The Operation Mode Strategies of Finnish Firms in South Korea with a Special Emphasis on Mode Switching, Mode Stretching and Mode Combination Strategies

Kansainvälinen liiketoiminta
Maisterin tutkinnon tutkielma
Heikki Huhtanen
2009

Markkinoinnin ja johtamisen laitos
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ABSTRACT

Foreign operation modes and their use are of crucial importance to any company that operates in an international environment. The previous research on foreign operation modes has tended to view these modes from a rather simple, static perspective, which, arguably, does not necessarily reflect the reality of foreign operation mode use in many international companies.

To better capture the nuances of the foreign operation mode use in contemporary international business environment, the newest research regarding foreign operation modes was reviewed in this study. It was seen that the new thinking of foreign operation modes significantly challenges the previous thinking on this field.

This study offered further research on foreign operation mode topics that have been somewhat neglected in the previous research. This research provided further evidence of mode switching that has not been covered extensively in the literature previously. This study also shed some more light on mode stretching and mode combinations, which are topics that are quite novel in the field of foreign operation modes. This research did one's bit in offering further research that has been called for by different scholars of foreign operation modes.

To shed some more light on the more novel approaches to foreign operation modes, this study analyzed empirically the foreign operation mode strategies of a selected group of Finnish firms in South Korea. A special emphasis in this analysis was placed on mode switching, mode stretching and mode combination strategies. The analysis was guided by a theoretical framework that was developed in the theoretical part of this study.

In the empirical analysis of the foreign operation mode strategies of a selected group of Finnish firms in South Korea, inter-mode switches turned out to be quite common. The inter-mode switches were mainly triggered by changes in the external environment of the studied case companies. Some evidence on mode combinations was received, although mode combinations did not turn out to be common among the case firms studied. Mode stretching was not common, either and intra-mode switches were very uncommon. The firms that did not change their foreign operation mode strategies mainly had their reasons in switching barriers and mode myopia.

The paper was finalized with the discussion of recommendations for future research. Clearly, more research is needed on these rather underresearched aspects of foreign operation modes and their use.

Keywords: foreign operation mode, mode switching, mode stretching, mode combination, South Korea, internationalization

TIIVISTELMÄ

Ulkomaantoimintamuodot ja niiden käyttäminen ovat ratkaisevan tärkeässä asemassa mille tahansa yritykselle, joka toimii kansainvälisessä ympäristössä. Aikaisempi tutkimus ulkomaantoimintamuodoista on yleensä katsonut ulkomaantoimintamuotoja hieman yksinkertaisesta, staattisesta näkökulmasta, mikä ei välttämättä vastaa todellisuutta ulkomaantoimintamuotojen käytöstä monessa kansainvälisessä yrityksessä.

Ulkomaantoimintamuotoja koskeva uusin tutkimustieto käytiin läpi tässä tutkimuksessa, jotta voitaisiin paremmin ymmärtää ulkomaantoimintamuotojen käyttöä nykyisessä kansainvälisessä liiketoimintaympäristössä. Tässä tutkimuksessa havaittiin, että tämä uusi ulkomaantoimintamuotoja koskeva ajattelu voimakkaasti haastaa aiemman näkemyksen tällä alalla.

Tämä tutkimus tarjosi lisätutkimusta ulkomaantoimintamuotoja koskevista aiheista, jotka ovat jääneet vähemmälle huomiolle aiemmassa tutkimuksessa. Tutkimus tuotti lisätodistusaineistoa ulkomaantoimintamuotojen vaihtamisesta, mitä ei ole aiemmin laajasti käsitelty kirjallisuudessa. Tämä tutkimus tarjosi myös lisätietoa ulkomaantoimintamuotojen venyttämisestä ja ulkomaantoimintamuotojen yhdistämisestä, mitkä ovat aivan uudenlaisia lähestymistapoja ulkomaantoimintamuotoja käsiteltäessä. Tämä tutkimus kantoi kortensa kekoon tarjoamalla lisätutkimusta aiheesta, mitä useat eri ulkomaantoimintamuotojen tutkijat ovat pyytäneet.

Tuottaakseen lisätietoa näihin uudenlaisiin lähestymistapoihin ulkomaantoimintamuotojen käsittelyssä, tämä tutkimus analysoi empiirisesti valikoidun suomalaisyritysten joukon ulkomaantoimintamuotostrategioita Etelä-Koreassa. Erityinen painoarvo tässä analyysissä asetettiin ulkomaantoimintamuotojen vaihtamiselle, ulkomaantoimintamuotojen venyttämiselle ja ulkomaantoimintamuotojen yhdistämiselle. Analyysiä ohjasi teoreettinen viitekehys, joka kehitettiin tutkimuksen teoreettisessa osiossa.

Analysoitaessa empiirisesti valitun suomalaisyritysten joukon ulkomaantoimintamuotostrategioita Etelä-Koreassa, havaittiin, että toimintamuotojen väliset vaihdokset olivat yleisiä. Syynä näille toimintamuotojen vaihdoksille oli pääasiassa muutokset tutkittujen case-yritysten ulkoisessa toimintaympäristössä. Todistusaineistoa toimintamuotojen yhdistämisestä saatiin hieman, vaikka toimintamuotojen yhdistäminen ei ollut yleistä tutkittujen case-yritysten osalta. Toimintamuotojen venyttäminen ei ollut myöskään yleistä. Toimintamuotojen sisäiset vaihdokset olivat erittäin harvinaisia. Niiden yritysten tapauksessa, jotka eivät vaihtaneet ulkomaantoimintamuotostrategiaansa, yleensä oli syynä vaihtamisen esteet ja toimintamuotoja koskeva lyhytnäköisyys.

Tutkimuksen lopuksi annettiin suosituksia ulkomaantoimintamuotoja koskevalle tulevaisuuden tutkimukselle. Voitiin selvästi havaita, että lisätutkimus on tarpeen tässä työssä käsiteltyjen ulkomaantoimintamuotoja koskevien uusien lähestymistapojen osalta.

Hakusanat: ulkomaantoimintamuoto, toimintamuodon vaihtaminen, toimintamuodon venyttäminen, toimintamuotojen yhdistäminen, Etelä-Korea, kansainvälistyminen

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1 INTRODUCTION

1.1 Background

Sune Carlson established a group to conduct international business research at Uppsala University in Sweden in the 1960s. He said that "international business is against human nature". His statement reflected the fact that companies that try to export or invest abroad always do so with an incomplete knowledge and a high degree of uncertainty about foreign markets and possible alternatives. In Carlson's view, doing business abroad was like taking cautious steps into unknown territory rather than a consequence of rational choice based on economic analyses. (Björkman & Forsgren 2000: 7) A lot has been gained through research on internationalization thereafter and these scary steps abroad are probably not that scary today. However, even though Carlson's view seems stunning, there is a pinch of truth in it.

Different markets always pose numerous challenges for a firm. For example, the following questions can be asked: which markets to enter, how to serve these markets, which products to offer to the market, how to organize the company to handle the international business activity, where to get personnel that has international skills and experience, how to finance the international operations, and so on (Luostarinen & Welch 1988: 85). In fact, the list could be continued on and on, because the challenges that a company faces in the international sphere are almost endless. Generally speaking, the level of complication increases as a firm enters more distant markets in terms of political, cultural and physical distance.

This study investigates the operation mode strategies of Finnish firms in the Republic of Korea, more commonly referred to as South Korea. Finland and South Korea may appear distant and different from each other but many similarities can be found as well (Korhonen 2005: 92). Personally, I was an exchange student in South Korea in 2007. Based on this experience, I concluded South Korea to be very different from Finland.

This applies also to conducting business in the country. Korean *chaebols*, conglomerates, which are usually family-controlled and government-assisted corporate groups, seemed to control many fields of business and it seemed like it was hard for a foreign company to enter to and operate in this market. Some fields of business seemed to be totally controlled by South Korean companies, whereas some other fields of business, such as fast-food and refreshment drink industry, seemed to welcome foreign entrants. All in all, I got an impression that there is something mysterious regarding doing business in this country and I became interested in business in South Korea because of this. I knew that some Finnish firms operate in South Korea successfully but at the same time, I felt that there would be possibilities for many more. Thus, the starting point for this research is personal interest in South Korea and the possibilities that the country could offer for Finnish companies.

This study strives to take a different stance towards the operation modes and strategies in their use. As discussed in the subsequent chapters of this paper, foreign operation modes have often been viewed in the international business literature as somewhat simple selections between different options. To be exact, foreign operation modes have tended to be viewed as 'singular entities' and the choices between different foreign operation modes have tended to be viewed as representing clear-cut changes from one operation mode to another. However, as declared by Benito et al. (2008: 1), "observation of business practice reveals a 'messier' reality: in particular, mode packages, mode changes and mode role changes, seem quite common." They continue that "these aspects of international business development have been relatively ignored in the literature and in theoretical and empirical research." (Benito et al. 2008: 1) Taking note of this novel approach that reflects this 'messier reality', this study sets forth at analyzing the operation mode strategies of Finnish companies in South Korea utilizing these new theories and concepts that have been proposed by e.g. Benito et al. (2008), Welch et al. (2007), Benito and Welch (1994) and Pedersen et al. (2002).

This research is closely connected to a bigger research program that is carried out in the Center for Markets in Transition (CEMAT) in the Helsinki School of Economics. CEMAT is running a research program called '*Managing Business in Turbulent Markets*', where they investigate the operations of Finnish firms and business opportunities available in the rapidly developing markets. The markets that CEMAT is interested in include China, India, Russia, South Korea, Baltic countries and Latin America. Also, the competitiveness of Finnish firms in these markets is analyzed. The empirical data is gathered by interviewing representatives of Finnish firms that are operating in these markets. The faculty of CEMAT writes a report on each market area as an operating environment for Finnish firms. For example, the report on South Korea will be labeled '*South Korea as an Operating Environment for Finnish Firms*'. The main sponsor of this research program is TEKES, the Finnish Funding Agency for Technology and Innovation.

As said, this research will be conducted alongside CEMAT's '*Managing Business in Turbulent Markets'* research program. To be exact, this research will be conducted alongside South Korean sub-program of this above-mentioned research program of CEMAT. Personally, I participate in the South Korean sub-program of CEMAT's study by conducting 10 interviews for CEMAT and analyzing them.

CEMAT is interested in three areas in the target market: Finnish firms' relations in South Korea to public sector, local partner companies and local employees. CEMAT is interested in the possible problems and solutions thereto in the above-mentioned issues. My research interest is, generally, on the operation mode strategies of Finnish firms in South Korea. More specifically, I will analyze the foreign operation mode switching, mode stretching and mode combination strategies of the Finnish companies operating in South Korea. Mostly the same interviews will be utilized for both the CEMAT's study and my thesis.

1.2 Research Problem and Gap

The research problem is to analyze the operation mode strategies of Finnish companies in South Korea. A special emphasis is placed on possible mode switching, mode stretching and mode combination strategies. These concepts, offered by e.g. Pedersen et al. (2002), Benito et al. (2008) and Welch et al. (2007) represent the new thinking regarding foreign operation modes and are, therefore, a central theme in this study.

In general, South Korea and the business of Finnish firms there have been studied quite little in Finland. Kristiina Korhonen who previously worked for CEMAT is an expert on South Korea and business in South Korea in Finland but her studies have focused on the investments between Finland and South Korea and on relations between Finnish and South Korean firms (e.g. Korhonen 2005; Korhonen et al. 2005; Korhonen and Kettunen 2006). The operation mode strategies of Finnish firms in South Korea have not been studied earlier in Finland. Thus, there is a research gap that this study sets forth to fill.

1.3 Research question

How and why are the foreign operation modes used in a particular country in terms of mode switching, mode stretching and mode combination strategies?

Empirically, this question will be answered in terms of a selected group of Finnish firms in South Korea.

1.4 Definitions

<u>Foreign operation mode:</u> Foreign operation modes (FOMs) can be defined as the institutional or organizational arrangements that are used in order to conduct an international business activity, such as the manufacturing of goods, servicing customers, sourcing various inputs – in fact, undertaking any business function. In principle, the alternatives are plentiful, ranging from various types of trade arrangements, often in

some form of exporting organizations, to investments in manufacturing operations in wholly-owned subsidiaries. (Welch et al. 2007: 18)

Foreign operation mode switching: Foreign operation mode switching refers to a situation in which a company changes its institutional or organizational arrangement, that is, foreign operation mode, from one FOM to another. Mode switching allows for more intensive operations to be developed in the markets concerned, supporting a strategy of deeper market penetration. Alternatively, mode switching may be used to recover a problem situation in a foreign market associated with existing mode use. Two types of mode switches can be identified: ‘inter-mode switches’ and ‘intra-mode switches’. Inter-mode switches imply a change of organizational form that is, in essence, the foreign operation mode in a given foreign market. In intra-mode switches, the entrant company maintains the organizational form, that is, FOM, but a new local operator is appointed. (Welch et al. 2007: 361-363)

Foreign operation mode stretching: Foreign operation mode stretching challenges the thinking of foreign operation mode switching. It is often thought that FOM switches present clear-cut changes between two distinct FOMs. However, FOM stretching views these switches as a great deal subtler, seeing a mode switch as an incremental process. Mode switches sometimes emerge as incremental processes in which one FOM virtually grows into another. The foreign operation modes that an entrant firm uses in a specific market over a period of time are not necessarily sequential, that is, mutually exclusive. It is not uncommon for entrant companies to add new FOMs to existing ones, thereby practising mode mode combination. Mode switches may also be incremental in the sense that within-mode changes precede as well as follow a formal shift of ownership and organizational form. (Welch et al. 2007: 367)

Foreign operation mode combinations: A FOM combination refers to a situation in which an entrant company adds one – or several – FOMs to an existing one, instead of replacing one FOM with another. The correct term to use for this phenomenon would be a ‘mode addition’ rather than a ‘mode switch’. The addition of one – or several – modes to an existing one may be a very temporary arrangement where the two FOMs overlap for a short, transitional period. In other cases, though, mode additions may take on the characteristics of a long-term, or even permanent, arrangement. (Welch et al. 2007: 393)

Internationalization: Broably speaking, internationalization is the process of increasing involvement in international operations. Internationalization can be expected to be associated with, and dependent upon, developments along several dimensions of the phenomenon, such as operation mode, sales objects, target markets, organizational capacity, personnel, organizational structure, and finance. (Welch and Luostarinen 1988: 84-88)

1.5 Limitations

This study investigates the foreign operation mode strategies of Finnish companies in South Korea. For its part, this research aims to some extent at helping Finnish firms to operate in South Korea more successfully. At the same time, this is a major limitation of this study: it only focuses on the Finnish companies, leaving the experiences of other firms from other countries uncovered.

2 LITERATURE REVIEW

2.1 Foreign operation modes

Whenever a company does business abroad, it is exposed to an array of new challenges and decisions have to be made regarding how its business activities in a foreign market should be conducted (Welch et al. 2007: 18; Benito & Welch 1994: 8). Also, a company may have to think how its linkages to a foreign actor should be organized (Welch et al. 2007: 18). Several definitions for foreign operation modes (FOMs) have been offered by different scholars. Welch et al. (2007:18), for instance, see that "foreign operation modes can be defined as the institutional or organizational arrangements that are used in order to conduct an international business activity, such as the manufacturing of goods, servicing customers, sourcing various inputs – in fact, undertaking any business function". Root (1994: 24) writes that "an international market entry mode is an institutional arrangement that makes possible the entry of a company's products, technology, human skills, management, or other resources into a foreign country".

While different definitions, in essence, depict the same phenomenon with slightly different words, the terminology used deserves a special note. Welch et al. (2007: 10) raise up an important point when discussing and analyzing different foreign operation modes. They see that in much of the academic literature on foreign operation modes the topic is dealt with under the heading of 'entry modes' which has become for many a generic term covering foreign operation mode use in all situations. This is the case even when modes are being switched and the actual entry context no longer applies. (Welch et al. 2007: 10) Welch et al. (2007: 10) claim that "this terminology is unfortunate as well because it has tended to focus mode thinking and analysis on the entry situation, rather than the longitudinal context in which mode use is applicable". According to Welch et al. (2007: 10), the research shows that mode change in individual foreign markets is common in internationalizing firms and mode development, sometimes even to a substantial degree, occurs with a given mode as its use proceeds. This could be called a 'within-mode' expansion in the use of a given mode. A change can be brought about also by the addition of a new mode to the use of an existing mode, rather than replacement of a mode altogether. In addition, a mode may be deleted from an initial mode package, consisting of several foreign operation modes used in conjunction in a given foreign market, after some time. Limited research indicates that mode additions to the initial mode arrangement are far from uncommon. However, there has been so little research on this phenomenon that it is hard to generalize on the circumstances, patterns of use and explanations of mode additions and deletions. (Welch et al. 2007: 10) Mode changes, mode additions and mode deletions are covered later in this study thoroughly but here they were touched upon to highlight the problem of discussing foreign operation modes as 'entry modes'. Because of the above-mentioned problem of using the term 'entry mode', the term 'foreign operation mode' is used in this study. Some researchers may refer to foreign operation modes as 'foreign operation methods', which, in essence, is the same as foreign operation modes, the terms 'methods' and 'modes' used as synonyms interchangeably.

2.2 The importance of foreign operation modes

Clearly, the selection of a foreign operation mode is of utmost importance to a firm that wants to enter a new foreign country. One could hypothesize that the selection of foreign operation mode in a particular market determines the success or failure of an international business endeavour. To highlight the critical role of this decision, we can turn to words of several well-known researchers on the field. Agarwal and Ramaswami (1992: 1) see the FOM selection as very important, if not a critical, strategic decision. Luostarinen and Welch (1988: 86), in their analysis of the development of the concept of internationalization, state that "one can perhaps argue that the future international success of companies will partly depend on their ability to master and successfully apply a range of methods of foreign operation." Welch et al. (2007: 20) see that in the short run, how a firm chooses to operate in a given foreign market is likely to have considerable impact on the revenues from and costs of being involved in that market, and the firm's exposure to the risks and uncertainties of operating there. Equally important is that such decisions have effects on the more long-term considerations regarding the degree of various types of risk, the degree of strategic and operative control, the level of resource commitment and the opportunities for the development of a company's capabilities and network connections (Welch et al. 2007: 20).

Having quoted some well-known researchers on the field and acknowledged the importance of foreign operation modes in international business, we will now turn to analyze foreign operation modes. First, the repertoire of different operation modes is presented in a cursory fashion. Due to the scope of this study, different mode options are only touched upon in this study. For a thorough review of different FOMs, please see e.g. Welch et al. (2007) or Luostarinen and Welch (1990).

2.3 The repertoire of foreign operation modes available to a firm

The options available to a firm in terms of foreign operation modes are numerous. The extant literature on the subject is vast and the classifications between different authors may differ slightly, but the general consensus among researchers classifies different operation modes roughly in three groups, that is, export modes, contractual modes and investment modes. These three broad groups are depicted in Figure 1 below:

Figure 1: The major foreign operation mode options

Exporting

- Indirect
- Direct: agent/distributor
- Own sales office/subsidiary

Contractual modes

- Franchising
- Licensing
- Management contracts
- Subcontracting
- Project operations
- Alliances

Investment modes

- Minority share (alliance) JVs
- 50/50 JVs
- Majority share JVs
- 100% owned

Source: Welch et al. 2007: 4

Exporting, contractual and investment operation modes can be termed primary modes (Root 1987: 7). As indicated by Welch et al. (2007: 3), some modes straddle such a broad classification, such as contractual joint ventures that would fit to both contractual and investment modes of entry. Welch et al. (2007: 3) continue that within these broad categories there can be many variations, and the multiplicity of mode options for firms allows for quite fine-grained variations from one market situation to another. To illustrate the multiplicity of options available to a firm and differences in terminology and categorization by different authors, another categorization of different operation modes as suggested by Root (1994: 26) is presented in Figure 2 on the next page:

Figure 2: The major foreign operation mode options, an alternative classification

Export Entry Modes	**Contractual Entry Modes**	**Investment Entry Modes**
Indirect	Licensing	Sole venture: new establishment
Direct agent/distributor	Franchising	Sole venture: acquisition
		Joint venture:new
Direct branch/subsidiary	Technical agreements	establishment/acquisition
Other	Service contracts	Other
	Management contracts	
	Construction/turnkey contracts	
	Contract manufacture	
	Countertrade arrangements	
	Other	

Source: Root 1994: 26

When analyzing the categorization of Root (1994: 26), it can be seen that Root uses the term 'entry mode' to refer to foreign operation modes. The problem inherent with the term 'entry mode' was discussed above. When the categorizations of Root (1994: 26) in Figure 2 and Welch et al. (2007: 4) in Figure 1 are contrasted, it can be seen that the main differences are in contractual and investment foreign operation modes, exporting foreign operation mode options being mostly the same. Root (1994: 26) identifies more mode options in contractual foreign operation modes than Welch et al. (2007: 4). In addition, Root (1994: 26) concentrates on differentiating between a newly-established sole venture and an acquired sole venture in investment operation modes, whereas Welch et al. (2007: 4) emphasize the different options as to how to divide the ownership in a joint venture (JV). In essence, however, the categorization by both of the authors discusses the same phenomenon, which, therefore, makes the minor differences in the content of the categories irrelevant, at least for this study.

Luostarinen (1989: 109-111) combined the different operation modes in homogeneous groups on the basis of the functional and investment character of the modes. His groupings can be seen in Table 1 one the next page:

Table 1: The combined categories of foreign operation modes

A	Non-direct investment marketing operations (NIMOS) 1. Indirect export operations for goods 2. Direct export operations for goods 3. Service export operations 4. Know-how export operations 5. Partial project export operations
B	Non-direct investment production operations (NIPOS) 1. Licensing operations 2. Franchising operations 3. Contract manufacturing operations 4. Turnkey operations 5. Coproduction operations
C	Direct investment marketing operations (DIMOS) 1. Sales promotion subsidiaries 2. Warehousing units 3. Service units 4. Sales subsidiaries
D	Direct investment production operations (DIPOS) 1. Assembling subsidiaries 2. Manufacturing subsidiaries

Source: Luostarinen 1989: 109-111

In this study, the question of how FOMs are categorized and how are they are termed is, although not irrelevant, but of minor importance. This study sets forth at analyzing the development of the use of foreign operation modes, that is, mode strategies, of Finnish companies in South Korea over time, thus concentrating on the possible changes in the use of different FOMs and their possible combinations in the course of Finnish companies' operations in Korea.

Export modes differ from the other two primary modes in that a company's final or intermediate product is produced outside the target country and subsequently transferred to it. Therefore, exporting is confined to physical products. (Root 1994: 27) Indirect export takes place when the exporting manufacturer uses independent organizations located in the producer's country and who actually do the exporting (Welch et al. 2007: 308, Root 1994: 27). In contrast, direct exporting does not use home country middlemen, although it may utilize target country middlemen (Root 1994: 27). In direct exporting, exporter sells directly to an importer or buyer located in a foreign market area (Albaum & Duerr 2008: 321). The target country middlemen, in the form of agents or distributors, are responsible for marketing exporter's product in the target market. Finally, exporting may take the form of an own sales office or a sales subsidiary. In this case, company's own operating units in the target country are responsible for marketing. (Root 1994: 27)

Contractual modes are long-term non-equity associations between an international firm and an entity in a foreign target country that involve the transfer of technology or human skills from the former to the latter. Contractual modes are distinguished from export modes because they are primarily vehicles for the transfer of knowledge and skills, even though they may also create export opportunities. On the other hand, they are distinguished from investment modes because there is no equity investment by the international firm. (Root 1994: 27) Contractual modes include franchising, licensing, management contracts, international subcontracting and project operations, with a wide range of forms within each of these categories (Welch et al. 2007: 3). In a licensing arrangement, a firm transfers to a foreign entity, usually another firm, for a defined period of time the right to use its industrial property, e.g. such as patents, know-how, trademarks, or manufacturing processes, in return for a royalty or other compensation (Albaum & Duerr 2008: 377, Root 1994: 27). Although quite similar, franchising differs from licensing in motivation, services and duration. In addition to granting the right to use the firm name, trademarks, and technology, the franchisor also assists the franchisee in organization, marketing, and general management under an arrangement that is intended to be permanent. (Root 1994: 27) Management contracts, subcontracting, project operations and alliances involve the transfer of services directly to foreign entities in return for monetary compensation or in return for products manufactured with those services (Welch et al. 2007; Root 1994: 27). Importantly, international companies often combine contractual entry modes with export or investment modes, reflecting the use of foreign operation mode combinations that is dealt with later in this study. (Root 1994: 27)

Investment entry modes involve ownership by an international firm of manufacturing plants or other units in the target country. In terms of production stage, these entities may range all the way from simple assembly plants to plants that undertake the full manufacture of a product. In terms of ownership and management control, foreign affiliates may be classified as sole ventures, meaning they are 100 % owned by the parent firm, with full ownership and control, or as joint ventures with ownership and control shared between the parent firm and one or more local partners, who usually represent a local company. An international firm may start a sole venture from scratch as a new establishment or by acquiring a local firm as an acquisition. (Root 1994: 27-28)

2.4 Foreign operation mode selection

Several theoretical perspectives have been offered to explain firms' choice of foreign operation modes. Such decisions can be very complex in their very nature. Because researchers with different theoretical and methodological backgrounds have examined them, the literature on foreign operation modes is rather heterogeneous. (Welch et al. 2007: 20)

Literature on foreign operation modes identifies two main approaches to foreign operation mode selection – a so-called 'economics-strategic' approach, and a behavioral or process approach (e.g. Welch et al. 2007: 20-42; Clark et al. 1997: 605-606; Pedersen et al. 2001: 326-327; Benito & Welch 1994: 7). The behavioral or process approach has also been termed 'internationalization process' approach by some scholars (Welch et al. 2007: 20; Benito & Welch 1994: 7) The two main approaches to operation mode selection are reviewed below.

2.4.1 Economic-strategic approach to foreign operation mode selection

The economic-strategic theories to foreign operation mode selection put a strong emphasis on rational decision making and economic considerations. According to the thinking of this ‘school of thought’, mode choice is an economic decision, and a firm is expected to choose the mode that offers the highest risk-adjusted return on investment (Zhao et al. 2004: 525). Companies are expected to choose the governance or operation mode that minimizes the costs of carrying out particular transactions (Burgel and Murray 2000: 37). Because of the strong emphasis of this approach on the effectiveness of transactions, this approach has also been termed ‘transaction cost economics’ (TCE) approach by many scholars (e.g. Burgel and Murray 2000: 37; Zhao et al. 2004; Brouthers and Hennart 2007). Brouthers and Hennart (2007: 400), in their review of international entry mode choice literature, concluded that transaction cost analysis (TCA), effectively the same issue as TCE, is the most widely used theoretical perspective in international entry mode research and appeared in almost half of the studies that they reviewed. Three TCA factors are seen to influence decisions – asset specificity, uncertainty, and frequency. Uncertainty is seen to mean both internal-behavioral and external-market specific uncertainty. (Brouthers and Hennart 2007: 400)

Asset specificity concerns a broad scope of resources particularly tailored to a relationship and reflects a company’s ability to differentiate its strategy and products. Specificity is seen to exist when one or both parties to the transaction make investment that involves design characteristics or unique resources specific to the transaction. This investment is likely to have a lower value in alternative uses. Knowledge- or information-based assets are often embedded in the people working for an organization. These intangible assets generate monopolistic advantages for companies to exploit in foreign markets but, at the same time, the very nature of intangibility and the difficulties of codifying and transferring knowledge also create a need for internalization, that is, to carry out transactions in-house instead of resorting to market mechanisms. Proprietary and specialized knowledge is also subject to maladaptation and opportunism, and this feature of specialized assets therefore requires safeguarding exchanges to reduce behavioral uncertainty. In a situation like this when it is hard to protect proprietary technologies, vertical integration simplifies protection. Therefore, it is seen that a high presence of specialized assets leads to a high degree of integration and control. What comes to external uncertainty, volatile environments are seen to compel companies to choose a flexible entry mode rather than an ownership-based entry mode. Internal uncertainty manifests itself in a company's deficient experience or knowledge of foreign markets – companies that lack international experience are hesitant to pursue foreign market entry aggressively. (Zhao et al. 2004: 526)

The economic-strategic stream of research on foreign operation modes has largely taken for granted that whenever a choice in foreign operation mode is made, it will be the most suitable one given the circumstances (Pedersen et al. 2001: 326). The principal line of reasoning in the 'economics-strategic' approach to foreign operation mode selection is that the choice is essentially a question of finding the appropriate degree of control. This degree of control has a bearing on risk exposure and companies' degree of strategic flexibility over foreign operations, given internal and external contingencies. (Welch et al. 2007: 20) The economic approaches are static approaches in their nature, examining a company's foreign expansion as a series of static choices that are dictated by efficiency considerations and relative costs and benefits (Clark et al. 1997: 605). Transactions, resources, assets, and firms are at the core of economics-based analyses (Welch et al. 2007: 42).

The economic approaches to foreign operation mode selection have been subject to a great deal of criticism, too. Benito and Welch (1994: 9) point to the concerns that have been raised about the limitations of the assumptions underlying the economic frameworks, such as their rather simplistic view of organizational decision-making behavior and the degree of rationality assumed. For instance, one simplifying assumption is the notion that different foreign operation modes entail different relative levels of control, resource commitments, and risk, which again are regarded as largely a function of ownership. Control, though, can also be gained by means other than ownership. A joint venture, for instance, may feature different levels of control – high, medium or even low control – depending on other characteristics of the actual arrangement. (Benito & Welch 1994: 9) A licensing agreement, for instance, in association with a joint venture may be an important means of raising the effective level of control, as originally pointed out by Luostarinen and Welch (1990: 39). Such combinations have rarely been dealt with in the literature as these frameworks do not encompass bundles or packages of foreign operation modes as viable alternatives. In addition, the perceived levels of control and risk, for instance, offered by a given foreign operation mode, may vary considerably across different companies. (Benito & Welch 1994: 9) Benito and Welch (1994: 9) point also to the lack of attention to the dynamics of foreign market servicing in the economics approach because of a primary focus on how firms, as rational economic actors, arrive at a more or less 'optimal' foreign operation mode into a particular market at a given point in time. They continue that less attention has been paid to changes to the initial entry decision, to how relationships between entities evolve over time and influence the decision-making process, and to how market servicing decisions interact with other aspects of the internationalization of the firm (Benito and Welch (1994: 9). Pedersen et al. (2000: 326) reinforce this point by stating that "the economics literature on foreign operation methods is basically static and tells little about *changes* of the initial entry mode". They see that the questions of how often firms change FOMs, what induces changes and what impedes them have only been paid modest attention by the international business scholars (Pedersen et al. 2002: 326).

2.4.2 Process approach to foreign operation mode selection

In contrast to the 'economics-strategic' school of thought with its strong emphasis on rational decision making, the internationalization process approach, also termed as the behavioral approach, takes as a starting point that a framework of unconstrained rationality provides limited understanding of the way companies actually make foreign operation mode decisions. Instead, the internationalization process approaches view such decisions through the lenses of limited rationality and organizational learning processes, theories that were originally presented by Cyert and March in 1963 and Simon in 1955 and 1979. (Welch et al. 2007: 33) In this approach, there is a strong emphasis on behavioral factors as driving forces over time in internationalization, of which any given step is seen as an integral part of the overall process (Benito & Welch 1994: 10). One of the reasons for the considerable attention on the foreign operation mode as a means of assessing a pattern of internationalization of individual firms is that it does represent a clearly overt manifestation of the overall process, although it is only one dimension of this process (Luostarinen & Welch 1988: 86). Being only one dimension of the overall process of internationalization, process perspectives also tend to take a more holistic approach (Welch et al. 2007: 34).

