage formation. However, as is explained above, less attention has been paid to the proactive actions taken by local suppliers and the role of local entrepreneurship. One of the reasons for disregard of entrepreneurship is related to the assumption of mainstream economics, in which entrepreneurs and entrepreneurial firms are assumed to come into existence readily upon the availability of profit-making opportunities. This view explains the emergence of local suppliers by “demand-driven” principle. It is widely observed in developing countries that TNCs’ local operations call for a supply of various locally-produced items, components and services, which can generate huge outsourcing demand to involve local suppliers. If such outsourcing demand may effectively stimulate the new entry of local suppliers, the role of government is considered principally complementary to markets: the government is expected to provide public goods such as educational and financial systems strengthening market mechanism. In this view, entrepreneurship does not play a major role; therefore, no specific entrepreneurship programme is needed.

However, from the perspective of entrepreneurship research, the above explanation is not readily acceptable. Such an “outsourcing demand-driven” view is over-simplified to understand the overall mechanism of linkage creation. In this regard, Glade (1967) proposes the situational approach, arguing that the entrepreneurial emergence is an outcome of demand and supply interaction. This approach is suggestive in the context of the present study in which local entrepreneurs appear as a supply element in successful linkage formation with TNCs.

Considering entrepreneurship has grave implications in linkage studies: individuals do not respond automatically to emerging profit-making opportunities. Not all individuals are alert and aggressive to take advantage of TNCs’ outsourcing demand. In reality, individuals do not behave in a similar way and, therefore, respond differentially to the availability of profit-making opportunities. Furthermore, individuals may differ widely in their nature regarding the ways of discovering, recognising and exploiting business chances. Such differences can be principally

explained by individuals' personality, psychological attributes and, in a broader term, entrepreneurship. It should be noted that entrepreneurship is clearly distinguished from capability-related attributes such as skills and human capital. I admit the importance and essentiality of the large pool of highly-skilled manpower to successful linkage formation with local TNCs; however, capability-related factors are not a sufficient condition for venture creation. Actually, not many but a small population of local individuals are keen to start own business. Furthermore, even after new ventures launched, only vigorous and ambitious entrepreneurial persons would try to find and capture TNCs' outsourcing demand, while others with weak or scant entrepreneurship may be inert or inattentive and, therefore, not respond swiftly and adequately such potential profit opportunities. Thus, it is reasonable to assume that entrepreneurship is an essential variable to explain the successful creation and development of inter-firm linkages between TNCs and local suppliers.

Based on this perspective, this paper examines the role of entrepreneurship in linkage formation. As is discussed above, entrepreneurship is defined as personal traits highly alert to market disequilibrium as a profit opportunity, and is extraordinarily venturesome, rather than rational, in taking risks to create his/her own organisation in order to exploit this opportunity. Entrepreneurial decision-making necessarily involves uncertainty and risk-taking, because entrepreneurial outcomes are inherently unforeseeable. This is incompatible with the framework of mainstream economics which is based on the assumption of perfect information including future events. Entrepreneurial uncertainty has another important implication in the sense that opportunity recognition is subjective and different from person to person. The manner how the opportunity is discovered, recognised and interpreted is principally determined by individuals' cognitive skills, as well as their experiences and entrepreneurial motivations. The mainstream economics does not pay a large attention to such differences. This further leads to another important proposition: entrepreneurship is more than a mere production factor. It can mobilise, array and supervise other production factors such as labour, capital, technology, and information. It also facilitates the functions of these factors in pursuit of entrepreneurs' own goals which cannot be identical from person to person. In this sense, entrepreneurship should be distinguished from human capital; the latter's full function is essentially under control of the former. Appropriate policies must take the nature and role of entrepreneurship into account. These theoretical considerations suggest that entrepreneurship is an important variable to determine the performance of linkage creation.

The following part of this paper aims to explore the factors and variables which are important in determining who becomes a successful supplier to local TNCs. The basic assumption of this study is that there are a number of existing, as well as potential, entrepreneurs in developing countries. They are found everywhere there; however, a majority of them remains informal, primitive, and unsophisticated in technological and management skill for a modern economic organisation. Becoming a supplier to TNCs needs a great leap from such an initial condition but this is not easy to fulfil. Thus, in this paper, two types of ventures are distinguished, i.e. non-TNC suppliers and TNC suppliers. For the former, their main customers are domestic-based and they are relatively inferior in commanding technology and management to work with global companies like TNCs. However, only a few may rise up above a flock of ordinary entrepreneurs to

