STROI-NETWORK

BUSINESS NETWORKS IN RUSSIA

FINAL REPORT 2009

PART 2: ACADEMIC ARTICLES

Finland *HAMK:* ***Niittymäki Seppo, Tenhunen Lauri and Weck Marina***
TUT: ***Lod Timo, Niittymäki Seppo and Tolonen Teuvo***
VTT: ***Kähkönen Kalle, Nippala Eero, Perälä Anna-Leena and Riihimäki Markku***

Russia *GSOM:* ***Minina Vera, Dmitrienko Elena and Krupskaja Anastasia***
HSE: ***Filinov Nikolay, Tretyak Olga, Settles Alex, Bek Nadejda, Buzulukova Ekaterina, Popov Nikita, Rozhkov Alexander and Vladimirova Nina***

TAMPEREEN TEKNILLINEN YLIOPISTO

HAMK UNIVERSITY OF APPLIED SCIENCES

VTT

Graduate School of Management
St. Petersburg State University

МЕНЕДЖМЕНТ

Contents

Tretyak, O. A., M. Weck, E. V. Buzulukova, A. G. Rozhkov, N. I. Popov (2009) "Developing marketing for the STROI-network. Report for Perspective 5: Marketing"

4.2 Strategic Process of Finnish Construction Companies, Building Networks in Russia (Bek, Vladimirova)

Nadezda Bek, State University – Higher School of Economics, General and Strategic Management Department, Moscow, Russia.

Nina Vladimirova State University – Higher School of Economics, General and Strategic Management Department, Moscow, Russia.

ABSTRACT

Globalization and growing competition force companies to look for new markets for their business. International operations give companies an opportunity to use their resources more efficiently and simultaneously the internationalization processes increase a firm's risks and strategic problems. The choice of an international strategy defines a company's priorities on partnership development, which are necessary for a quicker understanding of new markets' features, and also for decreasing strategic and commercial business risks. The strategic process is influenced by a number of factors, such as institutional and socio-political, and also business-sector specifics and national culture. Strategy development and implementation together with stable network relations define company's success in a new market. The paper presents the main results of an empirical research, devoted to analyses of international companies' strategies and factors, affecting strategic choice and implementation process in the Russian market.

INTRODUCTION

The processes of globalization and information technologies development erase borders between different national markets. In these conditions strategy development and implementation require account of new factors reflecting character of interaction with partners in a network, branch features, distinctions in parameters of business culture and the strategic management on national and foreign markets.

The problem of adjusting the firm-level strategy while entering a foreign market to the cultural peculiarities of the company's home and foreign cultures has been extensively studied (Barlett and Ghoshal 1995, Ohmae 1990, Prahalad and Hart 2002, Ghemawat 2001). The finding of this research was that international expansion strategy depends on several factors, both pertaining to the international context and company specifics.

Another research question that has been studied is "what occurs after the international strategy has been chosen and a company has already entered a new market?" A number of factors, which influence behavior of companies after entering foreign markets have been identified (Ghostal and Nohria 1993, Harzing and Noorderhaven 2006; Soledad and Mody 2004, Morrison, Ricks and Roth 1991). At the same time, the problem of strategic choice in response to interdependence of different business-cultures has not received appropriate attention in the literature.

One of the basic features of the "new" economy based on knowledge is network relations. These features not only change economic roles, rates, directions and mechanisms of strategic processes implementation. Changes also concern interaction forms between companies.

International inter-firm communications and network relations still, despite its importance, remain behind frameworks of traditional models of strategic and international management. Meanwhile the recent research in this area (Enright 2000, Ricart et al 2004, Hadjikhani et al 2008) gives grounds to assume that the account of socio-cultural and organizational and administrative factors, in particular, informal relations between companies, can have a critical value during strategic decision-making, concerning development and business dealing in foreign markets, geographical position of investment objects, suppliers and clients, creation innovative products, forms of partner agreements.

This article is devoted to the research of strategic processes features (decisions and actions) during business expansion outside national borders. The factors affecting strategic choice of internationalization strategy and organizational forms of it realization, establishment and development partner relations on markets, and also decisions regarding strategic control of international divisions (affiliated companies), are pointed out with respect to strategic context. National, regional, industry and intra-organizational conditions of business are considered as contextual factors.

