

The Internationalization of SMEs in Emerging Markets: Case Russia

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Stefan Nieminen

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Aalto University
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Stefan Nieminen
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The first goal of this study is to investigate and analyze the characteristics and challenges of the internationalization process of foreign small- and medium-sized enterprises (SMEs) to Russia. The second goal of this study is to create a model of the production unit establishment process, as designed especially for SMEs. Also, the key resources in succeeding in these processes are studied.

The theoretical framework studies several mainstream internationalization theories, mainly from the perspective of SMEs: stage models, innovation models, network models, early internationalization theories, international entrepreneurship and international business. In order to better understand and help to describe SME internationalization process, the methods by which large corporations internationalize are also studied and contrasted.

The source of data in the qualitative single case studies consists of four interviews based on semi-structured questionnaires, two company visits and one factory (production unit) visit. These interviews center on Finnish SME-owner/CEOs operating partly or fully in Russia, and also include one Russian CEO and one work safety manager of two Finnish-owned SMEs.

The empirical study reveals that stage models are the most suitable for studying the internationalization process of SMEs. However, given that stage models ignore the influence of entrepreneurs in the internationalization process, a new model is introduced – the entrepreneurial stage model of SME internationalization – in order to recognize the role of these key actors in the process. Additionally, a model of production unit establishment is introduced and described.

This thesis' case study widely supports previous studies focused on operating and internationalizing to Russia, and the study also introduces the main challenges and characteristics of the SME internationalization process to Russia. Finally, the key resources needed for successful SME internationalization and the establishment of production units are described. With respect to internationalization, the key resources are an SME's and entrepreneur's capabilities and networks, and also an entrepreneur's will to continually learn and gain experience. For production unit establishment, key resources are highly qualified employees, organization, local business knowledge, distribution and logistics systems, financing, and business operations.

Keywords

SME internationalization, production unit establishment, internationalization to emerging markets, business in Russia, SME internationalization challenges.

PK-yritysten kansainvälistyminen kehittyville markkinoille: tapaustutkimuksen kohteena Venäjä

Tämän pro gradu -tutkielman ensimmäisenä tavoitteena on selvittää ja analysoida PK-yritysten kansainvälistymisprosessin erityispiirteitä ja haasteita Venäjällä. Toisena tavoitteena on kehittää malli PK-yritysten tuotantoyksikön perustamisprosessista. Tutkielmassa selvitetään myös näissä prosesseissa onnistumiseen vaadittavia avainresursseja.

Tutkielman teoreettinen viitekehys koostuu tunnetuimpien PK-kansainvälistymisteorioiden ja -mallien selvittelystä. Näihin lukeutuvat vaihe-, innovaatio- ja verkostoitumismalli, kansainvälistymisen varhaisemmat teoriat, kansainvälinen yrittäjyys sekä kansainvälinen liiketoiminta. Näitä selvitetään PK-yritysten kansainvälistymisen näkökulmasta. Tutkielmassa on myös suuryritysten kansainvälistymistä käsittelevää teoriaa, jotta saadaan selville sen sovellettavuus PK-yritysten kansainvälistymisprosessin tutkimisessa.

Kvalitatiivisessa tapaustutkimuksessa käytettiin tiedonlähteenä neljää puolistrukturoitua kyselylomakkeeseen perustuvaa haastattelua, kahta yritys- ja yhtä tehdasvierailua. Haastattelut käytiin suomalaisten PK-yritysten (omistaja)toimitusjohtajien kanssa, jotka työskentelevät joko pää- tai sivutoimisesti Venäjällä. Myös suomalaisomisteisessa PK-yrityksessä työskentelevää venäläistä toimitusjohtajaa sekä työturvallisuuspäällikköä haastateltiin.

Empiirinen tutkimus osoitti, että PK-yritysten kansainvälistymisprosessin tutkimiseen soveltuvat parhaiten vaihemallit. Koska ne kuitenkin jättävät huomiotta yrittäjän vaikutuksen kansainvälistymisprosessissa, on tässä tutkielmassa kehitetty uusi yrittäjämäinen vaihemalli erityisesti PK-yritysten kansainvälistymiseen. Tutkielmassa esitetään myös tuotantolaitoksen perustamismalli sekä Venäjälle kohdistuvan kansainvälistymisprosessin ja tuotantoyksikön perustamisprosessin avainresurssit. PK-yrityksen kansainvälistymisprosessissa onnistumiseen vaadittavat avainresurssit ovat yrityksen ja yrittäjän kyvyt, suhdeverkostot sekä yrittäjän jatkuva halu oppia ja saada kokemusta. Tuotantolaitoksen perustamisen avainresursseihin kuuluvat työntekijät ja organisaatio, paikallinen liiketoimintatuntemus, jakelu ja logistiikka, rahoitus sekä liiketoiminta ja sen ohjaus.

Tapaustutkimuksessa myös esitetään Venäjälle suuntautuvan kansainvälistymisprosessin päähaasteet ja erityispiirteet. Tulokset tukevat laajasti aiempia tutkimuksia.

Avainsanat

PK-yritysten kansainvälistyminen, tuotantoyksikön perustaminen, kansainvälistyminen kehittyville markkinoille, liiketoiminta Venäjällä, PK-yritysten kansainvälistymisprosessin haasteet.

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1. Introduction

I studied internationalization of small- and medium-sized enterprises (SMEs) to emerging markets to get an understanding about the process, its challenges and potential gains for SMEs. This thesis narrows in on the study of Russia – a great emerging market with vast unexplored potential for SMEs. There are studies on the internationalization of big corporations to emerging markets, but not from the perspective of SMEs, thus making this study useful and interesting.

I moved to Saint Petersburg, Russia in September 2010 as part of my filial obligation to the family business, SGN Group, and assumed the responsibility of managing the company's foreign business affairs. At that time I was not familiar with neither the culture nor the business practices of the country, but one certainty was that the Russian market represented an essential part of SGN Groups current sales, and offered substantial growth potential in the future. I am interested in how foreign SMEs, such as SGN Group, can utilize Russia's opportunities and benefit from them, and also in identifying the major challenges that SMEs face when beginning operations in Russia.

In the theoretical part of this thesis I studied the best known SME internationalization theories, and in the empirical analysis the focus is on SMEs from Finland that have extended their international operations to Russia. In order to understand the process of establishing production units in Russia, I conducted a search for a Finnish entrepreneur with just such internationalization experience whom I could interview.

As the topic is quite specific, it thus adds to the uniqueness of the investigation within existing research of the field. As such, having been unable to locate articles on the topic in English, I consulted the staff from the Saint Petersburg Graduate School of Management in the University of Saint Petersburg for additional insights and material available only in Russian. Internationalization studies to Russian markets were done only from the perspective of big corporations such as IKEA, which I found surprising considering the size and potential of Russia for SMEs.

Given the size and strength of Russia's developing economy and the high volume of trade between it and other European countries, it is justifiable to argue that this thesis can concretely inform new insights and assist other organizations in their efforts to expand into Russia. Also, my case study about the establishment of production units in Russia by SMEs is unique, and similar studies were not found in any major article databases in Western countries.

2. The objectives of the study

The overall objective of this study is to create a clear understanding about the processes and challenges associated with establishing production units in Russia. I also study the internationalization processes of SMEs and the major challenges facing SMEs when establishing operations in Russia.

2.1 The objectives of the study and research questions

My research question is two-fold: first, “how do SMEs establish production units abroad, especially in Russia” and second, “what are the major challenges and risks concerning this internationalization process?” The sub-question of my study is: “what are a company’s key resources in achieving its goals when internationalizing?”

The aforementioned objectives take three different aspects into consideration when studying SMEs. First, the primary theories and models for SME internationalization, namely the stage model, the network model, the international new venture model and the international entrepreneurship model. If none of these models are sufficient in describing the internationalization process of the case study presented in this thesis, a new model will be introduced.

Second, the internationalization of SMEs to Russia is studied because the research question is part of this phenomenon. It is important and interesting to study the characteristics and uniqueness of the Russian market, along with the key factors and challenges associated with firms internationalizing there. This type of contextual approach provides a comprehensive focus to the study, thereby greatly contributing to the research that currently exists in the field.

Third, the empirical component of this thesis study consists of a case study on two firms, as well as a model for product unit establishment in Russia for the Finland-based company SGN Group. As said, the case study focuses on two firms, Hankitek SPb and Profima Emkost, both established by Finnish entrepreneur Hannu Kiljunen. The study also analyzes the internationalization process of SGN Group. Qualitative case study method is used as it allows holistic investigation of the topic. To gather data for the case study, key employees of the target companies are interviewed through series of open-ended questions.

2.2 Limitations of the study

As this is a study about the internationalization of small- and medium-sized companies, the investigation of large corporations or publicly traded companies is largely excluded. While some internationalization theories in the theoretical framework include large companies, this is done to demonstrate how large companies differ from SMEs when internationalizing.

To limit the scope of study, several steps have been taken to refine the focus of the research. First, the internationalization of service-oriented SMEs are excluded, as is the study of the differences between exported or manufactured products by SMEs in Russia, in favor of focusing on the process of internationalization itself. This study is also made from the perspective of Finnish SMEs with western backgrounds, and therefore the analysis of the Russian market and its behavior is made from within this context. This study also does not consider industry specialization, which might necessitate variations in the internationalization processes as some industries may internationalize differently than others. Finally, this study also excludes any inward processes of internationalization, such as importing.

2.3 Definitions of the study

This study regularly uses several key terms that are specific to this analysis. These terms are identified and defined with further detail below:

- **Internationalization:** Currently there is no universal definition, though Welch and Luostarinen (1988) define it as the process of increasing involvement in international markets, whereas Reid (1983) define it as a measure of the perceived difference between foreign markets and the home market space along economic, cultural, political, and market-strategic dimensions. The definition of Welch and Luostarinen (1988) is used in this study.
- **Small- and Medium-Sized Enterprise (SME):** Popular definitions of SME usually vary when considering employee counts, turnover or balance sheet figures. This study uses the definition for SME as presented by the European Commission (2005) which states that a small enterprise employs 10 to 49 people, has a turnover of two to 10 million euros, or has a total balance sheet ranging from two to 10 million euros. For medium sized enterprises the corresponding figures are 50 to 249 employees, turnover of over 10 million euros but

less than 50 million, and a balance sheet totaling more than 10 million euros but less than 43 million. Employee counts define the sizes of the companies focused upon in this study.

- **Manufacturing SME:** This is a small- or medium-sized company that manufactures goods through a wholly- or partly-owned manufacturing plant. Most of the research on manufacturing companies is from the viewpoint of large corporations or multinationals.
- **International Entrepreneurship:** This study favors the definition by McDougall and Oviatt (2000) in that it is a “combination of innovative, proactive and risk-seeking behavior that crosses or is compared across national borders, and is intended to create value in business organizations.” This definition is widely accepted and used in the field of international entrepreneurship research.
- **Born Global:** Servais et al. (2006) state that this is an SME that internationalizes within three years of establishment and more than 25 percent of its foreign sales or outsourcing are done outside the firm’s home continent (Table 1.). The born globals featured in this study are also characterized as SMEs, and not only have products with global market potential, but also combine this potential with accelerated internationalization capabilities and a global market vision (Gabrielsson et al., 2008). Born global is defined in this study as a synonym for an international new venture (INV).

Table 1. Definition of early internationalizing enterprise (Servais et al., 2006)

Classification of New Ventures	<i>No foreign sourcing after three years</i>	<i>Less than 25% of foreign sourcing outside Europe within three years</i>	<i>More than 25% of foreign sourcing outside Europe within three years</i>
<i>No foreign sales after three years</i>	Domestic New Ventures /Born Local Firms	Born International Sourcer	Born International Sourcer
<i>Less than 25% of foreign sales outside Europe within three years</i>	Born International Seller	Born European Firm	Born Global Firm
<i>More than 25% of foreign sales outside Europe with in three years</i>	Born International Seller	Born Global Firm	Born Global Firm

3. Internationalization of SMEs – past studies and theoretical frameworks

Since its inception, the field of SMEs internationalization has experienced constant change (Young et al., 2003). To make this study as timely and accurate as possible, the research questions posed in this thesis study must be compared to the dominant existing theories of the field.

In existing international business literature and theories, mature multinational corporations play a dominant role, whereas SMEs and their internationalization processes have only recently attracted broader interest from researchers. This could be seen as evidence that several countries, particularly those experiencing a balance of payment deficits, have attempted to increase the international business activities of their SMEs. The intent of this activity increase is to boost economic growth, cut unemployment and create potential mini-MNEs (multinational enterprises) for the future. In other words, in this context internationalization can be understood as the geographical expansion of economic activities over a home country's border.

The term "internationalization" grew to prominence starting in the 1920s when internationalization began to outshine imperialism as the dominant organizational principle when considering cross-border interaction between market economies. The economic internationalization process accelerated in the post-WWII era and dominated until the early 1970s, when the new phenomenon of internationalization of SMEs began to emerge (Gjellerup, 2000).

While this thesis study does not extensively discuss 'globalization', it does touch upon this phenomenon and its relationship with the internationalization of SMEs. According to Gjellerup (2000), the three main forces that drive the globalization of business are: the explosive growth of low-cost technology connecting people and locations; the steady lowering and/or dismantling of trade barriers and overall financial deregulation; and, the widespread economic restructuring and liberalization that followed the fall of socialism in Russia and Central/Eastern Europe, as well as the geographic expansion of markets in Asia, especially China. However, despite all of these driving forces behind globalization, it has not made obsolete the internationalization of companies, thus many of today's theories about internationalization remain credible.

The impact of globalization is more acute on SMEs than on large, highly internationalized corporations. While SMEs were previously considered more as passive victims than as active players of globalization, new evidence exists suggesting the contrary. In the last few decades alone

many SMEs have successfully built and coordinated business activities outside their home markets, which is increasingly crucial in order to contribute to future growth (ibid.).

Globalization and its associated issues have only been introduced to the development of small companies, and the research conducted to study it. Traditionally, SMEs restrict activities to the region in which they are based, or at least remain in their home country's borders. Today however, many SMEs are active in one or two regions of the world and are therefore described as international or regional players. The term "internationalization" is used to refer to SMEs' outward movements of international operations, while "globalization" refers to the international connectivity of markets and the interdependence of national economies that strongly affect all activities of SMEs. Internationalization also implies a changing state, where the growth of the company provides a context for internationalization, causing internationalization and growth to become intertwined (ibid.).

