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A STUDY ON INTERNATIONALIZATION OF COMPANIES

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A Study on Internationalization of Companies

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INTRODUCTION

Since the disintegration of the Soviet Union in 1989 all conditions and principles of doing business in the area has changed. The shift from a planned economy to a market economy is connected with rapid and basic changes in the political, social, economic and technological conditions in all the Eastern European countries.

The transition from a planned economy to a market economy will differ from country to country, since each individual country has to decide between a sudden or gradual transition period.

Basically, all countries have opted for a gradual transition, although the speed of the reforms varies from country to country. The transition to a market economy requires the abolishment of the planned economy bureaucracy and the reduction of central economic power. This decrease of central economic power leads to the liquidation of state monopolies in foreign trade and foreign currency management. (Fahey L & Narayanan V K, 1994) New markets have emerged as a result of the transformation in Eastern Europe and this has increased the number of markets in this region. The nine former communist states have been split into 27 new democratic states. Companies are given new opportunities to expand their business in this part of the world. Western firms face new type of problems with the internationalization process into the new markets that have emerged in the former communist states (Fahey L & Narayanan V K, 1994).

The markets of Eastern Europe have given a great opportunity to potential foreign investors, since 1989. This market consists of 400 million possible customers, with an unsatisfied demand and with a market with a low degree of competition. Before 1989 the investments in Eastern Europe were scarce and there were only a few joint ventures. Two years after the reforms of 1989, the number of foreign investments in Eastern Europe had increased tenfold (Dezutter, 1997, Djarova, 1999).

The countries of the former Soviet Union offer Western firms cost advantages, in terms of cheap labour, raw materials, energy and services, unutilised production capacities, a potential of highly qualified technical and executive employees and European like consumer behaviour. The companies that invest in the Baltic region are also attracted by the size of the markets in Eastern Europe. Foreign companies put up production facilities in the Baltic countries in order to supply the European market and the potentially growing post-Soviet markets, based on the availability of

a skilled labour force and relatively low labour costs. Another reason for considering the Baltic countries is that companies are heavily dependent of good transport and communication infrastructure in order to meet their customer's requirement of fast deliveries (Ivarsson, 1993).

The collapse of socialism and the ensuing transition process have revealed the position of Estonia, Latvia and Lithuania in an international economic perspective. The Baltic's have become competitive in sectors that generate little value-added as a result of their inferior level of technology relative to their trade partners, which are mainly the OECD-countries (Reardon 1996). Contrary to western perception the Baltic republics of Estonia, Latvia and Lithuania are not homogenous. They have different language, culture and history. Latvians and Lithuanians are the only surviving nationalities of the Baltic people, an ancient group that at one time extended all the way from Hungary to Siberia, whereas the Estonians are of the Finno-Ugric heritage. Lithuania is predominantly Catholic, whereas Estonia and Latvia are predominantly Protestant. The perception of a common identity is a consequence of fate. Each country was part of the Russian empire during the nineteenth century and briefly enjoyed independence between 1920 and 1940 before they became incorporated into the Soviet Union. Each declared independence from the Soviet Union in 1991 and has since begun a transition to a market economy.

Each country is legitimizing its independence as a historical continuum of the inter-war republics, interrupted only by the Soviet occupation. This means that they are modeling its constitution, currency and state institutions on those that existed during the independence period. (Reardon, 1996)

"Foreign direct investments (FDI) generally refer to investments where the investors purpose is to exert significant influence on the management of the enterprise in the foreign country. As opposed to passive investments such as portfolio investments where the investor is mainly motivated by the return foreseen on the investment, the emphasis in FDI is on controlling the management in the target company" (Hazley C & Hirvensalo I, 1998). FDI is done in mainly two different ways, 1. Green field investments that requires newly created enterprises or 2.

Acquisitions, which means that investors acquire existing companies or parts from them. Joint ventures refer to partly owned affiliates and subsidiaries refer to wholly owned affiliates.

"Therefore cannot co-operation agreements, subcontracting arrangements or other forms of non-equity linkages be considered direct investments, unless they involve capital transfers tied to voting rights from the investing company". (Hazely C & Hirvensalo I, 1998).

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