The main objectives of the research are:

1. To define group of factors, influencing network-level strategy and doing business outside national market

2. To select forms of strategic control used in international companies for management their subsidiaries

3. To determine, what factors affect choice of strategic control form during business expansion on new markets

Objects of the research are Finnish companies, operating in Russia in the construction sector. Mainly they are the diversified companies, running one or several businesses in the Russian market.

LITERATURE REVIEW

Strategic Processes in International Companies

A company involved in global expansion overcomes borders of growth in its domestic country, realizing its competitive advantages abroad, expanding international cooperation and increasing volumes of company's foreign economic activity. Decisions about internationalization influence all management levels of the company – network, corporate, business – and functional levels (de Witt and Meyer 2005). Two sets of decisions are the most important from a strategic point of view: choice about degree of business operations standardization on foreign markets and organizational form of its international divisions (affiliated companies). Both decisions predetermine the necessary level of centralization, degree of independence of its affiliated companies, including the decision about participation in different networks.

Proceeding from the definition of network as models of mutual relations of firms and institutes, network structure is not only the result of companies' choice between market, hierarchy or hybrid forms of joint management. It is also rules that drive decisions of firms about cooperation in the certain competitive markets (Kogut 2000). These rules, in turn, are defined by industry features, social norms and institutional factors.

Two basic factors influencing the choice of a company's international strategy can be defined: the possibility of standardization on the global market and gaining advantages from economy of scope (Yip and Tallman 2009). There are two main alternatives at the ends of the spectrum (with a number of intermediate options in-between) may be examined from the perspective of standardization of company's operations:

1. Multinational strategy, based on accounting and using of peculiar national features of particular segments of the world market on which the company operates;

2. Globalization Strategy, based on application of standardized approach towards particular segments of the world market on which the company operates with only minor changes in products, services, policies and procedures.

A multinational strategy is based on studying, accounting for and using distinctions of different national markets in consumer preferences, competition, and also specifics of political, legal and social systems and structures. An efficient multinational strategy implementation depends on the level of decentralization providing delegation the rights to make strategic and operative decisions to national enterprises. It allows for accounting for local features in a company's activity in a more flexible manner. However, growth of various businesses can lead to the loss of the advantages connected with usage economy of scale. A distinctive feature of global strategy is a high level of centralization and interdependence between foreign subdivisions when they implement production and competitive strategies.

In the choice of implementation one of these strategies is based on the company's decision concerning the degree of core competences' centralization. This requires the consideration of opportunities for the coordination and management of administrative costs (Morrison, Ricks and Roth 1991).

On the one hand, the strategy of the parent company can be focused on centralization of basic functions in a head office, while delegating some authority to foreign subsidiaries. This approach requires accurate specification, what areas of responsibility need to be delegated to foreign subsidiaries.

On the other hand, the head office can distribute functional areas of responsibility between various countries in such a way that the competitive advantages of each subsidiary can be used in the most effective way. This approach involves the highest administrative costs. Moreover, it requires a high level of complex integration mechanisms and also the sharing and supporting of the same organizational culture in all international divisions of a company.

The international behaviour of companies in the 20^{th} century moves from globalization strategies towards multinational. The fact that now a significant number of companies still uses a globalization strategy can be explained. Globalization processes in the world economy promote a higher level of uniformity of different national markets, which have made economies of scale a more important factor.

The choice of an organizational form of market entry is one of the key strategic decisions within the process of internationalization. In the literature two basic forms of market entry are considered: the creation of a new enterprise (greenfield) or company purchase (acquisition) (Meyer and Estrin 2001). However the transitive form,Brownfield, has also been examined. In this case the parent company buys an operating firm, but then almost completely replaces equipment, personnel and all business processes. After the transformation period material and non-material resources of the absorbed firm, such as brand or organizational culture, are aligned with the corporate strategy of the Head office. The basic difference between Brownfield and acquisition lies in deep re-structuring planned initially and realized according to the general strategy of the company. It is chosen by firms with core competence based on combination of firm-specific international resources with specific local assets.