Existing research on SME internationalization mainly focuses on an enterprise's international activities or operations by applying product, operation or market analyses (e.g. Luostarinen, 1979) or also network analyses (e.g. Johanson and Mattsson, 1993). Research on small firms tends to view the process of internationalization as evolutionary (Luostarinen, 1979), and during this process, small firms become increasingly committed to, and involved in international activities. However, at a certain point the firm can also become inverted, thereby resulting in de-internationalization. The majority of internationalization research focuses on the outward processes of internationalization such as exporting, franchising and foreign direct investments (FDI). The inward processes of internationalization, such as importing, are seldom included in research even though many companies begin their internationalization path on the inward side (Susman, 2007).

In the Nordic countries, the internationalization of SMEs is traditionally defined as "the process of increasing involvement in international operations" (Welch and Luostarinen, 1993) and this process is often understood as gradual and sequential, and consisting of several stages. In a network context, Johanson and Mattsson (1993) describe internationalization as a "cumulative process, in which relationships are continually established, maintained, developed, broken and dissolved in order to achieve the objectives of the firm". This view, however, seems somewhat fragmented as it focuses exclusively on relationships. Assuming that SMEs operate within their natural context, the view of Johanson and Mattsson (1993) appears more promising. They define internationalization as the "process of developing networks of business relationships in other countries through extension, penetration, and integration". In their definition, Lehtinen and Penttinen (1999) summarize the fundamental characteristics of the internationalization process based on the Nordic research findings. Their definition also covers two concepts occasionally

applied in the context of internationalization, namely international orientation and international commitment. International orientation refers to a company's general attitude towards internationalization, thus representing an evaluative dimension.

Reid (1983) defines internationalization as a measure of the perceived difference between foreign and home market space along economic, cultural, political and market-strategic dimensions. International commitment is associated with the requirements of the operation modes chosen and the size of international business. The latter seeks to position firms somewhere between the extremes of no involvement (a domestic firm) and full commitment (a firm with a realized foreign direct investment). Generally, the overall focus of research has shifted away from the definition and analyses of international activities to the resources needed for internationalization. With reference to the resource-based perspective, Ahokangas (1998) proposes a definition of SME internationalization in terms of resources within the natural context, e.g. within a firm's network. Therefore, an internationalizing firm is seen to mobilize unique and interdependent resource stocks that activate and propel a company's internationalization activities within its natural context. This definition thus implies that internationalization is the "process of mobilizing, accumulating, and developing resource stocks for international activities", regardless of the actual content of the international activities themselves.

Ahokangas, (1998) argues that all of the existing models of small firm internationalization are seen as presenting either a market, firm or entrepreneurship perspective. The market perspective of internationalization considers studies on internationalization or the diversification strategies of large firms. The enterprise perspective, which includes the stage models of internationalization, appears in literature about SME internationalization. In current internationalization research there is a clear difference in the focus of large and small businesses. Although global strategies, strategic international alliances and problems of diversification and control are frequently studied, Ahokangas' study focuses almost exclusively on large firms and multinational enterprises (MNEs). In contrast, SME research is more concerned with the various stages of internationalization.

Applying theories developed for, or based on large firms often leads to confusing and corrupted results, and when these results are applied to small firms they are not compatible in such smaller settings (Ruzzier et al., 2006). This too is one concern of this thesis study when considering the establishment of the case study's production unit in Russia. The concern lies in that the SME internationalization models will not support the highly integrating form of internationalization, especially when considering the uniqueness of the operational environment. I am confident that through the critical analysis of the models it will be possible to find theories to support the case study, even though the study may need the support of several theoretical approaches toward SME

internationalization. In the following chapter the main SME internationalization theories and research paths are introduced.

3.1 Stage models

Stage models are used to analyze small-, medium- and large-sized companies in explaining the development of internationalization and international activities. Stage by stage, companies in these models overcome obstacles, and the main knowledge and learning-related focus is on which market(s) the company occupies (Kaarna and Mets, 2008). A typical stage model includes indirect exporting/importing/sourcing; direct exporting/importing/sourcing; licensing; joint ventures; and wholly owned subsidiaries – stages.

The most widely used stage models in research are the Uppsala model and the Innovation model. Many variations of this pair of stage models exist as they have long since been in the mainstream of internationalization research (Ruzzier et al., 2006). This thesis study focuses on the Uppsala and Innovation models as well.

3.1.1 Uppsala Model

Developers Johanson and Vahlne (1977) created the Uppsala model to identify the four stages of entry into international markets, which was then expanded by Cavusgil (1984) to include a fifth stage. Other models were also developed on the basis of the Uppsala model, such as the Nordic models and the Learning models (Ruzzier et al., 2006).

The Uppsala model explains internationalization as a series of stages taken to increase a company's international involvement as a result of different types of learning. Each increase in involvement is a more progressive stage in the process of understanding the global environment and the competition. According to the model, the general and expert market knowledge and resource commitments of the company affect commitment decisions and current business activities, referred to as change aspects (Figure 1.). The changed aspects then increase the market knowledge and stimulate further resource commitment to foreign markets. This model states that companies increase their international involvement in small incremental steps within those foreign markets in which they currently operate. After that, the model states that the companies will start to

internationalize to countries located at a greater “psychological distance”; divided by factors like language, education, business practices etc. (ibid.).

In the Uppsala model, the commitment to foreign markets is composed of two factors: the amount of resources committed and the degree of commitment (Figure 1.) The former can be understood as the size of the investment needed (including all resources), and the latter refers to the difficulty of identifying an alternative use for the resources and then transferring them to that alternative use (ibid.).

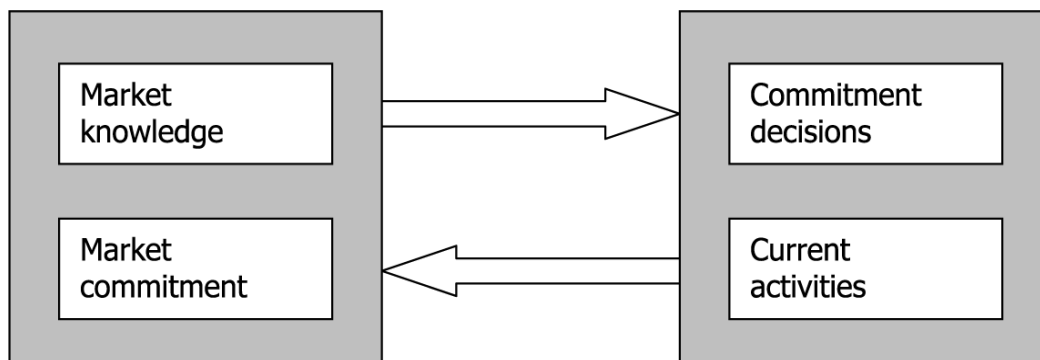


Figure 1. Uppsala Model (Johanson and Vahlne, 1977)

3.1.2 Innovation model

In innovation models, for a company internationalization is seen as a novel step (Gankema et al., 2000). In SMEs, innovation models focus exclusively on the export development process, and in particular those of small- and medium-sized companies. Innovation models can vary from three to six stages, but all models share three core stages: the pre-export stage, the initial export stage and the advanced export stage. According to Andersen (1993), even though the quantities of stages in the models differ, in practice the models are relatively similar. Typically innovation models point to the importance of individual learning and for top management to understand the firm’s international behavior (Ruzzier et al., 2006).

3.1.3 Critique of stage models used in internationalization studies of SMEs

Modern empirical findings throughout the world prove that SME internationalization modes are neither path dependent, emergent nor incremental. In a majority of the current SME internationalization research, stage models are still used to explain internationalization actions and

decisions of SMEs. However even the discontinuous stage models cannot cover the wide range of phenomena involved in SME internationalization, such as “born globals”, “backsourcers” (SMEs that reconstitute their international activities back to their home countries) and “born regionals” (SMEs that gain their force out of concentrating their business activities locally, and never shift capacity beyond export activities) (Schultz et al., 2009).

One major limitation of the stage model approach and the key target of its criticism is the assumption that the stages progress in controlled, predictable manner, thereby limiting or even eliminating the strategic choices that must be made by the entrepreneur. Also Wright, Westhead and Ucbasaran (2007) state that the Uppsala model (and other stage models), focus on *firm*, rather than *entrepreneur*. This kind of view limits the scope of study of internationalization, since in SMEs the entrepreneur is traditionally seen as one of the key factors of the company, and the entrepreneurial behavior is crucial in the company’s internationalization decisions. The same is true of many small businesses with high-tech products, or demand conditions that defy conventional patterns. Coviello and Munro (1995) determined that small high-tech firms rarely follow a stage approach to internationalization.

In the innovation-related models, defining the different stages is problematic and insufficient attention is given to the duration of the stages, along with how operations are structured within them. Determining the stage differences with reference to activities in them, is understood as a subjective opinion, rather than discovering real differences between stages. From the process point of view, innovation models fall short by only describing the process of change, and not the *dimensions* of change, nor the different approaches used by companies in developing their activities (Andersen, 1993).

3.2 Network model

In network theory, markets are seen as a system of relationships among a number of different players including customers, suppliers, competitors and private and public support agencies (Coviello and Munro 1995). Johanson and Matson (1988) suggest that a firm’s success in entering new international markets is more dependent on the company’s current domestic and international relationships, rather than the chosen market and its cultural characteristics. The bulk of network theory research focuses on the management of international relationships (Coviello and Munro, 1995). These authors also claim that existing domestic and international relationships help the firm to expand to new markets, and develop new business partners and market positions there. These

new contacts and relationships may be either formal (business related) or informal (friends and family).

From a network perspective, the opportunities created through these kinds of contacts affect market selection and entry decisions, rather than only the strategic decisions made by the management of the enterprise. Concurrently, a company's existing contacts may also restrict its internationalization process. Network theory research of SME internationalization shows that the strategic position and influence of individuals, especially entrepreneurs, is neglected. In SMEs the entrepreneur and/or other key company individuals have a substantial impact on internationalization through close social relationships (sub-network within the business network) with other individuals (Coviello and Munro, 1995). Related to this topic, Vahlne, Schweizer and Johanson (2010) wrote about the difficulty of international networking, which in many cases means working outside of one's national or regional comfort zone. They stated that networking internationally with greater physical distance, including cultural differences is often time consuming and takes great effort.

Johanson and Mattson (1993) emphasize the goal of interaction within networks as gradual learning and the development of market knowledge. In their four-stage model (early starter, late starter, lonely international and international among others) the position of the enterprise may be analyzed from both from a micro (firm-to-firm) or a macro (firm-to-network) perspective. According to the authors, internationalization of the firm means that the company establishes and develops relationships to other companies (or other participants) in a foreign network. The new relationships in new networks are achieved through the following means: international extension (establishment of new relationships in untapped country networks); penetration (development of relationships in those networks); and international integration (connecting networks in different countries) (Johanson and Mattson, 1993).

In Wright and Dana's (2003) study on the outcomes of the network approach on business competition, an airline industry example is used to demonstrate competitive strategy. In this example, two multinational airline companies moved from a uni-polar business strategy to a multi-polar business network (alliance) with mutual benefits. The authors claim that networks result in the fleeting nature of stand-alone firms. This is because through networks, the power and control can be divided among independent companies that cooperate voluntarily for a greater efficiency and shared benefit (Wright and Dana, 2003).

3.3 Early internationalization theories

To better understand central theories of SME internationalization, it is important to discuss how firms first began to internationalize. Several explanations account for the pressure felt by firms to quickly internationalize. For example, Zahra and George (2002) claim that new ventures in highly integrated and globalized industries, or those that have small domestic markets, are more likely to pursue internationalization in order to remain competitive (Zahra and George, 2002).

Committing deeply to any one, or several international markets is difficult for small, new ventures as the size and infrastructure of these firms is not robust enough to support such actions. In these cases, resources are simply too scarce and the size of the market commitment needed is too high to deliver success. Typically, resources are shared more widely between all the markets where the born global wants to enter (Madsen and Servais, 1997). Such high-commitment decisions can represent heavy investments to any one particular market, which also includes the establishment of self- or partly owned production plants overseas.

Mainstream internationalization theories fail to explain the formation process of new international firms. These theories assume that companies internationalize only after they have properly matured in their home markets. McDougall et al. (1994) discovered that no company studied that internationalized early followed the prescribed stages of internationalization. So, to understand the phenomenon of early internationalization, new theories and additional study is needed (McDougall et al., 1994).

Many studies of early internationalizing enterprises have been conducted in recent decades. According to Rialp et al. (2005), the most common influential factors for the rise of early internationalization are:

- New market conditions in many sectors of economy.
- Technological development especially in the areas of production, transportation and communication.
- The increased importance of global networks and alliances.
- Increased abilities of people, such as the entrepreneurs and founders who seek early internationalization for their businesses.

According to Baronchelli and Cassia (2008) additional reasons for the early internationalization of the SME include: falling trade barriers, deregulation, privatization, maturity in domestic markets, high technology investments that cannot be offset by domestic sales alone, shortening product life

cycles, globalization of competitors and industries, and the free movement of capital, goods, services and people.

The trend of early internationalization is only expected to grow in the coming years. As businesses and industries experience this phenomenon, any existing players ought to increase their international activities as well (Rialp et al., 2005). Despite the increased interest in the early internationalization of firms and born globals, the outcomes of the associated research include just new models and definitions of born global behavior (Gabrielsson et al., 2008), rather than widely accepted theories about the phenomenon.

The research of early firm internationalization was mostly conducted with hypothesis testing-oriented empirical studies, case-based approaches and special techniques used for comparative data analysis. The results not only point to the insufficiency of most existing SME internationalization theories, but also the high potential impact of insights on the network approach to this field of study. Also, the difference in studying several industries versus studying high-tech industries is only critical in the overall research of the phenomenon (Gabrielsson et al., 2008).

Madsen and Servais (1997) introduce a model developed by Johanson and Vahlne (1990) that they say enables the study of the internationalization of born globals. This dynamic theoretical model makes a distinction between state and change aspects of internationalization variables, where the company's present state is an important factor in explaining future changes and subsequent stages. According to the model, state aspects are represented by a firm's 'market commitment' to foreign markets. This market commitment is divided in two factors: first, the amount of resources committed (size of investments), and second, the difficulty of finding an alternative use for the resources and transferring them to this alternative use. According to this model, market knowledge is defined as employee knowledge and savvy about markets and operations that are remembered and recallable at a given time (Madsen and Servais, 1997).