Various patterns of operation mode developments over time, also called 'establishment chains', have been revealed by different empirical studies (Benito & Welch: 10). Johanson and Wiedersheim-Paul (1975) carried out an influential research on the internationalization process of four Swedish companies. They concluded that firms that were studied went through the following stages, which they termed the 'establishment chain', when they internationalized:

1. No regular export activities
2. Export via independent representatives (agent)
3. Sales subsidiary and
4. Production/manufacturing

This conclusion was based on the fact that of the 63 sales subsidiaries which were studied, 56 were preceded by agents and this pattern was the same for all the companies that were studied. What comes to manufacturing establishments mixed findings were found but nevertheless, in no case did a company start production in a country without having sold in the country via an agency or a sales subsidiary before. (Johanson & Wiedersheim-Paul 1975: 321-322)

In this seminal research on the internationalization of four Swedish firms, Johanson and Wiedersheim-Paul (1975: 307) maintained that each stage in the establishment chain requires different levels of resource commitment and brings different levels of information about the market to the internationalizing company. Obviously, no resource commitments are needed in the first phase of no regular export activities. Each successive stage requires more resources to be committed to the market and therefore involves the company more to the market. When the company is more involved in the market, it is in a better position to get information from the market, which facilitates learning concerning the market in question and operations in that country. (Johanson & Wiedersheim-Paul 1975) This mechanism was further elaborated by Johanson and Vahlne (1977), who saw this mechanism as a kind of 'feedback link' as termed by some scholars (e.g. Benito & Welch 1994: 10). In the model of Johansson and Vahlne (1977), market knowledge is a prime development factor. They see that market knowledge and market commitment affect both commitment decisions and the way current activities are performed – the more an entrant firm learns about a foreign market, the more it is ready to commit resources to this market, and this, in turn, yields additional market knowledge, which, again, leads to increasing market commitment. This knowledge is very important in their model because they see that when entrant firms encounter problems in a foreign market, they are likely to search for solutions 'in the area of the problem', that is, the problems and opportunities are handled in their contexts instead of the entrant firm seeking for totally new solutions to solve the situation. As a result, they see the internationalization as a process where the present state of internationalization is one important factor explaining the course of following internationalization. Current activities are a prime source of experience, that is, knowledge, of the foreign market and this knowledge would be hard-to-get by sourcing it from outside of the entrant firm. Instead, this knowledge has to be acquired through a long learning process in connection with current activities. This is an important reason, they claim, why the internationalization process often proceeds slowly. (Johanson & Vahlne 1977)

When discussing this important knowledge, Johanson and Vahlne (1977: 28) distinguish between objective knowledge and experiential knowledge. Their argument is that experiential knowledge is the critical kind of knowledge in internationalization because it can only be learnt through personal experience – in essence, through the operations in a given country. Objective knowledge, on the other hand, can be taught, which simplifies the acquisition of this type of knowledge. They also distinguish between market-specific knowledge and general knowledge. They see that market-specific knowledge can be gained mainly through the experience in the market, whereas knowledge of the operation can often be transferred from one country to another. (Johanson & Vahlne 1977: 28)

Luostarinen (e.g. 1989) has done remarkable research on the internationalization of Finnish companies. A major work by him was the research on the internationalization process of Finnish firms where he utilized responses from 1006 companies. In this study, the operation mode use of the studied companies was only one dimension that was studied as an indicator of internationalization but, largely, his findings support the notion of gradual internationalization as suggested by Johanson and Wiedersheim-Paul (1975) and Johanson and Vahlne (1977), for instance. To easen his analysis, Luostarinen combined the different operation modes in homogeneous groups on the basis of the functional and investment character of the modes as discussed above in part 2.3 and depicted in Table 1. Luostarinen found that 97 % of the companies that were studied started their internationalization by utilizing marketing operations instead of production operations. Non-investment marketing operations (NIMOS) were used first, before direct-investment marketing operations (DIMOS), in 98 % of firms. Non-investment production operations (NIPOS) were usually used before direct investment production operations (DIPOS). NIMOS were used by 98 % of the companies as the first penetration method abroad, DIMOS by 64 % of the companies as the second operation type abroad, NIPOS by 44 % of the firms as the third operation mode abroad and DIPOS by 60 % as the last penetration method abroad. (Luostarinen 1989: 122)

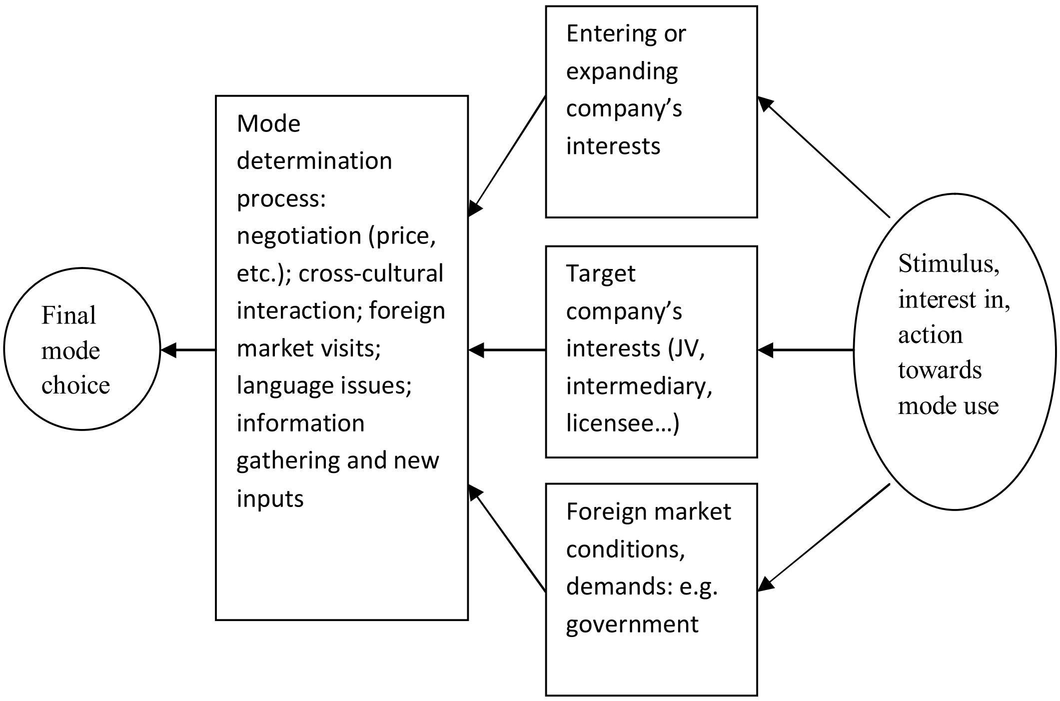
Despite having received empirical support, process models are frequently criticized for being too deterministic and for failing to take firm-specific factors other than experience into account. (Burgel & Murray 2000: 37) Clark et al. (1997: 608) point out that a number of studies fail to corroborate the notion that firms increase their commitment to individual markets through the four successive stages of the establishment chain. For instance, Hedlund and Kverneland (1985: 56) found contradicting evidence for the establishment chain when they investigated the entry of Swedish firms in Japan. They concluded that entry and growth strategies are changing to more direct and rapid entry modes than those implied by theories of gradual and slow internationalization processes. In their study, about half of the companies went directly from a sales agent to manufacturing in Japan, instead of taking the route via a sales subsidiary. Importantly, they claim, “the extent of companies’ general international experience is associated with the degree of directness of approach”. (Hedlund & Kverneland 1985: 56) The role played by general international experience is further emphasized by Clark et al. (1997) when they challenge the role of market-specific knowledge that was underlined by Johanson and Vahlne (1977). Clark et al. (1997: 617-618) make a strong argument against the underlying assumption that each entry decision and subsequent modal shifts in a market is made in isolation of the decisions in other markets. They claim that experiential knowledge from within a specific national market represents only one source of information to the firm but that the general knowledge of operating internationally has a critical impact on the market servicing decisions in individual countries. As a consequence of this, companies do not necessarily develop incrementally along an identical continuum in each market they enter. Instead, if a company enters different foreign markets via export, and subsequently enters other nations via sales subsidiaries, a move direct to foreign direct investment is not a fundamental deviation from the evolutionary model of internationalization that was suggested by Johanson and Vahlne (1977) – the sequential development has occurred at the company level rather than within individual markets. (Clark et al. 1997: 617-618) Welch and Luostarinen (1988: 91) reinforce this point by claiming that “as skills, experience and knowledge in the use of a more advanced form of operations are developed in some foreign markets we might expect that this will eventually allow a company to leapfrog some intermediate steps in others”. According to Clark et al. (1997: 618), this suggests that direct moves to FDI in individual markets should not be considered in isolation to the development of operations in other markets. They continue that “the pattern within individual markets may not be as neat and evolutionary as that indicated by the Nordic case studies, but nevertheless at the level of operating firm, when account is taken of the institutional development in all foreign markets, a stepwise pattern is observed.” (Clark et al. 1997: 618-619)

2.4.3 Models for foreign operation mode selection

Clearly, FOM choice is not a simple exercise for any company. As stated by Welch et al. (2007: 451), "mode choice is a difficult domain for companies". They see that the more a firm engages in systematic investigation as a prelude to FOM choice, the greater the number of mode options that are likely to be exposed, with increased complexity of potential combinations, and the more that unresolvable, conflicting objectives in this choice process may be unearthed (Welch et al. 2007: 451). Erramilli and Rao (1990: 137) see the company's choice of a particular FOM as a function of a large number of diverse factors. It varies with product characteristics such as degree of differentiation, importance, age and technological content. It may also depend on certain firm characteristics such as size and resources, degree of diversification, and corporate policies. Finally, FOM choice may also be determined by external environmental factors, such as host country trade and investment restrictions, host country market size, host country geographic and cultural distance, and exchange rate fluctuations. (Erramilli & Rao 1990: 137) Erramilli and Rao (1990: 137) term these product, firm and environmental variables as "nonbehavioral" determinants. They also acknowledge the role of the knowledge of foreign markets, and especially lack thereof, in connection with the "behavioral" factors that play a role in a wide range of international marketing decisions, such as initial involvement in foreign markets, choice of country markets, and choice of FOMs (Erramilli & Rao 1990: 137). The role of knowledge was discussed in part 2.4.2.

Having recognized the complexity of the foreign operation mode choice, it is worthwhile to simplify this phenomenon a little bit. It is outside the scope of this study to review and discuss each different model for operation mode selection, keeping in mind that this study investigates mode strategies – mode switches, mode stretches and mode combinations – of Finnish firms in South Korea, not exactly just mode choices. Therefore, only one mode selection scheme is presented here, that presented by Welch et al. (2007: 442). This scheme is presented in Figure 3 on the next page:

Figure 3: Foreign operation mode choice



Source: Welch et al. 2007: 442

The model represented by Welch et al. (2007: 442) that is depicted in Figure 3 can be read as follows: a firm's stimulus, interest in, and action towards mode use is mediated through the firms own interests, target or partner company interests and foreign market conditions, which leads to the mode determination process. This process, then, leads to final mode choice. However, the term 'final' is a bit misleading, since it can be argued that mode choices are made all the time, not just when a country is initially entered. As seen by Welch et al. (2007: 11), passage of time creates new influences, which may lead to a perceived need for mode change, and, as a result, choice of a new operation mode. This represents mode switching that is discussed later in this study.

The FOM choice model presented above in Figure 3 was only illustrated to bring the reader to the context in which FOM choices take place. As said, FOM choices are not in the focal point in this study, and therefore, further discussion on different FOM choice models is bypassed at this point.

2.5 Foreign operation mode switching

2.5.1 Why mode switching?

Despite increasing evidence of considerable instability in foreign operation modes, such as switches from one mode of operation to another, and even though companies often appear to use certain types of modes for relatively short periods only, these aspects have been largely neglected in the literature (Benito et al. 1999: 214; Pedersen et al. 2002: 326). Most firms with international operations will eventually experience switches of foreign operation modes. Some companies may even develop standard routines for such undertakings. (Welch et al. 2007: 361) Operating in a turbulent environment, firms by no means have a proven guarantee that a mode decision once made will remain the best way of servicing a foreign market (Pedersen et al. 2002: 325). Mode switching allows more intensive operations to be developed in a foreign market, which supports a strategy of deeper market penetration (Welch et al. 2007: 361). The entrant firms themselves evolve over time and as they grow larger and become more experienced, barriers to high-commitment operation modes tend to diminish (Pedersen et al. 2002: 325-326). Alternatively, mode switching might be used to recover a problem situation in a foreign market that is associated with the existing operation mode use (Welch et al. 2007: 361).

When companies do mode switches, internalization is a common outcome. Internalization in this context means a transition from serving the foreign market through an outside agent to an in-house operation in that market, most often in the form of an FDI. Examples of internalization processes are switches from independent local distributors to own sales subsidiaries, from licensing arrangements to production subsidiaries, and from franchised outlets to company-owned outlets. Mode switches in the form of externalization are less obvious but not uncommon, though. Examples are conversions from company-owned shops into franchised shops, and outsourcing of foreign subsidiary production to local contract manufacturers. (Welch et al. 2007: 361-363)

Welch et al. (2007: 363) see that both internalization and externalization processes in the foreign markets are so-called 'inter-mode' switches. Inter-mode switches imply a change of organizational form that is, in essence, the foreign operation mode in a given foreign market. In contrast to inter-mode switches, entrant companies also make 'intra-mode' switches. In these cases, the entrant company maintains the organizational form, that is, FOM, but a new local operator is appointed. As an example, an entrant firm may cancel its contract with a local sales agency and thereafter appoint a new sales agent. (Welch et al. 2007: 363) The reasons for the change of foreign intermediary are numerous. In some cases, the entrant firms simply have to find a new intermediary because the old one left the industry, went bankrupt, or was taken over by a competitor. In most cases, however, it is the exporter that takes the initiative to terminate the agreement with the existing intermediary and subsequently starts cooperating with a new sales agent or distributor. The exporting firm does so because it expects to do better with another intermediary, frequently arguing that the performance of the existing intermediary has not been satisfactory. (Petersen et al. 2000: 46) Petersen et al. (2000: 59) concluded that foreign intermediaries are generally appointed on loose grounds, and only in rare cases do the exporting firms' choices prove to be optimal. Their observation was in line with previous studies of companies' internationalization process that describe exporters' recruitment of foreign intermediaries as spontaneous and incidental, rather than thoughtful and planned. They saw that this was the case for both experienced and in-experienced exporters. Their results indicated that firms' ability to learn is rather limited and that their capability of selecting appropriate intermediaries is not enhanced by increased experience of doing business with foreign intermediaries. (Petersen et al. 2000: 59-60)

According to Welch et al. (2007: 363), companies switch FOMs for two basic reasons: either as a correction of managerial misjudgments or as an adaptation to new circumstances as foreign operations evolve. Decision-makers' perceptions regarding costs, risks, and benefits of being involved in a market change as they learn more about that market (Pedersen et al. 2001: 327). As a result, managers may find that the initial mode of foreign operations was founded on false premises, and, therefore, a mode shift seems compelling (Welch et al. 2007: 363). Quite often, managers are seen to rush into mode decisions that generate negative outcomes; companies do not necessarily make decisions in the rational manner suggested by classical decision-making models (Calof 1993: 116). The initial wrong selections having led to problems, sometimes managers or their successors recognize their FOM misjudgments and take steps to correct them (Welch et al. 2007: 363-364). Another and perhaps more important reason for mode switches is that internal as well as external factors may change considerably after the initial foreign market entry, sometimes in rather unforeseen ways, which renders the original entry mode less suitable given the new circumstances (Welch et al. 2007: 364; Pedersen et al. 2001: 326). The change factors that trigger mode switches are numerous and of very different character. In most cases, though, the changes relate to the local market, the local operator, or the entrant company itself. (Welch et al. 2007: 364)

Dissatisfaction with local intermediaries is a major reason for intra-mode switches but less so for inter-mode switches. Because the dissatisfaction is with the operator rather than the operation mode as such, entrant companies in many cases will remedy the situation by replacing the operator. Sometimes, though, suitable alternative operators may not be available, which forces the entrant firm to take over, that is, internalize, the local operations. The dissatisfaction with the local operator often prompts a critical appraisal of the existing operation mode. Companies may see that if changes are needed anyhow, perhaps the whole operation mode should be changed. Decision theory suggests that managers often take actions as reactive, ad hoc responses to emerging problems, in contrast to proactive follow-ups on recurrent appraisals of existing business practices. Thus, mode switches tend to appear as problem-solving devices rather than as systematic streamlining of the entrant company's organizational structure. The important exception to this, are mode switches in connection to changes of management in the entrant company. A new management team is more inclined to enforce changes and unlikely to indulge with the expectations of the organization. (Ibid. 2007: 364-365)

Growth aversion within local operators may lead to increasing dissatisfaction within the entrant company. Paradoxically, this dissatisfaction grows out of business success, that is, the increasing sales in the local market which at a certain point strain the management resources of the local operator. Normally, the local operator would just expand the management team and increase the delegation of management tasks. However, local operators may be closely-held companies in which the founders take pride in maintaining the daily control of all business functions. Because of these private reasons, the founder may resist management delegation and expansion of the firm beyond a certain size, reflecting the growth aversion of the company and forming, thus, a major barrier for the exporter to develop its business in the target market in question. (Ibid. 2007: 365)

Sometimes a change in foreign operation mode can be triggered by new ownership or management of a local operator. In principle, the entrant company can just accept the new ownership or management or appoint another local operator but only in principle. In practice, the suitability of a foreign operation mode tends to be closely related to the identity of the operator. In a management decision context, the two issues – FOM and the identity of the local operator – cannot always be separated. For instance, a license arrangement may be regarded as a superior FOM because of the manufacturing skills and market position of the particular licensee. However, in the case of the local operator's exit, licensing may not constitute an optimal FOM to the entrant company because an equivalent local operator may not be available or willing to become a licensee. In addition, replacing a local operator often evokes increased communication and bonding costs in relation to a new partner. It may take a long time to obtain the level of informality and confidentiality that characterized the previous relationship – the entrant company must foresee higher communication costs and more uncertainty during the first years of collaboration with a new operator. These additional costs, then, may tip the balance in favour of internalizing the local market activities. (Ibid. 2007: 365-366)

According to Welch et al. (2007: 366), local market growth is probably the most decisive factor for both re-localization and internalization of international operations. At a certain point in time, local market growth may justify local production instead of serving the market from home through exporting, for instance. Sometimes it may be preferable to include a licensing agreement as an intermediate stage. The change factor in these models is the growth of sales in the local market. Assuming that a production unit, such as a manufacturing plant, has a certain minimum efficient technical scale, below which unit production costs rise rapidly, at a certain point sales in the foreign market will reach a volume that allows for throughput and scale economies that are sufficient for running a local production unit cost-efficiently. (Welch et al. 2007: 366)

Market liberalization, in the form of a change of local government policy on foreign ownership, is a potentially important external factor. Often governments in emerging markets have imposed restrictions on foreign ownership of companies in certain, strategic industries, thus impelling entrant companies to form joint ventures with local firms. As these restrictions are lifted, entrant firms tend to switch to fully-owned subsidiaries. (Ibid. 2007: 367)

Change factors may also grow out of the entrant firm itself. The growth of the entrant firm can be important. (Ibid. 2007: 367) When a foreign market is entered, the entrant company may be constrained in terms of resources available, leading the entrant firm to exclude any mode of operation that involves substantial requirements of capital or management resources (Welch et al. 2007: 367; Welch and Luostarinen 1988: 93). This would obviously make the entrant firm to select a low-commitment operation mode in this situation. However, in the long run, the entrant company may accumulate capital and excess management resources. (Welch et al. 2007: 367) The more resources that are available, the stronger the ability to serve foreign markets through high-commitment modes such as setting up own sales forces (Pedersen et al. 2002: 332). In this new situation of abundant capital resources and underutilized management capacity, it would seem appropriate to replace the low-commitment foreign operation mode with in-house arrangements, such as sales subsidiaries or company-owned outlets (Welch et al. 2007: 367).

In addition, the entrant company may become less risk-averse as a result of business diversification: growing bigger, the entrant firm may become less risk-averse and therefore more inclined to take over operations in foreign markets. In the first phase of international expansion, companies usually pursue rather limited geographical diversification. Being novices in international marketing, they tend to be averse to risk and therefore they tend to avoid high-commitment modes such as having their own subsidiaries and rely on external intermediaries instead. Their foreign partners, such as a foreign sales agency or a licensee, often have no geographical diversification, either, but they usually spread their business risk over product lines or over several exporters, such as in the case of a sales agency. As a result, these foreign partners tend to be risk-neutral. As time passes, though, the risk profiles are likely to change. While the entrant company often increases the number of foreign markets in which it operates, the local sales agent or the licensee may find that a growing proportion of its total turnover is concentrated in the product lines of the entrant company. As a consequence, the entrant firm moves towards becoming less risk-averse and, eventually, becomes risk-neutral, whereas the foreign sales agent or licensee, for instance, move in the opposite direction, or keep their risk preferences unchanged. As a result of this development, at a certain point the entrant firm may find it economically beneficial to take over the business risk by integrating these overseas operations. (Ibid. 2007: 368)

Importantly, learning about the local market and different FOMs may evoke foreign operation mode changes. Decision-makers tend to perceive market risk as being high whenever they lack knowledge about a foreign market. (Ibid. 2007: 368) According to Johanson and Valhne (1977: 28), this knowledge that is central to the development of international operations of a given company in a given foreign market can be divided into two subcomponents: objective and and experiential knowledge as discussed earlier. Their argument was that objective knowledge can be taught, whereas the experiential knowledge can only be learnt through experiences during the operations in a given country. Experiential knowledge in a given foreign market is seen to be critical kind of knowledge in this context. (Johansson and Vahlne 1977: 28) Lacking this important experiential knowledge leads to increased uncertainty regarding market conditions in a given foreign market, which tends to restrict the choice of foreign operation mode of entrant firms to low-commitment arrangements (Luostarinen and Welch 1988: 95) As time passes, entrant companies gradually accumulate market knowledge, partly because information flows increase as a result of their interaction with local operators, but also by more actively seeking it through visits to foreign markets (Pedersen et al. 2002: 330).

Although the accumulation of market knowledge may occur at a decreasing rate, as entrant companies become more knowledgeable about a foreign market, the attraction of high-commitment foreign operation modes increases (Welch et al. 2007: 368; Pedersen et al. 2002: 330). Often, the main motive for entrant companies to form JVs with local firms is to benefit from the local market knowledge of the latter. Arguably, this market knowledge is difficult to buy on an arm's-length basis. (Hennart 1988: 365-367) After acquiring experience and knowledge on the local market through the JV arrangement, the entrant firm will no longer need the local JV partner and the entrant firm may convert the JV to a wholly-owned subsidiary (Gomes-Casseres 1987: 100).

2.5.2 Barriers to mode switching

While change-inducing factors, discussed above, certainly are important, such a description of mode changes seems one-sided, since it ignores that several factors can make mode changes difficult to implement, or even, from an economic perspective, poorer alternatives in the first place (Pedersen et al. 2002: 326). There are many barriers which may hamper firms' switch of foreign operation mode (Welch et al. 2007: 369). These barriers or factors have broadly been termed 'switching costs' (e.g. Weiss and Andersson 1992: 112; Benito et al. 1999; Pedersen et al. 2002: 326). To be exact, the concept of switching costs refers to difficulties – or costs – in changing the current behavior of companies, for instance regarding their foreign operation modes (Pedersen et al. 2002: 331).

According to Benito et al. (1999: 214), even if it becomes necessary later to adjust the initial entry mode, it is often assumed that changing to a completely different way of serving the market will be very difficult and costly. As stated by Anderson and Coughlan (1987: 71), "channel choices, once made, are often difficult to change". This point was further emphasized by Burgel and Murray (2000) in their study of operation mode choices of a sample of 246 UK high-technology firms on entry to the foreign markets in which they were operating. They concluded that the strongest predictor of the chosen foreign entry mode was the existing, domestic sales mode of the firm, underlining the importance of the presence of the embedded routines and experiences with the domestic sales mode (Burgel & Murray 2000: 54).

It was said above that mode switches have largely been neglected in the international business literature. In addition, it is seen that the concept of switching costs has also been overlooked in the international business literature. (Benito et al. 1999: 214; Pedersen et al. 2002: 326)

Some switching barriers are very distinct and tangible, whereas others are more subtle. Indemnification costs that are associated with termination of distributors, for instance, are an example of very distinct and tangible switching costs. On the other hand, the uncertainty about the true costs of acquiring a local distributor, including the estimation of post-acquisition costs, is an example of more subtle switching costs. (Welch et al. 2007: 369) Often, the switching barriers are not so much about expected costs but more about the opportunity costs of sales revenue that may be sacrificed as a consequence of dismissing an outside agent who maintains strong bonds with local customers (Welch et al. 2007: 369; Pedersen et al. 2002: 331). Local customers will often identify the export product with the local sales and service organization rather than with the manufacturer or exporter. Therefore, if the terminated intermediary manages to replace the products of the exporter with close substitutes, there is a considerable risk that many of the customers will stick to the intermediary. (Pedersen et al. 2002: 331) Thus, taking over the marketing activities could lead to a direct loss in sales, either permanently or for a time. Hence, switching barriers refer to outlays and expenses that are incurred as well as potential loss of revenues, as discussed above. What comes to expenses, a switch from a foreign sales agency to a sales subsidiary, for example, may entail switching costs in the form of severance payment to the former sales agent. This severance payment is a sum of money paid to the foreign agency to compensate for the premature cancellation of the contract. (Welch et al. 2007: 369) Another example, as suggested by Welch et al. (2007: 369), could be the legal expenses paid by an entrant company when a dispute regarding the conditions of terminating a local operator's contract is settled by litigation.

Cancelling a contract with a local distributor could also result, albeit more indirectly, in revenue losses elsewhere, by affecting the reputation of the entrant company adversely with the distributors in other markets. To illustrate, an exporter's termination of a distributor in one of its foreign markets gives rise to uncertainty among distributors in other markets about the exporter's general commitment to long-term collaboration. As a result, the other distributors may take precautions in response to this uncertainty. Either the distributors will ask for economic guarantees in the form of credible commitment to continued collaboration or the distributors will adjust their investments and activities accordingly, reasoning that operations which entail exposures to hold-up risk should not be undertaken. (Welch et al. 2007: 370) Thus, the loss of reputation regarding enduring relations may entail indirect switching costs in the entrant firm's markets as a whole (Ibid. 2007: 370; Benito et al. 1999: 218-219).

Although Weiss and Anderson (1992: 105) did not distinguish between outlays and revenue losses, they call these costs 'take-down' costs or barriers. According to Welch et al. (2007: 370), mode switches may also entail various expenses and revenue losses in setting up a new mode – the 'set-up' costs. For instance, by dropping an outside agent the entrant company must undertake what are often quite substantial investments in hiring and training people in order to establish its own marketing or production arrangement in the foreign market (Welch et al. 2007: 370; Pedersen et al. 2002: 331). In addition, as commonly noted in the internationalization literature, companies that are expanding into new markets or serving markets in new ways cannot usually rely entirely on their existing stock of knowledge (Welch et al. 2007: 370). Much of the knowledge that is needed is of an experiential kind, which can mostly be gained through a process of learning-by-doing (Luostarinen and Welch 1988: 94). Welch et al. (2007: 370) see that adjusting and fine-tuning business activities in order to become fully competitive in a new market context will take a while and the efficiency is likely to suffer during this time. In addition, since novice companies are more prone to making mistakes that result in lost sales, revenues may also suffer (Welch et al. 2007: 370). To the extent that firms are unfamiliar with the markets and operation modes in question, the anticipated learning costs, and, therefore, the loss of revenue, may act as an impediment to setting up new operations (Ibid. 2007: 370; Pedersen et al. 2002: 332).

The entrant company may switch operation mode by taking over the local operator either partly or completely instead of breaking up and starting from scratch with a new organization. This kind of acquisition may, however, be constrained by switching costs, just as with taking down operations, although these switching costs are of a different nature. First, the acquirer may incur 'bundling costs', which are the costs of acquiring assets of little value, but nevertheless imposed as part of a greater deal. To illustrate, the entrant firm may acquire a local distributor in order to get access to a valuable distribution network, but as part of the acquisition package inherit a number of distributorships of producers with which the entrant company has only vague, or no, relations. These distributorships represent assets of little or no value to the entrant company, and any price paid for these useless assets effectively constitutes a switching cost, indeed. (Welch et al. 2007: 371)

A conceptually different type of switching cost concerns barriers of a more qualitative kind, such as the way decision makers perceive risk and uncertainty, their relations with other people, or even an apparent attachment on their part to specific courses of action. This, in turn, may reflect a vested interest in maintaining the status quo. An important type of perceptual switching cost is the increase in assumed risk that decision makers perceive when they consider replacing a well-known, low-commitment mode with an unfamiliar, high-commitment FOM. Case research suggests that changes in the mode of foreign operation are sometimes delayed for a considerable time, or, in the extreme case, are not carried out at all, even though they might seem appropriate in an economic or strategic perspective. A critical factor appears to be the perceptions and opinions entertained by managers and entrepreneurs. Because the managers of an exporting firm may be reluctant to accept anything but a small incremental increase in the commitment of resources and the attendant market risk, a switch from a sales agent to a wholly owned sales subsidiary may very well be impeded by the higher market risk involved in setting up a subsidiary. (Ibid. 2007: 372; Benito et al. 1999: 219-220)

In addition to constituting set-up barriers, perceptual switching costs may also be in operation when it comes to discarding current business practices (Welch et al 2007: 372; Benito et al. 1999: 220). Thus, they may act as a take-down barrier, perhaps because personal ties have been developed with a foreign agent over a long period (Ellis

2000: 462). Also, since changing current operation modes can be interpreted as an admission of earlier mistakes in the choice of operation mode, decision makers may regard a change as carrying a personal risk, such as loss of prestige, or even a possible career setback. As a consequence, rather than exposing themselves to such risks, they retain their established practices. (Welch et al. 2007: 372; Benito et al. 1999: 219-220)

To sum up, there are different types of switching costs that are either easily quantifiable or more of a blurred nature, each of them having an impact on the decision to switch from one operation mode to another. These switching costs, also termed switching barriers, are depicted in Table 2 below:

Table 2: Types of switching barriers

Categories of switching barriers	**Take-down barriers**	**Set-up barriers**
Costs	• Termination compensation (severance payment) • Lawsuit expenses	• Hiring/recruiting and training costs • Foreign operation learning costs • Costs of acquiring local operator assets of little or no value to the entrant firm
Revenue losses	• Reputation effects among local operators in other markets • Loss of customers owing to their loyalty to current agent	• Loss of customers owing to failures in initial phase of own operation • Costs of integrating the acquired local operator
Perceived barriers	• Personal bonds to individuals in existing foreign operations • Loss of prestige for managers responsible for initial mode decision • Risk of career setbacks	• Risk associated with 'new' foreign operation method perceived as being unacceptably high

Source: Welch et al. 2007: 373

2.5.3 The implementation of mode switch strategies

According to Welch et al. (2007: 372), the ideal mode switch strategy aims for more than eliminating switching costs. It also ensures that the switch, or the anticipation of a switch, in no way makes the local operator disinclined to exploit the opportunities in the market. Put differently, the entrant company should see to it that its local operators consider a mode switch as a natural and acceptable, or even a welcome, part of the collaboration. As such, it should be seen as an event that is discussed and negotiated openly between the business parties. (Welch et al. 2007: 372-373) Petersen et al. (2000: 692) write that "given the tendency to seek greater control through alternative operation modes, it would seem important that companies put in place the means to facilitate the process of switching modes in a way that minimizes the associated difficulties and costs."