The choice and realization of an international strategy on a new national market are carried out under the influence of external factors. According to Enright (2002) different levels of factor analysis can be determined: subnational-, national-, clusters-, industry- and firm-level. In this research, we have examined the following factors on the firm-level: strategies, activities, governance structures of firms. Micro- or industry-level drivers include the nature of competition and cooperation in the given industry, policies that are specific to the industry, and skills and capabilities that are specific to an industry. Meso- or cluster-level drivers include inputs such as the linkages between suppliers and buyers; the nature of local demand; Macro- or national-level drivers include macroeconomic conditions, government policies at the national and regional levels, and aspects of society, including goals, interest groups, agendas, and social issues. Meta- or supranational level drivers include links with other economies outside the nation, the strategies of foreign multinational firms, and (supranational) regional linkages (Enright 2002).'

The context reflects not only institutional and cultural features of the country, but also behavior model of players - actors (Ford 1997, Hakansson and Johanson 1992) who are potential participants of a business network of the company. At national level, together with the direct participants - consumer and suppliers, institutes (the financially-credit organizations, trade unions, religious and social institutes, etc.) and state bodies can be referred to actors. Activities of such actors as the World Bank, IMF and European Union, in the field of creation, growing, or in contrast, reductions of integration processes in the world directly influence possibilities to operate abroad.

As a whole strategic choice concerning business operating in a new foreign market, is defined by corporate international strategy of the parent company and its participation in various networks. However, if the company is diversified, it can participate in different business networks, realizing different kinds of international strategy, proceeding from specificity of a certain business. Business expansion assumes an obligatory knowledge and best practice exchange between divisions (affiliated companies) in different countries. It predetermines development of internal networks within the company where constant interaction and resources and information exchange are taking place (Bartlett and Doz 1990, Kogut 1990). An internal network is a set of positions and interactions between subdivisions within one corporation. An external network should be analyzed from a perspective of separate division on foreign market as it is a link between internal and external networks (Figure 4.2.1).