Other researchers have made similar findings, such as Cavusgil and Knight (2004), who state that the superior performance of a born global firm is an outcome of the firm's entrepreneurial and managerial knowledge about international markets and operations. Also, the efficiency on which such knowledge is acquired is critical for the successful and superior international performance of the company. Zahra et al. (2000) suggest in turn that the breadth, depth and speed of technological learning are expected to enhance the international performance of a born global. This technological learning is necessary for maintaining a company's core competencies, and its ability to create new or updated product innovations.

Born globals face similar internationalization challenges as SMEs. However, the greatest differences are attributable to the newness of the business, as in the born global's relative lack of maturity that is unlike many long-standing SMEs that internationalize after fully maturing within their home markets. Due to newness, born globals are often associated with the poverty of resources and power. Also, unstable policies and lack of knowledge can be major hurdles for internationalizing born globals (Oviatt and McDougall, 1994).

3.4 International entrepreneurship

There are two branches to the study of international entrepreneurship. One focuses on the cross-national-border behavior of entrepreneurial actors, and the other focuses on the cross-national-border comparison of entrepreneurs, their behavior, and the circumstances in which they are imbedded (Oviatt and McDougall, 2005). The definition of "international entrepreneurship" is jointly influenced by the two distinct pieces of research from which the area of inquiry emerges – entrepreneurship and international business (McDougall and Oviatt, 2003). A series of varying themes and theoretical approaches are found under the umbrella of "international entrepreneurship" (IE), which is an interdisciplinary field of study (Schultz et al., 2009).

In this study, international entrepreneurship provides insights on modern internationalization that are useful in understanding the case study and generating conclusions. Because entrepreneurship is an essential part of international entrepreneurship, the aspect of entrepreneurship is also included in the following discussion. The meaning of international entrepreneurship has evolved in recent decades, and this evolution is presented in Table 2. below.

Table 2. *Evolution of international entrepreneurship definition*

Author	Definition
Johanson and Vahlne (1990)	A cumulative process in which relationships are continually established, developed, maintained and dissolved in order to achieve an enterprise's objectives.
Zahra (1993)	Nature and consequences of a firm's risk-taking behavior as it wades into international markets.
Wright and Ricks (1994)	"International entrepreneurship is a company-level activity that crosses national borders and focuses on the relationships between business and the international environments in which they operate."
McDougall and Oviatt (1996)	New and innovative activities that have the goal of value creation and growth in business organization across national borders.

Lehtinen and Penttinen (1999)	Developing networks of business relationships in other countries through extension, penetration and integration.
McDougall and Oviatt (2000)	Combination of innovative, proactive and risk-seeking behavior that crosses, or is compared across national borders and is intended to create value in business organizations.
Oviatt and McDougall (2005)	"International entrepreneurship is the discovery, enactment, evaluation and exploitation of opportunities – across national borders – to create future goods and services."

The first known reference of international entrepreneurship dates back to Morrow's (1988) discussions of the age of the international entrepreneur. Morrow suggested that advances in technology coupled with increased cultural awareness, has made once-remote markets accessible to companies of all sizes.

Soon after, McDougall's (1989) empirical study comparing domestic and international new ventures guided the way for academic study in international entrepreneurship. This study has provided rich insights into the differences between international companies and those ventures that avoid internationalization. In the early 1990s, Oviatt and McDougall developed a series of case studies that clearly showed that some young ventures have internationalized early in their life cycles. These case analyses clarify some of the approaches that new ventures have followed in going international. Oviatt and McDougall (1994) defined international entrepreneurship and provided a theoretical base for the study of international new ventures, which they defined as business organizations that "from inception, seek to derive significant competitive advantage from the use of resources and the sale of outputs in multiple countries". Thus, when international entrepreneurship began with an interest in new ventures, its definition was narrower than in the newer literature. Zahra (1993) was the first researcher to suggest that the study of international entrepreneurship should include both newly established firms and existing ones.

The inclusion of established companies also corrects an oversight in the entrepreneurship field, namely, the presumption that established companies are not innovative and refuse to take risks. Many respected, established companies work hard to foster innovation, support venturing and encourage their employees and management to engage in risk taking. Ignoring these firms in the research would effectively exclude an important part of many economies. A report by an entrepreneurship panel (Giamartino et al., 1993) called for a broader definition of international entrepreneurship. Zahra and Schulte (1994) also observed a need to go beyond the "born international" criterion highlighted in the early work of McDougall and Oviatt.

As additional studies were conducted and articles published, interest in the area increased, and the field of international entrepreneurship broadened from its early studies of new venture internationalization theory. For example, insightful studies on national culture, alliances and cooperative strategies, small- and medium-sized company internationalization, top management teams, entry modes, cognition, country profiles, corporate entrepreneurship, exporting, knowledge management, venture financing and technological learning have all helped move the field forward.

An early definition of international entrepreneurship focused on the international activities of new ventures while excluding established firms (McDougall, 1989). During the early 1990's the domain of international entrepreneurship broadened when the topics of relevant inquiry were seen as evolving rapidly. Wright and Ricks (1994) noted the growing importance of international entrepreneurship as an emerging research issue in the research of the internationalization of SMEs and international business. These authors also suggest international entrepreneurship is a "firm-level activity that crosses national borders and focuses on the relationship between businesses and the international environments in which they operate."

This definition helped researchers shift attention away from using a firm's age or timing of internationalization as the sole criterion in defining international entrepreneurship (such as in the studies about born globals). This definition also made new, young ventures and established companies worthy of study. Wright and Ricks' definition, moreover, highlights the context in which entrepreneurial activities occur, whether within new ventures or established corporations. A firm's business environment plays an important role in spurring certain types of entrepreneurial activities and determining any payoffs earned. Finally, an advantage of the Wright and Ricks' (1994) definition was the inclusion of comparative analyses of entrepreneurial activities within the domain of international entrepreneurship.

McDougall and Oviatt (1996) defined international entrepreneurship as "new and innovative activities that have the goal of value creation and growth in business organizations across national borders". However, in 2000 the same authors also developed the prevailing definition of international entrepreneurship, which as "a combination of innovative, proactive, and risk-seeking behavior that crosses national borders and is intended to create value in organizations" (McDougall and Oviatt, 2000). This definitive definition offered a more inclusive list of topics that fall under the umbrella of international entrepreneurship, such as corporate entrepreneurship research, among others. This research reflected an important change in McDougall and Oviatt's view of international entrepreneurship in that they recognized the importance of international entrepreneurship in established firms. Thus, international entrepreneurship behavior in large, established companies, often referred to as "corporate entrepreneurship", is included. Individual,

group and organizational levels of behavior and academic study are also included in this definition, whereas non-profit and governmental agencies remain excluded.

Lumpkin and Dess (1996) highlighted a variety of “entrepreneurial orientation” dimensions and distinguished them from the definition of entrepreneurship itself, which they equated with new entry, or the act of launching a new venture. Shane and Venkataraman (2000) state that the creation of a new organization is not a defining condition. For example, business opportunities can be sold to others. Thus, Shane and Venkataraman define the study of entrepreneurship as the “examination of how, by whom, and with what effects opportunities to create future goods and services are discovered, evaluated and exploited.” The authors explain that entrepreneurship has two parts: opportunities and individuals who strive to take advantage of them.

Increasingly, entrepreneurship is seen as focusing on opportunities that are bought and sold, or form the foundations of new organizations. Such a point of view leads away from an emphasis on entrepreneurial orientations, which McDougall and Oviatt (2000) rely upon for their definition of international entrepreneurship. Therefore Oviatt and McDougall (2005) adjusted their definition of international entrepreneurship according to the Shane and Venkataraman’s (2000) definition, and define it as discovery, enactment, evaluation and exploitation of opportunities – across national borders – to create future goods and services.

3.5 Links of international entrepreneurship theory with international business studies

The theories constituting international business have interconnections with international entrepreneurship in research of multinational corporations (MNCs) (Oviatt and McDougall, 2005). However, the links between international entrepreneurship studies concerning small and medium sized enterprises and theoretical foundations of international business are very weak, if not nonexistent entirely (Dana et al., 1999).

In this chapter, studies conducted on international business are compared, which since their inception are linked to studies of international entrepreneurship. This chapter argues that international business theories cannot effectively be used to produce generalized results in the study of SME internationalization.

According to Oligopolistic Reaction theory, enterprises in oligopolistic industries react to the business practices of their competitors, and imitate them to create a sense of marketplace harmony. However, one problem with this theory is that it does not apply to international entrepreneurs, who by definition operate outside of oligopolistic industries. Entrepreneurs create and innovate, and often seek to differentiate themselves from competitors. They often have first-mover instincts for capitalizing on opportunities, a behavior that is not adequately explained by oligopolistic reaction theory (Dana et al., 1999).

Monopolistic advantage theories are helpful in explaining why large firms invest heavily in a special class of assets – those that are long lasting, defensible and proprietary – which can assure firms long-term competitive advantages in markets at home and abroad. However, these theories are much less useful in explaining entrepreneurial advantages, which differ from those of larger firms in that they are entrepreneur-based, more ephemeral and more narrowly defined. International entrepreneurship is often based upon an increasingly diverse set of resources and processes. Entrepreneurs focus on advantages, and view the sources of these advantages as largely irrelevant (ibid.).

3.6 Challenges of internationalization of SMEs

Anderson et al. (2001) introduce three main challenges for SME internationalization. First, the SME must evaluate whether to, when to, and how to operate overseas. Second, the challenge is to design long-term planning processes and business systems to cope with the decisions made according to internationalization. Lastly, internationalizing SMEs must also attend to regulatory issues and payment security.

Anderson et al. (2001) study the challenges of SME internationalization from the manager's perspective. They also emphasize the managers' constant need for learning in the progressive process of internationalization, especially in terms of the provision of support, advice and interaction through personal and business networks. In their article, the authors conduct their study by sending questionnaires to the managers of 3000 SMEs in the UK that were involved in international business. The results stated that the biggest challenges for internationalization, from the viewpoint of the managers, were entry routes/methods, transport/logistic difficulties, awareness of tariffs and barriers and language problems. Also, payment issues were mentioned as a problem by 40 percent of respondents.

Anderson et al. (2001) emphasize the first major challenge which occurs in the initial pre-internationalization phase, when managers must make decisions regarding whether to, when to, and how to internationalize. The study of these decisions suggests that managers are often not fully aware of the different methods of internationalization open to consideration, and also the potential of long-term implications of their decisions are often unclear.

The authors identify two areas of learning that managers need when faced with these challenges: adaptive and generative learning. Adaptive learning enables those involved with small firms to consolidate market positions and customer relationships by developing cultural appreciation and empathy. Generative learning, then, centers on redesigning the underlying 'dominant logic' or 'paradigm' through which a firm operates. This is done through a process of management and organizational learning and is considered essential for the company in establishing itself as a truly international organization, rather than a 'domestic firm that also exports' (ibid.).

4. Russian market and its challenges

Since internationalization to Russia (and especially the establishment of a production unit there) is the main topic of this thesis, it is intriguing and crucial to study the characteristics and uniqueness of this market. In addition, the key factors and challenges of internationalizing and running SMEs in Russia are investigated. The literature available on SME internationalization to Russia is extremely limited (at least in Finnish, English, Swedish and German) and in these languages it was also difficult to find articles related to the internationalization of big or multinational corporations to Russia. As a result, several non-scientific sources are cited, such as Russian news, as well as interviews with entrepreneurs with long tenures of working in Russia. Luckily, the staff of the Saint Petersburg State University Graduate School of Management was helpful, and found some very accurate Russian-language material concerning internationalizing and operating in Russian markets, as well as one recently published study in English. Especially the Russian articles, which concentrate on the challenges of Russian economy from inside, provided intriguing insights for this study.

This literature about Russian businesses and economy confirms my assumptions that all of the aforementioned difficulties and challenges experienced by SMEs internationalized overseas, also apply to expanding to Russia. This chapter focuses on the study of the particular challenges of SMEs operating and internationalizing specifically to Russian markets.

4.1 Russia and its economy

If measured by square kilometers Russia is the biggest country in the world (17.075.400 sq. km.) covering about a ninth of the Earth's land area. Russia is also the ninth most populous nation with approximately 143 million inhabitants (as of 2010). Nearly 80 percent of the inhabitants live in the European part of Russia, and the majority, 73 percent, of the inhabitants live in cities. Russia has 11 cities with populations over one million people (Russian Federal State Statistics Service).

Russia is one of the largest economies among the developing countries and the tenth largest in the world by nominal value, and sixth largest measured by Purchasing Power Parity (PPP). In 2010, Russia's nominal Gross Domestic Product (GDP) was \$1.46 trillion, and \$2.22 trillion if measured by PPP. Russia's dominating export products are natural resources, such as oil and gas, which provides stability to the Russian macro economy (World Economic and Financial Surveys, 2010). In

2010, the average Russian's monthly salary grew to an all-time high of \$700 (РБК, RBK News). Besides raw material extraction, some of the main industries of Russia are mining, all forms of machine building, defense industries, shipbuilding, road and rail transport equipment, communications equipment, agricultural machinery, construction equipment, textiles, foodstuffs and handicrafts (Central intelligence agency).

However, the Russian economy is also facing many challenges. For example, the "shadow" or black market economy in Russia is significant. According to Surinov, the head of the Federal State Statistic Services, about 20 percent of the Russian economy is unobservable. Therefore, if this shadow economy accounts for 20 percent of Russia's GDP, then the size of illegal businesses is approximately \$293 billion (as of 2010); so about one in every five enterprises conducts its business on the black market (Shirokova et al., 2011). Also the long physical distances between cities and strong diversity of the country, culture and business practices challenge internationalizing and operating in Russia, particularly if the SME is operating in several regions of the country (interview with Sam G. Nieminen, SGN Group).

Even though the Russian government has instituted a number of programs and laws to improve its economic development and human rights record, independent research reveals that these have had little impact. The performance of Russian economy is hindered by many problems (Shirokova et al., 2011), and the macroeconomic growth numbers are tightly pegged to the sales of natural resources (World Economic and Financial Surveys, 2010).