become the latter. They are ambitious and upward-oriented, making tremendous efforts to upgrade the level of their overall capabilities to start business with global companies. TNCs' local affiliates generally welcome such aggressive local entrepreneurs as business partners, providing them with profit-making opportunities through purchasing their items. It is expected that alert and aggressive entrepreneurs may respond swiftly to such opportunities provided. Then, a question arises; why some entrepreneurs decide to take such ambitious actions and others do not. There are a number of factors which affected the individual decision-making at several turning points led to becoming a supplier to TNCs, or to remaining to serve for domestic markets as non-TNC suppliers. Resources, ability, personal characteristics and preferences are the main variables for assessing and weighing the risk and rewards expected from such entrepreneurial opportunities. This may result in different paths to becoming different types of entrepreneurs.

Entrepreneurship study is expected to provide reasonable and practical approach to this issue. The process of creating new form of organisation has been a central focus of entrepreneurship research (Gartner 1989, Timmons 1990, Bygrave 2004). In this field of research, there are broadly two types of approaches. The first approach is based on the use of "entrepreneurial intensity (EI)" (Morris 1998), or "entrepreneurial orientation (EO)" (Miller and Friesen 1982; Lumpkin and Dess 1996). One of the traditional approaches in entrepreneurship study is concerned with the question of "who is an entrepreneur?" There has been considerable interest in the capacity to identifying the components of these characteristics and the personal traits that would determine how entrepreneurs differ from other individuals (Shaver & Scott 1991). EI and EO are used for this objective; to distinguish two types of individuals, i.e. entrepreneurs and non-entrepreneurs, by combining many traits including ambition, need for achievement, risk taking, and locus of control (Brockhaus 1982).

The second is the entrepreneurial process approach. This aims to identify the factors and variables affecting entrepreneurial steps pursued by individuals to become a certain type of an entrepreneur (Cooper and Dunkelberg 1986; Feeser and Willard 1990). The present study sees that this approach is more useful than the above for my research: EI and EO include examination of the background of the individual entrepreneur and also of the motivations and attitudes associated with different entrepreneurial 'types'. However, typology as such may be useful to identify the potential entrepreneurs but not be immediately of practical use in understanding what circumstances and policies are applicable to support potential suppliers. On the other hand, the process approach is advantageous in this point: it is useful to identify what variables, factors and environments are relevant, supportive, or even adverse to the emergence and development of a certain type of new ventures. Based on this view, the present study principally uses the process approach to examine the different process becoming TNC and non-TNC suppliers.

### **3. The Process View of Entrepreneur Emergence**

Research on entrepreneurship has traditionally examined personal characteristics of entrepreneurs or selected aspects of the processes of individual company formation. A number of prior studies in this field have either focused only upon persons who founded a firm, or upon the processes of how the firm is established and developed. In these studies, the background, motiva-

tions, and psychological attitudes of individual entrepreneurs were examined in order to associate these characteristics with different entrepreneurial "types." Two types of entrepreneurs were identified; i.e. craftsman and opportunistic (or managerial) entrepreneurs (Smith 1967, Filley and Aldag 1978, Cooper and Dunkelberg 1986). In the context of the present study, the implication of entrepreneur typology studies is to highlight the fact that entrepreneurs do not constitute a homogeneous entity and the different types of entrepreneurs tend to result in difference performance of new venture (Woo et al 1991).

However, this line of research is based on the implicit assumption that entrepreneurship is inborn and, therefore, holds little premise for intentional enhancement of entrepreneurial development. The best one could hope for is to select a potential young person who might be seen belonging to successful entrepreneurial categories, and to encourage him/her to take specific entrepreneurial actions. However, what aspiring entrepreneurs need to understand is not so much what kind of person they ought to be, because that does not seem to be critically important in itself and could not easily be changed even if it were. More useful approach is to assume that entrepreneurship is acquired as a second nature, and to identify the processes in which entrepreneurial characteristics were developed, enhanced and sharpened along with individuals' experiences. Thus, we believe that much more fruitful line of research should concern the processes and environments in which a various types of successful entrepreneurs and organisations are nurtured and emerged. A process view of entrepreneurship is justified in this context.