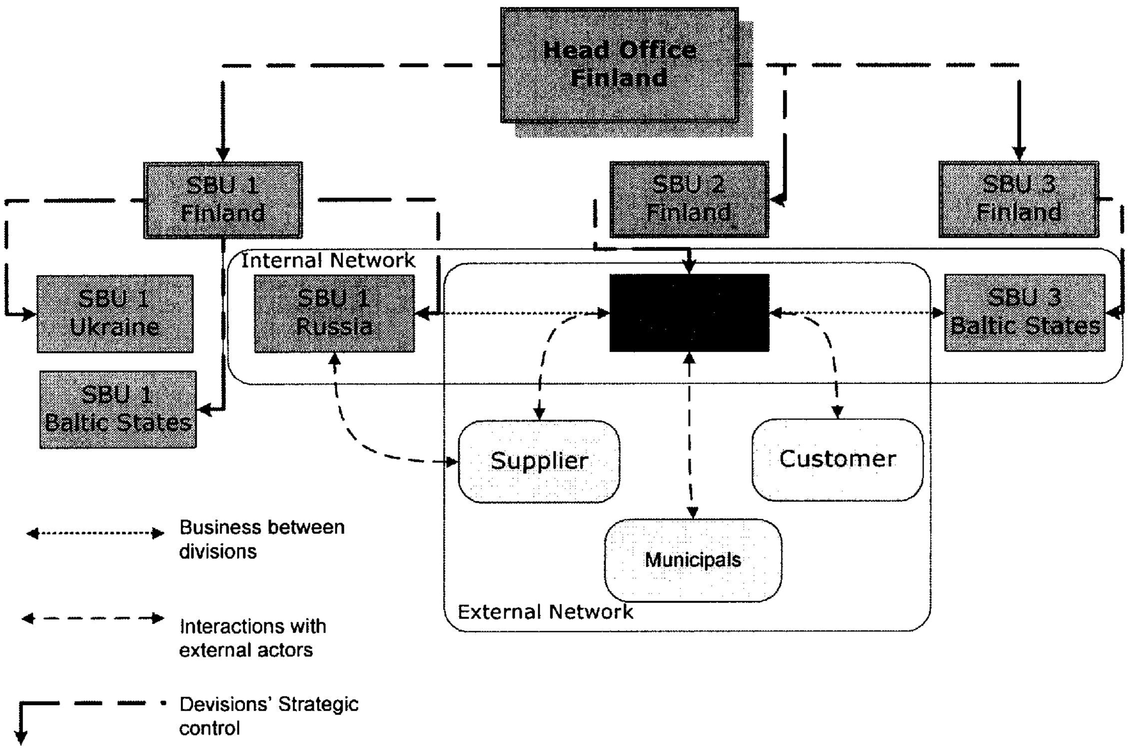

Figure 4.2.1. Interconnections between Internal and External Networks

Network development in a new national market depends on many aspects of strategy (corporate, business and functional) of a parent company. Network level strategy is an integrating link (de Witt, Meyer, 2005) that co-ordinates separate elements of strategic process (Figure 4.2.2).

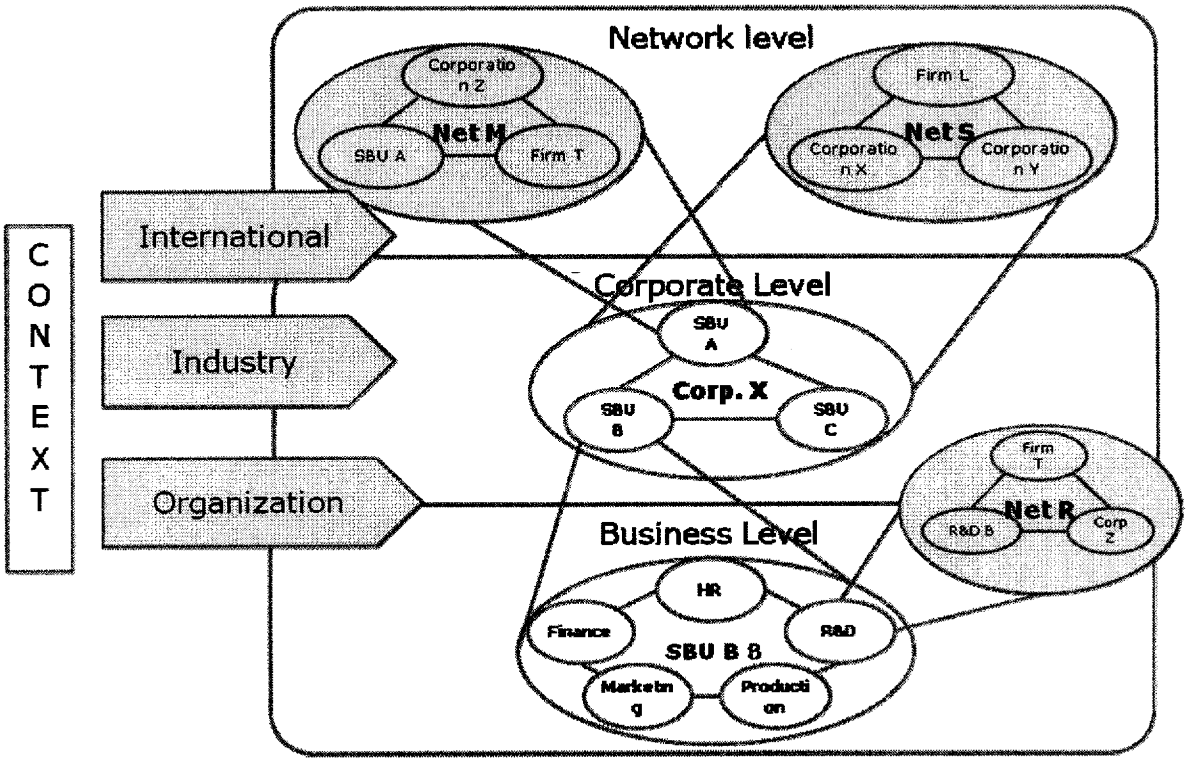

Figure 4.2.2. Network level strategy.