Entrepreneurship during Soviet Union times was rare. Iakoleva (2005) states that entrepreneurs in Russia, after the collapse of the Soviet Union, were truly entrepreneurial since starting an enterprise at that time was itself an entrepreneurial idea. Entrepreneurship in the East with a collectivistic orientation has received limited attention by the researchers, thus limiting the knowledge about the uniqueness of this phenomenon (Iakoleva, 2005). Still, it is clear that Russia, as an enormous country with a significant market, can provide entrepreneurs with great business potential and interesting possibilities. The following chapter studies the most significant challenges facing SMEs in operating and internationalizing to Russian markets.

4.2 The main challenges of internationalization to Russia

The main challenges of internationalization to Russia include corruption, bureaucracy, legislation, economical criminality and property rights, management and trust. As a term, "corruption" is a word with many interpretations. For example, searching for "corruption" in Wikipedia gives 11

different definitions (Wikipedia). Transparency International defines corruption as the abuse of entrusted power for private gain, and encompasses corrupt practices in both the public and private sectors (Transparency International).

Global Competitive Research (GCR) stresses that corruption is the biggest economic problem in Russia. Other global research conducted by the international civil society organization Transparency International shows that the environment in Russia is extremely hostile, and on par with some of the least developed countries in Africa or the Middle East. Hostile in an economic sense, Russia is an overall insecure environment with questionable business ethics, and aggressive, or unethical behavior by governmental institutions. For example, a study by Shirokova et al. (2011) shows that 70 percent of the respondents find the behavior of controlling officials (including police) “aggressive”. The Global Corruption Barometer (2009) states that corruption is seriously widespread in Russia, where even the public officials and civil servants were given 4,5 points out of 5 on a 5 points scale – 5 meaning “extremely corrupted”.

Rimskiy’s (2011) studies include the reasons for the continuing corruption and its connection with interpersonal trust in Russian society, and cite results from the Russian Institute of Sociology (PAH) research to build his study. Importantly, the study shows that the interpersonal trust in Russia is low. For example, about 57 percent of respondents trust close relatives, 41-48 percent friends and other relatives, colleagues 21-26 percent, and trust in other familiar members measured just 9 percent. When Rimskiy compared the results of Russia with similar studies worldwide, he still could not find a clear connection between interpersonal trust and corruption, the reason for which is likely lying in the system of the society.

In many cases it is difficult for an individual or entrepreneur to operate free of corruption as so much of it is built into society – they simply cannot compete. Depending on context, consequences of staying corruption-free can include bureaucratic problems (slowness or inability to obtain necessary documents or permissions), loss of market competitiveness, or significantly increased expenses. Rimskiy (2011) states that in many cases corruption in Russia is such everyday phenomenon that while committing acts of corruption, people do not even understand that what they are doing is actually illegal.

From these results, it can be clearly seen that economical criminality and corruption have become a market-wide phenomenon that touches nearly every aspect and industry of the Russian economy. These institutional circumstances create a model of doing business in a “Russian way”, rather than operating in a legally and ethically correct manner. In reaction to the lack of rule of law or commonly respected regulations, absence of regional autonomy and the pervasiveness of

corruption, many companies choose to leave Russia after entering, or do not internationalize there in the first place (ibid.)

Bureaucracy is traditionally a phenomenon studied by sociologic researchers and most scholarly literature stems from the writing of the German sociologist Max Weber (1864-1920). Typically the term “bureaucracy” is defined as the characteristic form of public administration for a state with extended territorial sovereignty (Niskanen, 2007).

After the collapse of Soviet Union until today, it is not rare to have bureaucrats simply refuse to perform their duties without a bribe. This means that in many cases entrepreneurs do not even have a choice – if they wish to do business, they have to bribe (Parikka, 2010). According to Rosstat, the Russian State’s statistics agency, the number of bureaucrats in the country has grown from 0,5 million to nearly 1,7 million between 2000 and 2009 (The Bank of Finland Institute for Economies in Transition, 2011). Russian Prime Minister and former President Vladimir Putin, as well as the current President Dmitri Medvedev have publicly spoken out against corruption. Though, during their respective tenures the power of bureaucrats suspiciously increased dramatically (Parikka, 2010).

According to Rimskiy (2004), companies (and individuals) are able to solve practically any bureaucratic problem by employing some sort of corrupt measure. Also these kinds of corruption-oriented problem solving methods are widely used in Russia, both in business and personal situations. The bureaucracy in Russia is seeking to get its “rent” in every sector of the society and for entrepreneurs this means plenty of work and expenses. To compensate for these expenses morally and materially, many entrepreneurs find illegal ways to avoid taxes and other official expenses. Rimskiy (2004), states that in the current bureaucratic system of Russia, it is practically impossible to realize a normative governmental administration.

Legislation, economical criminality and property rights in Russia also differ from those in the Western countries. Comparatively, the Russian legislative system is well developed and the laws are usually written in a very detailed way. The problem is that citizens and companies disobey these laws more so than in the West, mostly due to reasons stemming from the Soviet era. Still, one significant cause of the dearth in legal adherence is the insufficient enforcement of laws and corruption; it is just too easy to break laws and avoid any juridical consequences by paying bribes. Russia also has a number of unwritten laws that are often prioritized over written ones (Parikka, 2010).

Weak legislative control, widespread corruption and a lack of protection of rights can result in serious consequences for an SME that is establishing a business in Russia. PriceWaterhouseCoopers (PWC)'s 2009 research about Russian market behaviors gives the same picture that is also drawn by the evidence above. According to the survey, 71 percent of the respondents had experienced some form of economic crime, and 86 percent of respondents claimed that they felt heightened incentive or pressure to commit fraud. According to the PWC report, 96 percent of respondents experienced fraud either conducted through instances either inside or outside the company (Shirokova et al., 2011).

As an example of economical criminality, the CEO-owner of SGN Group Sam G. Nieminen states that it is not at all exceptional to hear stories of foreign entrepreneurs getting their business illegally taken over (raided) by criminal means, and the entrepreneurs being ousted from their businesses by fraudulent documents created to show new owners of the business. In these cases, when the entrepreneur seeks justice from the courts and even wins the case, the raiders have already sold or seized all significant assets and the company is left effectively bankrupt. This means that legislation is often helpless in protecting entrepreneurs in many incidents of economical criminality (interview with Sam G. Nieminen, SGN Group).

Even though economical crimes, such as raiding, have declined in recent years, protection of property rights is still an imperative consideration for an SME that decides to internationalize to Russia (interview with Sam G. Nieminen, SGN Group). Kulikova (2006) describes this phenomenon by stating, "it turns out that the biggest profit is reaped by those who can rob and sell, rather than those who produce and create something. This is a destructive system, which reduces economic efficiency." Shirokova et al. (2011) state that property rights are the foundations of the business. If the property rights are not well protected, the investment is less secure since the returns on investments are at risk of theft. Countries with less secure property rights gain fewer foreign direct investments, which thereby limits overall economic growth in that country.

Management and trust also differ between Russia and Western countries. Shirokova et al. (2011) recent research the influence of institutions on CEO succession in SMEs in Russia. That theme is relevant to this thesis study since from the viewpoint of foreign SMEs, it is often the entrepreneur that is not willing to permanently move to run the business abroad, thus needing to organize the management of the business in another way.

As the analysis of the study only includes Russian companies, few connections are made to studies involving foreign companies. It is clear that local entrepreneurs are more aware of the legislation,

business practices and other business- and market-related matters than foreign entrepreneurs, that plan to enter the market or to whom Russian markets are foreign and operating experience on the markets low. Still, the study expands viewpoints about entrepreneurs' concerns about managerial issues, and therefore is applicable to this thesis study.

The study of Shirokova et al. (2011) reveals that in Russia, the greatest hindrance of an owner-CEO deciding to pass management onto a hired CEO relates to the security of property and contract rights, compliance of the firm's practices with legal business rules and the conformity with the hidden, shadow economy. Over 34 percent of the respondents reported a medium, low, or extremely low level of confidence concerning security of property rights, and the ownership of key market players in the business field. In terms of contract rights, that confidence level measured 37,2 percent.

The authors assume that the insecurity of property rights is one of the biggest obstacles in passing the management responsibility on to a hired CEO. In one of the studied companies, the owner-CEO even got himself a law degree, partly to defend his assets in legal proceedings. None of the Russian owner-CEOs interviewed in the study decided to entrust the full management responsibility to a hired CEO. Therefore, trust issues are a real concern and challenge for the foreign SMEs who internationalize to Russia, particularly those that wish to find a hired CEO for the company (Shirokova et al., 2011).

5. Case study – theory and methodology

In this chapter different theories and approaches to case study are analyzed and compared. Also an analysis of typical kind of outcomes of these approaches is introduced.

5.1 In-case study vs. cross-case and other statistical methods

Case study research design collects observations on single or multiple cases. The in-case (hereafter referred to as “case study”) and cross-case methods are the two most popular approaches to case studies, in which the researcher can determine the number of cases to be the subject of investigation. These methods can also be used concurrently, which provides additional texture to the study and contributes to a more holistic understanding overall of a topic (Gerring 2007, 1-66).

Traditionally, case study analysis is associated with qualitative methods, and cross-case analysis with quantitative methods. This arises from the simple fact that when one is attempting to incorporate a large number of cases into a single analysis, it is necessary to reduce the evidence into a small number of dimensions. One cannot explore 1000 cases thoroughly, whereas this is possible with just one or a few cases. Cross-case methods and case studies define observations differently, and largely operate on different levels of analysis. The most significant contrast between these two case study approaches is illustrated in Table 3. below, where the characteristics of both case study and cross-case methods are shown (ibid).

Table 3. Differences of cross-case and case studies (Gerring 2007, 38)

	Affinity	
	Case Study	Cross-Case Study
Research goals		
1. Hypothesis	Generating	Testing
2. Validity	Internal	External
3. Causal insight	Mechanisms	Effects
4. Scope of proposition	Deep	Broad
Empirical factors		
5. Population of cases	Heterogeneous	Homogeneous
6. Causal strength	Strong	Weak
7. Useful variation	Rare	Common
8. Data availability	Concentrated	Dispersed
Additional factors		
9. Causal complexity		Indeterminate
10. State of the field		Indeterminate

Yin (2003, 3-6) analyzes the dichotomy of these different case study approaches. Yin states that the method of the study is dependent on the data and nature of the study. Qualitative and quantitative methods are not attributes of competing types of research, rather they are features of different types of data analysis and cannot be readily replaced by one another. There is no fundamental difference in the scientific credibility of either of the methods, even though many prejudices exist for and against both of the discussed methods.

Lundberg (2006, 137-142) wrote about a similar topic and compared in-case study with statistical methods claiming that these methods of research can make mutual gains if only they quit quarreling and began to borrow from each other. Lundberg also introduces arguments about the challenges in identifying the nature of the data and measurement techniques. For example, is “birth” a single event, or configuration of multiple events? He also asks if a human’s personality is numerically measurable, and if so to what extent. Lundberg emphasizes the usability of case studies especially in the conditions where formal statistical procedures do not exist. In these situations, case study is a method that can be used to gain the best possible analysis of the target of research. Lundberg claims that statisticians of the same basic character as those methods employ the case study method, though admitting that even the most complete case study still fails to take into consideration all possible variables. However, the ultimate number of aspects to consider is too high for any current statistical method to handle (Lundberg, 2006, 137-142).

An enticing prospect is that of combining qualitative and quantitative case study evidence. The combination of these data types can be highly synergistic and this approach to case study can yield many benefits to the researcher, such as: keeping him/her carried away by vivid, but false, impressions in qualitative data, and it can bolster findings when it corroborates those findings from qualitative evidence (Eisenhardt, 1989).

5.2 Theories and types of case study methods

To complete successful case studies, an important strategy is the reliance on theoretical concepts that guide the design and data collection. The goal of such theoretical concepts is to develop preliminary concepts at the outset of the case study. A second purpose of the theoretical concept is to help define the unit of analysis (what the case is about), in order to identify the criteria for selecting and screening potential candidates for the case to be studied, and to suggest the relevant variables (i.e. data) to be collected as part of the case study. Selecting the case(s) to the case study is one of the most difficult steps in case study research, and without the guidance of the preliminary theoretical concepts the choices during the process can be hard to make and prevent

the effective and consistent progression of the case study. The third major role of theory in case studies is its need in generalizing the results following the study (Yin 2003, 1-9).

5.3 Different approaches to case studies

First, the multiple case studies that follow replication logic are studied. The researcher makes literal or theoretical replications in order to verify, falsify or develop emergent theory. The number of the cases may vary significantly, but ideally for theory building, the case research should stop when saturation of the data has been achieved, and the optimal number of cases ranges between four and ten (Bengtsson et al., 1997).

The researchers following the positivistic approach argue that multiple cases are preferable to single case designs. They explain this by stating that ‘good theory is fundamentally the result of rigorous methodology and comparative multi-case logic’. The ideology behind this says that it is always better to study two cases than one, if possible, since the chances of doing a good case design will be better than by doing a single case (Fletcher and Plakoyiannaki, forthcoming).

Another approach is called a single case approach. In qualitative case study, single case studies are appropriate in certain conditions. A case may be argued to be a “critical case” which means that the established theory could be tested and found valid, or invalid based only on the study of the particular case. Single case studies are also relevant when they are considered unique and rare, or when extreme situations create unique access to a case where there has not been an opportunity to study the phenomenon before (Bengtsson et al., 1997). Fletcher and Plakoyiannaki (forthcoming) write that one case is enough to generalize, not a population, but analytical generalization to theoretical propositions, based on a real world discovery. Where a phenomenon is in question, only a single case is required to show that the phenomenon does exist.

To answer the positivistic thinkers and the more-the-better logic, there are authors who recognize the importance of a single case study design and argue that the benefits of a single case study far outweigh its drawbacks. Both Dyer and Wilkins (1991) and Siggelkow (2007) propose that the purpose of case study research is to generate deep contextualized insights of the investigated phenomena, and this is best done by a single case study design that constitutes the optimum form of case study research.

A third approach is called a positivistic approach. Yin (2003) identifies six different types of case studies, which consist of three different case study methods: exploratory, descriptive and

explanatory (causal). Each of these three case studies can be made on two levels, depending on if the study is based on one or multiple case studies. Yin defines the multiple-case study method by saying that the cases should replicate each other.