To implement a foreign operation mode switch from using a local intermediary to an in-house arrangement successfully, the relationship and its development with the local operator is of crucial interest. According to Welch et al. (2007: 375), the 'termination dilemma' adds to the difficulty of managing the relationship with a local intermediary. Poor performance, as seen by the entrant company, increases the likelihood that the collaboration will come to an end. Alternatively, the entrant company may replace the local distributor with its own sales organization that operates from home country or that is located in the export market. In this case, it is less obvious that dissatisfaction with the local distributor is the only decisive factor for the termination. In fact, the entrant company's decision to integrate the sales and marketing responsibilities may be triggered by large sales in the local market, which could actually be a result of the effort made by the local distributor. Interestingly, to the extent that ending the local distributor relationship can be attributed to the successful sales effort of the same local distributor, this is an unfortunate and somewhat paradoxical consequence as seen through the lens of the distributor. (Welch et al. 2007: 375)

According to Welch et al. (2007: 375), there are strong reasons to believe that local operators are generally aware of the termination risk that they face. As a result, in order to keep the assignment, local operators may, therefore, aim for mid-level performance. Yet, local operators cannot know exactly what the entrant company considers to be the basis for termination. In other words, there are limits to how well local operators know the utility functions of their foreign business partners, that is, the entrant companies. In addition, exogenous factors may affect the foreign market performance in an unforeseeable positive or negative direction. The sales revenue achieved in the foreign market, which is only partially controlled by the local operator, may turn out to be less than acceptable to the entrant company, but, at the same time, also more than sufficient for establishing a subsidiary. In both cases, a likely result is termination. (Welch et al. 2007: 375)

Interestingly, both low and high performance will put the foreign distributor at risk of being terminated. If the foreign distributor is performing poorly, the entrant company may lose its patience, terminate the relationship, and then appoint another local distributor in the foreign market. If the local distributor is doing well and boosting the sales in the foreign market, the entrant company may find it lucrative to terminate the distributor contract and take over the sales and marketing responsibilities. (Ibid. 2007: 375; Petersen et al. 2000: 692) Caught in this termination dilemma, the foreign operator is better off when providing a mediocre effort, that is, generating a certain level of local sales, but not reaching a volume that economically justifies the entrant company's establishment of a subsidiary in the local market. (Welch et al. 2007: 375)

Because of the inherent problems for the performance of the foreign intermediary due to the termination dilemma, Welch et al. (2007: 376) call for the entrant companies to release their foreign partners from this dilemma. If this is not done, the entrant company may lose out in several ways. First, in the absence of goal congruence between the two parties, the entrant company risks sacrificing potential sales revenue in foreign markets. Second, the entrant firm may incur the otherwise avoidable costs of prematurely establishing a subsidiary in a given foreign market. (Welch et al. 2007: 376) According to Welch et al. (2007: 376), the business press regularly refers to cases of exporters experiencing losses during the first years of operation of subsidiaries, sometimes leading to shutdowns of non-profitable foreign affiliates, supposedly as a result of over-ambitious entries into markets where the sales revenue generated did not support the considerable fixed costs of setting up and running a subsidiary. These issues are seen to be general for entries into any market. (Welch et al. 2007: 376)

As a strategy to tackle the termination dilemma and to switch FOMs, Petersen et al. (2000: 693) suggest the following framework, depicted in Table 3 below:

Table 3: Basic strategic alternatives for future switching of operation mode

Operation mode switch via: Approach to switching issue during initial negotiations	**TERMINATION**	**INTEGRATION**
CONCEAL	CONCEAL – TERMINATE	CONCEAL – INTEGRATE
REVEAL	REVEAL - TERMINATE	REVEAL - INTEGRATE

Source: Petersen et al. (2000: 693)

Table 3 presents some of the basic options that the entrant company may select, at the outset, to planning for a later operation mode switch. The switch options have been compressed into two main categories, termination and integration. Termination means the formal ending of the relationship with the local operator and the establishment of a new, unrelated entity. Integration means that the existing foreign operation is absorbed in some form into the entrant firm's concern, such as a switch from exporting via an agent to the use of a sales subsidiary. Alternatively, this may be a switch from a licensing arrangement to a wholly-owned production subsidiary. Also, this can take place by means of taking over, or merging with the existing agent's or licensee's operation. (Petersen et al. 2000: 692-693) Petersen et al. (2000) state that "while it is difficult for the entrant company to anticipate its future steps in the foreign market, we suggest that consideration of termination or integration options at the outset is an important basis for strategic flexibility".

In the framework of Petersen et al. (2000: 693), a more fundamental question is whether the entrant company should conceal or reveal its possible future intentions to the other party during the initial negotiations. Generally, an entrant company will conceal its intentions as to when or if termination or integration may apply. Therefore, to conceal may be regarded as the default option. Thus, during the initial negotiations most international companies will address the issue of termination in terms of stipulating the notice of termination, property rights subsequent to termination and sometimes the compensation, that is, severance payment. In addition, the agreement will usually stipulate that termination can take place in case of breach of contract by one of the contract parties, sometimes specifying what events may qualify as contract violation. However, companies in general seldom address the question of when termination or integration is likely to take place as part of the entrant company's overall strategy for the market in question. For instance, the entrant firm may have the intention of substituting a sales subsidiary for a local intermediary as soon as sales in the foreign market has reached a level that justifies the higher fixed costs of a subsidiary. (Petersen et al. 2000: 693-694)

Table 3 above shows four basic strategic alternatives open to a company when considering operation mode switches which may be deemed necessary, or appropriate, in the future (Ibid. 2000: 693). These options are described below.

In a 'conceal–termination' situation, the entrant firm conceals its ultimate intention to terminate the initial operation mode arrangement. The company may already have a firm idea of the form of operation it wants to switch to at a later stage, or may want to keep its options open as to the replacement operation mode at the time of termination. In both cases, the initial form is viewed as a 'stepping stone' to something else. As a part of this strategy, during the negotiation process the entrant company may be concerned that to reveal its possible or firm intention to terminate would be viewed as a sign of mistrust, which could jeopardize the whole deal. In many foreign operation mode negotiation situations, contractual terms relating to termination arrangements are normally raised as part of the process. However, agreeing to the terms does not automatically reveal intention to terminate. The ability to maintain a conceal-termination approach, and to have real options at a later stage, will also depend on how the initial operation form and the relationship with the local operator are handled in the implementation phase. (Ibid. 2000: 694)

Following a 'conceal-integration' strategy, the entrant company intends to integrate the local operation at some future point but, for various reasons, will conceal this purpose from the prospective local operator during the initial negotiations. Ultimately, it may be able to integrate with the consent of the local operator, but it will not necessarily require this. Thus, the firm may be prepared to go as far as a hostile takeover, if it is feasible in the relevant market. Alternatively, the firm can effectively integrate the local operation through strategic hiring of key local staff, such as specifically targeting personnel from research and development or sales departments as a means of obtaining critical know-how and networks. Of course, in some cases a firm may not have a clear intention to integrate but, unless it puts in place the means to do so, effectively the firm ends up in a conceal-integrate situation. (Ibid. 2000: 696)

If the intention to foreign operation mode switch is approached following a 'reveal-termination' strategy, the conditions under which the relationship is to be terminated at the completion of the term of the arrangement are negotiated and spelt out clearly. The formal agreement is likely to contain specific clauses relating to matters such as the obligation of both parties at the end of the contract, severance payment, extension options, buy-backs, intellectual property rights, and the like. Some firms have taken the reveal approach a stage further and sought to include comprehensive terms and conditions for termination of the contractual arrangement, particularly in the case of JVs. In such situations, the terms of the 'divorce' settlement are negotiated in advance, in the nature of a 'pre-nuptial' agreement, including such aspects as asset transfer prices. There have been strong arguments for including exit options in JVs and other alliances. This approach of revealing termination plans, though, may be difficult to apply in cultures where the notion of discussing 'divorce' before the parties have even embarked on a relationship is difficult to comprehend. (Ibid. 2000: 696-697)

A ‘reveal-integration’ approach involves a company signaling in advance to a future foreign intermediary or contractual partner, in whatever form, its intention to eventually integrate the foreign operation. Various forms and degrees of integration are feasible, including a takeover, a strategic alliance or JV, a share swap, or the transfer of capital assets and/or market information banks. Placing the option of future integration on the table in the initial negotiations does reveal the entrant company’s possible future intentions, but if the prospective local operator agrees to the integration proposal, the entrant company has created a switching option for the future. If a prospective licensee, for instance, agrees to the inclusion of an option-to-buy clause in the licensing agreement, the licensor has created a clear, legal option of future takeover. (Ibid. 2000: 697)

Petersen et al. (2000: 703) write that “only as future events unfold will the entrant firm know whether termination or integration is preferable, or achievable”. They see that while companies cannot be expected to correctly anticipate future events, they still have to make commitments than run into the future, especially with regard to operation mode decision. This is an important concern, particularly for firms in the early stages of internationalization. (Petersen et al. 2000: 703) According to Petersen et al. (2000: 703), “a low-commitment entry mode comprising a real option for a later switch to a high-commitment operation mode will clearly be preferable to a low-commitment mode *without* this option”. They also see that for the manager of such a firm, uncertain about the business opportunities in the foreign market, a low-commitment entry mode with real options for mode switch must appear as being ‘the best of all worlds’ – the manager avoids high market risk but maintains the option of exerting greater control over the business operation at a later stage. However, although a very tempting alternative for an internationalizing firm, this kind of switching option may be difficult to accomplish because of the possible reaction of the local operator once the intention has been revealed. (Petersen et al. 2000: 703)

The strategic framework in Table 3 above represents only one set of options that an entrant firm can resort to when negotiating with prospective future partners. Arguably, there are other approaches to mode switches but these are not discussed in this study. The reason this framework was raised up in this paper was to expose the reader to the importance of having strategic flexibility when a company is entering different foreign markets. This strategic flexibility is requested by Petersen et al. (2000: 689) who offered their framework to deal with the following problem that is best illustrated by their own comment: “Research has shown that when companies make operation mode decisions, they frequently do not consider, or plan for, future mode options, in spite of evidence that operation mode changes are quite common”.

2.6 Foreign operation mode stretching

In the discussion above, an implicit assumption has been that FOMs are mutually exclusive. This, according to Welch et al. (2007: 387), is a somewhat simplified assumption which does not reflect the reality of many FOM decisions made by internationalizing companies. This simplified assumption means that one FOM is replaced by another. In addition, the assumption has been that FOMs are distinguishable organizational forms in relation to which switches constitute clear-cut changes. A switch from a local outside agent to a fully integrated in-house operation, for instance, is very distinct. In practice, though, mode switches may be a great deal subtler. Sometimes mode switches emerge as incremental processes in which one operation mode virtually grows into another. The operation modes that an entrant firm uses in a specific market over a period of time are not necessarily sequential, that is, mutually exclusive – it is not uncommon for entrant firms to add new operation methods to existing ones, thereby practicing mode combination. Mode combinations are discussed later in this paper. Mode switches may also be incremental in the sense that within-mode changes precede as well as follow a formal shift of ownership and organizational form. Generally, there is a variety of ways of easing the path of mode switches which are not obvious in the overall form of operation mode. For instance, it is not uncommon for firms to hire staff from their former, or current, agent to facilitate the transition to use of a sales subsidiary. Cooperative forms of association with the agent may be used even after the sales subsidiary set-up, which represents a type of organic extension of the existing arrangement, as a way of easing the demands and risks associated with the mode switch. Sales subsidiaries can also be set up in a form that minimizes the degree of commitment by the company. In assessing the significance of a mode switch from an internationalization perspective, whatever the overt pattern, much depends on the changes that have taken place prior to the formal switch, and also on the form of the new mode. (Welch et al. 2007: 387-388) Interestingly, Welch et al. (2007: 388) state that "the essence of change is not simply captured by the existence of a mode switch".

Welch et al. (2007: 388) continue that "it is even conceivable that a mode change which would normally have been viewed as an escalation in international commitment might in fact amount to de-escalation". They exemplify this through a situation in which a firm has invested heavily in its agency operation as a base for exporting, then switches to a sales subsidiary in the foreign market, but this sales subsidiary is poorly supported, staffed on a part-time basis only and provides a very limited service to customers in that foreign market. This could be described as a de-escalation of commitment. (Welch et al. 2007: 388)

There is potentially a wide variation in the extent of a firm's commitment to its foreign intermediaries, which is reflected in aspects such as visits, support and internal company adjustments for the foreign market servicing operation. These can be generalized as within-mode changes along three main scales: activities, resources and organizational changes. The resources dimension is seen to be a very broad indicator of the extent of involvement with a foreign intermediary but it tells little about the nature of that involvement. It is the activities and organizational change dimensions that provide better indicators of whether there has been a significant change in the use of a particular foreign operation mode over time, including aspects such as the extent and form of communication, staffing, training and other forms of support. Extension of the range of activities may be a part of a process of extension of control over foreign market penetration, leading to the ultimate step of takeover or replacement by a company-owned sales function. The activity dimension can also be linked to likely changes in experiential knowledge, even though there may be substantial differences in the knowledge effects of different types of activities. Along with activity extension it might also be deemed necessary to make organizational changes to organize these within mode developments. For instance, an export department could be established at the home base of the entrant company, or other changes made in its structure. Extension of activities will normally require that staff be used in different ways, which may also require a variety of organizational changes regarding foreign market visits, additional staff deployment, training programmes, and so on. (Ibid. 2007: 388-389)

2.7 Foreign operation mode combinations

2.7.1 Multiple mode phenomenon

Instead of replacing one FOM with another, companies may add a FOM to an existing one. The correct term to use for this phenomenon would be a 'mode addition' rather than a 'mode switch'. The addition of one – or several – modes to an existing one may be a very temporary arrangement where the two FOMs overlap for a short, transitional period. In other cases, though, mode additions may take on the characteristics of a long-term, or even permanent, arrangement. (Welch et al. 2007: 393) The multiple mode phenomenon is seldom mentioned in the entry mode literature (Petersen and Welch 2002: 157). Mode researchers have viewed mode choice mainly as a choice between mutually exclusive modes (Welch et al. 2007: 387; Petersen and Welch 2002: 157). As a result, foreign operation mode has tended to be treated as a singular entity in the literature, even though firms often use multiple or mixed modes in the same foreign market (Benito and Welch 1994: 16-17; Petersen & Welch 2002: 157). Benito and Welch (1994: 16-17) describe the existence of multiple mode phenomenon extremely well with the following comment: "While this reduction in the decision-making situation [to concentrate on singular modes] has simplified model building and eventual testing, it has been at the expense of reflecting the reality of the situation that companies frequently face – of not simply choosing one method versus another, but rather of putting together the most appropriate package of methods for penetrating a foreign market". Following the same line of thinking, Benito et al. (2008: 12) write that "while the assumption of discrete alternatives obviously simplifies the research task, it should be acknowledged that business practices are somewhat messier".

Thus, this 'multiple mode phenomenon' can be translated to 'mode combination' or 'mode package', depending on the author discussing the topic but, in essence, they are the same issue (Benito and Welch 1994; Petersen and Welch 2002; Welch et al. 2007: 393-413). Welch et al. (2007: 438) concluded that "in general, international business theory remains closeted behind the idea of simple, singular mode change, whereas companies deal with the reality of mode combinations in the normal course of international operations".

The aim in the previous foreign operation mode studies has been to understand why firms choose one mode rather than another. In these studies, multiple modes are often ruled out by the way questions are framed in empirical studies, or because responding managers report only their main or primary mode. In addition, it is also possible that researchers regard cases of multiple modes as anomalies and exclude them from the defined population. (Petersen and Welch 2002: 157) As an exception to this inclination, Petersen and Welch (2002: 157-158) point the attention to a study of Valla (1986: 25-26). Valla (1986: 25-26) terms his finding of mode combinations 'mixed approaches', which accounted for 27% of the cases studied. Valla's study included 45 French exporting manufacturers and their 165 export marketing organizations in four European countries, namely Italy, the United Kingdom, West Germany, and Sweden, yielding 120 cases to be studied in terms of operation mode used (Valla 1986: 25-26; Petersen et al. 2002: 157-158).

According to Petersen and Welch (2002: 158), a number of studies of specific operation modes highlight multiple mode phenomena quite strongly. Management contracts, for instance, are often used as part of broader foreign market servicing strategies – they are often tied in with other operations as a means of improving the effectiveness of the company's thrust into a particular foreign market (Luostarinen and Welch 1990: 95). In addition, licensing operations are sometimes used in conjunction with JV operations to obtain greater control over foreign operations, for instance (Luostarinen and Welch

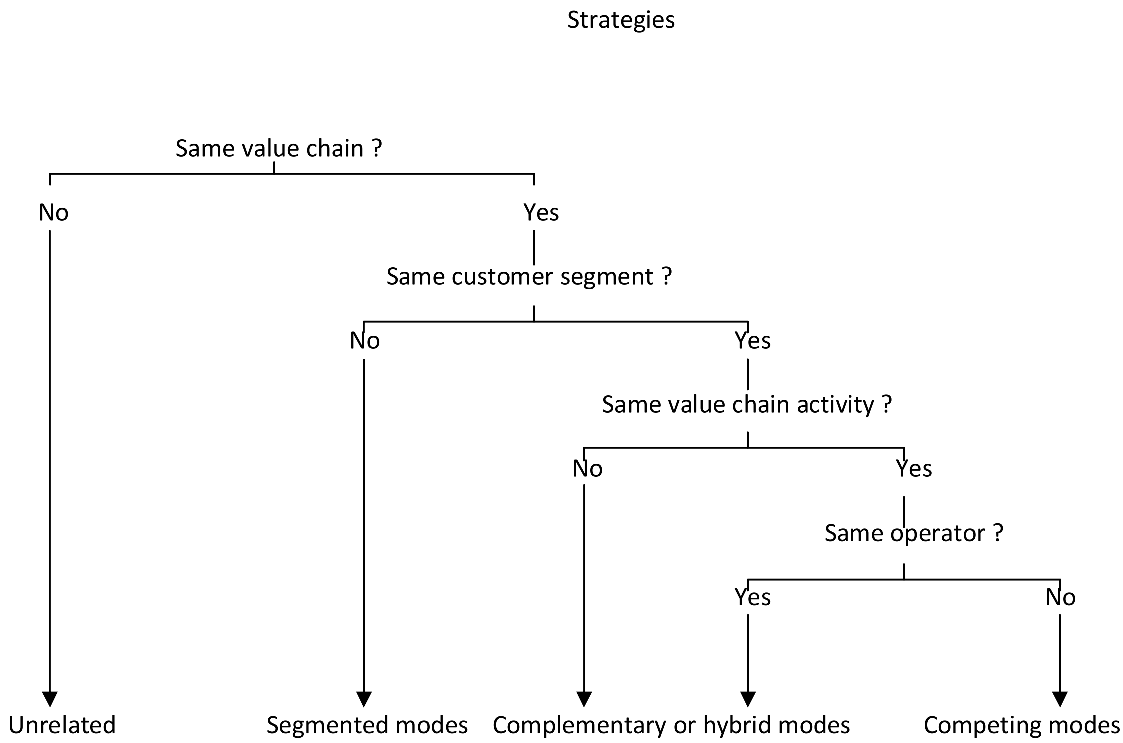
1990: 39). A study by Clark et al. (1997: 613-614) revealed that ‘mixed mode’ shifts, where companies combined two or more marketing modes simultaneously in a single foreign market, accounted for 18% of the cases in which a mode change had taken place.

The reasons to use mode combinations are numerous. Petersen and Welch (2002: 157) claim that “mode combinations may lead to improved international market penetration”. They also see that particular modes can be used in different ways to achieve various objectives such as enhancing the impact of another operation mode or to achieve outcomes which would be impossible using a single operation mode. (Petersen and Welch 2002: 160)

2.7.2 Five rationales for mode combination

Petersen and Welch (2002: 158-160) identify four forms of multiple modes: unrelated, segmented, complementary, and competing. Based on their original work, Welch et al. (2007: 395-396) took this categorization further with their framework of five rationales for mode combination, depicted in Figure 4 on the next page:

Figure 4: Different types of multiple mode operations



Source: Welch et al. 2007: 396

According to Welch et al. (2007: 395), the framework presented above in Figure 4 can be used to determine the underlying reasons for an observed mode combination in a foreign market. In addition, managers may also use the framework proactively, e.g. as a decision tree, to identify needs and opportunities for combining modes in a foreign country (Welch et al. 2007: 395). In the following, each of the five rationales for mode combination is discussed.

Unrelated modes occur when a company uses more than one mode in a foreign market but there is not connection between their uses within that market. This may reflect the operations of a firm that conducts business across different industries or markets. Thus, the operations of large, diversified multinationals in a foreign country are likely to be handled by different business units of the same firm. (Petersen and Welch 2002: 159) The operations of a Norwegian multinational, Norsk Hydro, in India are an example of this as illustrated by Tomassen et al. (1998: 7-14) in their study of operation mode choices of Norwegian firms in India. Five of Norsk Hydro's product divisions, using different market servicing modes, operate relatively independently in India, and were therefore treated as separate companies, as if strategic business units, in that study (Tomassen et al. 1998: 7-14). Importantly, Petersen and Welch (2002: 159) point out that if business units are the unit of analysis instead of firms as a whole, no mode combinations exist in this case.

A company may use multiple modes in the same industry or market to serve different customer segments. Valla (1986: 33) saw that segmentation was one explanation of the multiple modes that were observed in his study of French exporters. He noted that sometimes mode combination was used to handle separate customer segments differently – for instance, the largest customers may be handled directly, whereas others are handled through distributors or sales subsidiaries (Valla 1986: 33). According to Welch et al. (2007: 397), market segmentation based on firm size, to which Valla referred, is indeed very common. In addition to size of customers, for instance, other forms of segmentation may be used, including geographical regions, households versus business firms and infrequent buyers versus repeat buyers (Welch et al. 2007: 397).

In value activity specialization as termed by Welch et al. (2007: 398), multiple modes are used in a combined, mutually supportive way achieve the company's objectives. The entrant firm uses different FOMs for different value chain activities (Welch et al. 2007: 398). Valla (1986: 33) writes that "the objective of such combined approaches is clearly to increase efficiency, without being based on any specific segmentation". An example is a firm-employed person based permanently in the country to back up an agent or to complement the marketing action of a subsidiary (Valla 1986: 33). In this case, the multiple modes' focus is on the same segment but is concerned with different activities in the value chain. For instance, a multinational firm may hand over the manufacturing in a foreign country to a licensee but carry out sales and marketing through its own sales subsidiary and a clear division of labor exists between the two operation modes. Seemingly, the separation of manufacturing and marketing in foreign operations is seen most strongly in the global activities of sports shoe and clothing firms such as Nike and Reebok. (Petersen and Welch 2002: 159) The division of labor may be subtle: a sales subsidiary and local franchisees could both be subordinate to the same principal, such as a multinational franchisor, and cater to the same customer segment but the franchisees act as retailers, whereas the sales subsidiary takes care of the wholesaling activities (Welch et al. 2007: 398). In these cases, the division of labor necessitates coordination among different modes – they operate in a complementary way. Therefore, multiple modes are a package that cannot be easily unbundled. In the discussion above, the focus has been on the multiple modes working together in an integrated, cohesive manner in order to achieve foreign market objectives. (Petersen and Welch 2002: 160)

Entrant companies may also combine modes in relation to one specific value activity in the foreign market. This can be done in two very different ways: either the specific value activity is carried out by a local outside agent in tandem with the entrant company itself, such as in dual distribution where head-on competition prevails, or the entrant company conducts the value activity by itself but uses two combined governance forms – contracting and partial ownership. When two combined governance forms are employed, this arrangement can be termed 'hybrid modes' as in Figure 3 above. Reasons to use hybrid modes are numerous but they revolve mostly around bolstering commitment and control in a foreign market penetration arrangement. For instance, agency problems between the principal and the local partner are of crucial importance. In order to safeguard his interests and suppress moral hazard, the owner, that is, the principal, may insist on sharing ownership with his agent. In this way, the goal congruence between the principal and the agent is promoted – in the case where the agent mismanages the business he will impose a loss on himself to extent that his minority share loses market value. Agency problems can be seen to arise from moral hazard in combination with the difficulties of writing and enforcing perfect contracts – contracts that regulate any possible aspect of the agent's responsibilities and take into consideration all future contingencies. Usually, principals remedy these contractual inadequacies by monitoring the agents' behavior closely, but less so in the case of international business. Because of the considerable physical and cultural distances in international business, monitoring is a costly and sometimes unreliable control instrument. Therefore, another remedy for contractual insufficiencies, such as joint ownership or co-ownership, may be brought to use. To illustrate, management contracts are often used in hotel industry as a foreign operation mode and in some cases, minority ownership is linked to a management contract. This minority ownership may be requested by the local management contractee to act as a collateral that effectively prevents the possible opportunistic behavior by the foreign contractor. The same arrangement can take place in franchising, as well. The profitability of the franchisee's business very much depends on a continuous flow of new, saleable products and marketing support by the franchisor. Usually, the franchisee owns the physical assets of the local business operation, but in some cases the franchisor takes ownership of part of the assets, presumably as a token of commitment and good faith in the financial prospects of the local franchise operation. In addition, joint ownership in licensing can be explained by a bolstering of the principal's – the licensor's – commitment. Often times, the licensee is uncertain about the market value of the licensed technology and the extent to which the licensor is committed to provide services associated with the technology and to update the technology on a continuous basis. In addition, the licensor may also see the joint ownership as an opportunity for closer control, that is, monitoring, of the licensee. Licensors are often afraid that their licensees sell the licensed products outside the agreed-upon territory or misuse the licensed technology in other ways and possibly even become competitors or create competitors by disseminating the licensed technology elsewhere. To safeguard against this risk, the licensor may engage in a co-ownership arrangement which opens the door to the boardroom of the licensee's organization and, thereby, enables supervision of the licensee's managers. Sometimes the technology transfer goes both ways and the joint ownership secures commitment from both sides. The licensing agreement also has the potential to deliver a degree of control over marketing, management and other aspects of the JV's operations. (Welch et al. 2007: 399-401)

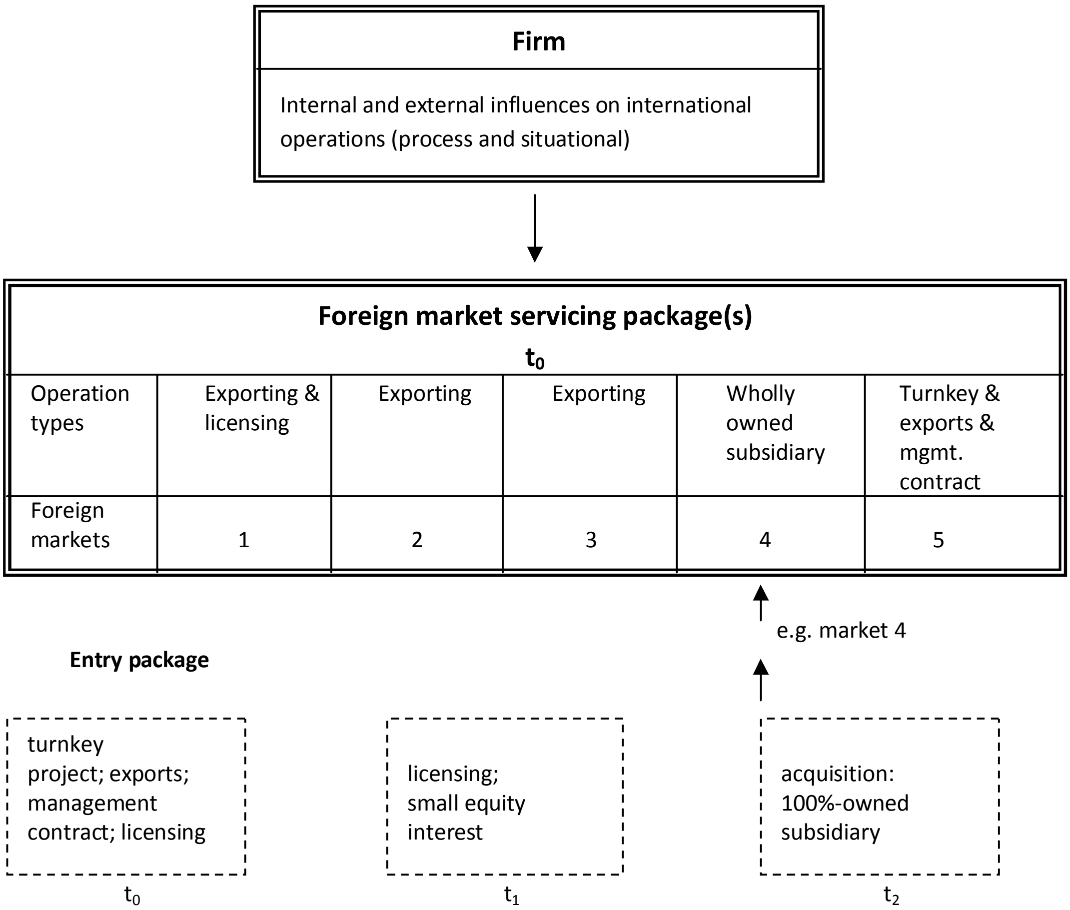
Finally, firms may use multiple operation modes to benchmark local operators (Ibid. 2007: 401). In this case, a firm actually uses more than one mode to compete with each other. The operation modes target the same segment or segments and perform the same business activities, but the ownership – in-house versus outsourcing - and location – home country versus host country – differ. (Petersen and Welch 2002: 160) This, in essence 'dual distribution', enables the foreign manufacturer to benchmark and exercise greater control over independent dealers by keeping house accounts that are served by their own sales people in the dealers' districts (Welch et al. 2007: 402; Petersen and Welch 2002: 160). Using dual distribution, a manufacturer can monitor the effort and capabilities of the dealers (Petersen and Welch 2002: 160). In addition, the manufacturer establishes a credible threat of taking over the dealer's district, provided that the take-down and set-up switching costs are likely to be moderate. This permanent termination threat may prevent the local operator from shirking. Also, the in-house sales channels may serve another purpose, namely to demonstrate new and more effective sales and marketing techniques. The concept of 'flagship stores' is well known from franchising where the franchisor is eager to show the full sales potential of its franchising format. Still, though, dual sales channels are challenging and fraught with the risk of conflict between the manufacturer and the local distributors – the two channels tend to view each other with a great deal of suspicion and treat each other as rivals. Also, business-to-business customers are keen to play in-house and outside channels against each other for their benefit. The Internet has also played some role in the development of dual sales channels. Lately, many companies have added direct, online sales channels to their existing sales network of foreign intermediaries. The addition of an extra online sales channel may be seen as an attempt to expand market reach by catering to new customer segments. From the perspective of the local intermediaries, though, the new sales channel can easily appear to be cannibalizing the existing export sales channels. By introducing direct online sales channels the entrant companies may easily evoke uncertainty and dissatisfaction among existing distributors, or, in the worst case, even open channel conflicts. (Welch et al. 2007: 402-403) Competing modes may also occur when a company attempts a hostile take-over of an export market. The existing local distributor might be able to resist giving up the market, depending on the nature of the contractual obligations, but the exporting firm still establishes a wholly owned, local sales organization. (Petersen and Welch 2002: 160)

In some situations, the distinction between the five rationales for mode combination becomes blurred because of the changes in the foreign market and in a company's strategy and organization - for instance, when separate distribution operations in a market are coordinated by a new subsidiary, which creates actually a more integrated system (Welch et al. 2007: 403-404). According to Petersen and Welch (2002: 160), the degree of integration or coordination of complementary modes can vary across different foreign markets even for the same company. They continue that although unrelated and segmented modes do not support each other, indirect support might be provided in a more general way, such as common staff training programs, staff transfers, sharing of some overheads, sharing of market information and contacts, and so on (Petersen and Welch 2002: 160). Petersen and Welch (2002: 160) see that "mode use is a dynamic process subject to transitions and modifications such as mode additions or deletions over time". They continue that "changes in mode combinations will occur in ways that are not reflected in studies of individual mode establishment chains and some combinations may be deliberately temporary, as firms seek to better position themselves for a move to a preferred form of operations in the foreign market" (Petersen and Welch 2002: 160).