Within one organization it is possible to allocate several networks where it participates. Decisions connected with interaction in a certain network, can be accepted at different levels of management. So, the company as a whole can be a part of one or often more networks. If the organization is diversified, each of its strategic business unit (SBU) can participate in another network. And, at last, some divisions, for example, research and development or marketing departments can develop relations with research institutes or consulting agencies. Therefore network level strategy uniting various networks, has a difficult mobile structure, and communications between external and internal networks influence strategy implementation of all managerial levels.

Strategic control of subsidiaries out of the national bounds

There is a strategic contradiction between necessity to have more freedom and flexibility for adaptation to the various national markets conditions and provision of common vision and development of the parent company. It leads to difficulties in coordination and strategic control of foreign divisions.

Strategic control can be implemented through Corporate Centers (CC), which in different markets play different roles. There are many publications, describing and analyzing roles of CC in international company relations. We are basing our further study on the work of Nathaniel Foote, David Hensley, Max Landsberg and Roger Morrison (2008). In their paper "Role of the corporate center" these authors have suggested a set of distinguished roles that CC may play in the international activity of companies. These roles constitute a certain continuum.

On one pole there is the "Financial holding" role. A "financial holding" type company consists of a set of independent business units that have weak communications with the corporate center. In this model the functions of the corporate centre include first of all of the financial control through the tasks of budgeting and careful profit and cash flows management. The role of the CC also includes hiring, performance evaluation and firing unit managers. Thus a head office does not attempt to co-ordinate activity of business units or to attempt to create any synergism between units.

On the other pole we find so-called "Operator" who usually develops only one line of business, but has some profitable divisions that either work in different regions, or produce different goods. Between these poles there are "Strategic architect" (SA) and "Strategic controller" (SC). Corporate center as a «Strategic architect», realizes two basic functions. First, it generates the general strategy while business units have freedom for development of their own initiatives. Second, it monitors the subsidiaries businesses, periodically initiating discussions concerning general strategy of divisions. The head office as «Strategic controller» focuses on careful and often functional analysis of business units' strategy and undertakes more efforts in achieving a synergy effect.

The choice of form of strategic control is influenced by set of both internal and external factors (Figure 4.2.3).

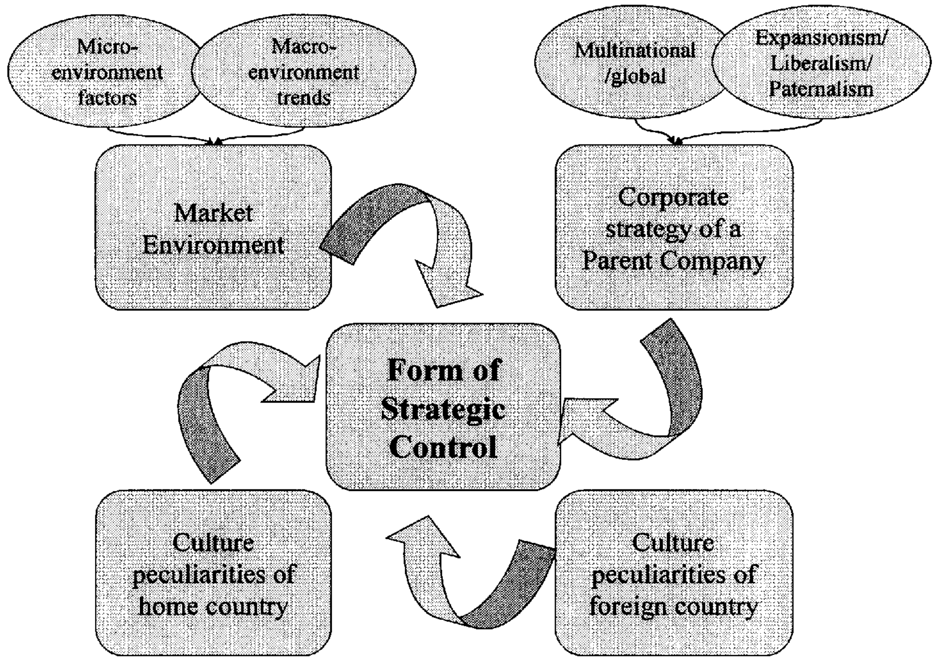

Figure 4.2.3. Factors, Influencing Strategic Control Form.