The present study focuses on the differences along the entrepreneurial processes leading to becoming either TNC or non-TNC suppliers. Various paths of becoming different types of suppliers presumably depend on specific environments and experiences each entrepreneur has gone through. For example, becoming a TNC supplier might need to possess higher technological capabilities which enable the innovative task of supplying high quality products, and of taking the initiative to contribute something creative to what a TNC customer needs. They might be formerly serving only for domestic markets but later decide to have personal risk-taking to approach local TNCs by, for example, investing more in human resources and capital equipments. On the other hand, non-TNC suppliers might be more conservative in technology by using, for example, cheaper second-handed machineries but more aggressive in searching and establishing personal business networks in order to discover an unexploited domestic market. Some of non-TNC suppliers might have tried to approach TNCs but might have abandoned this for some valid reasons (e.g. TNC's high technological requirement is not lucrative for them to sustain). It should be noted that all of these processes pursued by both types of suppliers are equally entrepreneurial and their entrepreneurial differences can be identified in the actual processes of their behaviours.

The process perspective is essential to examining the mechanism of new venture creation (Bhave 1994, Bygrave 2004). The process approach is applied to explain the difference in venture performance (Feaser and Willard 1990) and in types of business ownership (Cooper and Dunkelberg 1986). A new organisation emerges as an outcome of multiple steps taken by entrepreneurs, which may be either purposeful or unconscious. The paths leading to new venture creation are greatly diversified among entrepreneurs. Each entrepreneurial choice is not identical and it critically depends on entrepreneurs' goals, perceptions, motivations, and various

constraints which vary widely according to entrepreneurs' environments, experiences and personalities. This approach is applied to this study in order to explain the different entrepreneurial paths to becoming TNC or non-TNC suppliers.

#### 4. Dynamic Entrepreneurial Process Approach

The present study principally bases on the process perspective by which different entrepreneurial paths to becoming TNC or non-TNC suppliers are examined. In this study, the dynamic entrepreneurial process model is employed. The term "dynamic" is intended to emphasise the chain of causes and effects along the entrepreneurial processes. This point has received less attention in the traditional entrepreneurial process approach in which every process appeared merely as a "pass point." In these studies, each entrepreneurial choice is made in an independent, separated, or disconnected manner from entrepreneurs' previous choices and experiences. However, such a "disconnected" process model is unsatisfactory, because the model leaves it unexplained how preceding events affect the following entrepreneurial decisions and performance. In consideration of this shortcoming, my model emphasises the context in the process, in which an outcome of a particular entrepreneurial process is relayed to the initial condition of the next process. This implies that every entrepreneurial process is inevitably influenced by entrepreneurs' past career, experience, and environment. In this sense, the process is essentially path-dependent.

**Fig 1. Dynamic Entrepreneurial Process Model**

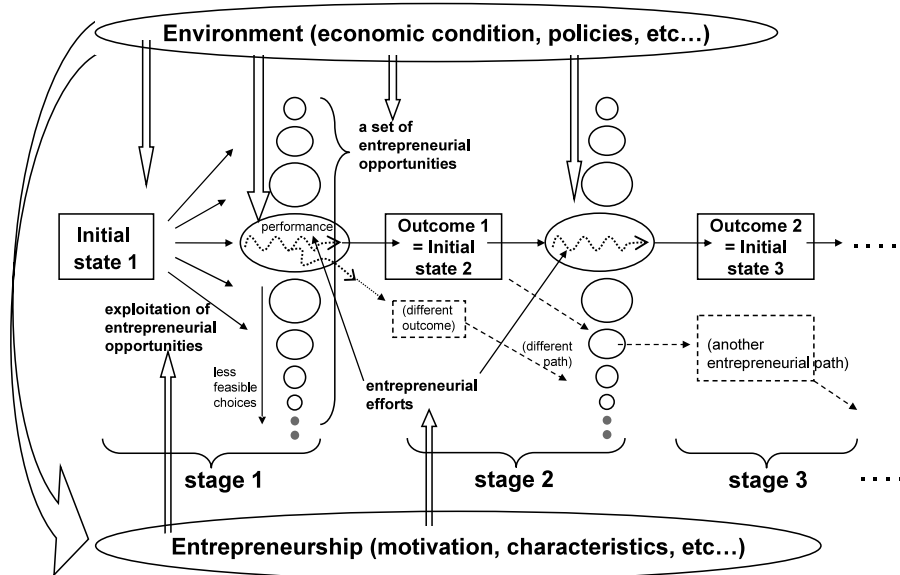


Figure 1 indicates the model, of which particular focus is the dynamic nature of the entrepreneurial process. This explains the interactions of key variables relevant to individual's entrepreneurial choices and the subsequent stages along the course of the process. Each option is chosen from *a set of entrepreneurial opportunities*. In general, the entrepreneurial opportunity structure is determined by these two independent variables, i.e. *environment* and *entrepreneurship*, which are presented at the top and the bottom in the figure, respectively. The environment variables include, for example, family background, hereditary ability, location, economic condition, while the latter covers personal motivation, goals, self-confidence, enterprising spirit, fortitude, and other individual characteristics. Correctly speaking, the latter is partly and essentially influenced by the former (e.g. repressive political environment may discourage individual's entrepreneurship, which was widely observed in the former communist countries), not vice versa. The large arrow at the left side indicates this causality.