2.7.3 Examples of mode combinations

According to Welch et al. (2007: 404), mode combinations may appear in a number of forms in foreign market operations. Benito and Welch (1994: 17) present an illustrative example of foreign operation modes that a firm might use in different foreign markets at a given point in time in response to different internal and external influences affecting the mode choice. Their example is presented in Figure 5 on the next page:

Figure 5: Foreign Market Service Packages



Source: Benito and Welch 1994: 17

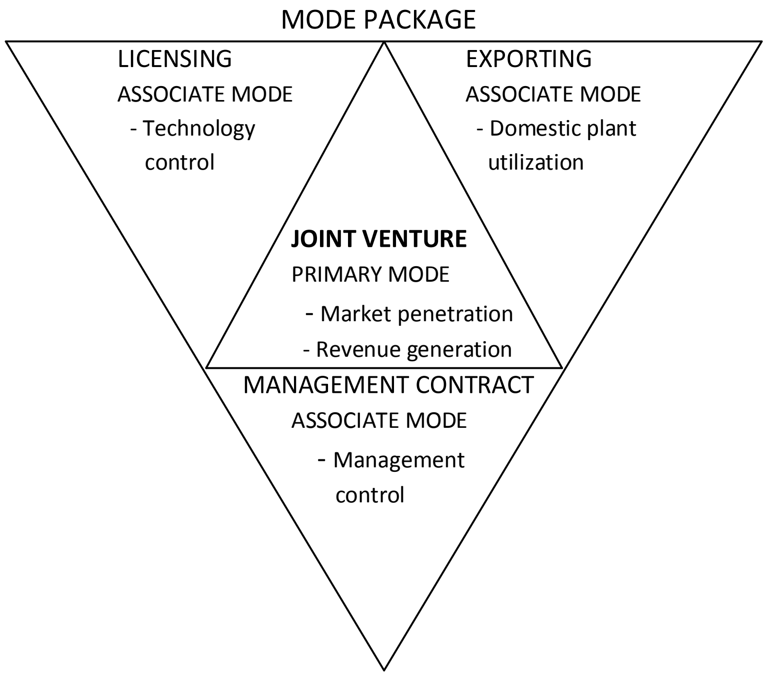
This hypothetical illustration of a firm's foreign market operation modes in different markets over time can be read follows: in some markets – markets two, three and four – a single mode may be used, whereas in others a combination of modes might be employed, such as in markets one and five. In addition, the company's foreign market servicing mode shown at time t_2 could be an outcome of a number of package alterations during preceding periods, as is the case with the foreign market number four. In this market, the firm used a broad package at its entry point – t_0. This led to an altered package at time t_1, and eventually, to the full acquisition of the operation at time t_2. (Benito and Welch 1994: 17)

2.7.4 The roles of individual modes in mode combinations

The roles of different modes in a mode package are important. Petersen and Welch (2002: 160) write that "the existence of multiple modes in an integrated system does not, of itself, indicate what roles they are performing and how they are interrelated". They continue that the role played by individual modes may change over time and vary across markets even for the same company. For instance, licensing might be the primary market penetration mode leading to some associated export sales, or it could be used in a supportive role to a foreign JV, creating additional income and facilitating control. (Petersen and Welch 2002: 160)

Petersen and Welch (2002: 160) see that the role played by different operation modes in achieving foreign market objectives can vary in importance. One mode is likely to play a primary role in ensuring foreign market penetration and revenue generation, whereas the remaining other modes play various types of supporting roles. These can include, for example, further market penetration and revenue generation, or specialized roles in relation to particular objectives such as technology transfer or developing a positive political profile such as through a licensing or technical assistance agreement. (Petersen and Welch 2002: 160) A hypothetical mode package is illustrated in Figure 6 on the next page:

Figure 6: Hypothetical mode package



Source: Petersen and Welch 2002: 161

In the mode package illustrated in Figure 6 above, the JV plays the primary role in achieving market penetration and generating acceptable returns from the foreign operation. The use of a JV might have been driven by foreign direct investment regulations or by resource constraints within the company. Management contracting and exporting are also used to achieve additional revenue, management control and better plant utilization. Licensing has a primary role in ensuring contractual control over the way the company's technology is used and that the technology is not disseminated elsewhere by the JV partner. In addition, the licensing agreement also has the potential to deliver a degree of control over marketing, management and other aspects of the JV's operations. In addition to technology control, the exercise of management control is strengthened through the use of a management contract. Needless to say, the driving forces regarding mode packages and the roles of the components parts are bound to differ as a result of variation in external factors such as government regulations, market pressures, the availability of suitable partners, as well as internal factors, such as control, resource availability, and previous international experience, including operation mode experience. (Petersen and Welch 2002: 160)

Given the complexity of mode packages, it is difficult to identify clearly the nature and significance of changes in operation mode and operation mode use over time, which is a key focus of internationalization research. A switch in roles for a given mode within a mode combination might amount to the equivalent of an overall mode change, such as when a company decides to change from exporting to licensing as the primary market penetration vehicle within an existing mode package. For example, the firm may have been using the foreign licensee to assemble the exported parts and distribute the final product. Sometimes, a firm is unprepared to invest in its own production facility in the foreign market, even though the licensing arrangement has resulted in inadequate servicing of customers. In this situation, the company might see the alternative as more fully involving the licensee in production and service provision, along with a reduced exporting role for itself. This way, the main structure of the mode package remains unchanged, but there is a significant change in the roles played by different modes. (Petersen and Welch 2002: 161) A further complication is added through adding and eliminating roles within an existing mode package (Welch et al. 2007: 409).

As a further illustration of the complexity of mode combinations and the difficulties of measuring changes between different modes in the combination, the example offered by Benito et al. (2008: 8-9) is very interesting. These authors refer to the case of Finnish elevator and escalator producer Kone and its endeavor in the Japanese market with a local company Toshiba as a partner. Over time, the FOMs used by Kone developed through a process of mode addition from a simpler to a more complex package, in line with the expansion of activities and its relations with partner company Toshiba. From a start via exporting with some cooperation in product modification, the alliance that was formed extended to a mode package that included exporting, widespread technical, market and systems cooperation, as well as licensing and cross-equity arrangement. (Benito et al. 2008: 8-9) Importantly, Benito et al. (2008: 9) state that “at no point was there a clear-cut shift from one mode to another, as is generally portrayed in the literature”. The nature of the alliance changed substantially through both mode addition and the evolving utilization of different modes within the overall mode package. The authors claim that it is difficult to tell what Kone's primary mode of operation was in the Japanese market because all modes in the package played an essential role in the overall activity. (Benito et al. 2008: 9) Challenging the previous analysis and empirical research on mode use, Benito et al. (2008: 9) make a very strong argument:

> *"Looking over the whole period of mode development, it is clear that the comprehensive mode package at the end is substantially different from the starting point, albeit within what could be loosely called the overall Kone-Toshiba alliance umbrella. It would be difficult to argue that the 'mode' remained unchanged, even to use the term mode is misleading given both the mix of modes used in the package and the diverse roles that each played in an individual sense as well as in concert. Positions in the package shifted over time: at the outset, exporting was the primary mode and defined the relationship, but it became less important as Toshiba took over more of the production activity, embedded within an expanded, interactive alliance at many levels. The dynamism imparted by mode addition and deletion, and the shifting roles of the different modes within the overall package is an important characteristic that is virtually missing from existing mode analysis and empirical research. Instead, existing treatment of operation modes tends to be in a relatively inflexible way, with a focus on overall, substantive mode change – induced by alterations in a company's internal and external circumstances."*

As discussed above, the way modes may be used within mode packages indicates the potential diversity of roles that are involved in foreign market entry and development. Supporting modes may play an important role in achieving particular outcomes that are of concern to the firm, in addition to, or in support of those sought through the primary mode. (Petersen and Welch 2002: 161) Adding a mode to an existing operation, or changing the roles of operation modes within an unchanged overall mode package, may be actually a more effective way of responding to a change in market circumstances than undergoing the disruption and dislocation of a complete mode switch (Welch et al. 2007: 409). According to Benito et al. (2008: 10), "mode package addition or deletion may provide flexibility while a core, successful mode form is retained." This also assists in maintaining knowledge, staff, and network assets that have been developed through a pre-existing mode arrangement (Petersen and Welch 2002: 162).

2.7.5 Barriers to mode combination

Welch et al. (2007: 409) state that "with its obvious advantages, one might expect mode combination, including mode packaging, to be a standard strategy ingredient of any international company". However, what is known about the internationalization behavior of companies, this seems not to be the case. Therefore, one might speculate about which barriers to mode combination would explain this seemingly moderate use of mode combination, including mode packages, which is shown in empirical studies of mode use. In chapter 2.5.1.2, switching costs were identified in many cases to make up an effective barrier to otherwise desirable mode changes. (Welch et al. 2007: 409-410) In relation to mode combination, Welch et al. (2007: 410-411) identify three further barriers to desirable mode arrangements – insufficient scale of foreign market value activities, fixed costs of setting up multiple modes, and cognitive limitations. These are discussed below.

First, insufficient scale of foreign market value activities may act as a barrier to combine modes. Managers are expected to make operation mode decisions in relation to each identifiable value activity of the company. Put differently, managers may take the individual value activity as the level of analysis in relation to the organization of their international activities. Thus, it is implicitly assumed that decision makers are able to distinguish different value activities in terms of the optimal FOM and mode package. Even though the individual value activity is taken as the unit of analysis, this by no means implies that all decision makers consider the same range or number of value activities in terms of the optimal FOM. The differentiation of value activities by FOM only makes economic sense if two preconditions are met: first, the individual value activity has to exceed a certain minimum economic scale in order to make it identifiable and independently amenable for benchmarking against market providers. Second, the value activities should differ substantially in terms of optimal FOM. Thus, the number of separable value activities in a foreign market that the decision makers can discern as to the optimal mode of operation is to a large extent contingent on the scale of the individual value activities. The number of different FOMs used by entrant companies is expected to be limited by the scale of the individual value activities. If the decision maker is unable to differentiate the value activities in terms of scale and scope economies, asset specificity and other economic characteristics, there is no cost-effective basis for introducing mode combination. (Welch et al. 2007: 410)

The fixed costs of setting up mode combinations may also act as a significant barrier for their use. Welch et al. (2007: 411) write that "the introduction of separate FOMs in a foreign market has to be economically justified by the cost savings or revenue gains of the value activities that result from allotting them governance forms of their own – after deduction of fixed costs associated with adding new modes". They exemplify their claim with the case of Danish pharmaceutical company Lundbeck that researches in, develops, produces and markets pharmaceuticals for diseases in the central nervous system. They see that when Lundbeck established a representative office in China to support and monitor the local distributor, one must assume that the fixed costs incurred by this mode addition, such as finding suitable premises, recruiting personnel, and so on, were justified by the extra revenue gained in the Chinese market as a result of this mode combination. Also, fixed costs of establishing a license arrangement, such as costs of writing, negotiating, and enforcing the license contract, in addition to an existing JV should be justified by the reduced risk of technology leakage. This, in turn, would result in diminished revenue gains. Again, scale is important because the set-up costs tend to be fixed – the 'ink costs' of a license contract are roughly the same irrespective of the market value of the licensed technology. As a result, mode combination is expected to be less common for small companies operating in small foreign markets. (Welch et al. 2007: 411)

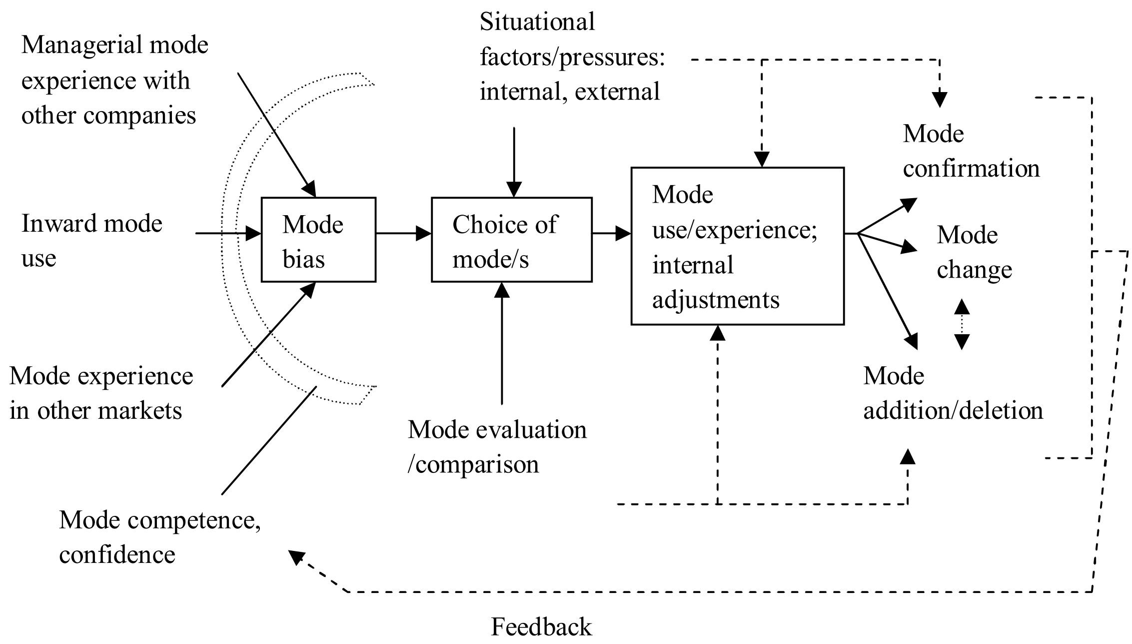
Finally, cognitive limitations may act as a barrier to mode combinations (Welch et al. 2007: 411). This can also be termed as 'mode myopia', as done by Welch et al. (2007: 411). They see that there is a danger that companies become too narrow and fixed in the range of foreign operation modes that they employ (Welch et al. 2007: 411). Firms tend not to consider the full array of operation mode possibilities when approaching foreign market entry and there is a risk of becoming locked into a particular FOM (Ibid. 2007: 411; Calof 1993: 109). For example, an operation mode that may have been used at first by chance becomes the mode best understood, or one bad experience means that a particular FOM is locked out (Petersen and Welch 2002: 162). Benito et al. (2008: 16) state this extremely well when they claim that "sometimes, only one mode form, or package, is evaluated, particularly when companies are approached with an offer to sell by a foreign company or an offer to act as a distributor or licensee in a foreign market". Thus, when international firms suffer from mode myopia, they find it difficult to introduce a previously unused mode into an existing package. There is comfort in continuing to employ those modes that the firm has become knowledgeable about, and adept in using, in different foreign markets. (Welch et al. 2007: 411) To cope with the mode myopia, Petersen and Welch (2002: 162) came to the following conclusion: "In general, therefore, a major task for the internationalizing firm is to ensure a high level of awareness and knowledge among key staff of the full range of operation forms and their potential to be packaged and used in ways that strengthen the process of foreign market penetration".

2.8 Synthesis of the literature review

So far in the literature review, FOMs have been defined, followed by a discussion on different FOM options and the importance of FOMs. Thereafter the attention was directed to foreign operation mode selection with the two main approaches – the economic-strategic and the process one – to this decision discussed thoroughly. This was followed by an example of a mode selection scheme.

Thereafter, the discussion moved on to more novel thinking regarding FOMs, that is, to mode strategies, with its subcomponents mode switching, mode stretching and mode combinations. Although these novel ideas are fresh and therefore, not a lot of research has been done on these frontiers, a very good effort to conceptualize all these thoughts to one model was done by Benito et al. (2008: 18). This model is depicted in Figure 7 below:

Figure 7: Theoretical framework - mode choice and change



Source: Benito et al. 2008: 18

The model presented in Figure 7 can be read as follows: managerial mode experience with other companies, inward mode use and mode experience in other markets all serve to affect the mode selection, thus creating mode bias. Based on this mode bias, situational factors, internal and external pressures, and mode evaluation and comparison, a choice of a foreign operation mode is made. After the selection, the FOM is used yielding experience in mode use, which may cause internal adjustments in mode use, along with situational factors, internal and external pressures, and mode evaluation and comparison. Through this experience in mode use and possible internal adjustments thereto, mode is confirmed, changed, or added or deleted to or from an existing mode combination. Again, this mode confirmation, mode change, or mode addition or deletion process is affected by situational factors, internal and external pressures, and mode evaluation and comparison. Finally, this whole process creates knowledge to the firm of mode use, which translates into mode competence and confidence through a feedback loop. Mode competence and confidence, then, serves to affect cycle of this process, possibly diminishing the mode bias that there was in the beginning.

Figure 7 sump up the theoretical discussion regarding foreign operation modes in this study extremely well. Therefore, this framework serves as the theoretical framework of this study, which somewhat guides the empirical part of this research. This research turns the attention next to information on South Korea and Finnish firms' business endeavors in this country.

3 SOUTH KOREA AND THE FINNISH COMPANIES IN THE COUNTRY

3.1 South Korea

South Korea, officially known as the Republic of Korea (ROK), occupies the southern part of the Korean peninsula. Communistic North Korea, a backward xenophobic country that is teetering on the brink of agricultural and economic collapse, forms the larger northern part. (Burns 1998: 183)

South Korea has been one of the world's most dynamic economies (Genzberger et al. 1994: 1). South Korea is the 12th biggest economy in the world and fourth biggest economy in Asia (Korhonen et al. forthcoming: 1). South Korea was an agricultural backwater with relatively few natural resources and it was dominated by its much-larger neighbors, China and Japan, throughout much of its turbulent history. Between 1950 and 1953 the Korean Peninsula was the scene of a devastating war between North Korea and South Korea, and subsequently served as a focal point of East-West tensions throughout the Cold War. After this Korean War, since the 1950s, South Korea has built a modern, internationally oriented industrial economy largely from scratch. (Genzberger et al. 1994: 1) The fast economic growth of South Korea started in the beginning of the 1960s and it averaged eight percent for decades. Even in the 2000s has the country been one of the fastest growing economies with a yearly average growth of five percent. (Korhonen et al. forthcoming: 1) Not surprisingly, the fast economic growth of the country after the Korean War has made people to refer to South Korea as an "economic miracle" – South Korea was among the first developing countries in the world which managed to achieve the economic level of rich Western countries (Korhonen & Kettunen 2006: 52). Interestingly, Korhonen et al. (forthcoming: 1), note that "although the role of the country is quite significant in the world economy, it has often remained in the shadows of its bigger neighbors, China and Japan".

The population of nearly 50 million inhabitants and the fast-growing markets make South Korea an attractive operational environment for foreign firms. Despite this, South Korea has been regarded as one of the most difficult countries both in terms of exporting and investing. In the past, the problem was the restrictive trade and investment policy of the country but also the suspicious attitude towards foreign companies. The investment policy of the country was liberalized practically overnight in 1998, coerced by the Asian Financial Crisis. Thereafter foreign companies have invested quite eagerly in South Korea. Although the attractiveness of China has decelerated the production investments to the other East Asian countries, almost half of the foreign direct investments that South Korea has received have still been directed to the production industry. (Korhonen et al. forthcoming: 1)

3.2 Distribution channels in South Korea

There is a whole variety of distribution channels that can be used in South Korea. These include agents, importers, distributors, wholesalers as well as liaison offices, the roles of which vary. Traditionally, foreign exporters and suppliers have used Korean commission agents to facilitate their sales into the Korean market. This is because these agents have been very helpful not only for the promotion of the exporters' products but also, importantly, for the smooth business relationship that foreigners are very difficult to handle directly in Korea. The sales channel that is used and the decision about establishing a sales office, a joint venture or an independent manufacturing or sales company depends very much on which field of business a foreign firm is in. (Francke 2008: 6)

The agents' and distributors' rights are stipulated by regulation but basically agreements may be written quite freely and the regulations are quite flexible. Written agreements between foreign exporters and Korean agents, importers or distributors are quite common in the start of a business relationship. Terminating an agreement is accepted if business is not going well. However, it is not so easy to terminate an agreement without justifiable reasons. (Ibid 2008: 6-7)

Korean agents seek principals whose products bring high profits with the minimum efforts and, therefore, they may have several dormant agencies if the principals are not alert. Korean trading agents are usually the first step to come into the Korean market. In case there are good business possibilities, liaison offices are considered. These liaison offices are often used as test marketing channels because the Korean authorities accept the fact that a liaison office is there for market research purposes and not for profit during the first two or three years. After that, the authorities may start looking deeper into the operations and a liaison office should preferably be changed into a company quickly. (Ibid 2008: 7)

There is one very specific feature in Korea regarding distribution channels, namely the small wholesale business. This wholesale business covers areas from consumer goods to industrial products, materials and half fabricates. The wholesale companies are very small stalls that are located in big cities in their specialized wholesale markets, such as textile market, tools market, shoe market, building materials market, for instance. Firms in these markets operate very quickly, they often use cash payments in order to avoid taxation and they hold very small stock. They also operate on thin margins but the turnaround of their commodities may be extremely high. This is a channel that is used by individual buyers, small retailers and big companies, from department store chains to industrial manufacturers, too. (Ibid 2008: 7)

3.3 Investing in South Korea

What comes to foreign investors, joint ventures used to be the first step of an entry strategy in Korea (Korhonen 2005: 134). The establishment of foreign companies in South Korea was hampered by the restrictive investment policy of the country, although South Korea, as a strong economy, has been an attractive target country for foreign investments for a long time (Korhonen et al. forthcoming: 27). Thus, South Korea has had a reputation of a relatively difficult target country for foreign investments (Korhonen et al. forthcoming: 29).

Importantly, however, the legislation concerning foreign direct investments was renewed in 1998, as discussed above (Nuutinen 2008: 18). As a result of the Asian Financial Crisis, from the end of 1997 onwards, it became harder to get foreign loans in Korea. Foreign direct investments were seen as a solution to the crisis and the President Kim Dae-Jung made the promotion of foreign direct investments his personal mission. In addition, the International Monetary Fund, which granted a record large loan to South Korea, recommended the liberalization of the investment policy. A large-scale liberalization was implemented by enacting a new liberal Investment Act in 1998. As a result of this new Investment Act, almost 16 billion dollars of foreign direct investments flooded to South Korea the next year after the new law was enacted. Foreign investors were especially interested in buying Korean financial institutions and companies from chemical industry. In addition to the liberalization of the investment policy, the Asian Financial Crisis with its favorable prices increased the popularity of South Korea as an investment destination. In practice, this new investment policy meant that the investment permits that were previously required were relinquished and foreign investments started to be attracted with different types of incentives, such as tax allowances. (Korhonen & Kettunen 2006: 56) The most notable reform was the permitting of foreign direct investments through mergers and acquisitions and the opening of real estate market to foreign companies. The branches that were open to foreign companies were increased. The branches that are totally closed are fishery and radio and television activity. The branches that are partly closed for foreign investors are related to national security, general maintenance of order, health care and telecommunications. (Nuutinen 2008: 18)

3.4 Chaebol

When discussing business in Korea, the term '*chaebol*' cannot go unmentioned. *Chaebol* means a 'financial clique' and it is used to describe a large business group, originally created by a talented entrepreneur and still largely family-controlled and spread over many diversified business fields (Lasserre & Schütte 1999: 97). These *chaebols*, large Korean conglomerates, dominate the business in the country, and therefore the South Korean market can be seen as an oligopolistic one. A major share of the *chaebols* was established in the 1950s and these conglomerates have had a significant role in the creation of the South Korean "economic miracle". The South Korean state used *chaebols* as tools in the implementation of the economic plans and steered the operations of *chaebols* through subsidies, loan guarantees and taxation. As a result, a tight network was formed between Korean politicians and businessmen. (Korhonen et al. forthcoming: 40)

Nowadays, there are over 50 *chaebols* in Korea. Originally, these *chaebols* were family-run companies. Although they are listed companies with a dispersed ownership today, still the founder and his successors exercise a very strong decision authority. It is typical for *chaebols* that they operate on many different fields of business, which means that one firm may produce almost everything from microchips to chemicals and from cars to oil tankers. The biggest *chaebols* also belong to the largest companies in the world. (Ibid. forthcoming: 40-41)

When the Asian Financial Crisis hit South Korea in 1997, 11 out of 30 *chaebols* run into bankruptcy. The structures of the *chaebols* started to be re-organized in the guidance of the South Korean state and according to the recommendations of the International Monetary Fund. The business of the *chaebols* was changed as more transparent, the rights of the shareholders were increased and the reciprocal loaning of conglomerate groups was restricted. *Chaebols* were directed to concentrate on core businesses instead of sprawling and the power of the founder family was striven to be decreased. However, the South Korean economy rebounded quite quickly after the Asian Financial Crisis, leaving a part of the reforms halfway done. As a result, *chaebols* still suffer from the problems that are created by the management approach of 'old times'. (Ibid. forthcoming: 41)

3.5 Chaebols and the other companies in South Korea

In addition to *chaebols*, there are roughly three million small and medium sized enterprises (SMEs) in Korea. These SMEs have remained in the shadows of larger *chaebols*. The SMEs and *chaebols* are, however, dependent on each other, as these SMEs serve as subcontractors to *chaebols* and deliver parts to *chaebols*' branded products. (Ibid. forthcoming: 41)

The role of foreign firms has been a minor one in Korea. Foreign companies, unlike the local SMEs, have to compete head-on with the *chaebols*. Foreign firms are at a disadvantage in a strongly networked environment where *chaebols* are dominating the market and have occupied the distribution channels. During the last ten years, the business model of South Korean firms has changed to a more international one but, still, there are anti-foreign attitudes in the South Korean business environment. (Ibid. forthcoming: 41)

3.6 Finnish companies in South Korea over time

The trade of Finnish companies to South Korea started in the later part of the 1970s and the first investment project was undertaken in 1984. Over time, only 25 Finnish firms have invested in South Korea but a part of the established or acquired units are not in the Finnish ownership anymore. However, the trade between Finland and South Korea is vivid. The imports have grown significantly faster than the exports from 2003 onwards, the exports basically getting nowhere fast. Both in the exports and imports the biggest merchandise group is machines, appliances and transport equipment. A significant share of the trade includes high technology. (Ibid. forthcoming: 1)

Mostly Finnish firms have engaged in direct exporting to South Korea, operating through an agent in the country. There are roughly 150 Finnish companies that are represented in South Korea. (Ibid. forthcoming: 72)

The biggest Finnish investors are Nokia, Ahlstrom, Fibox and Kone. Finnish firms have mainly invested in industrial production in Korea. (Francke 2008: 19) 11 Finnish companies have established production activities in the country but not all of these companies are in the Finnish ownership anymore (Korhonen et al. forthcoming: 72). A significant share of these investments has been directed to electronics and plastics industries. Nowadays, the interest of Finnish firms is biggest in information technology and telecommunications fields, especially in the software and research and development. (Francke 2008: 19)

The motive for the Finnish firms that established operations in South Korea in the 1980s and the 1990s was to increase the world market shares by developing the cost-quality competitiveness. To achieve this, companies transferred production to South Korea, which enabled taking advantage of favorable production costs without the quality suffering from this. The investors were mainly traditional export companies from forest and metal industries. However, the investments were quite small in terms of size and they were implemented by establishing Finno-Korean joint ventures. The relaxation of the investment policy in South Korea as a result of the Asian Financial Crisis also enabled acquisitions and the establishment of wholly-owned companies by foreigners in South Korea. Thereafter also the small and medium-sized Finnish firms started to invest in the country. The motive for these investments was still to enhance the competitiveness of Finnish companies but also to source new knowledge and technology by investing in South Korean research and development activity. The investments have taken place either as acquisitions or by transferring production to South Korea. In addition to the investments of traditional forest and metal industry companies, firms from chemical industry, information technology and telecommunications industry have invested in South Korea. (Korhonen et al. forthcoming: 1-2) The Finnish investments to South Korea have partly been directed to those industrial sectors where the *chaebols* were not very strong, such as paper industry (Ibid. forthcoming: 58).

Korhonen et al. (Forthcoming: 72) see that "in a nutshell it can be said that the spectrum of Finnish firms operating in South Korea has diversified to encompass SMEs in addition to the large companies". In addition, the spectrum of branches has diversified, although the activity is still mostly on a business-to-business basis. The same applies to exporting activity, which is due to the relatively small number of international consumer brands in Finland that the South Koreans could become interested in. A central reason for Finnish firms to establish operations in Korea is either to take advantage of the local knowledge in the company's own value chain or, alternatively, a significant customer in South Korea that the company wants to serve on-site. (Ibid. forthcoming: 72-73)

4 METHODOLOGY

4.1 Method of research

This research is conducted as an inductive research, that is, the empirical information is collected first and thereafter the phenomena visible in the empirical information is explained utilizing the latest research on the field of internationalization and FOMs. However, this study is reported as if it was a regular, deductive thesis because it is intended to be easier to follow and read as it is adheres to the general guidelines given to the Master's theses written at the Helsinki School of Economics.

A major reason why this study was carried out as an inductive research was that this research was done alongside CEMAT's study. CEMAT does research as inductive research and this basically forced this research to be carried out as an inductive research, as well. The research process started very quickly, basically immediately, after getting the assignment from CEMAT, which did not leave much time to go through the relevant literature. Studying the literature before starting the interviews would definitely have helped a lot in the interview process, possibly yielding opportunities to go deeper to some important themes for this study through additional questions, for instance. However, the fact that this research was done in parallel with CEMAT's study helped enormously in getting access to the case companies, since the personnel at CEMAT had good contacts to relevant companies and persons to be interviewed.

Through induction general conclusions are drawn from empirical observations. In this type of research the process goes from observations to findings and to theory building, as findings are incorporated back into existing knowledge to improve theories – theory is the outcome of the research in this approach. Inductive type of research is often associated with the qualitative type of research that this study represents, as well. (Ghauri & Gronhaug 2005: 15)

Deduction, on the other hand, means that conclusions are drawn through logical reasoning. In this type of research, the researcher builds or deduces hypotheses from the existing knowledge and literature, which can be subject to empirical scrutiny and thus can be accepted or rejected. In this type of research, theory, and hypotheses built on it, come first and affect the rest of the research process. Deductive type of research is often associated with the quantitative type of research. (Ghauri & Gronhaug 2005: 15)

In the research process, methods begin with ideas and facts that lead to propositions, theories and predictions. New theories and predictions lead to new ideas and facts, and a new cycle begins, leading researcher to new theories. When observed facts are utilized in generating a theory that is consistent with these facts, researcher is doing induction. Put differently, induction is the process of observing facts to generate a theory and is perhaps the first step in scientific methods. While doing the research, propositions are formulated after observing the relationship between different variables in the study. (Ghauri & Gronhaug 2005: 15-16) Ghauri and Gronhaug (2005: 16) claim that "most researchers in business studies go through this method, observing facts that lead them to propositions and later to theories".

In deduction, consequences of a theory are analyzed. Deduction involves the gathering of facts to confirm or disprove hypothesized relationships among variables that have been deduced from the existing knowledge. (Ghauri & Gronhaug 2005: 16)

Interestingly, the processes of induction and deduction are not totally exclusive of each other – induction includes elements of deduction and vice versa (Ghauri & Gronhaug 2005: 16). In this research, there was no deduction involved with the induction since the empirical information was completely gathered before going through the relevant literature to explain the phenomenon visible in the empirical information. This was mostly due to lack of time because the time schedule of CEMAT for the interviews was quite strict – CEMAT basically needed the interviews "as quickly as possible" so that they could continue with their research regarding Finnish companies' relationships in South Korea to public authorities, local partner companies and local workforce. In addition, I personally participated in the writing work of the CEMAT's book labeled "*Korea as an Operating Environment for Finnish Firms*" by writing a chronology of

Finno-Korean trade development and the chapter concerning practical problems of Finnish firms in South Korea and solutions thereto.

However, although the study of CEMAT kept me quite busy in the beginning part of this study, I benefited enormously from being part of the CEMAT's project. The first thing was the easy access to relevant companies as discussed above. Another, very important issue was that I received very helpful tips and constructive feedback for my study, especially from Kristiina Korhonen at CEMAT who was in charge of CEMAT's research on South Korea.

The empirical data for this research has been collected through a total of 13 in-depth interviews in nine case companies. The information that was received in these interviews was supplemented with secondary sources such as the Internet-pages of the case companies and other written material. Personally, I interviewed 8 persons in the case firms – Heikki Lehmus from Cargotec, Jouni Puura from Proventia Emission Control, Interviewee One from Company A, Hannu Ylinenpää from Lappset, Petri Talala from Futuremark, Interviewee Two from Company B, Interviewee Three from Company C and Tapani Niemi from Fibox. In addition, I did two other interviews for CEMAT but these interviews were not utilized in this thesis. In addition to these eight interviews that I carried out myself, I had access to five other interviews that were done earlier by the personnel of CEMAT. These five interviews concerned three case companies – Company A, Fibox and Company D. From Company A, Interviewee Four was interviewed by the personnel of CEMAT on 6th March, 2003 and 24th April, 2007. The personnel of CEMAT also interviewed Interviewee Five, a high ranking director of Fibox in Korea, on 16th December, 2004 and 23rd August, 2006. Lastly, the personnel of CEMAT also interviewed Interviewee Six from company D on 4th February, 2008. The information received in these five additional interviews was utilized as supplement information to the information that was received in my own interviews.