In exploratory case study, fieldwork and data collection are undertaken prior to the final definition of the study question and the generation of the hypothesis. It is typical in exploratory case studies that the research follows intuitive paths of thinking, and therefore can be perceived by others as sloppy. However, the goal may justifiably be to discover theory by directly observing a social phenomenon in its specific form. The exploratory case study has been considered a prelude to social research, because according to Yin, researchers commonly decide to assume another form of study (other branch of research methods) although starting the study with the case study method (Yin, 2003).

Descriptive case study method can be used when description is the main objective of the study. In this form of study, the theory is important in determining the priorities for data collection. “Let’s collect information about everything” is not an effective way of proceeding with the study and the descriptive theory helps the researcher to limit the study’s scope. A descriptive case study is not an expression of a cause-effect relationship, but rather a theory that covers the scope and depth of the case being described (ibid).

In explanatory case study, the phenomena are so complicated that it is not possible to study them with traditional survey methods. The theory in explanatory case study is useful if it helps the researcher to produce an adequate explanation for the observed phenomena. The target of explanatory case study is to develop or create theories that explain the observations made by the researcher (Ryan et al., 1992). Explanatory case study is interested in the causal relationships (or the mechanisms behind them) of the complicated real life phenomena. It can provide the researcher with a very deep understanding of an event, and helps in the summation of what is known about the object. It also aids in seeing the studied phenomena in its context and in a historical perspective (ibid).

Yin (2009) states that explanatory case studies best deal with “how and why” questions and use deductive logic to test propositions, revise existing theories and establish causal relationships. This means that explanatory case studies are also well-suited to not only discover, but also verify new theory, and the theory produced by the explanatory case study is suitable to be used in the future research. The target of explanatory case study is to develop or create theories that explain the observations made by the researcher (Ryan et al., 1992, 115).

Welch et al. (2010) introduce a positivistic approach to case study, called inductive theory building. The proponents of this method identify the main potential of this approach in the capacity to build new theory from the empirical findings of the study. The main aim of inductive theory-building research is to propose associations between constructs and variables that can be tested. According to this approach, case studies cannot provide law-like generalizations, but they can create the theoretical statements upon which large-scale quantitative testing is based (Welch et al., 2010).

Even though inductive theory building cannot build new theories itself, it has a great potential to inspire the research field with new ideas and can be a valuable starting point for new research. Inductive theory building also plays an important role in sharpening or questioning existing theories. It can be done by pointing out the gaps and beginning to fill them. Inductive theory building can also be used as a valuable tool in illustrating a phenomenon. By doing so, the research can illustrate how the theory works in the real life, removes the speculations of the underlying factors of the study, and thus eliminates remarkable shortcomings of the purely conceptual arguments. By illustrating the phenomenon with an inductive theory building case study, this often makes the study easily readable and more illustrative for the reader, and therefore also a powerful tool for the researcher in enhancing the study. According to the inductive theory building approach, a case study does not eliminate the need for the theory to stand independently, but rather together with the solid theory it builds a great combination of interesting illustration and credible justification for the arguments (ibid).

Dubois and Gibbert (2010) introduce a deductive approach called “natural science model”, which also includes a strongly positivistic view on research. Four criteria are commonly used in the natural science model: construct validity, internal validity, external validity and reliability. Construct validity refers to the extent to which a procedure leads to, and accurate observation of reality, and the quality of the conceptualization of the relevant concept. Internal validity refers to the presence of the causal relationships between variables and results. External validity is grounded in the intuitive belief that theories must be shown to account for phenomena not only in the setting in which they are studied, but also in other settings. The last criteria ‘reliability’ refers to the absence of random error, thus enabling subsequent researchers to arrive at the same insights if conducted along the same steps again. This goal can be best achieved with enhancing transparency and replication throughout the whole study, by careful documentation, clarification of the research procedures and by producing a case study protocol. Replication can be accomplished by building a case study database – a database that includes the case study notes, documents and narratives collected during the study (organized in a way to facilitate retrieval for later investigation) (Dubois and Gibbert, 2010).

The fourth approach is called an idiographic approach. Welch et al. (2010) introduce the idiographic approach with the name “interpretive sense making” that seeks to understand the particular, rather than generate law-like explanations. The idiographic approach to case study often rejects positivistic approaches and emphasizes the uniqueness of the social sciences, in which subjects ascribe meaning to their own behavior and researchers are part of the world they study.

The importance of the case study is heavily weighted toward understanding the phenomenon, not simply describing it. Particularization is emphasized instead of generalization and the deep understanding of the uniqueness of the phenomenon and embracing of context, narratives and personal engagement on the part of the research, is usually pointed out in the study. The idiographic approach aims to giving a 'thick description' of the phenomenon, which can be understood as an appreciation of how the social context fulfills the human action with meaning (Welch et al., 2010). The idiographic approach to case studies also often contributes especially by providing new and unexpected insights and by building new theories and concepts. These types of contributions are often based on an in-depth understanding generated by thick descriptions and time-consuming studies of the uniqueness of the study, which should result in new insights (generally it is not enough just to verify established theories) (ibid).

The fifth approach to case study is called critical realism. Roy Bhaskar (Welch et al., 2010) introduces a method of case study called “contextualized explanation”. This approach to case study is distinct from the other methods of theorizing, as critical realism forms the ontological basis for this method. Critical realism holds that the explanation for social phenomena is both casual and interpretive, and thus combines the philosophical bases of positivism and hermeneutics. In other words Bhaskar provides a possibility to reconcile the explanation and understanding of the phenomenon. Causal explanation lies in understanding the constituent nature of objects, or what objects are capable of doing. Causal explanations are developed not by collecting observations, but rather by digging beyond the field of the observable to understand the necessity inherent in objects and theorizing them more as a process of conceptualization than discovery. When explanatory accounts are necessarily context-bound, this presents a contextual explanation - an escape of the explanation/contextualization trade-off. There is no need to contextualize every event, but contextual explanation is a way of explaining an event or phenomenon 'without laws' and enables a wider and freer explanation of the researched matter (Welch et al., 2010).

5.4 Comparison of the different case study approaches and their outcomes

The selected approach to the case study crucially influences the entire case study process, and especially the findings and the theorizing that arises from those findings once the research is concluded. Naturally, this leads to the fact that also the evaluation and the quality of the study varies dramatically.

Also, the analysis stemming from the data in cross-case and case study method varies significantly. In the cross-case method, the goal is to prevent a researcher from making premature or even falsified conclusions, based on limited data. This can occur when the researcher is overly influenced by the vividness of the data or by more elite respondents, and thus ignores basic statistical properties. To perform the cross-case method properly, the data must be analyzed and compared in several different ways. Tactics for this varied approach to the analysis include selecting categories or dimensions, and then looking for the within-group similarities coupled with inter-group differences. In identifying the dimensions, they can be selected by the researcher, or dictated by the research problem.

The researcher can also select pairs of cases and then list the similarities and differences between each pair. This tactic forces researchers to look for the subtle similarities and differences between the researched cases. A third tactic in preventing falsified outcomes of the research is to divide the data by source. For example, one researcher works with the interviews, another combs through observational data, while a third takes responsibility of the questionnaire evidence. This 'data triangulation' approach leads to the separation of the analyses of qualitative and quantitative data, and exposes the unique insights possible from different types of data collection (Eisenhardt, 1989).

With respect to the case study method, one possibility for the researcher is to enhance the internal validity, generalizability and theoretical level of the case study to tie the emergent theory to existing literature. This is particularly important in theory-building research, because the findings of the case study often rest on a very limited number of cases (ibid).

A strength of theory-building from cases is the high likelihood of generating novel theories. Creative insights often arise from the juxtaposition of contradictory or paradoxical evidence. The emergent theory can also likely be tested with constructions that can be readily measured, and hypotheses that can be proven false. Measurable constructions are likely because they have already been measured during the theory-building process. The resulting hypotheses are likely to be verifiable for the same reason. Another strength of theory-building from cases is that the resulting theory is likely to be empirically valid, because the theory-building process is so intimately tied

with evidence. This leads to the resulting theory to be consistent with empirical observations, thus very closely reflecting reality (Eisenhardt, 1989).

Dubois and Gadde (2002) write about sample size in case study research as relative and dependent on the purpose of the study. This view is often considered as a ‘depth versus breadth’ dilemma, where case researchers have to choose between multiple, or single case study designs. Welch et al. (2010) made a large-scale comparison of different approaches to case study. To do so, they used research materials from 199 different kinds of case studies in the field of international business during a ten-year period. The four methods, which the researchers themselves introduced, are positioned in relation to each other on the basis of emphasis on casual explanation and/or contextualization. The next comparison goes deeper in specifics of each approach and will give an understanding of the main differences of the effect of the approach selection to the case study and its results (Welch et al., 2010).

Case studies made according to inductive theory-building approach are fully positivistic in their assumptions and identify their theoretical contribution as exploratory. This approach is the most diverse of the four, and in particular the articles differed in the extent of theory development that was reported to have occurred prior to entering the field. In this approach context is a feature, but not as a means of providing explanation and rich process data of these studies usually does not translate into process theorizing (ibid).

A common conclusion to inductive theory-building case studies is the standard warning to the readers about the lack of generalizability due to the nature of small-N studies and the context-specific nature of the findings. Compared to inductive theory building, natural experiment shares many of the basic principles of positivistic approach. The main difference is that when the researchers using inductive theory-building approach identify their theoretical contribution as exploratory, the researchers using the natural experiment approach positioned their theoretical contribution as theory-testing. This means that the researchers provide rival explanations, or apply an established theory in their research.

Also the language used in the natural experiment studies is more precise and pronounced compared to the language in inductive theory-building articles. Researchers using the natural experiment approach take care of selecting the naturally occurring conditions that were the most appropriate test of the theory given, and the researcher cannot control the environment. Moreover, context is de-emphasized or even isolated by the researchers, when they issued the generalizing claims and provided context-free models as their contribution (Welch et al., 2010).

Researchers using interpretive sense making approach are generally clear expressing their philosophical stance (interpretivism and/or social constructivism) and their rejection of positivist assumptions. Compared to positivistic methods (inductive theory-building and natural experiment) a distinct and clear approach to reflecting on and representing the theorizing process is more common among the researchers of this approach. Generalizability of the theories is often not discussed or even rejected explicitly. In many cases the theory and evidence were interwoven throughout the paper, in keeping with the belief that theory and observation cannot be separated. These researchers tend to use narratives in a deeper way than just descriptions – they have explanatory purposes in answering key questions of the research. The researchers using this approach to case studies also tend to include themselves as a part of the context, rather than taking an objective stance, and some (especially researchers adopting a social constructivist approach) even examine their own sense making (ibid.).

The last of the four approaches to case study introduced in the article of Welch et al. (2010) is contextualized explanation. The researchers following this approach mostly do not reveal their philosophical assumptions, but some do explicitly obey the traditions of critical realism, while others vary between social constructivism/interpretivism and mild positivism. In these studies the researchers tend not to separate theory building from theory testing. The theorizing process goes from one extreme (directly challenging an established theory); to the other (deductive approach in combining insights from existing theories), and many examples fall in between, recognizing both inductive and deductive elements in theorizing. In general, researchers of this approach are more open about the explanatory aims of their research. In the studies, the language represents a very particular view of causality (in the critical realist tradition) as a complex and dynamic set of interactions, which are treated holistically. In the papers using contextualized explanation as their approach, the context is seen as a necessity, not a problem, in constructing rich explanations.

Differentiating from the other approaches to case study, only contextualized explanation holds promise in that it offers a high degree of contextualization without sacrificing the goal of causal explanation. This approach bases its main value on its different view of how to generate theories about social world – explaining it ‘without laws’ (ibid.).

6. Empirical Analysis

This thesis studies the phenomenon of internationalization of manufacturing SMEs, and asks “how SMEs establish a production unit abroad, especially in Russia” and “what are the major challenges and risks concerning this process?” The research also asks “what are the company’s key resources in achieving its goals in this internalization process.” This thesis’ empirical analysis consists of a case study about internationalization and opening production units in Russia.

This thesis applies single case study method where three different case companies are studied in all, with Profima Emkost as the critical case. The other two companies are studied to give additional insight into the understanding of the internationalization process to Russia, the results of which are reflected within the theoretical framework. Using a constructivist approach, cases are studied practically and their particulars are observed in order to gain a profound understanding about the cases, and then compare them against the theoretical background.

The first two cases feature two companies, Hankitek SPb and Profima Emkost, both either partly-owned or fully-owned by Hannu Kiljunen from Finland. Profima Emkost specializes in producing stainless steel tanks for different industrial uses. Predominately, this case study focuses on Profima Emkost’s process of opening a production unit in Russia. Since Hankitek SPb and its CEO Kiljunen are vital to this internationalization process, the parent company Hankitek SPb is included in the study as well. The third case of the study is a Finnish-owned family company SGN Group, which internationalized to Russia in 1995. With the results and information of the case study about the process of establishing a production unit in Russia, a model for establishing production units in Russia is established.

6.1 Interviews

This study uses a constructivist viewpoint as the preferred research method. As qualitative studies focus on understanding a case in its own setting, a constructivist method fits this study because according to Wigren (Christnsen and Poufelt 2006, 159), entrepreneurship is dependent on its cultural-historical context. The goal of the interviews was to have a free conversation about the subject, and open-ended questions were used to help guide the conversation (see Appendix 1.). I interviewed Hannu Kiljunen, the General Director and majority owner of Hankitek SPb, and full owner of Profima. The first interview lasted about four hours and was carried out in the office of

Hankitek SPb. After the interview we visited Profima's factory, completed a tour of the site and spoke for an additional thirty minutes, during which I asked Kiljunen some additional questions about the factory. All of the interviews were recorded and transcribed.

Two executives of the SGN Group were also interviewed. The first interview was with the General Manager of SGN Group, Sam G. Nieminen, and the second with the General Manager of OOO Sumeko, Sergei Yakimets. Both of these interviews lasted about two hours. The goal was to gather all information needed about the internationalization process and operations (focusing on international ones) of SGN Group. The interviews were also based on open-ended questions and dialogue (see Appendix 1.). The respondents described the internationalization process, as well as the history of all international activities until the present. Both of these interviews were recorded and transcribed for further reference.