In this figure, persons start their careers at the stage 1 where they choose entrepreneurial options from a set of entrepreneurial opportunities. The set of the opportunities available to potential entrepreneurs is not objectively deterministic, but it may differ significantly from person to person, by the different expectancies of opportunities they perceive. Thus, the recognition of entrepreneurial opportunities would be heavily influenced by entrepreneurship as well as individuals' environment, including parents, family culture, friends, and economic conditions. Naturally, the choice is highly subjective as well as entrepreneurial, because this is based on individual interpretation, motivation, and ability wishing to exploit this opportunity. For most persons, the first entrepreneurial option should be probably learning opportunities, which may be conducted at school, after school, and even at home. Decisions are made on, for example, what subjects s/he takes, what level of attainment s/he aims to achieve, which school and university s/he choose, to what extent s/he concentrates on studying, and so on. All of these decisions differ in individuals, critically influenced by individual's entrepreneurship.

To establish a set of entrepreneurial opportunities, the present study emphasises individual difference in the nature of entrepreneurship. There are personal variations in the way of searching, interpreting, evaluating and exploiting entrepreneurial opportunities (Shane 2000). The process of search and opportunity recognition can be influenced by the cognitive behaviours and entrepreneurial motivations of individuals. Search behaviour and its result can be bounded by the decision-maker's knowledge of how to process information as well as the ability to gather an appropriate amount of information (Woo et al 1992), all of which attribution is deeply rooted in entrepreneurship. Therefore, even if individuals were placed in an identical environment, they would identify different sets of entrepreneurial opportunities. In view of this, entrepreneurship does matter on personal recognition of the entrepreneurial opportunities.

Entrepreneurship plays an important role not only in recognition but also in decision-making of what option is chosen among the opportunities recognised. *The exploitation of entrepreneurial opportunities* critically depends not only on environments but also on personal value, evaluation and feasibility to exploit opportunities. This is essentially entrepreneurial and subjective, influenced by personal motivation, perception, self-confidence, and other psychological characteristics. The choice is not necessarily optimal or rational as mainstream economics assumes; rather, it is often irrational, emotional, or excessively ambitious in order to bring oneself closer to

personal fulfilment. It is clear that such a behavioural deviation from simple optimisation principle can be partly attributed to entrepreneurial factors.

During the entire entrepreneurial process, entrepreneurship also influences every outcome through the implementation they have made. Fig 1 clearly shows this. Potential entrepreneurs' work performances may vary widely. The performance is determined by the efforts they made and *the entrepreneurial efforts* are critically influenced by individuals' entrepreneurial elements. For example, some may study hard at school or work diligently night and day, but others may not. The difference in their attitudes partly depends on, for example, motivation, eagerness, the degree of self-independence, persistence, and ability to pursue personal goals. All of these psychological factors constitute entrepreneurship. The different performance naturally results in different outcomes, and this, in turn, becomes the initial condition for the next stage. Thus, different persons will be placed in different environments at the next stage. They will encounter there different sets of entrepreneurial opportunities from which they will make different entrepreneurial exploitations. As a result, every individual takes different paths and, eventually, reaches different types of occupational status, including farmer, fisherman, worker, clerical, operator, engineer, manager, government officer, and various types of self-employment (e.g. craftsman or managerial in Smith's (1967) terminology). It is clear that different persons take different entrepreneurial processes.

Despite the difference to be observed in individuals' career paths, the immediate objective in the present study to use the dynamic entrepreneurial process model is to identify the ' typical ' paths to become TNC supplier and non-TNC suppliers. The dynamic approach emphasises the path-dependence of the entrepreneurial process: the outcome at one stage is relayed to the initial state for the next stage. This suggests that becoming a certain type of a business person is essentially determined by the accumulative consequences of past entrepreneurial choices and experiences. It may also say that TNC, as well as non-TNC, suppliers are not built in a day.

The entrepreneurial process should involve all the functions, activities, and actions associated with the opportunities entrepreneurs perceived and intended to exploit. My investigation is intended to identify critical variables presented at each entrepreneurial process and examined their influence and interactions on the entrepreneur's decision-making and efforts leading to becoming either TNC or non-TNC suppliers.