The method of multiple-case study research was selected as an empirical research strategy for this study. According to Yin (2009: 4), case study method allows researcher to retain the holistic and meaningful characteristics of real-life events. A case study is an empirical inquiry that investigates a contemporary phenomenon in depth and within its real-life context, especially when the boundaries between phenomenon and context are not clearly evident. The case study inquiry copes with the technically distinctive situation where there will be many more variables of interest than data points, and as one result relies on multiple sources of evidence, with the data needing to converge in a triangulating fashion, and as another result benefits from the prior development of theoretical propositions to guide the data collection and analysis. (Yin 2009: 18) In business studies, case study research is particularly useful when the phenomenon under investigation is difficult to study outside its natural setting and also when the concepts and variables under study are difficult to quantify (Ghauri & Gronhaug 2005: 114). Case study has a distinct advantage over other research techniques in a situation where "how" and "why" questions are to be asked and when a contemporary set of events over which the researcher has little or no control are investigated. (Yin 2009: 13)

To be exact, this research is conducted as a holistic multiple-case study, holistic instead of embedded because there is only one unit of analysis in this study (Yin 2009: 46-60). This unit of analysis is the operation mode strategies of the case companies in South Korea – the analysis takes place on a micro level at each individual case company.

The interviews were carried out as open-end interviews in which a pre-formulated questionnaire was utilized. This questionnaire can be found in Appedix 1. This questionnaire was received from CEMAT – it is the same questionnaire template that CEMAT was using in all of its individual market studies in its program *Managing Business in Turbulent Markets*. I was instructed to go through all the themes and questions in the questionnaire sheet but I was also asked to go deeper to some themes that the interviewee was very knowledgeable of at the expense of some other themes that he or she did not have that much information, though. This meant that CEMAT received information on different themes to varying degrees from different interviews but, importantly, it was possible for CEMAT to get a good amount of information on each theme when the information from all the interviews were combined. Importantly, I was allowed to add my own questions to the question sheet. Three questions that I added were the following: "what was the impulse to enter South Korea in the first place?", "at which stage of internationalization did the company enter South Korea?" and "why exactly to South Korea?" These questions were all added under the heading

"Background information on both the parent company and the subsidiary". In addition, I tried to make as many additional, particularizing questions as possible when the operation mode issues of case companies were discussed with the interviewees, the number of additional questions naturally depending on how extensively the interviewee responded to the original questions that were presented. The interviews were prearranged to last for one hour. However, the length of different interviews varied considerably, some interviews lasting one and half hours and some only 50 minutes. However, all the necessary information was still received in all of the interviews.

4.2 Selection of case companies

The case companies were selected in two different ways – either they were pre-selected by CEMAT or I selected the companies personally. The companies that were pre-selected by CEMAT represented those companies that CEMAT was especially interested in because the companies had not been interviewed before regarding business in Korea. For these companies, CEMAT pointed me a person that would be very interesting to be interviewed and I approached this person thereafter and asked for an interview. The interviewees were first contacted with an email message, after which I contacted the interviewees over the telephone and asked for an interview. The email message template sent to the potential interviewees can be found in Appendix 2. In some cases this person was a close acquaintance to CEMAT's personnel and had an extremely long history in the operations of his or her company in Korea. The firms that were pre-selected by CEMAT for this study included Cargotec, Company A and Fibox.

I selected the other companies by going through the article archives of a Finnish business paper, *Kauppalehti*. I searched for articles with a keyword "Korea" to find articles on Finnish firms that were active in Korea. Based on this article search, I identified Proventia Emission Control, Lappset, Futuremark, Company B and Company C very interesting to be interviewed for both the study of CEMAT and my own study. Naturally, I had to have these companies to be interviewed accepted by CEMAT. Company D was interviewed by the personnel of CEMAT earlier. This interview turned out to offer interesting insights for my study, as well, and was therefore selected as the ninth case for this thesis.

Admittedly, this way of selecting the case companies is far away from being of any scientific nature. The case companies do not represent any special field of business and they are of different age, different size, and their time of doing business in Korea varies considerably, as discussed in subsequent chapters. In short, the sample of case companies is very heterogeneous. This makes it very questionable to draw any generalizations regarding operation mode strategies of certain types of Finnish companies or companies on some specific fields of business, for instance. However, keeping in mind the exploratory nature of this research on a rather under-researched topic and, importantly, the paucity of Finnish companies operating in Korea, the selection of case companies becomes a bit more justified.

4.3 Data analysis

The interviews of the representatives of the case firms were recorded using an mp3-player. Thereafter, these interviews were transcribed word-by-word from the records, as recommended by Hirsjärvi et al. (2005: 210). There is no unequivocal guideline regarding the accuracy of the transcription. In this study, all the interviews were transcribed on a word-by-word basis, either by the researcher himself or by the partner company of CEMAT. Those interviews that I did myself I transcribed myself, too. The interviews that I received from CEMAT were already transcribed either by CEMAT or by a partner company of CEMAT.

Based on these interviews and other sources such as company websites and other presentation material, for instance, a case description of each case company was written. I would have had access to an analysis program of qualitative data, N-Vivo, at CEMAT. This program can be used to categorize research material according to specified themes. However, I made a decision not to use N-Vivo, because the interviews turned out to offer different types of information with different order and importance. It was necessary to read through each interview many times and write out a case report on each case company, which basically told ‘the story of each case firm in South Korea’. The interviews were supplemented with other sources as discussed above. When utilizing the interviews that I did not do myself, I encountered some problems, since not all the questions that I would have asked were asked in the interview. For example, one interview that CEMAT had done earlier was about a firm and its operations in two countries, South Korea and Taiwan. As a result, the information that was South Korea specific was quite limited, and therefore, I needed to complement this interview extensively with other sources. However, this interview offered interesting insights for my study and was, therefore, selected as one of the case studies for this research.

The interviewees were done in Finnish. The case studies were written in English, meaning that the translation took place at this point. The case studies look quite same in this paper as they did after initial writing of them, with some minor modifications done along the way. Some companies, though, have been anonymized because of their wish to remain anonymous in the final report. After the case studies were written, each case was analyzed in the cross-case analysis utilizing the theoretical framework presented in the literature review of this study.

4.4 The reliability and validity of the study

The reliability of the research refers to repeatability of the research results. The reliability of a measurement or a research, thus, means its ability to create non-random results. (Hirsjärvi et al. 2005: 216) The goal of reliability is to minimize the errors and biases in a research. The objective is to be sure that, if a later investigator followed the same procedures as described by an earlier investigator and conducted the same case study all over again, the later investigator should arrive at the same results and conclusions. An important aspect is the documentation of procedures so that the other researcher would do the research in a similar way. (Yin 2009: 45) The reliability of a qualitative research is enhanced by the researcher's detailed description of the research process (Hirsjärvi et al. 2005: 217).

In this research, the reliability is strongly undermined by the fact that this was an inductive study. Admittedly, I was not very confident at the time of the interviews that what the interviews will produce. In other words, I was still on my way to conceptualize the phenomenon that is being studied, which meant that I could not document the procedure and follow a detailed protocol as to how to proceed from one case to another. Because of this, it is highly likely that another researcher would arrive at somewhat different results, especially because of the open-end interview structure which meant that the interviewer could have directed the discussion with the interviewee to paths at his or her own discretion and understanding, which could probably have yielded different results. At the same time, though, it could be argued that a researcher with the same level of understanding of international business issues and FOMs would have arrived at somewhat same results, since, the path of each individual case company in South Korea only has followed one track. Of course, differences in interpretation of the same interview answers could lead to different conclusions, but, arguably, two researcher with relatively similar background information on this topic would arrive at somewhat same results.

Another concept related to the evaluation of a research is validity. Validity means the ability of the measurement or research methodology to measure exactly what is meant to be measured. The measurements and methods do not always reflect the reality what is thought to be measured. The validity of a research can be measured from different perspectives. (Hirsjärvi et al. 2005: 216-217)

The construct validity of a research refers to its ability to identify correct operational measures for the concepts that are studied. To increase construct validity, multiple sources of evidence should be used, a chain of evidence should be established and key informants should have had to review a draft of a case report. External validity refers to defining the domain to which a study's findings can be generalized. Internal validity only relates to explanatory or causal studies, and therefore, is not discussed in this study as this study is an exploratory study. (Yin 2009: 40)

The construct validity of this research is quite high, as the operational measures were somewhat easy to define in this research. These were the foreign operation mode strategies, especially mode switching, mode stretching, and mode combination strategies of the case companies in South Korea. Indeed, multiple sources of evidence were used – interviews were complemented with other information such information from case companies' websites and with other written material. However, there was a strong reliance on only one source of information, that is, interviews, in this research, which decreases the construct validity. The chain of evidence was quite strong in this research, as it is easy for the reader of this paper to follow the case descriptions and cross-case analysis to either directions when searching for the basis of the conclusions that were made. Seven interviewees reviewed a draft of the case descriptions of the companies that they represented, which somewhat increases the construct validity of this research.

The external validity of this research is mediocre. The external validity problem has been a major barrier in doing case studies, critics typically seeing that single cases offer a poor basis for generalizing (Yin 2009: 43). Obviously, this critique hits its target in this research, as well, for two important reasons. First, the FOM strategies of only nine firms were studied in this research. When this number is compared to the total number of Finnish companies that are active in South Korea, roughly 150, it can be seen that this sample is not very representative of the whole population. However, case studies rely on analytic generalizations, striving to generalize a particular set of results to some broader theory, which is quite different from the approach of survey research that aims at statistical generalization (Ibid. 2009: 43). Because of the scope of this study, it would have been impossible to investigate the foreign operation mode strategies of all Finnish firms that are active in Korea. In addition, Benito et al. (2008: 21) raise up an interesting point worth noting here: "The extent of detail and nuance required is unlikely to be obtained via large questionnaire surveys: the burden on informants' knowledge, reflection and memory are just too excessive. Longitudinal research is needed to obtain acceptably accurate accounts of companies' internationalisation patterns and processes."

Therefore, when only analytic generalizations are considered, the generalize ability of this study is enhanced. However, one needs to keep in mind that the FOM decisions and FOM strategies are always very company and situation specific, which makes the generalize ability of the research findings a bit irrelevant in this study.

5 EMPIRICAL FINDINGS

The empirical information has been collected by interviewing representatives from the following nine case companies: Cargotec, Proventia Emission Control, Company A, Lappset, Futuremark, Company B, Company C, Fibox and Company D. The selection of the interviewee from each case firm was based on the position of the interviewee in the company and his or her experience in the company's operations in Korea. In every case, the person that 'knew most of the company's business in Korea' was sought. Usually this person turned out to be a person from the executive or Vice President level in charge of strategy, business development or commercial operations, for instance. Sometimes these persons had a title of a marketing director or an export manager. The titles and positions of each interviewee have been more thoroughly covered in each case description. However, in case of anonymous interviewees, the exact position in the company is not revealed for the sake of confidentiality.

First, nine cases are presented in a very detailed way describing the case firms' 'story in Korea' regarding their operation mode strategies and other relevant business issues. These 'other relevant business issues' are discussed and included in the case descriptions for two important reasons. First, the information obtained through the interviews is meant to help other Finnish companies that are either interested in starting or already engaged in business in Korea as comparative information which they can utilize in their own decision making. Second, when analyzing the operation mode strategies of the case firms in Korea, it is important to preserve the context in which the strategic moves take place. Therefore, this 'other information' is offered quite extensively in this study besides the information that is directly connected to the operation mode strategies of the case companies in Korea. After presenting the individual cases, a cross-case analysis is offered where all the cases are wrapped up, which helps in reading this thesis and in assessing the operation mode strategies of Finnish companies in Korea.

5.1 Cargotec

Cargotec is a cargo handling company, headquartered in Helsinki, Finland. Cargotec offers cargo handling systems and related services for loading and unloading of goods. Cargotec offers its solutions under three brands – Hiab, Kalmar, and MacGREGOR. Hiab offers on-road load handling solutions for moving, lifting, loading and unloading products, goods and raw materials to and from vehicles. Kalmar is a provider of container and heavy duty materials handling equipment, automation applications and related services for ports, terminals, distribution centres, and heavy industry worldwide. MacGREGOR is a provider of marine cargo flow and offshore solutions and their related services for commercial cargo, offshore support and naval logistics vessels as well as for oil rigs and bulk terminals around the world. (Cargotec; Lehmus 17.1.2008)

The interviewee from Cargotec was mr. Heikki Lehmus, Vice President of Business Development and Quality. Lehmus represents Hiab brand and therefore wanted to discuss only Hiab's Korean operations. Therefore, the Korean operations of Cargotec are analyzed only concerning Hiab's activities in Korea, excluding the other business units' operations even though from time to time some references to those were made. Thus, in this interview Hiab represent a Strategic Business Unit of Cargotec, having its own business strategy, objectives and competitors than those of the other brands. (Lehmus 17.1.2008) A more detailed description on Strategic Business Unit, SBU, can be found in Welch et al. (2007: 431), for instance. For purposes of this study, Hiab is seen as an SBU of Cargotec and Hiab will be seen as if it was the internationalizing firm in this case.

Hiab's equipment is used in local transportation, building industry, waste handling, recycling, agriculture and forestry, public service utilities and the defence forces. Hiab's product range includes loader cranes, demountable lift systems, truck-mounted forklifts, tail lifts, and forestry and recycling cranes. The roots of the present Hiab date back to the 1970s, Hiab having developed mainly through a series of company acquisitions to the shape that it has today. In 2007, Hiab's sales were 931 million Euros. In the end of 2007, Hiab employed 4418 people. Hiab has 15 production units in Sweden, Finland, the United States of America, the Netherlands, Ireland, Spain, Poland, Estonia, China and Korea and sales companies and representative offices throughout the world. (Cargotec)

The interviewee, mr. Lehmus, was employed by Hiab roughly between 1997 and 1998. He was strongly involved in the Korean operations right from the beginning of his career at Hiab, being responsible for business development in the unit at that time. (Lehmus 17.1.2008)

According to Lehmus, Hiab started its Korean operations 'some day in the 1970s'. Hiab has been a global player for decades, which was illustrated by its strategy to have its own sales company on each significant market already in the 1970s. Korea belonged to these 'important markets', leading to the decision to start Korean operations already then. However, the interviewee had only red reports on Hiab's Korean operations from that time and could not specify the exact operation mode used during that time. Today, the interviewee sees that the Korean market is among the 'eight most important markets' for Hiab. Especially cranes are selling good in Korea. (Lehmus 17.1.2008)

In the beginning of 1990s, Hiab established its own sales company in Korea. At first, it was in the form of a JV with a local firm and thereafter it was acquired completely by Hiab. When Lehmus was employed by Hiab in the end of 1990s, he saw that the sales company in Korea had been operating for years in very established conditions. He saw that the volume development had been quite good in the beginning of 1990s. However, a drastic change took place in 1997 at the same time as the Asian Financial Crisis broke through. The demand plunged and competitive situation in relation to local players collapsed. Even though straight competition at the same technological level did not exist, there were still Korean providers of load handling solutions and the relative competitive advantage of these Korean companies rose significantly. The words of mr. Lehmus probably describe the situation that Hiab was facing in 1997 the best way:

> "*Although you are recording and it is so long time ago – nearly 10 years – we were in piss big that time! It was (...) roughly 15 million, 10 million Euros our turnover and we were doing manly losses. So we were in a situation to decide what we do next? In autumn 1997 we had two basic options – first, either pack*

your suitcases and go home and record N million Euros of losses, or, second, 'believe in sports and stay in the game!' The only way to stay in the game was to take a quick measure to shift to local production very strongly." (Lehmus 17.1.2008)

The interviewee, having just entered the company and being responsible for business development, was in charge of the solution to the problem Hiab had encountered. A decision was made to continue operations in Korea by shifting to local production. Hiab acquired a local firm, that best suited to be transformed into the objectives of Hiab. The Korean firm, Hana, was a little bit of a competitor, producing some cargo handling equipment, among other things. Due to Asian Financial Crisis at that time, these kinds of acquisition targets were very cheap, many target companies being in liquidity crisis. This applied also to Hiab acquisition – Hiab acquired this Korean firm very cheaply because this company was in liquidity crisis like many other Korean firms. As a result of the acquisition, Hiab's sales company and local production firm Hana were integrated to form a new company, Hiab Hana. The valuations of the companies were done in a specified way and Hiab invested much-needed working capital in the new firm. Even though the original investment was 'very cheap', Hiab has been investing continuously to new firm to maintain capacity. The interviewee states that the amount of total investment is hard to measure. At the time of interview, Hiab Hana employed 82 persons and estimated turnover for 2007 was nearly 30 million Euros. (Lehmus 17.1.2008)

According to the interviewee, when the two companies embarked on the common route, the arrangement was a joint venture. Hiab owned 70% and the local Korean management 30% of the new company. Out of this 30%, the Chief Executive Officer of Hana owned half of it and there were eight members from the Korean management team that held shares. JV worked well and there were no major conflicts. However, after a few years, the CEO of the Korean company wished to leave, he had had some problems submitting to be 'only the local leader' in a big international company instead of an independent CEO of a local firm that he was used to be. The firms had signed a redemption agreement and the CEO of Korean company started selling his shares in the JV immediately after the redemption agreement allowed it. Because the situation was hard for both parties, Hiab naturally did not object this but redeemed his shares. Again, a few years after this, Hiab redeemed also most of the shares of other members of management team. These persons were very eager to have their shares redeemed, since when forming the JV during the Asian Financial Crisis they did not get money for their shares. However, technically Hiab Hana was still a joint venture at the time of the interview, since some members of the management team still held shares, seeing that holding the shares of the JV is a better investment for them than holding money on a bank account. The persons that still hold shares have said that they are ready to sell them but Hiab allows them to keep the shares if they wish since, according to the interviewee, there is a certain public relations advantage if a firm is registered as a JV in Korea. On regular commercial sector this PR advantage does not help but in public and military projects a JV status 'lifts a foreign company one step forward'. (Lehmus 17.1.2008)

At the time of the interview, Hiab Hana had a large marketing and service center in southern Seoul and a production plant for special cranes in Chungpu. The share of exports of the production in the plant is small, roughly 25% but Hiab Hana aims at increasing it. The exports from this plant are mainly to Japan, Taiwan and Vietnam. Due to the JV arrangement, Hiab has been forced to reorganize its operations in Korea extensively. Before the acquisition, Hiab had a large service center in Incheon and a sales company in Seoul that acted also as a sort of headquarters for the Korean operations. Hana had a production plant in Chungpu and a small marketing and service center in Seoul. In addition, both companies had their own dealer networks. A few years after acquisition, Hiab Hana divested Hiab's service center in Incheon and the sales company and headquarters from Seoul was relocated next to the production plant in Chungpu. At the same time, Hiab Hana strongly enlarged the marketing and service center formerly owned by Hana that was located in Seoul, also moving this unit to a new and better-known address. (Lehmus 17.1.2008)

What comes to management of Hiab's Korean firm, expatriates have been utilized as Chief Executive Officers. When Hana was acquired, the operations of Hiab were led by a Swedish expatriate. This person headed Hiab for five years and left after the acquisition was made. He was followed by a Finnish expatriate, who has lived in Korea for 30 years and, naturally, speaks Korean, which helps both him and Hiab greatly in the leadership of the company. (Lehmus 17.1.2008)

Culturally, Korea has been a very hard place to operate for Hiab. The most apparent cultural problems have been related to language and communication issues because in the acquired company there was from one to three persons that could tolerably speak English. These people became some kind of 'gatekeepers', all the information and communication went through these gatekeepers. Hiab never knew how the information was understood in the place where it was to be acted upon and there were scary misunderstandings, luckily in minor issues. This problem applied especially to technical knowledge, Hiab had to verify many times that the original message was understood correctly because the information often changed many times as it passed through the information chain. Over the years, however, Hiab has been able to find personnel with better English skills. Another cultural-related problem for Hiab has been Korean authoritarian organizations and structures, making the cooperation a bit hard. According to the interviewee, Hiab has to be very careful when giving instructions to the employees because Korean workforce does not question anything. Instead, they change their working procedures immediately after getting instructions, even though the manager had meant the instructions as to critically evaluate current practices, not as direct orders to execute immediately. In short, there is a lack of discussion between Korean workforce and Finnish managers, which is different from what Finnish firms are used to when dealing with problems in Western World. (Lehmus 17.1.2008)

5.2 Proventia Group

Proventia is an international automation and environmental technology group whose products reduce the harmful impact on the environment caused by industrial and other activities. Proventia has organized its operations into two business groups, Emission Control and Production Technologies, respectively, and a separate Ventures unit, the mission of which is to expand Proventia's operations into new areas. The Emission Control business group provides solutions for controlling engine and power plant emissions and the Production Technologies business group supplies production technology for making production processes more efficient. The turnover of the company was roughly 16,7 million Euros in 2007. Proventia employs 30 people in Finland, Switzerland and Asia. (Proventia)

The interviewee was Mr. Jouni Puura, President of Liaison Office in Korea, who represented Emission Control business group. Emission Control is the only business group of Proventia that is present and active in Korea. Therefore, the operations of Proventia in Korea are analysed from the viewpoint of a Strategic Business Unit, Emission Control. As a result, Emission Control is seen as the internationalizing firm in this context, instead of parent company Proventia. (Puura 31.1.2008)

Proventia Emission Control has its roots in Finnkatalyt, a company founded in 1994 to develop solutions for exhaust gas purification. Since the establishment, the company has operated on the international market and exports have always accounted for a considerable part of its net sales. The share of international business of Emission Control is over 90 %. Proventia Emission Control was one of the firms that were awarded the internationalization award of year 2007 of the President of the Republic of Finland as recognition of important activities in an international operating environment that benefit the Finnish economy and business. (Proventia)

The solutions that Emission Control offers are diverse. The basic product, emission purifier, is offered in many altered variations to different emission sources. The emission purifiers are offered to various diesel-driven machinery, such as material handling machines, excavation machinery and agricultural and forest machinery. Purifier solutions are also offered for power plants and ships using various fuels. In addition, Emission control offers purifier solutions as retrofits to diesel engines that are already in use. Emission Control has participated extensively in many retrofitting projects globally from California to Korea. In Hong Kong and Korea, for example, purifiers of Emission Control have been installed in tens of thousands of vehicles used in city areas. (Proventia)

According to the interviewee, Korea is of utmost importance as a market for Emission Control. In the words of the interviewee, "Korea is probably even too important a market for us!" Emission Control has operated in Korea more permanently for a very short time, as a liaison office was established in September 2007. The first Asian office was established in the beginning of 2003 as Finnkat Asia in Hong Kong, the name Finnkat instead of Emission Control because Finnkatalyt Oy was another company from which Emission Control was formed in 2007 in addition to Swiss ENWA GmbH. A liaison office is the lightest operational form in Korea, without the obligation to bookkeeping, even. The liaison office in Korea was legally established under Finnkat Asia in Hong Kong. The business in Korea for Emission Control has increased rapidly and there has been a lot of activity, which led to the decision to transfer activities from Hong Kong to Korea. Emission Control considered if they would handle Korean business from Hong Kong as they had done earlier but the decision was made to come to Korea more permanently. Technically, the office in Hong Kong still exists although there was physically no one at the time of the interview. (Puura 31.1.2008)

The interviewee is the only person from Emission Control who is physically in Korea. A major driving force for Emission Control to engage in business in Korea was a sort of 'business foray trip' in 2003 when the fast growth was discovered. As a result, Emission Control had to find a partner quickly, and Finpro was selected to aid in the selection process. Emission Control was in a rush to catch a project that was about to start, making the selection to happen very quickly. The interviewee says that 'luckily there was Finpro's knowledge about this partner', making the selection process a lot easier for Emission Control. In addition, Finpro continued the cooperation with Emission Control also after the selection, which further made the decision making easier. The partner of Emission Control, basically working as an agent, is engaged in many other businesses, as well, and has other cooperative agreements, even with another Finnish firm. This agent is active on many frontiers, importing building materials from Central Europe, for instance. The most important assets of this agent for Emission Control are the connections to various important players in the Korean market and language skills. These 'connections' are of utmost importance for Emission Control as the business of Emission Control is very legislation-driven, that is, as the environmental laws become stricter, it helps the business of environmental solution providers. Often times, according to the interviewee, the main customer is the local Ministry of the Environment and the personal connections to this ministry and its subinstitutes are extremely important. For instance, in a large retrofitting project where emission purifiers are installed in local diesel-driven vehicles, in which Emission Control is engaged, the Ministry of Environment is controlling the project but the actual work is carried out by certain subinstitutes of the ministry, making the connections to these sub institutes also crucial for Emission Control. As a result, Emission Control has been trying to establish connections also these sub institutes as much as possible. (Puura 31.1.2008)

Certain kind of 'introducers' are important when dealing with government officials in Korea. After being introduced, company representatives may present their cases and suggestions to government officials and can start building the relationships on their own. As said, the agent of Emission Control has very good connections to both ministries and their sub institutes and to other key players in the market, as well. In addition, the agent has a long experience in business in Korea and with foreign companies. This partner has offered Emission Control facilities in Seoul, Emission Control does not have any own production or other facilities in Korea. Instead, the liaison office is actually in the facilities of the partner. The interviewee is in charge of the Korean office but the actual business and financial flows are between the headquarters in Oulunsalo, Finland and the Korean customer, the interviewee basically controlling the operation and supporting the partners and customers. The cooperation and communication between Emission Control and the agent partner has been good. The interviewee and the agent jointly visit ministries and customers in Korea, the agent acting as an interpreter to overcome huge language barriers that the interviewee highlighted. The interviewee saw that the English language is a major problem in Korea, even many of the government officials do not speak English. Therefore, the language skills of the partner are extremely important. (Puura 31.1.2008)

Emission Control is also engaged in cooperation with another partner on the Korean market, namely SK Corporation, one of the biggest *Chaebols* in Korea. SK Corporation, which has its main business operations in oil and chemical industry, also has an environmental business group. Interestingly, Emission Control is representing the environmental sector products of SK in Europe, showing a sign of two-way cooperation that can take place between a principal and a partner. The products of SK are a bit different than those of Emission Control. The interviewee terms SK Corporation a kind of 'customer partner', being something between customer and a partner in cooperation in Korea. In the first project of Emission Control in Korea, in which a complete end product was delivered from Finland to the end customer, SK Corporation as a customer partner took care of the installation. However, in the second, bigger project that was still in-progress at the time of the interview, certain components are delivered from Finland and the agent partner takes care of the installation. (Puura 31.1.2008)

A major activator for the business development of Emission Control in Korea has been good reference deliveries, such as in Hong Kong, for instance. As a result of good references in Hong Kong, Emission Control has been able to act as an adviser for Korean ministries that are in charge of environmental investments. Emission Control had good references for many years in Hong Kong, having participated in three different projects there, out of which the first was the biggest large-scale project in the world actually. Due to these good references, information on Emission Control has passed on to the persons working in the Korean Ministries. Before Emission Control started its cooperation with SK Corporation, it had already started projects in Korea with the aid of the actual agent partner as a result of interviewee's 'business foray trip'. A ministerial delegation from Korea went to Hong Kong to acquaint themselves with a project in Hong Kong and one member of this delegation was a contact from SK Corporation. This person came to talk with Emission Control as the operations in Hong Kong were presented, which sparked off the cooperation between SK Corporation and Emission Control. (Puura 31.1.2008)

In addition to the language problems, the interviewee highlights the cultural differences that can bring about problems when operating in Korea. According to the interviewee, many things do not work as they do in Finland and issues are not treated in the same way. He sees that the communication is different regarding different issues and when negative issues, especially, are raised up, they are handled in a totally different way than in Finland. The interviewee sees that cultural sensitivity and cultural knowledge, naturally, helps to overcome cultural barriers that he sees to exist. (Puura 31.1.2008)

5.3 Company A

Company A is a log house manufacturer established in 1981. The log houses are marketed throughout Finland and exported to the Nordic countries, Central Europe, Russia, Japan, Korea, China, Indonesia and Thailand, among others. (Company A; Interviewee Four 6.3.2003 and 24.4.2007) Company A offers its log houses and related services, such as installation, to both detached house buyers and leisure-time house buyers. In addition to family living purposes, Company A log houses are built also for the needs of tourism and representation. (Company A) The turnover of the company is roughly 17 million Euros. Company A employs approximately 80 people. (Interviewee Four 6.3.2003 and 24.4.2007)

Two persons were interviewed from Company A and the information from these interviews is merged to depict the development of the operations of Company A in Korea. The main source was the interview on 31st January, 2008 with a high-ranked manager Interviewee One. This information was supplemented with information from two distinct interviews with Interviewee Four. The interviews with Interviewee Four took place on 6th March, 2003 and 24th April, 2007. (Interviewee One 31.1.2008; Interviewee Four 6.3.2003 and 24.4.2007)

There was a time when Korea was a more important market for Company A than it is today. In the end of 1990s, just before the Asian Financial Crisis, Korea was seen as one of the 'stake markets' for Company A. The first exports to Korea took place in 1995 and the firm has sold yearly a small quantity of log houses to Korea, roughly from five to 10 houses a year. During the most recent years, houses have not been sold at all to Korea, leading Company A to concentrate more on the Central European and Russian markets and changing the status of the Korean market from a 'stake market' to a regular, ‘among-others market’. However, the company has not totally given up its Korean operations, the basic approach to sales to Korea is that Company A sells houses to Korea if somebody is interested in buying them. Still, though, the firm is neither targeting resources nor devoting interest and energy to the Korean market. (Interviewee One 31.1.2008)

Company A selected Korea as a market basically by accident, because a good partner was found. The partner, who became the importer of Company A log houses to Korea later, attended a permanent housing exhibition in Stockholm and came to the exhibition house of the company. Showing his interest, the Swedish representative of Company A asked him to contact the headquarters in Finland, which sparked off the cooperation that was to follow. Company A neither planned an entry to Korea nor screened the Korean market with a result that it would be worthwhile to enter Korea. Instead, it was the approach of this Korean importer who bought several houses from the company and could show that Korea was a good, developing market and worth the stakes to put there. (Interviewee One 31.1.2008)

Company A does not have personnel of its own in Korea. The company has one representative, working as an importer for Company A. This importer, located in Seoul, sells also other firms’ products along with Company A log houses and has sub representatives in the Korean market. The production takes place in Finland and the deliveries are made as sea freight in containers to Korea. The installation is handled by the importer, with the aid of Company A if needed – from time to time the company has sent or suggested a group of independent carpenters from Finland who have installed log houses in Finland and in other parts of the world to take care of the installation. These carpenters have then been able to educate local carpenters and installers to do the job. (Interviewee One 31.1.2008)

After a good start with export operations in Korea from 1995 onwards, Company A had high profit expectations on the Korean market, the yearly turnover was expected to triple or quadruple if a sales subsidiary was established (Interviewee Four 6.3.2003 and 24.4.2007). Partly as a result of this, a decision was made to establish a sales subsidiary in Korea in 1997, named ‘Company A Korea’ (Interviewee One 31.1.2008). A further, and perhaps more important, trigger for this development was the request from the importer to move to a sales subsidiary strategy, as the sales had started to go down after a good start and the importer saw that a sales subsidiary strategy offers a stronger way of doing business in Korea. The importer saw the local presence as very important to be able to sell log houses in Korea. Actually, South Korea was the first target country for Company A in Asia and the second country to be served through a sales subsidiary strategy, the first country having been Germany. The suggestion of Korean importer to become the CEO of the Korean sales subsidiary easened and speeded up this establishment significantly. The original plan was to penetrate ever deeper into the Korean market and make Korea as the Asian area headquarters from which China, Japan, and Thailand, for instance, would have been served. (Interviewee Four 6.3.2003 and 24.4.2007) The importer, indeed, became the CEO of Company A Korea and he had three salesmen in the sales subsidiary that was established (Interviewee One 31.1.2008; Interviewee Four 6.3.2003 and 24.4.2007)

However, everything did not go as planned: this new unit failed in Korea (Interviewee Four 6.3.2003 and 24.4.2007). The sales figures did not grow as expected even though Company A had invested quite a lot to establish the company and to running expenses. Simply, the sales figures did not justify the sales subsidiary, leading to the decision to divest this unit and dissolve this arrangement. After the sales subsidiary was run down, Company A returned to serve the Korean market using an importer. (Interviewee One 31.1.2008)