6.2 OOO Hankitek SPb

Hankitek SPb (thereafter "Hankitek") provides full mechanical services and equipment installation for commercial and industrial needs. As mechanical engineering contractors, the company specializes in heating, ventilation, air conditioning, comfort cooling, plumbing systems and building management systems. The company has experience in all aspects of mechanical contracting works, including design, installations, commissioning and start-up services and guarantee and comprehensive maintain services.

During its existence, the company has worked on many prestigious projects involving complex water, air and heating installations for industrial and commercial projects in Saint Petersburg, Pskov, Ekaterinburg, Tver and Surgut. Hankitek is a full-service company, providing services from initial planning and estimation to completion. With its vast experience, highly qualified staff and quality products, Hankitek guarantees long-term operational integrity and efficiency of the equipment and installations. Hankitek's philosophy is based on the priority to satisfy the customer's needs by providing outstanding quality, reliability and performance.

6.3 Profima Emkost

Profima Emkost (hereafter "Profima") manufactures storage tanks made from stainless steel, and began its operations in Saint Petersburg in 2002. Considering constantly increasing competition,

Profima aspires to achieve its main targets: maintaining the tradition of high quality and the prestige recognized by the most demanding clients, and making production competitive for a wide range of customers. For example, Profima uniquely serves the dairy industry as manufacturers there have extraordinary compliance requirements for technology and hygiene of their products. Big players in this industry such as BMJ Division and Tetra Pack have praised the high quality of Profima's production performance.

The three main product categories of Profima's production are food equipment, chemical processing equipment and tank equipment for other industries. The stainless steel food equipment provided by Profima covers food industry branches such as brewing, and milk, wine and juice manufacturing. Profima produces more than twenty different kinds of food equipment, including tanks for gathering and storing milk, partial-capacity refrigeration, advanced milk processing, and auxiliary equipment for tank sanitation, pipeline components and tare. Profima also supplies tank equipment for the chemical industry that is used in chemical production and washing. The company also delivers a full range of tank equipment for other industries including: CIP washing, tanks with cooling systems, container and metal thermoses, metal tanks, blender devices, numbering and cube tanks, pressure sensors, temperature sensors, level sensors, samplers, motor-reducer, thermos and coils.

6.4 Development of Hankitek and Profima

Hannu Kiljunen began working at Böge Larsen in 1983, in a then Leningrad-based filial of the company, specializing in climate control planning and installation. Kiljunen moved back to Finland in 1989 to continue his studies and in 1992 began working for the same company in the city of Surgut. After 11 months, Böge Larsen offered him work in Saint Petersburg. In 1999, the Finnish owners of Böge Larsen sold the company, and the new owners held that maintaining operations in Russia was no longer strategically appropriate. Before this, Kiljunen had already considered starting his own company with his long-term colleague Vladimir Travin. When the news came of Böge Larsen shedding the Russian business, the two colleagues seized the opportunity and together established Hankitek, splitting the ownership 70/30 with Kiljunen holding the majority share. Even though Kiljunen started this new company from scratch, the new owners tried to fully leverage their learnings from experience with Böge Larsen. At first Hankitek mainly worked with climate control system installation, but soon expanded to establish their own climate control design department after finding no trusted design partners in the field. Kiljunen and Travin successfully developed the business from approximately a half million euros in 2000 to over three and half

million euros by 2009. Hankitek currently has 62 employees, nine of them working in the climate control design department, and 36 in charge of installations. Four employees, including Kiljunen, are responsible for managing the company, and the remaining handle sales, accounting or administrative work.

Finnish entrepreneur Kyösti Karlsted started Profima by establishing a factory in 2002. Four years later, following the bankruptcy of Fimatec Oy, Profima's Finnish parent company, Karlsted, a friend of Kiljunen's and former owner of Fimatec Oy, suggested Kiljunen to acquire the factory. After agreeing on the conditions, Kiljunen bought the business and assets of Profima in 2006, thereby establishing the new company Profima Emkost to continue Profima's old operations.

As Profima Emkost assumed Fimatec's debts from the bankruptcy, Kiljunen first took out a loan to cover these payments. He immediately changed the factory management and renewed all of the company's necessary operational certificates. In all, the process of acquiring the business, including due diligence, renewing the management, organizing the financing, paying of debts and reorganizing the business, took about three months. A lawyer helped Kiljunen negotiate with all the creditors to relinquish the interest on all of the debt payments, thus making the debt burden significantly smaller. For the company's start-up and internationalization processes, Kiljunen organized financing through Finnvera, a Finnish state-owned financing company specialized in financing Finnish-owned SMEs.

With the help of a new, trusted factory manager with whom Kiljunen was already familiar, the company started operating more effectively and soon reached the plant's existing maximum capacity for stainless steel tank production. After this, Profima's significant growth potential was clear to Kiljunen and he soon started looking for larger, more suitable locations for a new factory. In October 2010, Profima moved from the old 800m² factory to a new, nearly 2000m² factory approximately eight kilometers from Saint Petersburg's city center. The new premises allowed Profima to produce considerably more stainless steel tanks, hire ten more employees, and keep the factory open six days a week. Kiljunen stated that depending on the size and purpose of the tank, it takes two employees on average a week and a half to four weeks to manufacture one tank. Now the factory is running one shift and Kiljunen says that a logical way to increase the effectiveness of the factory would be moving to two shifts. Dmitri Kiiski, the commercial manager of the factory, stated that Profima will produce at least 80 tanks in 2011, but does not find the yearly production of 100 tanks impossible either. In the old premises, the quantity of the produced tanks was remarkably smaller.

Since Kiljunen already had experience in working in Russia, he knew the risks and caution needed when taking over a company's business. Kiljunen stated that he did not face any notable setbacks during the process, but he mentioned that in a couple of cases concerning the former debts, the sum turned out to be bigger than he expected. He also did not think that the process included steps that proved to be easier, less expensive or faster to accomplish than he had estimated. Kiljunen's vast experience, knowledge, thorough planning and calculation helped him complete the takeover process smoothly. Regardless, Kiljunen stressed that a comprehensive investigation of the business should be carried out in acquisitions of any kind in Russia.

6.5 SGN Group

SGN Group is a family business, founded in 1933 by Sven G. Nieminen. The company is operating mainly in Finland, but already nearly 30 percent of its net sales come from foreign markets. SGN Group operates in Russia, Kazakhstan, Belarus and Baltic states, with Russia currently as the most important foreign market of the set by far.

Sven G. Nieminen founded an import and wholesale business for plant seeds in 1933 despite having no prior agricultural experience. As Finnish agriculture was undergoing a period of strong growth after the Depression there was a continuing demand for high-quality seeds, and trading relations with European seed merchants were established as early as the 1930s. A significant part of the Finnish seeds trade was soon conducted through Sven G. Nieminen.

During WWII, Sven G. Nieminen served as a Finnish seeds trade agent assigned by the Ministry of Supply; in practice his company assumed responsibility for the supply of agricultural seeds for all of Finland. During the reconstruction period, operations focused on the import trade, and business activities were expanded to grain processing machinery in the 1950s. This was followed by the addition of gardening machinery and recreational products in the 1960s, and then industrial equipment and components were added in the 1970s. A strong trust in partners and extensive cooperation networks helped Sven G. Nieminen create new businesses. In the 1980s a generational transition occurred when Sam G. Nieminen, son of Sven G. Nieminen, joined the business and eventually assumed leadership.

An entrepreneur-based sales network was established in the 1980s to support the operations of new business areas, namely the import of farming machinery. Significant reforms were carried out during the recession of 1990s, which enabled new growth for the company. Operations in the

neighboring Baltic States and Russia were started in the mid-1990s. The trade in sports products, initiated in 2006, was a natural step forward for SGN Group in looking for new business areas.

The traditional and sustainable growth of SGN Group operates in cooperation with independent dealers. The employee respect, customer orientation and the continuity of operations are the values on which the Finnish seed supplier has grown into a recognized and respected Group focused on the wholesale of international branded products.

Table 4. Summarizes chronologically the main phases of SGN Group's development from the 1930s through 2011.

Table 4. – The key development phases of SGN Group

<p>1933 - S.G. Nieminen Oy established.</p> <p>1938 - S.G. Nieminen acquires distribution for Ginge machinery.</p> <p>1950 - Importation of Damas seed and grain processing machinery begins.</p> <p>1963 - Sumeko Oy established.</p> <p>1965 - Importation of Kawasaki motorcycles begins – expansion into recreational products.</p> <p>1970 - Importation of Spraying Systems nozzles begins.</p> <p>1983 - ‘SGN-tekniikka’ trade name adopted for operations related to technology importation.</p> <p>1986 - Agritek Oy is established – expansion into farming machinery and the tractor trade.</p> <p>1992 - Agritek Oy acquires distribution for New Holland tractors.</p> <p>1993 - Sumeko Oy starts representing Harley-Davidson.</p> <p>1997 - Sumeko Oy acquires distribution for Arctic Cat snowmobiles and Derbi mopeds.</p> <p>2000 - SGN acquires Tuko Gardenia; Garden and scooter sales depts. moved to Kerava, Finland.</p> <p>2001 - The distribution for Case IH tractors is transferred to Agritek Oy.</p> <p>2003 - OOO Sumeko, a subsidiary of Sumeko Oy, is established in Saint Petersburg.</p> <p>2004 - Sumeko Oy acquires Piaggio, Gilera and Vespa moped and scooter businesses.</p> <p>2006 - SGN Group acquires the Sportia wholesale business (trade in sports products).</p> <p>2007 - A holding in the Bike Planet bicycle chain is established.</p> <p>2008 - New office building for the SGN Group is built.</p> <p>2008 - SGN Group acquires the business of Truebell Finland Oy.</p>

2010 - New product group is established: Griino fertilizers.

2010 – Recreational product retail shop (outlet) OOO Motopride established in Saint Petersburg.

2011 - The distribution for Aprilia-motorcycles begins.

By 2010, SGN Group consisted of 11 active companies, had 175 employees and net sales of approximately 188 million euros. The development of SGN Group's turnover from the last years is shown in Figure 2. and employee counts in Figure 3. The owner-CEO Sam G. Nieminen states that the equity ratio should be high at all times, definitely over 50 percent, but preferably 60 percent or more (Figure 4.). This stems from the values of the company, as securing the continuity of the business has always been one of the core priorities and values of SGN Group.

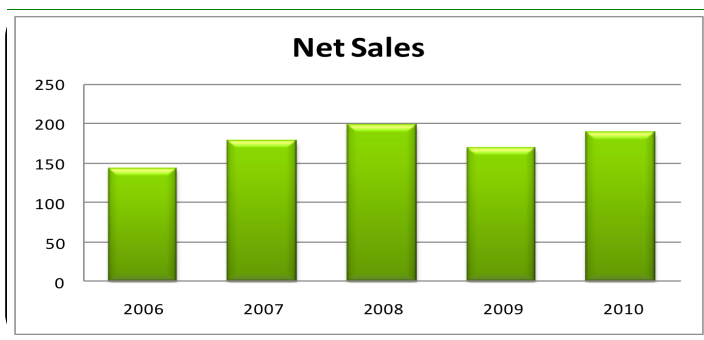


Figure 2. The net sales of SGN Group

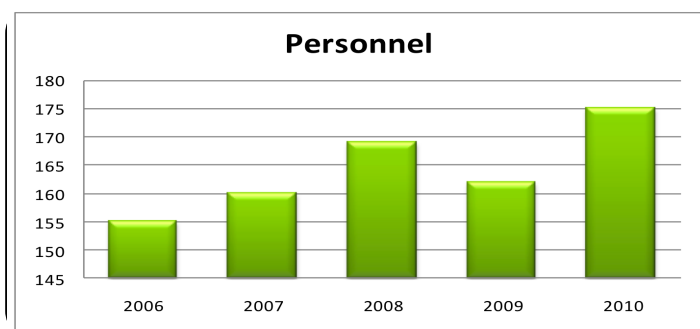


Figure 3. The number of employees in SGN Group

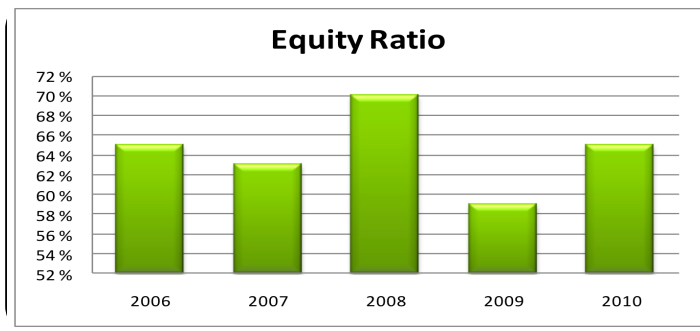


Figure 4. The equity ratio of SGN Group

SGN’s vision is to be the best supplier to their partners, and the best choice for international companies in managing their wholesale business in SGN’s specialized areas in Finland and neighboring countries. In addition to the continuity of the business, the other main values are customer orientation and staff appreciation. Nieminen states that customer satisfaction is reached through motivated and professional staff that is satisfied with their work. “We take good care of our staff and show them respect and appreciation for their work” states Nieminen.

6.6 Internationalization processes and challenges of the case companies

Kiljunen considers that good and reliable business partners and managers are the key resources and cornerstones of internationalizing to Russian markets. It is extremely difficult and risky to establish a business in Russia without a local key person involved. He states that it was crucial that a Russian was engaged and acting as a reliable business partner in running the business. In many situations, it is the highly qualified local partner who understands the Russian culture, business practices and interaction habits better than anyone (Parikka, 2010). Since Kiljunen is the majority shareholder in Hankitek he makes all final decisions, but nonetheless always listens to the suggestions and opinions of his local business partner.

Regarding the most important challenges of the internationalization process and operating in Russia, Kiljunen states that the hardest task is finding good and trustworthy employees that are engaged and motivated by their work (Anderson et al., 2001). Especially talented professionals in industrial handcrafts, such as welders and sheet metal workers, are exceedingly difficult to find. This is the main reason why Profima has yet to add a second shift of production. In the tank manufacturing process, there are several critical phases that must be done correctly on the first attempt, to which only the most capable workers can be entrusted.