## 5. Linking Dynamic Entrepreneurial Process to Hypotheses

I propose totally five major stages of development in entrepreneurs' life. *A stage of the entrepreneurial processes* is defined as a specific period in entrepreneurs' life related to venture creation and development. The features of these four stages are explained as follows. Every stage has a certain length of period in entrepreneurs' life of careers, in which several entrepreneurial events are included. The events are specifically indicated in Table 1.

(i) **Background:** this stage is related to the initial status of entrepreneurs' demographic, social and economical conditions. The stage includes personal environments such as parental occupation, family culture and wealth, and educational opportunities enjoyed by entrepreneurs.



**Table 1. Five Stages of Dynamic Entrepreneurial Process**

| Stage  | Specific Events  | Features of the stage   |
|--|--|---|
| (i) Demographic characteristics  | family background<br>family wealth<br>education  | Environments in which potential entrepreneurs were initially embedded may heavily influence individuals' entrepreneurial expectencies, choice, and subsequent career paths at later stages.   |
|  After finishing schools, would-be entrepreneurs start working, an important milestone for independence.          |  |   |
| (ii) Work experience   | age to start working<br>career development<br>acquired skills  | Choices of work place, industry, occupation, and function appear as the first entrepreneurial decision-making. In turn, these choices and work performance should influence entrepreneurs' career paths at later stages.  |
|  During the period working for others, potential entrepreneurs start thinking to be independent.                  |  |   |
| (iii) Nascent process  | motivation<br>opportunity recognition<br>networking<br>trigger events  | Nascent process is a latent activity stage to become independent. Concrete start-up actions are not made at this stage; but would-be entrepreneurs start recognising opportunities, creating specific business plans, building business networking, seeking partners and so on.   |
|  By preparations in nascent stage, entrepreneurs finally decide to start-up and to make concrete actions.         |  |   |
| (iv) Start-up  | financing<br>finding first customer<br>creating organisation<br>first equipment                              | At this stage, would-be entrepreneurs become independent and make specific actions to start-up. They need to make decision on financing, finding reliable staffs and stable customers, upgrading technologies, what type of equipments to install, approach to subsidies, and so on.  |
|  After successful start-up, entrepreneurial firms need to take further entrepreneurial actions for development. |  |   |
| (v) Company development  | additional customers<br>additional equipments<br>R&D investment<br>ESI commitment<br>other upgrading efforts | To be an established supplier (either to TNC or to non-TNC), new firms are required to develop their capabilities. The efforts may include finding additional customers and new source of finance, upgrading technologies, how to commit TNCs' early supplier involvement (ESI) partnership, expansion of social networks (e.g. industrial association), and so on. |

(ii) **Work experience:** this stage refers to entrepreneurs' work experience while working for other established companies. Most entrepreneurs had work experiences as employees. The experience may crucially influence on entrepreneurs' motivation and accumulation of practical skills. These are useful for independent business.

(iii) **Nascent stage:** the nascent stage is defined as the period during which individuals are planning and preparing to start an independent business (Reynolds 1997). This stage is considered important as a transitional period prior to actual start-up, which includes entrepreneurial opportunity recognition, business networking, and specific trigger events for start-up decision-making.

(iv) **Start-up stage:** this stage is distinguished from (iii), as this process is exclusively concerned with the actual start-up events such as financing, investment decision (particularly machine instalment), initial marketing efforts, approach to government supports, and so on.

(v) **Company development:** Entrepreneurial process cannot be ended at the stage of (iv). My investigation needs to be continued until becoming an established firm as either TNC or non-TNC supplier. During this stage, infant firms experience more advanced processes of entrepreneurial events such as advanced technology acquisition, expansion of marketing base, additional investment of new equipment, how to penetrate TNCs' early supplier involvement (ESI) partnership, approach to industrial association, establishment of relationship with government and so on.

## 6. Conclusion

The present study provides a theoretical framework to examine the emergence of entrepreneurs. A dynamic process approach is proposed to trace every step a potential entrepreneur may pursue. Entrepreneurial differences are emphasised in this study in which every entrepreneur takes different entrepreneurial paths leading to different types of entrepreneurial outcomes. The differences largely depend on entrepreneurs' traits, motivation, capabilities and perspectives. The mainstream economics implicitly assumes an automatic venture creation; however, the framework of this study does not follow this assumption but intends to provide a systematic explanation on how a capable entrepreneur comes into existence. This framework is applicable to empirical case studies.

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