First of all, the company, making the decision on the form of strategic control, considering corporate international strategy as a vector of foreign subsidiaries' development. There are also other significant factors, such as market structure, power distribution between players, and general industry dynamics. However, it is necessary to consider cross-cultural issues as they influence control implementation directly. In practice, it is usually not easy to specify a company as one belonging to the certain type as combined forms are often used. Moreover, forms of strategic control differ across the set of subsidiaries (Filinov, Bek and Vladimirova 2009).

Besides, organizational form and mechanism of strategic control are defined by power and influence of division and its position in the whole business networks (Forsgren and Pahlbereg 1992). Influence possibility is a question of possession the central position with access to resources and to important participants of a network. Both parent company and separate division can possess these resources (Figure 4.2.4).

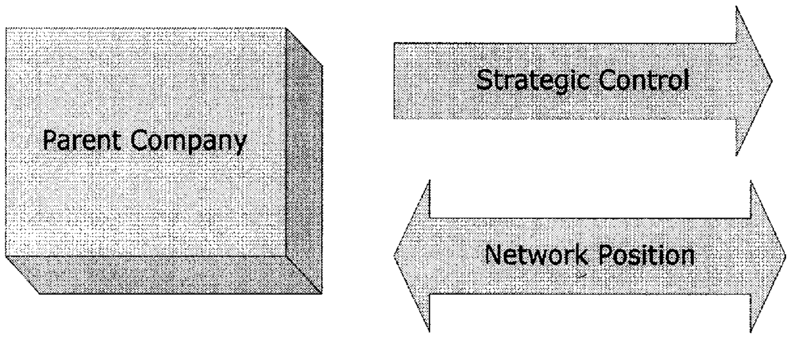

Figure 4.2.4. Interdependence of parent company and its subsidiary.

If the division possesses the possibility to control resources and takes the central position in a network on a new market, the possibility of its control through hierarchy is limited. Therefore, Head Office, implementing global strategies, can meet serious difficulties connected not only with an external context, but also with intra-organizational factors.

Divisions in different markets can vary their perception of parent company's strategy. One of the tools, allowing realizing strategic control, is Balanced Scorecard (BSC). BSC can provide control function in such mechanisms as Financial Holding, the Strategic Architect or the Controller.

RESEARCH PROJECT

Project description and objectives

The research was devoted to investigating strategic process specifics in Finnish companies, operating in the Russian market.

Research methodology

The research is based on qualitative and quantitative data analysis methods. Qualitative tools included structured interviews with top and middle management, based on a list of 40 questions covering various aspects of companies' activities. Internal documents of companies and secondary information (company websites, WEF and WB materials) were used as addition to interview results.

RESEARCH RESULTS AND INDUSTRIAL IMPACT

International strategies and forms of business ownership

The majority of the investigated companies adhere to a multinational strategy. Regionally adapted products are the main characteristic for this type of strategy. The type of business, Russian legislation, and business practice support the choice of the given strategy. However, general quality assurance and following of shared standards are complicated because of the high degree of decentralization of decisions. It is difficult to copy initial partnership models in new national market due to various influences on the companies by industries actors.

According to the parent company strategy, several businesses can enter the same market. It influences the network structure. The researched companies have confirmed that if there is another affiliated company in the same market, it will be in most cases chosen for projects development. The research has shown that companies use typical legal organization forms of development on t hRussian market. Some companies buy active businesses. However, the majority of the companies created new affiliated firms for business operations in Russia. Such organizational form as an acquisition was not examined in the considered companies. Though this form could be the most suitable to form a partnership. On the one hand, there are already established relations with suppliers, consumers and the third parties, and on the other, the introduction of new rules and procedures from the parent company allows implementing global international strategy.