For finding qualified employees, Kiljunen sometimes uses headhunters or otherwise turns to his personal network (Coviello and Munro, 1995). Kiljunen evaluates employees by their professional knowledge, character and ability to fit into the company culture. He finds that a person's nationality does not play an important role, and with the exception of one Finnish employee Profima employs only Russians. Hankitek has several foreigners working in the company, mostly from former Soviet Union countries and one from Austria. Kiljunen gladly employs Finns, but does not prefer them to employees of other nationalities. He states that when a person is highly qualified, salaries are equal and nationality does not factor into compensation. However, as the business language in his companies is Russian, there is no special need for foreign employees. Kiljunen himself handles communications with all Finnish suppliers of his companies.

Kiljunen characterizes that Russians generally want to be led and instructed with great detail. The Western culture of independent decision-making does not work well in Russian business culture. Specific managerial skills are therefore vital in operating in Russia, as well as for establishing new businesses there.

According to Kiljunen, the second most notable challenge is the issue of trust (Shirokova et al., 2011). Also, Rimskiy (2011) stated that interpersonal trust is low in Russia, thus validating Kiljunen's observation. Kiljunen states that even though his employees are loyal and hardworking, he personally wants to be in control over the business. According to Kiljunen, it could be possible to entrust the company management and control to someone who he really trusts, but he still finds it more comfortable to personally control the employees and the business (Shirokova et al., 2011). Trust is even more crucial when working with new companies, especially if no long-term relationships exist with key contacts. Kiljunen states that when some people are left to work with loose control they might do something 'tricky', or something detrimental to the company. Regarding tricky behavior, Kiljunen gave an anecdote where the former development manager of Profima decided to increase the vacation for all the workers at the factory without consulting Kiljunen. During his long work career in Russia, he has also heard or witnessed first-hand many cases of the misuse of trust, and once suspected an employee of committing fraud.

Kiljunen finds the role of networking in the internationalization process as well as operating in Russia important, especially in the customer sector (Johanson and Matson, 1998; Coviello and Munro, 1995; Wright and Dana, 2003). He states that since uncertainty is normal between different players in the market, the long-term relationships where companies have developed mutual trust into each other are highly valuable. These kinds of networks can develop into partner-like relationships with other companies, which can be of great support to both parties and provide stability. Kiljunen also states that he uses his own networks, as well as those of his employees, in

gathering market information and headhunting. In some situations though networks can also be a burden to the company (Coviello and Munro, 1995). Kiljunen mentioned that especially in the past, Russian customers tended to opt for long-term customer relationships in order to get free benefits, such as complimentary guarantee services several years after the guarantee period had expired.

Kiljunen states that his long-term contacts have helped his company in getting some very notable contracts, such as those ordered by the government. For example, Kiljunen negotiated a sizeable planning deal with the government through a seasoned architecture office that guaranteed the high quality of Profima's work. In the same project Kiljunen also came into a deal of climate control installations through a Russian army General in charge a local construction company owned by the army. Kiljunen knew the General from his days at Bøge Larsen and stated that this particular contact "opened the door" to a notable deal, which would have been practically impossible to get without such networks.

Kiljunen points out that especially in the business of producing goods, customers can cause two major risks. The first risk is payment issues, which is one of the most typical risks and challenges in SME internationalization (Anderson et al., 2001). The second risk is related to the customer behavior and uniqueness of the produced goods. Kiljunen states that in the tank producing business two orders are never alike, and all of the tanks are made according to customer requests. A few important customers can sometimes place such difficult conditions onto orders that they become difficult to deliver, and therefore risky for the manufacturer.

As an example Kiljunen mentioned one order placed by a major beer manufacturer, in which advance payment was fully excluded and the payment term was fifty days after the delivery. Kiljunen states that the risk in this case was not so much tied to credit, but rather the customer commitment and obligation fulfillment. "We refused to take the order and heard afterwards that one of our rivals, who took the deal, remade the tanks several times because the buyer changed his plans during the process" Kiljunen states. The tanks are manufactured according to the specific measurements and for this reason it is possible to only make very limited modifications to the tanks. In most cases, if any changes are needed the tank must be remade entirely. In that kind of troublesome situation the manufacturer has to decide whether to manufacture the new tanks at their own expense, or refuse the change and suffer the loss of the deal and any work done thus far. Either way these kinds of situations cause losses for the manufacturer and at least today the juridical systems in Russia poorly protects manufacturers from contract violations, especially made by "big players". Kiljunen states that already a 5-10 percent down payment makes the buyer much more committed to the project and then this kind of misbehavior seldom appears.

According to Kiljunen, corruption is not a major problem in internationalizing and operating in Russia, at least in the fields of business where he operates. In the past, especially in the 1990s, the situation was different and requests for personal benefits came constantly from not only from civil servants, but also from the representatives of customers. Today, while most of the customers work on the basis of tender, Kiljunen states that corruption happens daily and is part of Russia's current business behavior. This observation correlates with the studies of Shirokova et al. (2011) and Rimskiy (2004; 2011). The few requests for bribes to Kiljunen's business might be due to the fact that he strictly operates his business "by the book" and does not get involved in illegal actions.

In Russia, he says, especially as a foreigner getting into illegal business activities and tax fraud, an entrepreneur is exposed to a continuous demand of bribes and becomes an easy target for blackmailing and other forms of exploitation. Also the risk of getting raided rises if the company gets involved in illegal businesses. Today, Kiljunen states that the only officials who are keen on asking for bribes are the fire security inspectors who visit Profima's factory once a year. Some of them are so aggressive that they constantly threaten to shut down the factory if bribes are not paid. For this purpose Kiljunen hired a work safety manager, who ensures that the factory is running legitimately and who is responsible for the negotiations with government inspectors. When the factory's safety issues are fully in order the inspectors usually lose interest. Instead, they frequent factories that lack in safety measures, which means more personal earn-out possibilities for the inspectors, Kiljunen continues. The summary of the international development of Kiljunen's enterprises is presented in Table 5.

Table 5. *The internationalization process of Hankitek*

In 1999, after Kiljunen had worked in company Bøge Larsen for more than a decade, the company was sold and the new owners decided to end Russian operations.
Together with his colleague Travin, Kiljunen took over the abandoned business and established Hankitek.
After successfully managing Hankitek's business, in 2006 Kiljunen acquired Profima, a company specializing in producing tanks from stainless steel for foodstuffs, chemicals and other industrial purposes.
In 2010 Hankitek employed over 60 people with a turnover of over three and half million euros.

6.7 The internationalization process of SGN Group

SGN Group made its first export sales to Russia in 1995 through its subsidiary Sumeko. Sumeko imports recreational products, such as snowmobiles, all-terrain vehicles, motorcycles and outboard engines to Finland, and at that time also secured exclusive rights to sell a part of these products to Russia. In 1995 Sumekos sales to Russia were conducted through Frankardi, a dealer operating in Saint Petersburg with two shops. This kind of indirect exporting is a typical way to start the SME internationalization process according to the stage models (Kaarna and Mets, 2008). Sergei Yakimets, an employer of Frankardi, was responsible for taking care of the relationship management between SGN Group and Frankardi.

SGN Group's first export products were Arctic Cat snowmobiles and Tohatsu outboard engines. Annual sales grew by about 10 percent each year but essentially came to a halt in 1998 when Russia fell into a deep recession. After the recession, sales started to grow quickly and Frankardi sold a significant amount of products also to its sub-dealers, just as a distributor would operate. The overall economy of Russia and the sales of competitor's products in Russia were growing fast in the early 2000s, and Frankardi started to show signs of reaching its limits of economical endurance. At that moment, SGN, together with Yakimets, started to seriously discuss another opportunity – establishing their own office in Russia and taking care of importing and distribution themselves.

In 2003 an office was established in Russia and Yakimets was the first employee of the new OOO Sumeko, the Russian subsidiary of the Finnish Sumeko. Nieminen states that at the time it was a significant and risky decision. "Most of the international companies internationalized to Russia through their sales offices, but we wanted to fully control the processes of importing and distribution in Russia" Nieminen explains. SGN Group opened the office of OOO Sumeko in Saint Petersburg in a building suggested by the Finnish commerce of trade, which was at that time managed by a Finn and hosted multiple foreign offices of Finnish SMEs. A few months after establishing OOO Sumeko, Yakimets, the main bookkeeper Anna Volkova, and logistic manager Sergei Laiko transitioned away from Frankardi to this new company. Sales grew quickly and exceeded those levels seen at Frankardi. Obviously the owner of Frankardi was upset about losing the distribution-like business, which SGN decided to do on its own.

Starting in 2003, Yakimets began to face personal threats and was even assaulted multiple times, resulting in Yakimets hiring a private security detail. It is impossible to say for sure whether the assaults were intentionally planned by someone, or were unrelated petty crimes. In 2003 Frankardi

harassed OOO Sumeko. Nieminen and Yakimets got a letter from the owner of Frankardi, which stated that the ownership of the Trademark “Tohatsu” is property of Frankardi and OOO Sumeko should pay a stated sum of every Tohatsu product that it sells in Russian Federation. This was possible since Tohatsu Motor Corporation had not registered their trademark in Russia. However, no money was ever paid to Frankardi and the issue was later resolved in court in favor of OOO Sumeko.

Nieminen states that the decision to establish OOO Sumeko in Saint Petersburg came after a seven-year-long relationship with Yakimets, Volkova and Laiko. “They already knew our business, people, premises and way of working, and even more important, there was a mutual trust between us”, “opening an office to the capital city Moscow would have been another potential choice, but we didn’t want to start working with unknown people to us and didn’t have even any indirect experience in working in Moscow” Nieminen states (Shirokova et al., 2011). Besides, the idea of opening a second office in Moscow had been constantly on Nieminen’s mind and it seemed that sooner or later it is going to be desirable, due to the tremendous role of Moscow in Russian business and networking. The summary of the development of SGN Groups international activities is presented in Table 6.

Table 6. *The key phases of SGN Groups internationalization process*

SGN Group starts its internationalization process in 1995 by selling products through a dealer in Saint Petersburg.
In the year 2000, the business development through the dealer grows much less than the markets and SGN Group starts to think about other possibilities to develop its export activities.
In 2003 SGN Group establishes its own subsidiary in Saint Petersburg and employs three key personnel with whom SGN Group has had a business relationship from the beginning of the internationalization process. During this time OOO Sumeko’s business is harassed and CEO Yakimet’s personal safety is threatened.
During the 21 st century the international operations develop constantly, other than a significant drop in sales during the financial crisis in 2009. In year 2010 the international sales represent about 25 percent of the total sales of SGN Group, exceeding over 45 million euros.

6.8 Reflecting the internationalization theories with the empirical study and summary

Since SGN Group is a traditional and mature company working mostly in the wholesale business, stage models are appropriate in characterizing its internationalization process. Stage models work

best to describe companies that internationalize after first maturing in their home markets before seeking more opportunities abroad, and do not take major risks instantly. The internationalization “style” of these companies, such as SGN Group, is rational and even conservative – the internationalization process is slowly developing through successes in the target market, and risk/reward ratios are kept reasonable at all times. When the experience of working in the target market grows, the ability for risk-taking grows as well. Companies with similar characteristics to SGN Group tend not to “bring a knife to a gunfight”, in other words the risks are understood, as is the business actions and market activities that the company is pursuing.

Network models are also appropriate in studying the internationalization process to Russia. Studies show that the role of networks both in professional and persona contexts have a substantial meaning in the internationalization process of SMEs. Since the philosophical gap between Finland and Russia’s approaches to business practices and overall culture is so vast, networks can provide entrepreneurs with support, information and help to decrease insecurity and to grow professional knowledge. Trusted contacts also play a major role in the decision to internationalize, and guide the entrepreneur through the internationalization process.

The study stage and network models developed for this study are more useful than the newer internationalization theories of international entrepreneurship and born globals. This is because existing theories mostly concentrate on the internationalization process of less mature or new ventures. Many of these new ventures, especially those studied in born global research, focus on niche markets and often cannot exist if they operate only in their home markets (due to the need for covering major technology expenses and maintaining the R&D organization for business, etc.). These kinds of companies usually base their competitive advantage on new technological products or innovations, and then end up having limited resources to sell these products to as many markets as possible; a point of difference from the companies I investigated for my case study. Whereas born globals usually want to quickly access many foreign markets all at once, mature companies want to penetrate foreign markets more deeply and focus their resources on a more limited number of target markets. The desire to access many markets quickly (for example, accomplished through simple sales offices and/or local partners), leads to shallow market penetration due to time limitations and lacking resources.

International entrepreneurship theories have a boarder view on the entrepreneurial internationalization process, and thus can provide more usable insights for this case study. Whereas stage models are criticized for focusing more on the company and thereby undervaluing the role of the entrepreneur, international entrepreneurship theories concentrate more on the entrepreneur and the role of entrepreneurship in the internationalization process. Still, SGN Group’s business

competency is not solely dependent on the will and wishes of the entrepreneur. Since the manufacturers have the right to decide which product rights they give to the wholesale company, the entrepreneur does not have the possibility to freely choose his foreign business activities.

The stage models, network- and international-entrepreneur theories provide a rich theoretical background for this study. Referring to the traditional nature of SGN Group and its internationalization strategy, and by taking into consideration the strong local characteristics of the business of the company, stage theories provide the most useful theoretical background for this thesis.

Analyzing the internationalization process of Kiljunen's business is more complicated as he did not internationalize his business in the typical sense. Taken into consideration Kiljunen's long career in Russia and the Soviet Union, it is fair to characterize his business as local already, and he continues to work in his home markets. In Kiljunen's case, both the Finnish and Russian markets can be described as home markets, where his "internationalization process" occurred upon his takeover of Böge Larsen's Russian operations. I find that this process is best analyzed with the network- and international-entrepreneurship theories, emphasizing the entrepreneurial behavior amongst them.

When Kiljunen and his business partner took over the business, by using their business contact networks they successfully retained Böge Larsen former clients, thereby skirting the challenge of developing an entirely new customer base. Through his contacts, Kiljunen was also able to find reliable product suppliers and organize financing for the business takeover, as well as the acquisition of Profima's business.

Acquiring and maintaining Böge Larsen's previous business portfolio is an entrepreneurial act in itself, and as it was done by a Finn in Russia the process can be considered as international. Even though Kiljunen had worked for nearly two decades in Russia and the former Soviet Union, he still holds Finnish markets as "home markets" and Russian markets as "foreign". The fact that he is a foreigner and having been raised in Finland makes a clear difference. The establishment of Hankitek truly seized a ripe opportunity, and Kiljunen can be described as the entrepreneur who strove to take advantage of it. Long before his takeover decision Kiljunen had thoughts about establishing an enterprise, but until then he had decided not to act. Kiljunen stated that it would have been too much of a pity to simply allow Böge Larsen's Russian business to close, and he would have deeply regretted not making the move.