A number of reasons for the failure of subsidiary operations in Korea can be identified. A major failure was the appointment of a wrong type of person to head the subsidiary operation as the CEO. This person was a natural selection to lead the operations because he was acting as an importer for Company A in Korea, and when he proposed the subsidiary operations to be started and agreed to head the operations, Company A obviously did not even consider other alternatives. Lack of knowledge of this person led Company A to make the wrong selection. Initially, he had seemed like an ideal person to be in charge of the Korean operations. He was a Korean but he had lived in Sweden for 25 years. Being of Korean ethnicity, he naturally knew deeply his home country. In addition, he knew a lot about construction business, management systems and marketing methods. More importantly, he knew also about Scandinavia and Finland since he had been for decades in Sweden. However, all these qualities did not live up to expectations. Company A admits frankly that this recruitment was a mistake and later development in Korea can verify that this really was the case. (Interviewee Four 6.3.2003 and 24.4.2007)

Even though Company A had expected this CEO to be a ‘unique leader’ who knows both the Korean and Nordic business culture, he had lost his contact with the Koreans, to say. After those 25 years in Sweden, he was not an ‘insider’ anymore in Korea but changed to a foreigner that did not have access to important Korean networks. One Korean board member of Company A Korea questioned the selection many times but the message was hard to catch by Company A due to Koreans being very polite people – this board member could not openly question the selection but tried to convey this message indirectly. It took three times before Company A realized that he was trying to tell that the selection was totally wrong. The selling of log houses was seen to be a trust business, since the houses were large investments and they enjoyed a status of a luxurious product in Korea. To be able to even contact wealthy and influential potential customers, the CEO had to have a high, respected position in the networks. The person that was erroneously selected did not have this position neither the networks because he had lived for such a long time abroad. (Interviewee Four 6.3.2003 and 24.4.2007)

Another mistake was the neglect of monitoring the CEO properly. This led to a couple of problems. First, the CEO located a model house, in fact also functioning as the sales subsidiary, of Company A in a completely wrong place to be fruitful for the company in its marketing efforts in Korea. The model house was opened in Koyang city in the Gyonggi province that surrounds the capital city Seoul in April 2002. Every third year an international flower exhibition is organized nearby in the city of Ilsan. Company A did not ask carefully, where the subsidiary will be located. The company thought it is in Ilsan city and saw it to be a beautiful flower city, a very good spot for a model house. Yet, to a great astonishment, when invited to the opening ceremony of the subsidiary, Company A was only to realize that this CEO had placed this model house outside the city in rural areas behind trees – the location was awful and access to this house was very difficult. Company A admits that they should have been with this subsidiary development from the very beginning and follow carefully instead of trusting this CEO too much as to where to locate the unit. Second, the CEO was handling his own businesses instead of concentrating on the business of Company A in Korea. The company was to realize some odd issues – the CEO, along with three other persons employed in the subsidiary, was selling ties to Sweden and special bed-sheets for hospitals. At the time that this CEO had his own office, this office was totally for different purposes than selling Company A in Korea, although it had signs of Company A and the walls of the office were fitted with pictures of log houses. Clearly, this CEO did not concentrate on the operations of Company A. (Interviewee Four 6.3.2003 and 24.4.2007)

Company A came to realize also that this CEO was good in socializing in small circles but not an extrovert as expected from a CEO. This CEO was reported to be quite shy and insecure about himself – in short, he did not have the capacity to be a CEO. As a result, he did not manage to sell log houses to the extent expected. Company A had hired him with a constant salary, which turned out to be a mistake since he still received his pay even though he did not perform. Later Company A changed his salary arrangement to a bonus-based one, agreeing to pay actually even more than the constant salary in the case of good sales but he still did not manage to sell the houses. After not getting bonuses due to insufficient sales, this CEO moved to another company. Even before this CEO left Company A Korea, Company A had sent an expatriate, a construction engineer, to remedy and control the situation that the CEO had created. This expatriate was in Korea and in Thailand for a long time, acting as a regional director. Now, Company A is deciding where to locate the area headquarters, possibly having even production capacity, a major possibility being at the time of interview China. This decision definitely has its effect also on the Korean subsidiary, as well, which, based on the interviews, still technically exists, even though it has been essentially run down and does not have any personnel. (Interviewee Four 6.3.2003 and 24.4.2007)

However, not all the troubles can be attributed to the mistakes made by the CEO of the subsidiary and poor monitoring by the parent company. Asian Financial Crisis between 1997 and 1998 was immediately visible in the sales of Company A in Korea – no houses were sold during that time. The products of Company A became significantly more expensive in Korea due to the plunge in the value of Korean currency Won, which meant that finding customers became troublesome. (Interviewee One 31.1.2008) This hard market situation combined with the erroneous selection of CEO, which led to poor location of the model house, took away the basis for good sales development in Korea. (Interviewee Four 6.3.2003 and 24.4.2007) After this total slowdown in Korean sales, the sales have recovered. In some years Company A has exported more, in some other years less, depending also on the situation at the importer because he is representing also other companies in Korea. (Interviewee One 31.1.2008)

Despite major problems with the sales subsidiary operations in Korea, Company A has operated quite comfortably in Korea, even though it has not achieved its objectives there. Interviewee One indicated that exporting to Korea has been very easy – "I would compare it to exporting to Sweden!" Interviewee One sees that it is extremely beneficial for a small manufacturer to have a local person who knows the local systems and, therefore, can do things in the way they should be done in Korea. Company A has strong confidence in the local importer in terms of organizing personal relationships in Korea and in public relations and Goodwill activity. The relationship network of the importer is seen to be of extreme importance, almost invaluable. At least it would be very hard to operate on the Korean market without this relationship network, as indicated by Interviewee One. He sees that the development of relationships always takes so much time and resources, which means that a company cannot create those relationships to the end customers but a foreign firm is better off when it establishes relationships only to the Korean partner and its personnel, instead. In addition, the language abilities of the importer are seen to be important because, according to Interviewee One, it is almost always a necessity to have a translator when dealing with the Koreans. The importer and its staff are proficient in English, solving essentially this language problem for Company A. The translation work done by the importer for installation and reception instructions for log houses and for other documents has been of great importance, too. (Interviewee One 31.1.2008)

5.4 Lappset Group

Lappset Group is one of the leading providers of playground equipment in the world (Lappset). The product range of the company includes playground equipment, public fittings and sports equipment. A major share of the turnover, 90%, comes from playground equipment, followed by a 6-7% share from public fittings and the rest from sports equipment. (Ylinenpää 21.2.2008) In 2007, the firm's turnover was 45,6 million Euros and the company employed 324 persons (Lappset). The history of Lappset dates back to the end of 1960s when the founder of the company started to realize his vision to make playgrounds softer and warmer using wooden playground equipment instead of metallic solutions that were mostly used during that time. After a rapid growth and following the founder's vision that the Finnish market is way too small to concentrate on exclusively, the company was already in the 1970s selling in Scandinavia, Benelux-countries and Japan, even. Having continued on a successful path, Lappset operates today a subsidiary in four countries, exports are directed to over 40 countries and 70% of the group's turnover comes from abroad. (Lappset; Ylinenpää 21.2.2008)

The interviewee from Lappset was Mr. Hannu Ylinenpää, the marketing director. The interviewee has been in contact and cooperated with the Korean importer extensively during the last five to 10 years, thus being a good informant for this research. (Ylinenpää 21.2.2008)

Interestingly and surprisingly, Korea is the biggest export market for Lappset Group, having held this position for three consecutive years, possibly being the biggest export market still in 2008, according to the interviewee. The sales volumes to Korea are roughly equal to Spain, another big export market for Lappset. The fact that Korea is the biggest export market for Lappset is, indeed, very surprising, since usually the biggest export markets for small and medium-sized Finnish companies, to which Lappset can roughly be categorized, are found nearby in the neighboring countries such as Germany, Russia, or Sweden. Clearly, therefore, Korea is as a market of great importance to Lappset. Lappset is a powerful actor in Korea but in other Asian countries the market shares are very small, even though these other countries have huge potential for the company, as admitted by the interviewee. The share of Korea out of Asian sales of Lappset is roughly 80-90%. As a result of the importance of Korea as an export destination, Lappset has given Korea a higher priority. Korean market gets 'special treatment' because of the ABC-classification of Lappset, in which ten most important export countries get faster delivery and service regarding certain products and quicker responses to inquiries. (Ylinenpää 21.2.2008)

Lappset has served the Korean market through an importer. This importer acts as the reseller for the company. The cooperation began in 1993 when the importer approached Lappset at a trade fair in Germany and suggested cooperation in the Korean market. During this time, Lappset did not have a deliberate internationalization strategy but the firm entered different export markets in twists of fate almost, as admitted by the interviewee. If Lappset was approached by a potential agent or distributor, the firm first screened the approaching company to see whether it was reliable, did business on the right segment, had good customer contacts and did not represent competing products. If this screening did not produce negative results, a one-year tryout period was usually granted to the company. Later, if business worked out fine, an official resale agreement was written between the parties. (Ylinenpää 21.2.2008)

The Korean importer does not only represent the products of Lappset in Korea but has also other principals. However, Lappset is the main supplier of this importer, having a share of roughly 80% of the business of this importer. When the cooperation began in 1993, the importer had other products to represent from the field of construction business but over the years the products of Lappset grew in relative importance to the importer. Again, during the last couple of years, the importer has taken on new construction business products from other principals to represent on a solitary basis. The importer has four principals to represent in Korea, Lappset being the main supplier today, still. According to the interviewee, the Korean importer is quite exceptional to other resellers of Lappset. This is because the Korean importer is active only on one customer segment, that is, the Korean construction firms. Normally, Lappset categorizes customers in a very subtle way, the customer segments ranging from public customers to private customers, consisting of housing companies, construction firms, kindergartens, to business-to-business customers, consisting of amusement and theme parks, pubs, camping sites, hotels, and finally to 'passive customers', consisting of construction designers and architects. In Korea, however, the importer does business with only roughly 20 construction companies. To facilitate growth in the fear of maturing market in Korea after a couple of years, the Korean importer has also started to create contacts with public sector lately. So far, however, the way this Korean importer does business has been very simple when compared to Europe. The importer has its sales function, consisting of two salesmen and 20 construction firms as customers. This is way easier than in Europe where Lappset has 8000 customers to serve and maintain contacts with. For the importer, it has been quite easy to create new business because the customer count has been so narrow. Lappset has been the market leader in Korea for the last three to five years. (Ylinenpää 21.2.2008)

According to the interviewee, a major reason for Korea being the biggest export market for Lappset is the sheer size of the Korean market. In addition, although the importer has served only a narrow segment, the housing production has been vivid in Korea, which has boosted the business for the playground equipment of Lappset at the same time. However, there is perhaps a more important reason and thrust for Korean market to be so important for Lappset and, on the other hand, Lappset being in such a commanding position in Korea. This is the managerial decisions made by Lappset during the Asian Financial Crisis in 1997 and 1998. As a result of this crisis, the housing production declined and, therefore, the number of projects available to Lappset and its competitors declined. Lappset managed to direct its importer through these hard times so that it was among 'the winners of this crisis'. Lappset granted special discounts to the importer by binding the discounts to the value of the Korean currency won. Won was bound to the value of the US dollar and when Euro appreciated against the US dollar, this made the purchases by this importer from Lappset more expensive. Lappset helped the importer with this problem by offering these special discounts. In addition, Lappset offered the importer longer payment terms. After the importer survived from this crisis, the number of competitors declined. As a result of being among 'the winners' with the help of Lappset, the importer has been able to grow the business of Lappset in Korea, the growth equaling roughly 20% during the last five years. (Ylinenpää 21.2.2008)

The Korean importer buys the products from Lappset to their own account and then sells the products by itself. Lappset does not even know the price charged from the end customer even though the firm has tried to ask the end prices often. The importer has bypassed these questions by stating that the prices charged from the end customers have been determined on a project basis, essentially hiding information from Lappset. All the production takes place in Rovaniemi, Finland and the products are exported to Korea in containers usually on a weekly basis because of high volumes. Nowadays the exports take place mainly over the sea route but earlier also the Trans Siberian railway was used, but congestion on this route caused delivery delays, which can be harmful in the construction business where project schedules are very important, leading to the decision to utilize mostly sea route. Lappset takes care of the delivery until the port of Busan in Korea and thereafter the delivery is handled by the importer. The installation work is handled by the importer either by itself or with the help of its cooperative partners. A fruitful solution to the delivery arrangements has been the offer of Lappset to the importer to take the most sold products to its warehouse and pay in half a year payment term, which, in effect, creates the importer a possibility to deliver products with a shorter delivery time. This arrangement has been in place for the last three years and has offered the importer a competititive advantage, since Lappset has been the fastest supplier from Europe because of this arrangement. Korean importer has utilized extensively so-called ‘my design’ department of Lappset in its business. This department creates customer-specific solutions from standard modular components, a service that has been highly valued by Korean customers. (Ylinenpää 21.2.2008)

In addition to pure sales volumes, Korea has been an important market for Lappset because the Korean importer has been able to sell and install playground equipment throughout a year, thus balancing the utilization of production capacity at the firm’s factory. In Finland, for instance, the high season is on the second and third quarter of the year, which creates pressure in the production and could possibly cause shutdowns in production during the winter times when the installations are not possible. However, sales to countries such as Korea have meant that Lappset has actually never had to stop production because of winter conditions. (Ylinenpää 21.2.2008)

The cooperation with the importer has always been at a good level. Lappset has actually never encountered any problems in this relationship, minor language problems being the exception. According to the interviewee, Korea has been quite an easy market for Lappset since the company has been able to allow the importer to work alone to a large extent in Korea. Korea has not required a lot of effort from Lappset – visits to and from Korea have been quite rare and normally the contacts are handled through email and by phone. The importer has had good contacts to its customers and the prices have been lower than those of the main competitors on the market partly with the help of Lappset, especially during the Asian Financial Crisis years. The possibility of buying customer-specified solutions has helped the importer to a large extent. In addition, the shorter delivery times because of the warehousing option discussed above has helped the importer to build a strong market position in Korea. Lappset has greatly appreciated the importer's way of giving feedback. Even though the importer has concealed the resale prices as discussed above, the feedback mechanism works strictly and honestly. According to the interviewee, the Korean importer is quite exceptional from other importers because it takes up the defects in products in a constructive way and offers a solution right away, thus assisting Lappset in product development and quality control. Many other importers are seen just to identify the defects and concentrate on complaining about the problems instead of trying to offer solutions. (Ylinenpää 21.2.2008)

Even though Lappset started its Korean operations quite randomly after an approach from a potential importer, nowadays the company is assessing rigorously where it wants to be present and where to direct resources to. Asia is seen to be a very important market area because the markets are not growing in Europe. As said, although Lappset is strong in Korea, the market shares are very small in other parts of Asia. China, Japan, Taiwan, Thailand, Singapore and Vietnam are seen to offer a lot of potential in the future. As a result of this huge potential and to devote more resources to China, a sales office was opened in Shanghai to better serve local resellers, including the Korean one, too. There is a possibility to establish a warehouse in the Chinese sales office. If this warehouse was built, Lappset could deliver products to the Korean market in a week instead of four weeks that the deliveries take at the moment. (Ylinenpää 21.2.2008)

Although the cooperation with the Korean importer has worked out smoothly, the language barrier has been seen to create problems, especially in the beginning of the cooperation. Initially, the English abilities of the contact persons at the Korean importer were poor and caused difficulties in the cooperation:

> *"They [Koreans] sent a fax stating 'please send the airplane', meaning that they wanted the delivery as air freight, but we had to ponder what they actually mean!"* (Ylinenpää 21.2.2008)

Later, these people have been replaced and there are people with good English skills working for the importer. Lappset raised up this language problem issue with the importer, which, for its part, offered a solution to the language problem. The importer understood the problem and took measures to remedy the situation. (Ylinenpää 21.2.2008)

5.5 Futuremark

Futuremark, founded in 1997, is a company that is focused on the state of the art 3D graphics programming. In a nutshell, Futuremark develops and sells performance measurement programs for computers and mobile devices. The company has divided its operations into three separate units – PC Products and Services, Mobile and Embedded, and Futuremark Games Studio. (Futuremark)

PC Products and Services unit is the most known part of Futuremark, revolving around the graphics and performance measurement of personal computers. Futuremark's 3DMark and PCMark benchmark products and related online services are world famous in the PC industry. PC Products and Services unit serves world's leading chip companies, PC brands, component manufacturers, independent PC media, and millions of individual private customers. (Futuremark) This 'PC side' is where it all started ten years ago and it still forms the biggest part of the business, in terms of both resources committed and turnover generated. (Talala 5.3.2008)

The Mobile and Embedded unit is the second biggest business unit for Futuremark and this unit is growing clearly most strongly, having achieved a tremendous 114% growth in turnover in 2007. This ‘mobile side’ brings the strongest growth for the company at the time of the interview, whereas the markets for ‘PC side’ have saturated relative to ‘mobile side’ during the recent years. (Talala 5.3.2008; Futuremark) Mobile and Embedded business unit does benchmark software development and licensing to 3D graphics firms, chip manufacturers, cellular phone and other handheld device manufacturers and wireless network operators. In addition, a growing part of the business is the licensing of Content Creation Tool Chain for automotive, cellular phone and embedded industries. (Futuremark) The business on the ‘mobile side’ is mostly concentrated on the newest technology and products – Futuremark tests the usability and performance in the newest and finest mobile devices. For instance, the more a mobile device has multimedia, video, photographing and gaming features, the better it is for Futuremark. (Talala 5.3.2008)

Futuremark Games Studio is engaged in the development of games for personal computers (Poropudas 2008; Futuremark). In addition to these three business groups, Futuremark provides a website YouGamers.com, where PC players can test their computers regarding how well one can play different new games and the website can then give recommendations as to how to update the computer to overcome possible bottlenecks in performance. (Talala 5.3.2008)

Futuremark is headquartered in Espoo, Finland and the firm has a subsidiary in Silicon Valley, USA. The company also has a sales office in China and sales and distribution partners around the world. (Futuremark) In 2007, the turnover of the company was a bit less than four million Euros and the number of personnel was 65, out of which 59 were working in Finland (Talala 5.3.2008). Futuremark has been praised for its fast growth – the firm was RedHerring Hot-100 EMEA winner in both 2006 and 2005, and the company was the 85th most rapidly growing technology company in Europe according to Deloitte’s Technology Fast 500 Study (Futuremark).

The interviewee was mr. Petri Talala, Vice President of the company and in charge of the mobile business. At the time of the interview, he had been working for Futuremark for roughly two years. At the time the interviewee was hired by Futuremark, the company had differentiated the mobile business from the regular business, that is, the 'PC side' of Futuremark. The newly-formed mobile business needed a leader, and the interviewee was selected for that spot. According to the interviewee, Futuremark very soon realized that a major share of mobile business activity is in Asia and the company already had one customer there as a very active one, Samsung, one of the biggest *chaebols* in South Korea and one of the biggest companies in the whole world. Therefore, in effect, Samsung already existed for Futuremark as a customer in South Korea when the mobile business was started and Futuremark also saw that there were a number of mobile, high-technology firms as potential customers and partners for Futuremark. As a result, a decision was made to put a lot of effort and resources to the South Korean market. (Talala 5.3.2008)

As said, the mobile business is growing most strongly in the company at the moment and this growth comes mainly from Asia, to be exact from South Korea, China and Japan. These three markets are strategically extremely important for Futuremark today. What makes South Korea even more important as a market is that South Korea is in many ways a forerunner in the development of mobile business. There is a large mobile industry in the form of LG and Samsung. There are a huge number of small firms from the field of mobile business, too. Also, the chip development for mobile components is very strong. Lastly, the South Korean people are very much into all kinds of game, mobile television, mobile, and multimedia services. The interviewee did not specify which market is more important, but said that South Korea and Japan are clearly the forerunners in the mobile business and therefore, extremely important markets for the company. To identify other major markets for Futuremark, the United States is an important market for the whole company, not just to the mobile business. On the other hand, Europe and Finland are not that important markets for Futuremark, the company serving basically only one customer in Finland, for instance. In South Korea, Futuremark serves almost purely just mobile business customers, with some exceptions. (Talala 5.3.2008)

Futuremark is running its business in South Korea through a sales agent located in Seoul. In principle, this sales agent, a South Korean person, works alone. He has his own mobile software company that develops all kinds of mobile software for South Korean mobile phone manufacturers. This agent representation is a 'side business' to this company or person and the agent is also representing another firm, of Finnish-Japanese origin, in South Korea. (Talala 5.3.2008)

The sales agent basically helps in opening doors to new firms by finding valid contacts and is personally quite active in the development of Futuremark's business locally in South Korea. The role of the sales agent is not big in the sales process because after the initial contacting and meetings with potential clients the deal is driven through by Futuremark itself and the South Korean customer, the sales agent basically just receiving his commission from those sales cases that end up to an agreement. However, this sales agent is extremely valuable to Futuremark. His value is in the experience and knowledge of the South Korean mobile industry. He knows the South Korean mobile industry and South Korean mobile business firms well, especially small and medium-sized companies. (Talala 5.3.2008)

> *" (...) why it works so well for us, is that this guy is an old hand, knows a number of persons and even on high level, so when I say that this meeting should be arranged, this agent digs out a number from his phone book to that company and calls there and that is it! It is of great importance to us."* (Talala 5.3.2008)

As highlighted by the interviewee, everyone knows global South Korean firms such as LG and Samsung but the smaller firms are also extremely important for Futuremark as potential customers. There are a massive number of small and medium-sized companies that Futuremark has been negotiating with in South Korea. These firms have engaged in a very high-level high-technology product development in mobile environment for new types of mobile applications and mobile user interfaces. (Talala 5.3.2008)

The agent, being an experienced player in the market and knowing valid contacts, basically contacts relevant South Korean firms interested in Futuremark and arranges meetings. These meetings with potential South Korean customers are then attended by both the agent and the interviewee but quite soon the deal-making is taken care of by the interviewee himself, the sales agent providing linguistical help if necessary. In short, the sales agent does the first introduction and the rest of the process is handled by Futuremark itself. If this initial contact leads to interest on both the customer's and Futuremark's side, then the deal is closed after an email exchange between the parties, a phone call or another visit to the customer. As stated by the interviewee, this arrangement is very light for Futuremark but it has worked very efficiently and well. The delivery of software is handled completely electronically, the only things moving physically are the agreements on paper between the parties. (Talala 5.3.2008)

Samsung has been a triggering customer for Futuremark for its South Korean operations. As said by the interviewee, Samsung was received as a customer before nothing was actually done in South Korea. (Talala 5.3.2008)

> *"If I am honest, Samsung was received before we had done nothing in South Korea. We created our first mobile product and they noticed, in one way or another, that 'this is what we need, let us contact Futuremark!' But right after that we got an such impulse that we examined the South Korean market in a more detailed way and realized that a lot of effort and resources should be put there and pay visits there and investigate the market even more."* (Talala 5.3.2008)

The first mobile product was created by Futuremark roughly four to five years ago and Samsung was one of the first customers for this product. When the mobile business was differentiated from PC business, Futuremark immediately saw, partly because of the impulse from Samsung, that the growth of mobile business is in Japan and South Korea, and all the available resources and effort was put to these countries. Therefore, South Korea came to be seen immediately as an important market when the mobile business was started on its own. (Talala 5.3.2008)

The story of Futuremark in South Korea has been helped by two important issues. First, the fact that this company has developed a 'de-facto' standard product for performance measurement, basically Futuremark being the world leader in performance measurement, has meant that it has not had to search for all the customers itself but some customers have also approached Futuremark, such as large South Korean Samsung. The value of getting Samsung as a customer lies not only in large purchases of Samsung itself but the purchases of performance measurement products from those companies that want to be suppliers to Samsung. Once Samsung informs its potential suppliers that it uses Futuremark's performance measurement products to assess which supplier gets the deal, this triggers the potential suppliers to purchase Futuremark's performance measurement products to make sure their offering gives a good account of itself when Samsung testes it. In effect, the sales in South Korea have partly worked through this type of 'snow-ball effect' – first from a huge customer to a number of smaller firms. Second, the state sponsored research institute, Electronics and Telecommunications Research Institute, ETRI from now on, has played an important role as a customer for Futuremark. Although not big in terms of financial profit, this cooperation has a lot of reference value for Futuremark. ETRI uses Futuremark's products to assess the future requirements of mobile devices from mobile games point of view. ETRI examines what is required from the mobile devices of the future so that they can run mobile games from a higher, more developed level. ETRI then shares the research findings with the South Korean mobile game sector and, indirectly, brings Futuremark's name to the awareness of the South Korean game industry. (Talala 5.3.2008)

The agent relationship of Futuremark is actually very interesting for two reasons. First, the agent has, for one reason or another, ended up assisting Finnish firms quite similar to Futuremark earlier, too. Actually he has worked for a small Finnish software company and he has even set up a South Korean office for that company at one time. Second, this agent was found in quite a creative and clever way – with the help of another small Finnish software company. This small company was later acquired by a large international firm but when it was independent, it was very active in South Korea. People from this small company and Futuremark worked on the same field and shared extensively ideas and thoughts, and this small Finnish company told Futuremark that it uses this agent in South Korea. Thereafter Futuremark contacted this person and asked if he was interested in cooperation, which led to the cooperative agreement. At that time, this person was working for another Finnish firm that was partly also acquired by an international company and partly run down. As a result, this person had extra time to devote to Futuremark's business in South Korea and he already knew a lot about Finnish mobile knowledge and working culture. According to the interviewee, there is a lot of 'shared community' type of thinking at least between the smaller Finnish firms, leading to sharing of information and experiences from abroad. (Talala 5.3.2008)

The cooperation between the agent and Futuremark has remained similar to how it actually started. Neither of the parties has neither had time nor priority to deepen the cooperation. The cooperation is quite a lot on a practical level, basically the interviewee telling the agent that he is coming to South Korea and listing the firms that should be contacted for the possible business negotiations. According to the interviewee, the cooperation is of an 'ad-hoc' type more or less, the agent receiving his commission for those contacts that actually lead to a new deal. From time to time the agent has expressed his interest in taking on the representation of Futuremark in other countries, as well, such as Taiwan, but so far he has been quite busy with his own software firm, leaving the representation to remain just on the South Korean market, still. The fact that the South Korean agent is very knowledgeable of the mobile business helps Futuremark a lot because usually it is sufficient to send a documentation of new solutions to keep him aware of new developments so that he can communicate those to South Korean customers. He only may have something to ask about new solutions through email or phone. On the other hand, he is very active in communicating the requirements and needs of potential customers to Futuremark, this communication usually taking place on a weekly basis. (Talala 5.3.2008)

Major problems in South Korea for Futuremark have been of two types. First, there has been a linguistical and a cultural barrier. The English skills of South Koreans are seen to be weak and the interviewee does not speak Korean, leading to misunderstandings from time to time. (Talala 5.3.2008)

> *"You only need to be strict in the language issues. You may agree on something in an appointment and even try to verify through email, for instance, that this was our common understanding, but still it may be that the South Korean counterparty has understood the issue wrong, even when the*

> *issues have been written on paper. So you just need to verify many times that this really was what we agreed on."* (Talala 5.3.2008)

The cultural barrier relates to how issues proceed after the agreement has been made. According to the interviewee, a Finn is used to trust that if somebody promises something, he actually does it. In South Korea, sometimes people speak and promise but nothing happens, as highlighted by the interviewee. This is not a South Korea-specific phenomenon but happens in many other parts of the world, as well, but it is different from Finnish culture. According to the interviewee, often the best way to get things done in South Korea is to be in face-to-face contact with South Koreans instead of trying to get things done from Finland. The interviewee says that when one is in South Korea with the customers and the sales agent, things proceed quite smoothly, but when one goes back to Finland, it may be that there is a stopping in the smooth flow of the issues. (Talala 5.3.2008)

Second, a major problem in the South Korean business culture is the neglect of paying invoices on time. This is totally different from Finnish business culture, where invoices are mostly paid on time duly. (Talala 5.3.2008)

> *" (...) if an agreement is written and we deliver the products and send an invoice, the basic starting point is that nothing will be paid!"* (Talala 5.3.2008)

Futuremark needs to do rigorous follow-ups on invoices and ask the customers to pay their invoices and usually even twist arms a bit to get the South Korean customers to pay. This problem applies to all kinds of South Korean customers of Futuremark, small and large. Futuremark is a global firm but it has only encountered this problem in South Korea, not even in other countries of Asia, meaning that this is a very South Korea-specific problem. As a solution to this problem, Futuremark does not deliver anything to South Korean customers before the product has been invoiced and the invoice is actually paid by the South Korean customer. The South Korean customers have accepted this change with a good grace and this arrangement in payments works fine. (Talala 5.3.2008)

5.6 Company B

Company B is the world's leading designer and manufacturer of silicon capacitive acceleration and pressure sensors (Company B). Company B is active in the field of electronics, having its core competencies in measurement techniques, measurement equipment and sensors. Mostly Company B's solutions are concentrated on measuring motion and pressure. (Interviewee Two 6.3.2008) Company B's sensor design and production is based on a path breaking technology, the name of which is not stated here due to confidentiality reasons. Company B is actually the sole manufacturer of this unique technology that was originally developed in the 1970s (Company B; Interviewee Two 6.3.2008; Company B Business Review 2007). Much of the success of Company B can be attributed to this own unique technology (Company B). Company B offers sensors for the measurement of acceleration, motion, inclination, shock, vibration, angular rate and pressure (Company B Business Review 2007; Company B). The application areas of these sensors range from the automotive industry to a wide range of other industries as well. Applications in the automotive industry include Electronic Stability Control (ESC) and Antilock Braking Systems (ABS) as well as car alarm and navigation system applications. (Company B) Company B is the leading manufacturer and supplier of a certain type of acceleration sensors for the automotive industry (Company B Business Review 2007). Other industries where Company B's sensor products are utilized include sports and wellness, medical and instruments and terminal applications. The measuring needs are gaining importance in these industries. Applications in these industries include, for instance, activity monitoring of adaptive cardiac pacemakers, altimeter for navigation, activity monitoring for training effect and calorie consumption, and inclination measurement for electronic levels and laser instruments. (Company B; Company B Business Review 2007)

Company B has divided its operations into two business units. (Company B Business Review 2007). The business unit serving automotive industry creates 85% of Company B's turnover and is, thus, by far the more important business unit for the firm. However, the business unit that offers sensing solutions to other industries is becoming more important all the time, since new application areas for sensors are emerging all the time.

(Company B; Interviewee Two 6.3.2008) In Korea, Company B is active with both of its business units, the 'automotive side' being where it all started but the other business unit increasing its relative importance all along (Interviewee Two 6.3.2008).