Factors, influencing network-level strategy and doing business outside national market

Firstly, it is possible to define distinctions in the institutional and social environment in Finland and Russia among a group of factors influencing strategy choice of partnership. The economy of Russia and Finland differs in many parameters. Technological development, dynamical integration in global processes and preservation of national interests allow Finland to be considered as an information society. Key features of such a society are knowledge generation through information technologies, occurrence of network relations in various branches, development of infrastructure for effective network processes (Castells 2002). The Russian economy is still at the stage of industrial society. Traditional market mechanisms and more rigid organizational structures, are still strong within this economy.

Rules of the game within the market in many cases are defined by existing institutional mechanisms along with level of economic relations development. It is possible to make a conclusion that the most significant parameters of doing business in Russia and Finland differ. According to World Bank and IFC Finland is in 14th place in the rating "Doing Business" (https://russian.doingbusiness.org), while Russia is 120th . It is much easier to get permission to start a business in Finland than in Russia (43 place against 180). International trade possibilities in Russia are strongly limited in comparison with Finland (4 and 161 place respectively). (Figure 4.2.5)

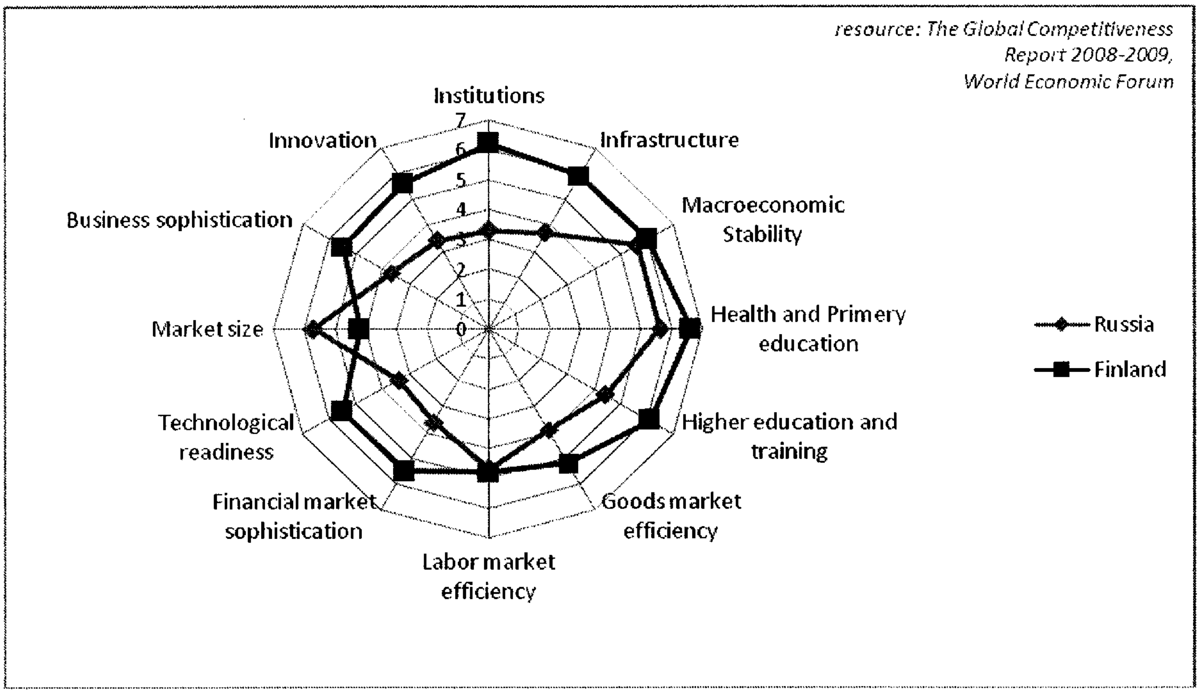

Figure 4.2.5. Macro factors in Finland and Russia.

Thus, the economies of Finland and Russia represent different economic models. This means that companies entering the Russian market need to change strategic management and adapt it to new conditions of doing business. However, the research has shown that not all companies are ready for radical changes of already developed business processes and management mechanisms.

Partnership strategies are defined not only by political and cultural features of the whole country, but also of a certain region. Complexity of defining unique dimensions for