The acquisition of Profima's business was clearly risk-seeking behavior with which entrepreneurs are often characterized. Kiljunen admits the absence of prior experience in the manufacturing business and the tank manufacturing industry. Still, he saw the opportunity to develop the business and was eager to learn how to do so successfully. This kind of daring and willingness to challenge oneself are certainly a part of entrepreneurial behavior.

7. Entrepreneurial and production unit models

Since I did not find any of the SME internationalization models fully capable of supporting the findings of my empirical study, I decided to introduce my own model. Also in this chapter a model of production unit establishment is introduced.

7.1 The Entrepreneurial Stage Model of SME internationalization

Since SME internationalization takes numerous forms and can vary tremendously, as demonstrated in this study, it is unreasonable to suggest any one internationalization theory is best for studying all forms. By analyzing and interpreting the information of this study I designed the entrepreneurial stage model (Figure 5.), which explains the internationalization process of an SME that is a mature or semi-mature company in its home market. The model is less suitable for studying early internationalizing companies, though it emphasizes the entrepreneurs' role throughout the entire internationalization process.



Figure 5. The entrepreneurial stage model of SME internationalization

According to the entrepreneurial stage model of SME internationalization, the target market of the internationalization process depends on the opportunities, skills, networks and strategic choices of the entrepreneur. By opportunities, it is meant those business possibilities and proposals that can come and go, where the entrepreneur can identify opportunities to be seized. While entrepreneurs can systematically seek opportunities, they may also appear unexpectedly. The ability to discover these opportunities and act upon them is a critical part of entrepreneurship, and it is these opportunities that act as catalysts for the internationalization process.

The skills of the entrepreneur include a wide range of capabilities that the entrepreneur then uses to gain information about target markets, and of the business practices within them. Better entrepreneurial skills give the entrepreneur added confidence in the actions within target markets, and allows a higher commitment to those markets. By strategic decision, it means the internationalization decisions that fit the company's overall strategy. In the entrepreneurial stage

model, the engagement to the target market develops through the company and entrepreneur's experiences, development of skills and trust formation. Networks also play a significant role in this process, and according to the model entrepreneurs do not seek the easiest internationalization possibility, but rather that which is most suitable and lucrative. This is why I argue that the philosophical business, practice and culture gap does not play a major role in identifying markets targeted for SME internationalization.

The Stage of Pre-Internationalization is the first stage of the model, where the entrepreneur is still thinking about the potential of the opportunity and whether or not to internationalize, or has already made the decision but is still planning and preparing the process. The entrepreneur in this stage is seeking information about the target markets and its legislation, possible partners and potential customers. The entrepreneur is also activating networks in order to gather information, and planning the management processes of the internationalization action.

In the second stage, Stage of Early Internationalization, the internationalization process has already commenced but the company is unfamiliar with the new business abroad. It is in this stage when the entrepreneur is adapting to the new market, and is learning through trial and error methods. The company is typically working closely with a local partner to mitigate risks, and is gaining more knowledge about operating in the new market and the growth potential there. In this phase the entrepreneur is also considering whether or not to commit to the identified target market.

During the stage three, Stage of Evolving Market Commitment, the entrepreneur feels more comfortable operating in the target market and clearly sees its potential. In this stage the entrepreneur is willing to take on more risk and become more committed with the target market, thus finding new ways how to organize and develop international operations. This stage can be characterized with actions such as establishing more profound co-operations with the local partners, joint ventures and even the establishment of their own office.

High Market Commitment is the final stage of the model. In this stage the entrepreneur already has profound experience and knowledge of the target market, and is willing to take on substantial risk. For this stage establishing their own office abroad and making high investments in the market are typical actions, and the entrepreneur feels more comfortable working within a market similar to their home market. During the fourth stage, the entrepreneur further develops contact networks and advanced skills in working on the market, thus further developing the international business.

7.2 Model of production unit establishment

Several factors and challenges exist when establishing a production unit. This model does not focus on these challenges, but rather the establishment the process itself. The model consists of the most important factors of the establishment process, from the beginning to the point where the factory is operating. The model's use is not restricted only to Russia, and it can be used to describe the process regardless of the market. To make the model accurate in describing the factory establishment process in a market, the specific characteristics and challenges of the market should be known. For example, considering Russia this means that the challenges described in the previous chapter (corruption, distrust, etc.) should be well known and their effects taken into consideration during all the steps of the model.

The steps of the model are not necessarily in chronological order, since many of the steps can be executed simultaneously. The factory establishment process can also differ substantially depending on the volume and type of the goods manufactured in the unit, a difference that is not taken into consideration in this model. This model is an example of the final stage of high market commitment in the entrepreneurial stage model of internationalization, thus assuming that the foreign company establishing a production unit has already internationalized to the target market and has a running organization with profound knowledge of the markets. Using the information of the study, I introduce a model of the process in Figure 6.

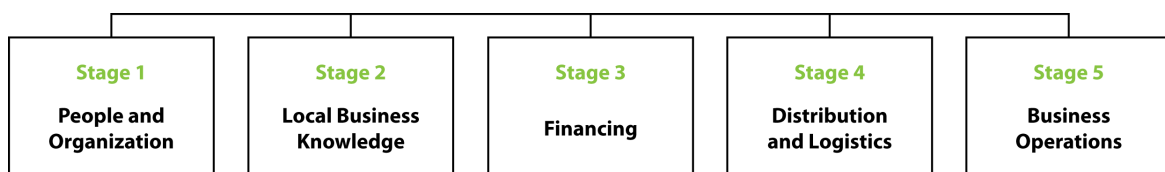


Figure 6. The model of production unit establishment

The first stage of the model, People and Organization, consists of the local organization and manager, which are needed to establish and operate the production unit. Also the local networks of the organization and people are an important factor of this stage.

The second stage, Local Business Knowledge, is tightly connected with the first stage, since the personnel should have a clear understanding about their work, and the managers should be capable of taking control and command of the challenges and processes of the establishment project. The company should as well be aware of the local bureaucracy, laws, utility services and infrastructure

to be able to choose a proper location for the production unit and successfully establish its operations.

The third stage, Financing, has three key factors: minimizing cost, minimizing risk, and maximizing the engagement with the foreign markets. Since the model assumes that the company behind the factory establishment project is of foreign origin, there are two different approaches to this stage. The first approach is to use the financing institutions in the company's home markets or by using only the company's own assets. Since the model also assumes that the company is mature in its home markets, getting the financing can be easier there. Often the company is also capable of securing a bank loan with lower interests in its home market as it has done business there for a long time. It is possible that the company can also receive a security for the bank loan from a state-owned financing institution (such as Finnvera in Finland), thus minimizing its liabilities for the loan.

The second approach is to organize the financing through a local financing institution. Especially in developing markets where the infrastructure is still developing and high risks of economical criminality or unstable political situations might exist, maximizing the engagement with the markets should be considered. In this case the company could decide to use a local financing institution even if it would be of higher costs, in order to involve local institutions on the project. By doing this, the company ensures that local interest groups have a stake in the deal and work to keep it secure. The company should evaluate the situation and risks, and find the best possible solution to finance the project at hand.

Organizing and managing the Distribution and Logistics of the production unit is the fourth stage of the model. Distribution and logistics are of great importance when the company is considering the location of the factory. The transportation of raw materials and components as well as final products should be carefully considered. This stage also includes the building of the distribution network through which the final products are sold. The distribution network and the type of produced goods substantially affect the location and requirements of the production facilities.

The fifth and final stage, Business Operations, consists of the everyday business actions that are required to successfully run the production unit. In addition to personnel management that was introduced in the first stage of the model, knowledge and planning of the factory running and performance are needed to optimize the operations of the production unit. Finally, the ways and principles of how the control of the production unit operations is planned are an important part of this stage.

8. Discussion and conclusions

The purpose of this thesis was to study the foreign SME internationalization process to Russia, and to develop a model for how an SME establishes a production unit. Another objective of the study was to identify the key resources needed to succeed in this process. Since no models currently exist describing the production unit establishment process, I created one using the information gained from the empirical study. This model illustrates how the production unit establishment process is accomplished and the main stages therein. The SME internationalization process to Russia was first studied through existing, popular SME internationalization theories and studies about operating business in Russia. Second, the internationalization and production unit establishment processes were investigated through the empirical study, which included interviews with owners and CEOs of Finnish companies that operate in Russia.

The theoretical framework of this study consists of the main SME internationalization theories and models: stage model, innovation model, network model, early internationalization theories, international entrepreneurship and international business. By studying these theories I developed an understanding of the process of SME internationalization and its challenges, and then moved on to study the specific theme of this thesis, internationalization to Russia and the production unit establishment process.

The theoretical framework considering internationalization and operating on Russian markets clearly showed that the particular challenges for SMEs in Russia are corruption, bureaucracy, legislation problems and enforcement of laws, economical criminality, property rights, management and trust issues. Corruption was found to be the most significant challenge, one from which many other challenges stemmed, thus forming a substantially different operating environment in Russia for Western SMEs compared to their home markets.

The empirical study of this thesis consists of case studies, which were conducted through interviews based on free discussion with the help of semi-structured questionnaires. Altogether, four interviews were completed during two company visits and one factory tour. Some additional and corrective questions were also placed by phone and e-mail. The respondents were Finnish owners or owner-CEOs of Russian companies, working partly or full-time in Russia. Also interviewed were a Russian CEO (without ownership) and a work safety manager.

The single case studies of constructivist approach worked well in this thesis. It provided a deep understanding of the SME internationalization process to Russia, as well as the production unit

establishment process. The most notable weakness of the empirical study was the scarcity of reference cases. It was very hard to find suitable cases for the study, thus limiting the number of studied companies. Due to the lack of existing studies, the generalizing potential of the new models introduced in this thesis is low, and therefore further study is needed on the subject.

The interviews widely supported past studies of internationalizing and operating in Russia, and the study found answers to the research questions posed initially. For instance, practically all of the major challenges of internationalizing to Russia – corruption, bureaucracy, legislation problems, economical criminality, property rights, and management and trust issues – were stated by the respondents. The only major difference between the comparison of theory and empirical study was that the respondents did not highlight the negative effect of corruption as strong as the literature had, nor was it found as an equally large challenge as the former literature indicated. This could be due to the fact that the case study companies are foreign and operating their business in a law-abiding manner, without exposing themselves to abuse or corruption on behalf of other businesses and law enforcement.

The empirical study also indicated that the most suitable internationalization models for studying the SME internationalization process are stage models. Since existing stage models largely ignore the influence of entrepreneurs in the internationalization process, I decided to come up with my own model, the entrepreneurial stage model of SME internationalization. This model is also a stage model, thus it is based on the idea that the company commits to the international target market incrementally through learning and experience. This new model differs from existing ones through its strong emphasis on the capabilities, networks and will of entrepreneurs in the internationalization process. Also, constant learning and experience gaining are at the center of the model and are related to the higher risk taking and implementation to the target markets.

The entrepreneurial factors listed above are the key resources in the success of the SME internationalization process. The entrepreneurial stage model is designed to analyze the internationalization process of SMEs, which are mature or semi-mature in their home markets, and are not suitable for studying internationalization processes of early internationalizing companies.

In this thesis I also introduced a model of product unit establishment process. This model is formed on the case study about OOO Profima Emkost. In this model the process is described, as are the characteristics of the process' stages. The key resources for successful execution of the process are well planned and highly qualified: people and organization, local business knowledge, financing, distribution and logistics and business operations. The model is valid not only for use in Russia, but in all countries. Since production unit establishment can take various forms and has different

priorities depending on the size and type of the unit, the model cannot describe these details, thus functioning as a general tool in describing the basis of the process.

The study has two main limitations. First, it does not concentrate on early internationalizing firms, such as born globals. I came to the conclusion that the internationalization process of the early internationalizing firms differs significantly from similar processes of companies that are mature or semi-mature in their home markets. The theories of early internationalizing firms did not compare with the empirical study either, which is why the entrepreneurial stage model introduced in the study does not apply to early internationalizing firms. The second limitation is the lack of the studied cases. Even though the case study provided this study with the necessary information about the internationalization and factory establishment process, a larger case study is needed to scientifically prove the entrepreneurial stage model's plausibility.

The subjects of this thesis, the internationalization process of SMEs to the developing countries, especially to Russia, and production unit establishment process, are poorly studied subjects. The study introduced new, specific information about these processes and their challenges, but around this theme there are several interesting subjects that would prompt new and important insight to the SME internationalization studies. For example the effects of poorly working administrative systems and political imbalance to the internationalization process of the SME would be an interesting theme to bring the study of SME internationalization forward.

Further research could also analyze the differences in internationalization models and patterns of SMEs, as well as production unit establishment processes could be compared between various industries to gain an understanding about what kind of role the industry plays in these processes. Also the maturity level of researched SMEs could be included in the study to gain an understanding about how the maturity level of an SME influences the internationalization behavior.

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10. Appendix

Interview questions

What made the company to internationalize to Russia?

In which business sectors the company was working in its home market when you started the internationalization process to Russia?

Was the company working in other international markets before internationalizing to Russia and were there any other potential internationalization choices than Russia?

How long did the company work in its home markets before internationalizing and how long did the company consider the internationalization decision?

What all things were affecting the decision-making and what kind of impulses there were for and against the decision?

How did the company execute its internationalization plan? What were the first steps and how did the process continue?

What were the goals of internationalizing to Russia, and how did the company meet these goals (in a short- and long-run)?

Did the company hire any foreign key persons to manage the internationalization process or how was the management organized?

Were there any trust issues during the internationalization process and how did/does the company control its foreign activities?

How big is the role of networks in internationalizing and operating in Russia?

What matters turned out to be the corner stones in the internationalization process to Russia?

Questions solely concerning OOO Profima Emkost

When was the factory established?

How long did the process last, after the establishment decision was made until the moment when the factory was running in full speed.

Did you have a clear time plan for the process and how did you succeed in working according to the plan?

What kind of challenges were you expecting and how did it compare with reality?

Who was responsible of the establishment process and how was the management organized?

How did you control the process and budget?

What were the worst setbacks?