Interviewee Two was an executive in charge of Company B's strategy. He has actively participated in the development of Company B's Korean business right from the beginning. Company B was owned by an American parent firm from 1995 to 2002, Company B, in effect, being a subsidiary of this American company. At that time, the interviewee got to know the manager of Korean operations of this parent firm. This manager and interviewee then examined whether there would be demand in the Korean market for Company B's sensors. According to the interviewee, it was roughly 10 years ago that this screening process started. After some initial examinations, it was discovered that the Korean automotive industry is developing quickly. Korean car manufacturers equip their cars well, in the same way as Japanese car manufacturers, so that the standard equipment usually contains almost everything that is available for a car. This is very different from the approach of, for instance, German car manufacturers who sell different equipment and features to a car as options to be selected by a customer. The fact that Korean cars are so well equipped already as 'standard cars' means that a lot of assisting systems, to which Company B provides sensors, are sold to Korean car manufacturers, which makes Korea quite an important market for Company B. After the realization of the potential in the Korean market, the first projects started in roughly 1999 or 2000. It took roughly three years for Company B that it could start producing significant turnover in Korea. Step by step, Company B started to get into projects and those projects running. It required time to get designs accepted by Korean car manufacturers but as time passed, those cars that had such systems to which Company B provided sensors started to be mass produced, Company B's sensors enjoying a 'standard status' in the systems installed to these cars. From 2003 onwards Company B started producing turnover in Korea because of getting its sensors to the mass production of Korean cars. For Company B in Korea, it all started from braking systems such as ABS and moved on to suspension systems. The company could have participated in the boom of airbag systems 10 years ago as its first endeavor in Korea but the company did not have a sensor for airbag systems at that time. After serving braking system and suspension system developers, Company B has also started to provide sensors to Electronic Stability Programs (ESP) that are aimed at correcting the driving mistakes. Besides the automotive industry, the electronics industry has grown to be an important customer for Company B in Korea. The role of Korea in the global electronics industry is growing continuously and the Korean electronics industry has put itself to a strong global position on those areas of electronics outside automotive industry where Company B wants to enlarge its business to. (Interviewee Two 6.3.2008)

By far, the most important market for Company B is Germany today. The reason for this is obvious: the world's largest suppliers of electronic control systems for automotive industry are in Germany. Out of the 85% of Company B's turnover that comes from the automotive industry, a major share comes from Germany, because the sensors are mostly delivered directly to Germany or to a destination country indicated by a German company. However, the Korean market is very important for Company B because the penetration rate of those systems to which Company B provides sensors is higher in Korea than in many other markets. In addition, roughly 10% of the world's car production takes place in Korea, which is significant. According to the interviewee, the Korean automotive industry has developed remarkably during the last 15 years. Initially, the Korean car manufacturers just put together parts purchased from around the world without their own design but nowadays they have engaged in design of the cars and are competing with the Western car designs almost on par. (Interviewee Two 6.3.2008)

The turnover of the company was over 70 million Euros in 2007 out of which less than five percent comes from Korea. 99% of Company B's production is exported. Company B employs roughly 700 persons, from which almost 500 are working in Finland and almost 200 in Mexico, with the rest in subsidiaries in Japan, China, Germany and the United States. In addition to the headquarters and its production in Finland, Company B has a production site in Mexico. (Company B; Interviewee Two 6.3.2008) In Korea, there is no personnel, since the Korean market is served through local sales agents (Interviewee Two 6.3.2008).

At the time of the interview, Company B was running its business in Korea through two different sales agents, both located in the capital city Seoul. Another serves the automotive industry and the other serves other industries. In effect, the sales agent responsibilities in Korea are divided according to the strategic business unit division of the company. (Interviewee Two 6.3.2008)

As discussed above, the automotive industry was where it all started for Company B in Korea. Having started its Korean operations as a subsidiary of an American firm, Company B became 'independent' in 2002 when a Scandinavian investment company acquired Company B to its portfolio. This investment company basically bought Company B out of the American company. As a result, Company B could start its Korean operations by its own. The connections were dissolved to the previous parent firm's subsidiary in Korea. However, the manager of this subsidiary organized issues very much in favor of Company B: a company, engaged in automotive component business different from that of the American parent company, was established in Korea and Company B orchestrated its 'own man', a Korean person, to that company to sell Company B's products in Korea. Company B officially transferred the representation agreement from the subsidiary of the previous parent firm to the new company, and there was a dedicated person educated to sell Company B's products in Korea and his salaries were paid directly by Company B. Company B, obviously, did not own this newly-formed company but had this above-mentioned person situated in the small new company. Still today, this agent is the main channel of Company B to the automotive industry. In effect, this sales agent is literally an agent because all the agreements are written between Company B and the Korean customer and the financial and merchandise flows take place directly between Company B and the Korean customer. (Interviewee Two 6.3.2008)

Another representative was selected in 2006 and it had operated one and a half years at the time of the interview. This representative is geared towards consumer goods business and instrumentation. Company B utilized the services of Finpro, an advisory firm providing internationalization assistance to Finnish firms, to search for this representative. Company B was looking for a representative that operates outside of automotive industry. This representative is purely independent, Korean reseller of electronic components. This partnership has slowly produced results – as stated by the interviewee, 'it takes time to get designs in." The consumer electronics market is seen to be a very competed one and Company B is not very strong in this market in Korea yet. (Interviewee Two 6.3.2008)

Neither of the sales agents is exclusively serving Company B in Korea. The sales agent in the automotive industry is enlarging its business closer to Company B's products, one clear sign of this being fixing itself up with an American-French principal and trying to increase the volume in the automotive industry to the same customers that Company B's products are directed to through this arrangement. In addition, this agent is also trying to approach firms outside of automotive industry. Another sales agent, on the other hand, has for a long time served a number of electronics producers, both American and European, whose products this agent has sold to mobile phones, navigators and many other handheld electronic devices that are manufactured in Korea extensively. This agent was selected because it has a strong technical expertise, it has a lot of engineering knowledge to design products to the customer and create prototypes, and it has sound abilities to handle the commercial business when the product to which Company B provides a sensor goes to production. Neither of the sales agent representation agreements is on an exclusive basis, meaning that Company B has not written exclusive sales agreements in Korea but the company has a free hand in the selection of more intermediaries, if needed. According to the interviewee, it is quite easy to enter into a non-exclusive agreement with a Korean partner firm because Korean firms are quick to change principals if the business is not developing as expected. In other words, the loyalty of the agent towards the principal is not very strong in Korea. (Interviewee Two 6.3.2008)

Korea is the only country where Company B has a representative in the automotive industry. In all other markets Company B does the selling function itself with its own personnel. This arrangement has been in place in Korea right from the beginning but Company B has been contemplating whether it should replace the intermediary with its own personnel as many competitors have done. At the time of the interview, the company did not see it worthwhile replacing the intermediary. The networking is in the focal point here. The network of an agent is seen to be of crucial importance to Company B. (Interviewee Two 6.3.2008)

> *"I would emphasize the network, you need to have certain relationships and proceed with them. The building of this network and finding right persons is essential so that you can build the first contacts to some firms – to be able to do this, you should either have someone recommending you or another way of reaching this network (...) if you have relationship activity, it brings you quickly quite far compared to if you start sending brochures and calling to completely strangers (...) Building up this without a Korean agent would be impossible."* (Interviewee Two 6.3.2008)

However, at the same time, Company B sees that an agent can use its network primarily to its own benefit and only uses this network secondarily to the principal's benefit. This secondary benefit for Company B is that it gets more easily inside the Korean market through the network of the agent. The agent has another interest, though, namely to find another principal through its network if Company B's product is not competitive temporarily. In the case that the agent changes the principal, Company B would naturally be in a stronger position if it had developed its own network of relationships in Korea. (Interviewee Two 6.3.2008)

A major challenge for Company B in Korea has been the language issues. The interviewee sees that the language barriers are quite big:

> *"One of the biggest problems of the Korean national economy is the lack of people able to speak English. You can see it in our business, too, for example in the automotive industry, in the system supplier companies, there are a few persons that have been abroad during their studies who of course speak good English but those who have not been abroad have not been able to develop their English skills. It is clearly on a lower level than in Finland, for instance. And obviously it is a matter of culture – maybe they do not want to speak if they feel they cannot. All in all, it is very hard to get English text out from them [Koreans]. They rather speak the local language and they would like*

someone to translate the text rather than to speak themselves (...) It is a drag clearly." (Interviewee Two 6.3.2008)

In solving this language problem, the sales agents are of crucial importance to Company B. The persons at the sales agents are reported to speak rather good English. Company B has not had any other options but to trust the sales agents' language and translation skills. (Interviewee Two 6.3.2008)

Another challenge has been the propensity of Koreans to copy foreign products. According to the interviewee, the Koreans try to protect their own industries as much as they can and there is a will to start producing locally some advanced technologies that are imported. To receive the maximum utility locally, one Korean university has suggested that the silicon technology and sensor technology are worth of investments and efforts and this suggestion is implemented in some form at Samsung with partly funding from the state of Korea. The interviewee sees that the copying of products is wide in Korea, regarding mostly products that can be produced with small investments and efforts. The technology of Company B is very unique and requires large investments in production technology, which has prevented Koreans from copying. However, the fear of copying is always present for Company B in Korea:

> *"All the time you need to be on the alert for sharing of information so that it will not be misused. Either so that it is forwarded to competitors or so that it is forwarded to players that can copy the products. There you need to be very careful. This kind of 'confidentiality' mark, its value is not that high as it is in Finnish culture and business life, for instance. If someone has stamped such a mark it may be that it will not be appreciated. Someone may even try to remove such a stamp from documents and forward the information or even forward as such."* (Interviewee Two 6.3.2008)

As a result of the risk of copying and the attitude of Koreans towards confidential information, Company B has limited the sharing of information to only that information that the Korean customer needs and not further. The company avoids sharing of information that could have confidential value in Korea. (Interviewee Two 6.3.2008)

5.7 Company C

Company C is a global technology company, serving the pulp and paper industry, mining and construction industry, energy industry, automation industry, and recycling industry. Company C was formed in a large merger in 1999. However, the history of different parts of the present Company C dates back to the 1750s, even, Company C being a very traditional Finnish engineering works company, indeed. The company employs over 28,000 persons in more than 50 countries. (Company C) At the time of the interview, Company C had divided its operations in three different business units (Company C 2007; Company C; Interviewee Three 26.2.2008). After the interview, though, the corporate structure of Company C was changed. Today, the business units are termed segments or business lines. There are still three business lines, though. (Company C) However, the content and functions of these business lines are still mostly the same as in the previous business unit division. For the sake of simplicity and consistency with the interview, the former business unit division is followed in this study.

Company C's Division A provides paper, pulp, tissue, board and panel board machines and equipment for the paper and pulp industry. These solutions are complemented with process automation and power generation technologies. (Company C 2007; Company C Division A) Company C Division B offers rock and minerals processing systems and equipment and metal recycling systems to customers in quarrying, aggregates production, construction, civil engineering, mining and minerals processing. Company C Division C provides process industry analyzers and sensors, automation and information management application networks and systems to power generation, oil and gas, metals recycling and pulp and paper industries. (Company C 2007; Company C) All business units offer maintenance and aftermarket services (Company C 2007).

In 2007, Company C's total net sales were over 6 billion Euros, Division A having roughly a 46% share, Division B a 42% share, and Division C a 12 % share, respectively (Company C 2007; Company C). Company C is truly a global company, having production on all continents. The main market areas are Europe and North

America, which account for over half of net sales. (Company C) However, Asia and South America are becoming increasingly important, Asia-Pacific region commanding roughly 25% of net sales and South and Central America 15% (Company C 2007; Company C).

Interviewee Three was a highly-ranked Vice President in the company. This person was probably the most valid person to be interviewed when considering the scope of this study, even though he admitted not having exact information on certain aspects of Company C's operations in Korea. The interviewee indicated that he knows generally a lot about the operations of Company C everywhere in the world but his knowledge on particulars in Korea might be limited because 'Korea is operating mostly on its own', the last Finnish person having returned six to seven years ago. Therefore, in some issues the information received is second-hand information but, at the same time, still very useful for the purposes of this study. (Interviewee Three 26.2.2008)

In principal, all three business units of Company C are active in Korea, the operations of Division A being the most extensive. However, the business of Division B is relatively small in Korea, naturally since the mining activity is a very small-scale operation in Korea – Korea is not a mining country. As a result, Division B is not physically established in Korea. Divisions A and B are physically located in the same address in Seoul but they are administratively differentiated from each other. Company C everywhere and always differentiates the business units from each other administratively, even though sometimes they are actually located in the same place physically. (Interviewee Three 26.2.2008) In this location, a sales office, from which both business units are served in Korea, was established in 1995 and it employs 4 persons. In addition, Division A established a service center in Daejeon in 2004. This service center employs 8 persons. Daejeon service center provides a wide scope of services for the Korean pulp and paper industry, services ranging from providing spare parts, to rolls services and to maintenance services. In addition, this service center acts as an extensive back-up for Division A's deliveries in Korea. (Company C 2007; Interviewee Three 26.2.2008)

Today, Korea is only a 'mid-important' market for Company C. Company C reports country-specific turnover figures on the 10 most important markets and Korea does not belong to those. However, a change has taken place since there was a time that Korea was an important paper machine market for Company C. A major influencer for the development of sales was the Asian Financial Crisis in 1998 and 1999. Before the Asian Financial Crisis, Korea was shortly a very important paper machine market, possibly even the biggest for one or two years. During this time, a number of Korean firms ordered paper machines simultaneously, forming a significant peak in demand. After the crisis, new paper machines have not been ordered, changing the focus of Company C in Korea from new investments of customers to modernization and service business. From the very low sales volumes during the Asian Financial Crisis, the sales have recovered to a decent level. Yet, Company C is far away from the pre-crisis peak sales volumes mostly because new paper machines have not been sold in Korea. Paper production is quite significant in Korea, although there are almost no raw materials, namely wood and pulp, in the country. Finland, a large producer, has a capacity of roughly 13 million tons, whereas Korea, regarded usually as a minor producer, has a capacity of over 10 million tons. What makes Korea an interesting market for paper production is that the population is large and that the Korean culture is quite advanced, meaning that masses of books, papers and advertising material are consumed in the country. In addition, there is a strong export industry requiring packaging materials. (Interviewee Three 26.2.2008)

Before the sales office was established in Seoul in 1995, the Korean market was served through sales agents. Originally, Company C had entered the Korean market by following demand when the Korean paper producers started to invest in production. According to the interviewee, maintaining a sales agent network is sufficient for a long time in this kind of business where customers' investments are large and require years of decision making before the actual contract is signed. The purchase processes of customers are long and they have many phases and as long as customers are just considering whether to purchase, an agent can do the job for Company C. When the sales prospects start finally realizing, then establishing a local presence becomes a matter of consideration. (Interviewee Three 26.2.2008)

Company C enjoys a very strong market position in Korea. Neither paper nor pulp machines have ever been manufactured in Korea, which clearly helps the business of Company C. The country entered the paper business quite late – the first pulp mill in Korea, Donghae Pulp, was established in roughly 1976 and the establishment of this pulp mill led to paper machine investments by the customers of Company C. (Interviewee Three 26.2.2008)

When the paper machine business really started to grow as a result of sales prospects transforming to actual sales, Company C saw that it should be present physically in Korea to be able to handle the business better. Having perceived the use of sales agents to be insufficient, an own unit, a sales office, was established as a greenfield investment. Company C, following the company policy to own all units completely wherever the local law allows this, owns 100% of the Korean unit. (Interviewee Three 26.2.2008)

Company C has staffed its Korean operations completely with local employees, the last Finnish person having left Korea six to seven years ago as discussed above. All the sales and other activities in Korea take place between the local Korean staff and customers. Company C strives to appoint a local management to its foreign operations everywhere, not just in Korea, for two important reasons. The first, and most obvious, reason is that a Finnish expatriate is very expensive compared to a local employee, especially if a family is accompanying the expatriate. Also, Company C does not see that a foreign expatriate can bring a lot of additional value to leading the local operations, especially in a case such as Korea where the local language forms a major cultural barrier. It would take enormous efforts from an expatriate-to-be to study the local language and utilize it. The second, and perhaps more important, reason is the relationship network of the local employees. This is seen to be of extreme importance in Korea:

> *"It is truly important to use local people because it is a society that is not very transparent. These large chaebols do a lot of business among themselves. And then there is this relationship network issue and so forth. There are a number of such issues that are hard for an outsider to learn and 'get in' (...) Generally*

speaking, I see that using local partners or local employees, is important." (Interviewee Three 26.2.2008)

The business of Company C is carried out quite in a simple way in Korea. In a paper machine project, for example, it is typical that core components come from the factories of Company C but standard steel structures are sourced locally. Company C has not engaged in technology partnerships or other forms of cooperation with Korean firms. (Interviewee Three 26.2.2008)

When operating in Korea, the interviewee sees only one minor problem that Company C has encountered. That is the language barrier. However, he at the same time admits that there are a number of persons in the management of Korean companies that have studied in the Western countries, mostly in the United States, that speak good English. But he sees also that for a part of the Koreans English still is a challenge, English being relatively hard for Koreans. However, the interviewee sees that Company C has actually never suffered from this problem, all the Korean employees of Company C speaking good English. The interviewee sees that one can find well-educated, language-skilled employees in Korea nowadays, which solves the language barrier problem for Company C. All in all, Company C has been very pleased with the local management. (Interviewee Three 26.2.2008)

For the future, Company C is quite careful with its expectations on the development of the Korean market. Company C sees that the Korean market is quite saturated and that the growth mainly comes from other countries. However, the company is actively monitoring the internationalization efforts of its Korean customers and seeks to follow them outside of Korea. According to the interviewee, good reference deliveries in Korea greatly help in getting in on foreign investments of Korean customers. (Interviewee Three 26.2.2008)

5.8 Fibox

Fibox, a privately-owned Finnish company, is one of the largest enclosure manufacturers in the world. The company is the market leader in thermoplastic enclosures that are used for protecting electrical and electronic components operating in hostile environments. (Fibox) Fibox offers enclosing solutions to electric and electronic devices – typically the enclosures of Fibox go to industrial devices to protect their control electronics (Niemi 18.2.2008). Fibox has subsidiaries in 10 countries, production units in four countries, and a number of local distributors on each continent (Fibox). The production units are located in Finland, Germany, Korea, and China. (Fibox; Niemi 18.2.2008) The main market areas for the firm are the Western Europe, the United States of America, Korea, and China. The turnover of Fibox is roughly 60 million Euros and the personnel count is roughly 500. The interviewee from Fibox Oy was Mr. Tapani Niemi, the main owner of the company who has actively participated in the development of the Korean operations of Fibox. (Niemi 18.2.2008) Niemi was the main architect of the management buy-out deal where the active management acquired the enclosure business of Fiskars to form Fibox in 1991. Fiskars, established in 1649, is one of the oldest industrial firms in Finland. Fiskars had started its enclosure business in the 1960s. (Fibox) The information that was received from Niemi was complemented with two distinct interviews with Interviewee Five on 23rd August, 2006 and 16th December, 2004. Interviewee Five was a high-ranked director of Fibox in Korea.

Today, the Korean operations of Fibox consist of a production plant in Incheon, a little bit west of the capital city Seoul, and a supporting sales office in Busan, the harbor city in the southern part country. Korea is very essential as a market for Fibox – Korea is the Asian base of the firm. All the operations in Asia are built on the foundations of the company's operations in Korea. In addition to the local Korean market, Fibox serves Japanese, Australian, Taiwanese, and Singaporean markets from Korea, for instance. Fibox employs roughly 40-50 people in its Korean operations. Fibox has a company policy not to reveal country-specific turnover figures. Fibox is a well-established brand in Korea, enjoying actually a market leader status. (Niemi 18.2.2008)

Initially, the thrust for the Korean operations of the company was a trade fair contact in Germany in the beginning of the 1990s. A company that later became the importer for the firm's products in Korea approached Fibox at this trade fair indicating its willingness to represent Fibox in Korea. According to the interviewee, Fibox has always had a strong brand value in its offerings, which naturally attracted the Korean importer to make its move. However, Fibox was looking for a distributor to Korea at that time on purpose. Therefore, the start of the company's operations in Korea was not a random move dictated by an approach from a potential importer but also a part of a deliberate strategy. At that time, Fibox had sold to the Japanese market for a long time and the company was ready to exploit market opportunities in other Asian countries, as well. (Niemi 18.2.2008)

Right from the beginning and even today, Fibox has had many partners in its sales in Korea. These partners are electric wholesalers and special distributors, the total number of these partners equaling roughly 20. The cooperation with these partners started in the beginning of the 1990s and the number of these partners has increased over time. In fact, it was the Korean importer of Fibox that organized the relationships to these partners. Interestingly, a major part of the business in the industrial goods market in Korea takes place through fixed 'tool markets' that always should be attended. These tool markets can be found in different cities in Korea – there are three tool markets in Seoul, for example. For Fibox, the electrical supplies tool markets are very important in Korea. (Niemi 18.2.2008)

This importer-led operational form was in place for three to four years. This had worked quite well but Fibox felt the lack of transparency between the importer and itself. More specifically, Fibox 'could not see the market' and it was not sure whether everything was done correctly. A major change factor was a request and recommendation by the importer to engage in own production in Korea because of copying of the company's products in the country. This copying issue is well described with the following comment:

> *"In Korea, if business starts to look interesting, copiers come around. And then we heard that people are beginning to copy our products there. If we had*

not entered the country with our own production, our market would have started to decline. At that time, the local production had a different significance as now (...) Korea was a very inward-oriented state at that time." (Niemi 18.2.2008)

The importer said Fibox that it would be wise to engage in own production in Korea. However, this importer was looking for a joint venture, a common operational form between a local and a foreign firm in Korea at that time. Fibox, though, rejected this approach because the role that was offered in this arrangement was not suitable for the company. According to the interviewee, the management of the JV would have been next to impossible, leading Fibox 'to lose the case anyway' and the Korean firm to be able to control everything in the new company. The interviewee sees that a foreign firm needs to be very careful when negotiating a possible JV arrangement with a Korean firm:

"Here you need to be very careful, this kind of JV case, suddenly you realize that you are about to receive a role where you are to lose!" (Niemi 18.2.2008)

Many types of JV arrangements were planned and tested but none of them ever materialized. According to the interviewee, "it was luck we did not do it!" As a result, Fibox decided to establish a production plant itself as a greenfield investment in 1995 in Incheon, west of the capital city Seoul. In fact, Fibox was seemingly the first foreign firm to establish a 100% own production plant in Korea. The importer, naturally disappointed at the decision and also low in significance after the establishment of the local production, was removed from the sales channel, Fibox basically taking on the role of the importer and handling the relationships to the sales partners itself. The cooperation with these sales partners has worked out extremely well, since Fibox enjoys the status of a market leader in Korea. (Niemi 18.2.2008)

When the decision to engage in own production was made, there were also other motivators for this than the ones described above. At that time, roughly 1993 or 1994, Fibox was contemplating where to establish its Asian base. The company wanted to establish a production unit in East Asia. China was already then seen as a very lucrative option. However, the infrastructure in China was seen to be underdeveloped at that time. Japan was another option under consideration but the Japanese market was way more developed, that is, closer to saturation than the Korean market that was just emerging. Fibox saw that it had a lot of good business starting in Korea, which made the company to establish its Asian base there. In addition, the central location of Korea affected the decision, since it is a short way from Korea to China, Japan, and Taiwan. Also, Korea was itself a big industrialized country already then. Just like Japan, Korea has traditionally been a large producer of machines, equipment and industrial automation, being of extreme importance to Fibox as the company sells its products to machine and equipment manufacturers. (Niemi 18.2.2008)

The Korean subsidiary of Fibox, consisting of the production plant in Incheon and supporting sales office in Busan, is engaged in production, sales, and research and development activities. (Niemi 18.2.2008) The enclosures produced in the Korean production plant are labeled with the company's own trademark (Interviewee Five 16.12.2004). Major sales activities are also handled in Incheon besides pure production. The company has divided the Korean market into three distinct market areas – the northern market covering Incheon and the capital city Seoul region, the central market, and the southern market with a major harbor city Busan. The office in Incheon is responsible for sales to northern and central markets, whereas the supporting sales office in Busan has assumed the responsibility of sales to the southern region. The Korean unit has been led by a Finnish expatriate that has lived in Korea for a long time and can speak fluent Korean, which helps him a great deal in his work. (Niemi 18.2.2008)

Later, Fibox will move its operations in Incheon to Songdo, a high-tech region close by. This high-tech region, being a very ambitious undertaking and meant to be developed as the new international business hub in Northeast Asia, has been built on reclaimed land and it is connected to the Incheon international airport via a bridge. (Niemi 18.2.2008)

Originally, establishing a company in Korea was not easy for Fibox. For instance, buying land was extremely hard because a foreigner was not allowed to own land before the relaxation of the investment legislation in the country in 1998 as a result of the Asian Financial Crisis. (Niemi 18.2.2008)

> “*It is a lot harder than in Finland, for example. Not the investment, that is easy, but with all these authorities and bureaucracy, they [Koreans] say it is easy there, but it was very hard compared to Finland. And 1994 or 1995, it was really, really hard!*” (Niemi 18.2.2008)

Thereafter, according to the interviewee, all this bureaucracy has become a lot easier in Korea. He says that today Korea has manners and infrastructure to handle these kinds of investments and foreign firms. When the investment legislation was relaxed in 1998, Fibox received a status of “foreign investment company”, which granted it the same rights that the Korean firms were enjoying. (Niemi 18.2.2008) This status included many benefits for Fibox. The use of foreign personnel became easier, Fibox was allowed to buy buildings and land, and the repatriation of profits became easier. The state of Korea also encouraged foreign investors – after Nokia, Fibox was the second Finnish firm to receive the export award from the state of Korea. (Interviewee Five 23.8.2006)

According to the interviewee, knowledge of the Korean language is a requisite if successful operations are sought in the country. It has been very hard for Fibox to find personnel that are able to speak English. The company employs highly-educated Korean persons with university backgrounds, which greatly alleviates the language problem. (Niemi 18.2.2008)

To get inside the Korean market, one should obtain a Korean organization that is able to create the necessary contacts and relationships in the market. For a foreigner, it is next to impossible to get such an understanding of the market that a Korean person can have. (Niemi 18.2.2008)

Anticipating the future, the interviewee sees that the business of Fibox will develop along with the market in the country. The company plans to increase the product offerings to the country slightly. However, an interesting point is raised up by the interviewee, namely the possibilities coming from North Korea:

> *“But what can really change a lot, if it breaks through, is that North Korea is integrating more and more to South Korea. Then the ‘low-cost’ function that*

China has had, vanishes. Because North Korea is even cheaper and, moreover, South-Korean firms know Korean way better than Chinese. And it is so close [geographically]. It can change it, it can change the structure very quickly. Then, Korea would be in a situation where it has the 'high-tech' knowledge item and the 'low-cost' item. This would be a unique situation in the world." (Niemi 18.2.2008)

5.9 Company D

Company D is a global leader in the development, manufacture and marketing of high-performance fiber-based materials. Nonwovens and specialty papers of the firm are used in a large variety of everyday products, such as filters, wipes, flooring, labels, and tapes. The unique fiber expertise and innovative approach has yielded Company D a strong market position in several business areas in which it operates. The company employs 6,500 persons and operates sales offices and production facilities in 20 countries on six continents. In 2007, the net sales of the company were 1.8 billion Euros. The main geographic markets of the company, in terms of net sales, are Europe, North America, Asia Pacific, and South America. Europe is the biggest market area with a 62 % share of the net sales, followed by North America, with 23 %. Asia Pacific commanded seven percent and South America six percent of the net sales, the rest being distributed to the rest of the world. Company D has divided its operations in two segments – Fiber Composites and Specialty Papers. These two segments comprise six business areas – Filtration, Advanced Nonwovens, Home & Personal Nonwovens, Glass Nonwovens, Release & Label Papers, and Technical Papers. (Company D) Company D is a public company listed on the Nasdaq OMX Helsinki Stock Exchange and it is mainly owned by the Company D family (Company D; Korhonen 2006: 100).

The interviewee from Company D was one Senior Vice President and a member of the board of the Korean subsidiary at one time. (Interviewee Six 4.2.2008) The information received in this interview is complemented with information from Korhonen (2006: 100-109).

Company D established a production plant, a paper factory, as a joint venture with a Korean partner in 1987 (Interviewee Six 4.2.2008). The joint venture was named Company D Korea and it was the first production investment of Company D in Asia. At that time, Company D was present in Asia only through a sales office in Singapore and agents in Japan and South Korea. Asia was seen to be an important market, but understanding of the region was limited and in the case of South Korea, non-existent. During the first visits of the company's representatives to South Korea the country was found to be attractive with its rapid economic growth. Especially, the rapid growth of the Korean automotive industry was seen to create strong sales potential for the company. (Korhonen 2006: 103)

This paper factory produces filter materials for the automotive industry, namely oil, fuel, and air filters for car engines and other engines (Interviewee Six 4.2.2008). To be exact, the customers of Company D Korea are producers of filters for automobiles, trucks and heavy-duty equipment, as well as for specialty filter markets (Korhonen 2006: 103). In addition, there is a research and development department at the factory, producing valuable results for the company. At the time this Korean production plant was established, the main location for the filter materials of Company D was Italy. Therefore, Italians were responsible for the start of the Korean project. (Interviewee Six 4.2.2008)

Initially, the main thrust for the start of Company D's Korean operations was an approach by a Korean businessman who saw that the products of Company D should be produced in Korea, although Company D had also recognized the market potential in Korea at that time as discussed above (Interviewee Six 4.2.2008; Korhonen 2006: 103) Already then, Company D was the leading producer of filter materials for the automotive industry in Europe. In addition, the Korean car industry was starting to grow to the power that it enjoys today. (Interviewee Six 4.2.2008) In addition to Company D, the major competitors of the firm had plans to establish operations in Korea, but importantly, it was seen that there was room for only one engine filter paper producer.

Therefore, Company D needed to hurry and try to find a trustable Korean partner who could manage the local business environment. (Korhonen 2006: 103) After evaluating several possible partners, this Korean businessman then contacted Company D and asked whether Company D was interested in the cooperation. (Interviewee Six 4.2.2008; Korhonen 2006: 103) Having responded in the affirmative, Company D provided the know-how and mostly the financial resources, too, for the new JV. (Interviewee Six 4.2.2008) Company D representative concluded the nature of the investment as follows:

> *"The Korean partner had the market knowledge and relations, while we had the know-how and technology"* (Korhonen 2006: 103)

A joint venture was established with Korean On Yang Pulp Company, later known as Shin Ho Paper. This partner firm was a highly diversified *chaebol* that had never had a foreign partner before. Interestingly, Company D was interested in Shin Ho Paper also because it was a family-run company like Company D. (Korhonen 2006: 103) The joint venture bought a former box-board factory on an industrial site just outside of Daegu, the fourth biggest city in Korea in the southeastern part of the country (Korhonen 2006: 103; Interviewee Six 4.2.2008). This former box-board factory was transformed into a specialized paper mill (Korhonen 2006: 103). The Korean partner and its customer relationships strongly influenced on the location and acquisition decision that was made. (Interviewee Six 4.2.2008)

The first years of the South Korean unit from 1988 to 1992 were difficult. Marketing and sales remained below expectations, the operations were making losses, and the relationship with the local partner was problematic. As the situation got worse, Company D management even discussed the closure of the JV. However, the engine filter paper market in Korea and Southeast Asia was growing faster than any other market, creating a potential for Company D Korea. In addition, a new global management structure was being implemented at Company D at that time and it was seen that this might be able to solve the problems in the Korean unit. (Korhonen 2006: 103) After a couple of years from the start of the JV, Company D decided to buy the Korean party to the JV out, and continued the operation on its own (Interviewee Six

4.2.2008). In addition, in 1992, Company D decided to relocate its regional sales office in Singapore to Korea because the Singaporean sales office had not been able to penetrate Asian markets quickly enough (Korhonen 2006: 104). This sales office is located in Seoul and it sells all the products of Company D. Nowadays, Company D is operating a sales office in all relevant Asian countries. (Interviewee Six 4.2.2008)

The production unit in Daegu serves mainly the Asian market. A major share, 80 %, of the production is exported and the remaining 20 % is sold locally to Korean customers. China is the biggest export destination from this factory, other main export destinations being Indonesia, Thailand, Pakistan, Malaysia, India, Japan, and Taiwan. A couple of years ago, Company D was struggling with the capacity of the Korean production plant – the production capacity of filter materials was to be increased in Asia. (Interviewee Six 4.2.2008) As a result, Company D added another paper machine to the Korean production plant in 2004 to support the growing customer demand in the Asian region (Interviewee Six 4.2.2008; Korhonen 2006: 107). China was the main export market of the Korean plant already then and, therefore, China was seen to be an option for the location of the new machine, as well. However, according to the interviewee, a decision was made to locate the new machine to Korea for a couple of strong reasons. First, there was ample space on the site of the existing production plant for another machine. Second, according to the interviewee, it is always more efficient the more there are machines on the same plant. Third, Company D had already learnt significantly about operating in Korea, which further affected the decision making in favor of locating the paper machine to Korea. (Interviewee Six 4.2.2008)

The production plant in Korea employs roughly 100-120 people (Interviewee Six 4.2.2008). There are almost 20 employees in the sales office in Seoul (Korhonen 2006: 109). These operations are mainly staffed with local employees, with only two Europeans physically located in Korea. The factory manager is Italian and the factory controller is Finnish. There was a time, however, that there were more Europeans in Korea. This was in the beginning of the Korean operations roughly 20 years ago. At that time, there were a number of Europeans and Finns teaching the locals and creating the necessary know-how to be utilized. Then, it was many years that there were no people with European origin at all present. It was with the adding of the second paper machine to the production plant that these two Europeans, an Italian factory manager and a Finnish controller, were sent to Korea on a more permanent basis. (Interviewee Six 4.2.2008)

Company D is engaged in a wide business network in Korea. The company has a significant number of Korean customers and it purchases quite a lot from Korean subcontractors and cooperative partners. According to the interviewee, it is best to leave the actual business to the Koreans since they are best at handling it in their own country, naturally. However, no unit should be staffed with only Koreans but there needs to be persons with other nationalities, too. This is because a multicultural staff helps the interaction and enhances the materialization of different business objectives in the firm. In addition, through this kind of policy Company D can assure that certain corporate procedures are followed throughout different business units of the whole firm. (Interviewee Six 4.2.2008)

What comes to problems in Korea, the Korean hierarchic society has been sometimes in conflict with the Company D style of management when the company has been trying to fully integrate the Asian units into its global network. In this network, all units despite their location will have the same cumulative knowledge, which is shared with other units. The parent firm shares its values also with the Asian staff making no difference between the home country and host countries. Sometimes this, though, means that local practices are overrun, which creates potential for conflict. (Korhonen 2006: 109) In addition, the language skills of the Koreans have been a bit of a problem for Company D. It has been hard to recruit highly-educated people with adequate English skills. (Interviewee Six 4.2.2008)

Despite some problems in the beginning of the operations in Korea, Company D has achieved notable success in the country. The role of the production unit in Korea is more important than ever for Company D's Asian business. Since its establishment in 1987, it has been one of the most profitable units of Company D, and a figurehead of the company's internationalization. (Korhonen 2006: 109)

5.10 Cross-case analysis and discussion

The sample of the Finnish companies operating in Korea was very heterogeneous in this study. This heterogeneity applies to many aspects of firms' characteristics, such as age, turnover, number of personnel, and the branch, for example. The sample included both very old firms, such as Company C and Company D, and very young ones, such as Futuremark and Proventia. Some of the companies could probably also be characterized as Born Global companies or international new ventures because they have targeted international markets right from their inception. Oviatt and McDougall (1994: 49) define an international new venture as "a business organization that, from inception, seeks to derive significant competitive advantage from the use of resources and the sale of outputs in multiple countries". These international new ventures have also been termed "born globals" and "global start-ups" (Madsen & Servais 2004: 645). A Born Global label could be stamped on Proventia, Futuremark, and Company B. The size of the companies in the sample varied enormously both in terms of turnover and the number of personnel. There was Futuremark with a turnover of less than four million Euros and then there was Company C with over six billion Euros in turnover in 2007. There was Proventia with only 30 employees and there was, again, Company C with over 28,000 employees. The branches that the companies are active in varied also greatly - from load handling business to environmental technology, from log houses to programming, from playground equipment to engineering works firms, and finally from enclosure solutions via electronics to fiber-based materials. In case of two firms, Cargotec and Proventia, the Korean operations were examined from a viewpoint of a strategic business unit instead of the whole firm. In addition, the present internationalization stage of the firms varied also significantly. Some firms were quite far in their internationalization, serving their customers on a global basis through advanced international operations on many continents, whereas some firms were still on their way to further internationalization.

What comes to the interviewees selected for this study, they were almost all strongly involved in the development of their companies' operations in Korea right from the beginning. The interviewee from Company C admitted that the information he could provide was partly second-hand information because the Korean operations of the company are handled by the local Koreans nowadays. Otherwise, the interviewees in this study included different types of Vice Presidents, executives, different types of managers and directors, a main owner, and a President of the liaison office, all strongly involved in the Korean operations of their firms and therefore, able to respond extensively and precisely to the questions presented.

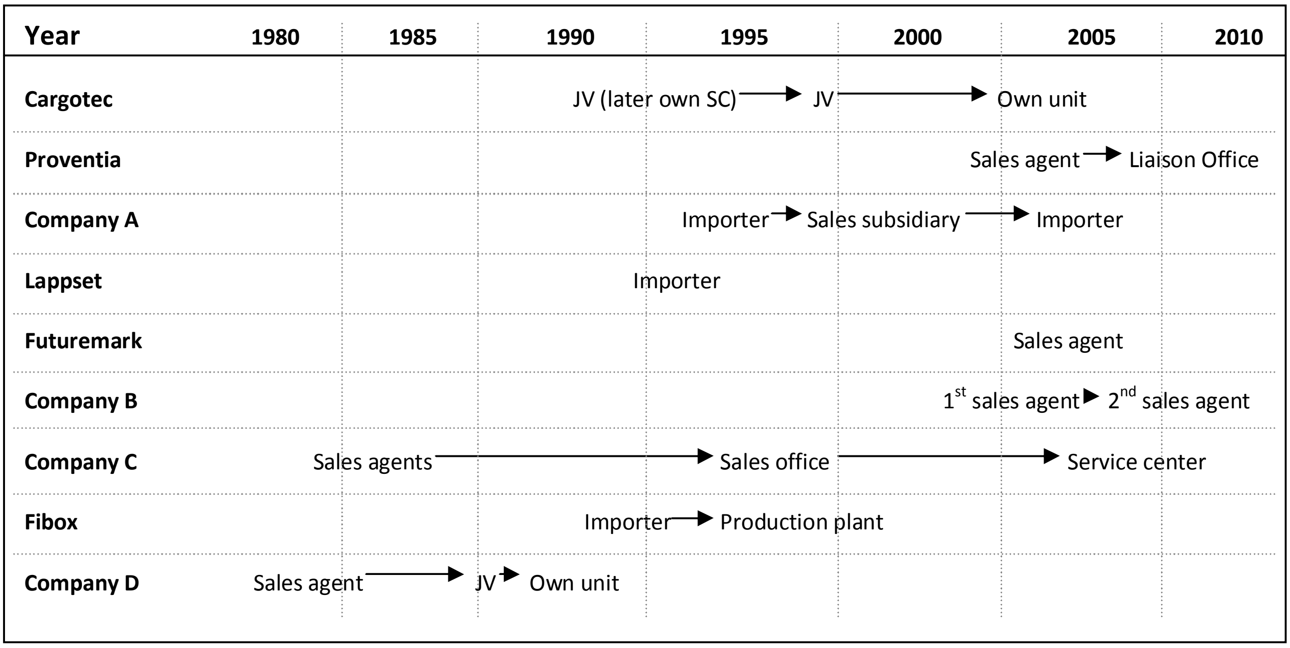
For the most of the studied firms, Korea was an important target market. For Proventia, Lappset, Futuremark, and Fibox, Korea was of utmost importance as a target market. For Cargotec, Company B and Company D, Korea can be seen as an important market. Korea has changed in significance as a market for Company A and Company C – for both companies, there was a time that Korea was more important but the country has lost its relative importance to other countries thereafter.

A vast majority of the studied firms entered Korea either in the 1990s or 2000s. Cargotec's Hiab was a pioneer since it entered Korea already in the 1970s. Company D was also quite an early-mover in Korea, having served the country through a sales agent before entering the country on a more committed basis in 1987 with a production plant.

The majority of the companies started their business in Korea intentionally, that is, as a part of their internationalization strategy. Cargotec's Hiab had a strategy to have an own sales company on each significant market, including the Korean one, already in the 1970s. Proventia, Company B, Company C, Fibox and Company D basically followed demand to Korea. Company A, Lappset and Futuremark, on the other hand, did not enter Korea on purpose. For these companies, the start of the Korean operations was somewhat random – they did not plan the entry to Korea as a part of their strategy. For Company A and Lappset, a triggering force was an approach by a Korean partner who wanted to represent the company in Korea. After starting the operations in Korea, these firms have come to realize the market potential in the country. Futuremark already had Samsung, a large Korean *chaebol* as its customer when it started its mobile business, which aroused the company's interest in the Korean market and made Futuremark to realize the huge potential for its products there.

When analyzing the development of the operation mode use in the selected case companies, it can be seen that actual development has taken place in six out of nine studied companies. The operation mode use in the case firms over time in Korea is depicted in Figure 8 below:

Figure 8: The development of the operation mode use in South Korea in the selected case companies



As can be seen from the Figure 8 above, the firms that have seen actual development in their operation mode use are Cargotec's Hiab, Proventia Emission Control, Company A, Company C, Fibox and Company D. These developments on an individual company level are analyzed below.

Cargotec's Hiab established a sales company originally as a joint venture with a Korean partner in the beginning of 1990s but acquired this sales company completely thereafter. As a solution to the hard market situation in the end of 1990s, Hiab acquired a part of a Korean company in 1997 and formed a joint venture with this company. Later, Hiab purchased most of the shares of the Korean management team that originally had 30 %

of the JV's shares but, still, the arrangement is technically a joint venture because there are still some members of the management team that hold the JV's shares. However, in essence, this Korean unit of Hiab is now an own unit. Thus, it can be seen that major inter-mode switches, some mode combination and some mode stretching has taken place in the case of Hiab. Changing initially from a JV sales company to a completely-owned sales company represent a major inter-mode shift. In addition, a change from own sales company to a JV again represents another inter-mode switch. Unfortunately, the case study of Cargotec's Hiab did not specify the exact reason for the first inter-mode switch from a JV sales company to a wholly-owned sales company. The reason for the second inter-mode switch, from an own sales company to a JV again, was clearly the drastic change in the competitive environment, to be exact Hiab needed to adapt itself to new market circumstances as the external environment suddenly changed to its disadvantage. The change from a JV to a wholly-owned unit, in essence, represents inter-mode switching, mode packaging and mode stretching. Inter-mode switching because Hiab, technically, owns the Korean unit nowadays. However, at the same time this new operation mode solution represents a bit of a mode package, because there are still some members of the Korean management team who hold shares. In other words, the former JV and new 'own company' have grown together to some extent, although, admittedly, it can be questioned whether a wholly-owned subsidiary and a JV can exist in a mode package. Simply, there is no rationale for this kind of mode combination – rationally, these two operation modes could exist as opposed to each other but not in a combination. Clearly, the difficulty of identifying, assessing and measuring mode combinations as suggested by e.g. Welch et al. (2009: 6-11) is palpable here. Instead of terming this new arrangement of Hiab in Korea a mode package, perhaps a more correct term would be a mode stretch – the previous organizational form of a JV has virtually grown to be an almost wholly-owned subsidiary, 'almost' being a keyword here since this arrangement is purely neither a JV nor a wholly-owned subsidiary.

Proventia started to serve the Korean market through a sales agent after a business foray trip in 2003 and established a liaison office in Korea in 2007. However, this kind of refinement in the operation mode can be seen as a very minor one, since the liaison office is the lightest operation mode in Korea and there is only one person physically in this office. Still though, a mode package can be identified here, exactly as in Valla's (1986: 33) example of a firm-employed person based permanently in the country to back up an agent or to complement the marketing action of a subsidiary. The rationale for this mode package is clearly value activity specialization – modes are used in a mutually supportive way to achieve Proventia Emission Control's objectives.

Company A first served the Korean market from 1995 onwards through an importer but soon established a sales subsidiary in the hope of deeper market penetration and earnings. Clearly, the reason for this inter-mode switch was the expectation of strong market growth in Korea. This inter-mode switch also had some characteristics of mode stretching as the importer of the company in Korea was hired to work as the CEO of the newly-formed sales subsidiary, which eased the path to the mode switch that Company A undertook. However, this sales subsidiary was unsuccessful, leading Company A to run down this unit, which is essentially a sign of de-internationalization that can occur at any stage of internationalization, as the internationalization literature suggests (e.g. Welch and Luostarinen 1988: 84). Thereafter, Company A returned to serve the Korean market through an importer, this time different than the original one that had also participated in the sales subsidiary arrangement. When Company A changed its operation mode from a sales subsidiary to an importer again, this inter-mode switch was triggered by the admittance of managerial misjudgement that was committed both when the decision was made to establish a sales subsidiary and during the implementation of this sales subsidiary strategy.

Company C served Korea first through sales agents and established a sales office in 1995 and a service center in 2004. Unfortunately, the case did not specify exactly why the inter-mode switch from using sales agents to establishing an own sales office took place. However, at the time Company C established this sales office, it enjoyed strong demand for its paper machines in Korea, and a strong hypothesis can be drawn that the reason for this establishment was to better serve the Korean customers with a more committed operation mode. Also, the establishment of the service center in 2004 can most likely be attributed to the same cause.

Fibox started its sales to Korea through an importer in the beginning of 1990s but soon, after three to four years, established an own production plant in 1995 although it was tempted into a JV arrangement that it rejected. The reason for this inter-mode switch was a change in the external conditions in the form of fears that Fibox's products will be copied in Korea if the company does not start own production quickly in the country.

Company D entered Korea with a sales agent originally and established a production plant as a joint venture with a local partner in 1987. Later, a couple of years after the start of the JV, Company D bought the Korean party to the JV out and continued the operation on its own. The reasons for the first inter-mode switch – from a sales agent to a JV – seemed to be the strong market growth in Korea, that is, a change in external environment, and Company D's desire to benefit from the market knowledge of the JV partner. This is line with Hennart's (1988: 365-367) argument that "often, the main motive for entrant companies to form JVs with local firms is to benefit from the local market knowledge of the latter. Arguably, this market knowledge is difficult to buy on an arm's-length basis." The subsequent inter-mode switch from the JV to an own unit can probably best be explained with Gomes-Casseres's (1987: 100) argument that "after acquiring experience and knowledge on the local market through the JV arrangement, the entrant firm will no longer need the local JV partner and the entrant firm may convert the JV to a wholly-owned subsidiary. In the light of information that the case of Company D provided, it seems that this is exactly what happened in this inter-mode switch. The argument of Gomes-Casseres (1987: 100) could probably also be used to explain Cargotec Hiab's switch from the JV to a wholly-owned unit but that mode switch is a bit more complicated having features of mode packaging and mode stretching, as well, as discussed above.

For these six companies, the direction of the development in the use of foreign operation modes in Korea is from low-commitment operation modes to high-commitment operation modes, just like the foreign operation mode and internationalization literature suggests. An exception to this stage pattern of internationalization is brought about by Company A, which had to divest its sales subsidiary in Korea and return to serving the market through an importer. This was a sign de-internationalization that can occur at any stage of internationalization (Welch and Luostarinen 1988: 84).

The companies that have not seen development in their operation mode use in Korea are Lappset, Futuremark and Company B. These firms have continued to serve the Korean market with the same arrangement that the operations in Korea were originally started with. Lappset has continued its business in Korea utilizing the same importer that was selected originally in 1993, mainly because the business has flourished and it has not needed a lot of effort from Lappset to serve the Korean market with this type of arrangement. Futuremark has seen its business to continue with the same sales agent that was selected in the beginning. As the interviewee from Futuremark stated, "neither of the parties has neither had time nor priority to deepen the cooperation". In addition, this kind of light arrangement where the sales agent basically only provides contacts has worked out extremely well for Futuremark. Company B has continued its business in Korea through the same sales agent that was selected in the beginning but the company has also added another sales agent to serve a different customer segment than the first agent serves. This could be seen as an intra-mode switch, although Company B has not replaced its intermediary but added another.

For these three companies – Lappset, Futuremark and Company B - that have not seen a change in their FOMs in Korea, a number of reasons can be identified for this mode change inactivity. When going through these three cases, an obvious impression is that the business has worked out so well through these arrangements that there has not been a real reason to undertake a mode switch. This can be translated loosely to a number of switching costs or barriers. What comes to take-down barriers, these companies may fear the loss of customers owing to their loyalty to current agent or importer and appreciate the personal bonds to individuals in existing foreign operations. Set-up barriers, on the other hand, are probably in play in the form foreign operation learning costs and loss of customers owing to failures in initial phase of own operation. Also, this mode inactivity could probably be attributed to mode myopia (Welch et al. 2007: 411). Petersen and Welch (2002: 162) wrote that "an operation mode that may have been used at first by chance becomes the mode best understood". This mode change inactivity also reflects the notion of Benito et al. (2008: 16) that "sometimes, only one mode form, or package, is evaluated, particularly when companies are approached with an offer to sell by a foreign company or an offer to act as a distributor or licensee in a foreign market". However, the cases did not exactly specify why these firms did not undertake mode switches, which means that serious conclusions for mode development inactivity for these firms cannot be drawn.

The magnitude of the operations of the case firms in Korea is dictated by the selected operation mode. Naturally, those companies that have invested in the country have more extensive operations. If the magnitude of the operations is measured in terms of number of personnel in Korea, the companies that have established production facilities have widest operations in the country. Company D employs the largest number of people in Korea – from 120 to 140 – in its production plant just outside of Daegu and the sales office in Seoul. Cargotec's Hiab that operates a marketing and service center in Seoul and production plant in Chungpu employs 82 persons in the country. Fibox, having a sales office in Busan and a production plant in Incheon employs from 40 to 50 people in its Korean operations. After the companies that have engaged in production in Korea comes Company C that has established a sales office in Seoul and a service center in Daejeon. Company C employs 12 people in its Korean operations. After Company C, there is Proventia's Emission Control that has established a liaison office in Seoul that could be regarded as a very small-scale sales office. Proventia Emission Control employs only one person in Korea. Those firms that serve the Korean market through direct export, either through agents or importers, do not have their own personnel in the country. Therefore, the operations of Company A, Lappset, Futuremark and Company B can be regarded as quite minor in the country in terms of number of personnel employed. However, the number of personnel is only one indicator of the magnitude of the operations in the country and, therefore, should not be looked at exclusively. Other indicators, such as turnover generated in Korea, might be very useful, as well. However, because of the scope of this study and the reluctance of some interviewees to go deep in country-specific turnover figures, the magnitude of the Korean operations of the case companies in terms of turnover is not addressed in this study.

Those case companies that had invested in Korea and, therefore, had own personnel in the country mostly staffed their Korean operations with local Koreans. The management of the Korean operations, however, has often been made the responsibility of foreign expatriates. Cargotec's Hiab and Fibox have employed expatriates as Chief Executive Officers in their Korean operations. Both in the case of Cargotec's Hiab and Fibox, the Finnish expatriate working as a CEO has lived in Korea for a long time and can speak fluent Korean, which naturally helps greatly in managing the operations. Company D used to have more foreign expatriates in its Korean operations when the operations were started but there was a time there were no expatriates at all present in Korea. Later, when the production capacity was increased in Korea, Company D sent an Italian factory manager and a Finnish controller to manage the Korean operations. Proventia's Emission Control has had a Finnish expatriate in its liaison office since it was established in 2007. Company A and Company C, on the other hand, have relied on the local Koreans to manage their operations. At the time Company A had a sales subsidiary in Korea, the CEO of this subsidiary was a Korean person that had lived in Sweden for 25 years. All of the personnel of Company C in Korea are locals, the last Finnish person having left six to seven years ago from the country.

The companies that served Korea through direct export utilizing middlemen had found their partners in various ways. For three firms, Company A, Lappset and Fibox, the initial contact to a Korean middleman was a trade fair contact. In addition, Proventia's Emission Control found its second partner when a Korean ministerial delegation came to familiarize itself with the company's projects in Hong Kong. This could loosely be seen as a trade fair contact, as well. Two firms, Proventia's Emission Control and Company B, have found a partner with the help of Finpro, a Finnish internationalization service provider organization. Proventia's Emission Control found its first partner, a sales agent, in Korea with the help of Finpro, whereas Company B found its second sales agent utilizing Finpro's services. In the first place, Company B had organized its own person, essentially working as a sales agent for Company B, to a new company that was formed in Korea after Company B was acquired by an investment company. Interestingly, Futuremark found its sales agent with the help of another small Finnish software firm. Company D, first engaged in direct export through a sales agent in Korea and thereafter a partner in a JV with a Korean firm, found its JV partner due to an approach by this Korean partner.

For the majority of the case firms that used direct export through local middlemen, the middlemen were also serving other principals. This was the case for Proventia's Emission Control, Company A, Lappset, Futuremark and Company B. Unfortunately, it did not become evident in the company cases whether the sales agents of Company C and Company D and the importer of Fibox served other principals at the time when these arrangements were in place.

What comes to major problems when operating in Korea, all case firms report the low level of English skills of the local people. This problem is reported by truly all firms, the ones that have served Korea through direct exporting and the ones that have invested in the country. However, the seriousness of this problem as seen by the case companies differs quite a lot. Some case firms see that the level of English skills among Koreans is very bad and can lead to serious misunderstandings and problems in the running of business in Korea, whereas some case firms see that the level of English skills is, indeed, a problem but it has not created major problems for the operations. Other problems in Korea as reported by the case companies are related to wider cultural issues, such as the authoritarian Korean organizations, the neglect of paying invoices on time as in the case of Futuremark, the propensity of Koreans to copy foreign products, and cultural differences in general.

What comes to the most important assets of the Korean partners of the case firms, three important assets clearly stand out: the relationship network of the partner, the knowledge of the local market and the language abilities of the partner. By relying on the partner's connections and market knowledge, many case firms have proceeded significantly in their endeavor to penetrate deeper into the Korean market. The language skills of the partner are seen to be very important, even invaluable, by many case firms.

6 SUMMARY, CONCLUSIONS AND RECOMMENDATIONS FOR FUTURE RESEARCH

This study contributed to the knowledge of foreign operation modes both theoretically and empirically, yielding interesting insights on both domains. Theoretically, this study pointed attention to the novel approaches when analyzing foreign operation modes and their use. The newest research regarding FOMs was reviewed in the theoretical part of this study. It was seen that this new thinking of foreign operation modes significantly challenges the previous thinking on this field. Taking note of the newest research regarding FOMs, this study applied these new concepts empirically on Finnish firms' operation mode strategies in South Korea, which offered insightful views that are of interest both academically and practically.

Importantly, this study offered further research on foreign operation mode topics that have been somewhat neglected in the previous research. This study provided further evidence of mode switching that has not been covered extensively previously. This study also shed some more light on mode stretching and mode combination, topics that are quite novel in the field of foreign operation modes and, therefore, in the need of further evidence to refine the theories. This study did one's bit in offering further research that was asked on these topics by e.g. Benito et al. (2008: 21-22) when they invited more longitudinal research to uncover these aspects more. More specifically, they stated that "more exploratory, in depth and longitudinal qualitative studies would seem to be a critical first step" (Benito et al. 2008: 22).

To shed some more light on the more novel approaches to foreign operation modes, this study analyzed the foreign operation mode strategies of a selected group of Finnish firms in South Korea. This study placed special emphasis on mode switching, mode stretching and mode combination strategies. In order to answer the research problem, first a theoretical framework that was depicted in Figure 7 was presented. Based on this framework, or to be exact on the subcomponents of this framework – mode switching, mode stretching, and mode combinations -, nine empirical cases of Finnish companies in South Korea were analyzed.

Inter-mode switches turned out to be quite common in this study, which further corroborates the notion that they are, indeed, common, although the existing literature on the topic has neglected these aspects. A total of five case companies out of nine had engaged in inter-mode switching, either once or more times. Mainly the inter-mode switches were triggered by the changes in external environment. Some evidence on mode combinations was received, too, although mode combinations did not appear to be common among the case companies. Only in one case, Proventia Emission Control, was there a clear occurrence of a mode combination. The case of Cargotec's Hiab was a lot more difficult to assess, whether there was a mode combination or not. If the mode combination of Cargotec's Hiab is accepted, then there were two companies out of nine that engaged in mode combinations. Mode stretching, neither, was not very common among the case companies, as it occurred in only two case companies out of nine. Intra-mode switches turned out to be very uncommon, this basically having taken place in only one case company and it was also questionable whether the addition of another sales agent by Company B can be seen as an intra-mode switch, even. The companies that did not change their FOMs had their reasons for this largely in switching barriers and mode myopia.

This study also gave some further evidence supporting the theory of gradual internationalization that was originally presented by Johanson and Wiedersheim-Paul (1975). By far, the majority of the mode switches were from low-commitment FOMs to higher-commitment FOMs, which is in line with the notion of the establishment chain that was presented by the above-mentioned authors.

Clearly, there is an apparent need for future research on these newer approaches to foreign operation modes that were dealt with in this study. These newer approaches – mode switching, mode stretching, and mode combinations – are rather underresearched but still, according to scholars studying FOMs and according to this study, the reality of many companies that operate internationally. Therefore, more research on these topics is called for.

There are a number of ways to respond to this call. Each researcher, naturally, has his or her own discretion as to how to approach the research that is to be conducted. If the footsteps of this research are followed, a first step would be to investigate the foreign operation mode strategies of other Finnish firms in South Korea. This could possibly corroborate the findings of this study, or, interestingly, yield contrasting results, the reasons of which would be very interesting for drawing a more complete picture of these newer approaches FOM strategies. Alternatively, these newer approaches to FOM strategies could be studied in other country contexts, be it then Finnish firms in some other country or companies from any country operating in another country. Directing the attention from a country level to a company level, investigating FOM strategies in multiple countries for a single firm would be of great interest, as then there would be more knowledge as to if the FOM strategies of a single company differ from one target country to another. To highlight the interest in this aspect, the attention can be turned to Petersen and Welch (2002: 160), who saw that the degree of integration or coordination of complementary modes can vary across different foreign markets even for the same company. Directed by these thought, one could make a hypothesis that the FOM strategies of an individual company might vary across different national markets. It is natural that the FOM strategies vary across different markets for an individual company because, as was discussed in theoretical part of this paper, there is no pre-agreed formula that helps a company to make its operation mode decisions. As a result, the variance in the FOM strategies is likely to be high for a single company across different markets. However, it would be interesting to see if the FOM strategies in terms of mode switching, mode stretching and mode combinations also vary across different markets for a single company.

In addition, the idea of Clark et al. (1997: 618) that the sequential development of a firm's internationalization can take place at the firm level rather than within individual markets raises up an interesting aspect for future study of FOM strategies, as well. Namely, it would be interesting to see if a firm's strategy with regards to mode switching, mode stretching and mode combinations follows the same line of development as that expressed by Clark et al. (1997:618) with regards to operation mode development. For instance, it would be interesting to see if an introducing of a mode combination by a single company in one target country leads to introducing of mode combinations in other target countries, as well.

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7.3 Interviews

Interviewee One

A high-ranked manager

Company A

Finland

31st January, 2008 approximately 40 minutes

Interviewee Two

An executive in charge of strategy

Company B

Finland

6th March, 2008 approximately 60 minutes

Interviewee Three

A highly-ranked Vice President

Company C

Finland

26th February, 2008 approximately 45 minutes

Interviewee Four

Company A

Finland

6th March, 2003 and 24th April, 2007

Interviewee Five

A high-ranked director

Fibox

Finland

23rd August, 2006 and 16th December, 2004

Interviewee Six

Senior Vice President and a member of the board of the Korean subsidiary at one time

Company D

Finland

4th February, 2008 approximately 70 minutes

Lehmus, Heikki

Vice President of Business Development and Quality

Cargotec, Hiab business unit

Helsinki, Finland

17th January 2008 approximately 85 minutes

Niemi, Tapani

The main owner

Fibox

Kirkkonummi, Finland

18th February, 2008 approximately 65 minutes

Puura, Jouni

President of the Liaison Office in Korea

Proventia, Emission Control business unit

Seoul, Korea

31st January 2008 approximately 65 minutes

Talala, Petri

Vice President in charge of mobile business

Futuremark

Espoo, Finland

5th March, 2008 approximately 80 minutes

Ylinenpää, Hannu

Marketing Director

Lappset Group

Rovaniemi, Finland

21st February, 2008 approximately 75 minutes

APPENDIX 1 – Interview questions

Helsinki School of Economics/ Center for Markets in Transition

Interview questions

Managing business in turbulent markets

1. Background information on both the parent company and the subsidiary

- Line of business
- Size of the company in Finland and host country (turnover, personnel)
- Main products and markets
- Role of the target country for the company
- Value of the investment (€, $)
- Location (eg capital, special economic zone)
- Other locations that were considered suitable
- Share of ownership (majority, minority, 50-50, 100%)
- Way of establishment (greenfield investment, acquisition)
- Main operations of the subsidiary (eg production, R&D, sales office)
- What was the impulse to enter South Korea in the first place?
- At which stage of internationalization did the company enter South Korea?
- Why exactly to South Korea?

2. Influence and implication of the recent changes (eg Estonia's EU membership, China's WTO membership, South Korea's financial crisis)

- What have been the major changes in the host country during the past 15 years (1991-2005)?
- What are the impacts on the business environment?
- What are the impacts on the firm?

- What makes the country attractive for foreign investors?
- What are the major deterrences to investment?

3. Company's relationship with the public sector

- Courts of law and legislation (implementation and interpretation of laws in practice)
- Role of personal relationships with government authorities and state authorities (who and in which issues or problems)
- Role of lobbying in business
- Role of public relations, goodwill
- Role of corruption in business
- Major problems related to the public sector
- Major solutions of the problems related to the public sector

4. Company's relationship with the foreign partner company

- How did the cooperation begin?
- Who took the initiative?
- How has the cooperation developed?
- What were the factors affecting the partner selection?
- What were/are now the motives for cooperation?
- Were/are the motives for cooperation of both partners similar?
- Were/are the expectations about cooperation realized?
- What is the distribution of work between partners?
- How has the know-how been transferred?
- How has the trust been built?
- Role of written contracts in cooperation? How detailed are contracts?
- Role of personal relationships in cooperation?
- Role of friendship relations in cooperation?
- What have been the major problems in cooperation?

- How have these problems been solved?

5. Company's relationship with the local companies

- What are the major competitive edges of the local companies?
- What kind of cooperation or contacts do you have with other local companies (e.g. customers, subcontractors)
- Are there any differences in practices when doing business with the local companies (compared to Finnish companies) with respect to following issues: role of written contacts, role of personal relationships, role of friendship relations, and differences in problem-solving?
- What have been the major problems with the local companies?
- How have these problems been solved?

6. Company's relationship with company employees

- Attitude towards foreign employer?
- Education and professional skills of the local workforce in relations to the wage level?
- What motivates local workforce?
- Are local employees given responsibility and are they willing to take responsibility?
- Are there any social responsibilities of the employer towards employees (eg health care, housing, children's day-care)?
- The role of labour unions? Development of unionization level of local workforce in the future?
- Role of local hierarchies in the organisation?
- Equality (eg female managers)
- Role of etnic/religious groups in business (eg Russians in Estonia, Chinese in Malaysia)

7. Future of the host country, local companies and Finnish businesses there

- How the cooperation with the local partner is expected to develop in the future?
- What are the major risks related to the business environment in the future?
- What are the major risks related to the Finnish business in the host country in the future?
- Are there problems, which are common for all Finnish companies operating in the host country?
- How the problems could be solved?

APPENDIX 2 – Email approach to potential interviewees

Email message that was sent to the potential interviewees:

Dear "Interviewee"

The Center for Markets in Transition (CEMAT) at the Helsinki School of Economics is running a research program on rapidly developing markets (among others Russia, China, South Korea, Baltic countries, India, Latin America) that investigates these markets in terms of their business environment and business opportunities from the viewpoint of Finnish companies. We ask You for an interview for the part of the research that deals with South Korea.

The research aims at explaining:
- which factors contribute to enlargement of operations or to transfer of operations outside Finland and the selection of the target country
- challenges that companies encounter in a changing business environment
- what the enlargement or transfer of Finnish firms' operations to these areas means in practice
- how the Finnish companies view their operations are integrating to local society
- what problems there is in the activity and how these problems could be solved
- what differences and similarities are there regarding the themes mentioned above between different areas

The empirical material for the research will be collected by interviewing the representatives of Finnish companies operating in the target country and of local partner companies of those firms. Interviews will be conducted as confidential and responses will be treated as anonymous. The research information will be used in the research projects of CEMAT and in the academic refinement of this research project. The research results will be published in a publication series of the Helsinki School of Economics and a report will be delivered to each interviewee.

We will contact You during the next couple of days to agree on a possible interview.

Best regards,

Kristiina Korhonen, research manager
Anu Penttilä, research assistant
Mayumi Shimizu, research assistant
Heikki Huhtanen, research assistant

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