INTERNATIONAL MARKET ENTRY STRATEGIES AND THEIR IMPACTS ON MARKETING IN CENTRAL EUROPE

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Abstract

Cultural differences between East and West have determined the chosen market entry strategies when foreign marketers and investors entered markets of Central and Eastern European countries and the transition toward market economy started. Both parties, e.g. foreign marketers and host country governments had their various motivations when foreign investment and other market entry forms have taken place. The paper discusses the main elements of cultural differences, motivations and expectations that have influenced market entry strategies of foreign marketers and investors in CEC as well as the question how expectations have been fulfilled. It emphasizes the impacts of foreign investment – with a special attention to investment from EU – on the development of marketing environment and the marketing capabilities of firms, especially in Hungary.

Keywords: international market entry strategies, cultural differences, motivations of foreign investors, impact of foreign investment, development of marketing environment, marketing capabilities of companies in CEC countries.

Almost a whole decade has passed from the beginning of radical political, social and economic changes in Eastern and Central Europe (ECE). A decade is a period long enough for looking back and to evaluate changes and impacts of different factors that participated in producing changes. For us, an important question of changes is the progress in transition toward market economy. This paper discusses the motivations, entry strategies chosen by foreign investors and development in marketing environment and marketing capabilities of companies, thanks to their presence in the ECE geographic area, especially in Hungary. This latter question is an important one since some of the countries from this are candidates for becoming members of the European Union.

1. Cultural Differences and Gaps

As a general rule, for international marketers the country's or region's attractiveness can be defined by two important factors: the industrial structure and the income distribution in the different countries or regions. The industrial structure determines what products and services are needed and produced. The income distribution is related to employment level and determines demand and consumption.

Western firms which intended to invest in ECE countries have found a marketing situation very different from that of the developed market economies. *Differences have manifested in many fields, such as in marketing, technology, capital, management, motivation and others* [1]. All of these elements can be considered as those of culture, thus the main cultural differences have been identified by the following gaps:

Marketing gap. In centrally planned economies products were normally distributed, not marketed. Demand was greater than supply. The marketing concept and the importance of customers were almost unknown. Market research was unfamiliar. The distribution channels and the advertising infrastructure were limited.

Technology gap. There exists an important gap between Western and Eastern technologies, especially in machinery, equipment, know-how as well as in the concept of technical standards and plant efficiency. Two or three generations gaps may exist in terms of productivity and infrastructure.

Capital gap. The investment capabilities are much lower in the East than in the West. Western firms face difficulties in finding partners which own capital to invest.

Management gap. It was very difficult for foreign firms to organize effective agents, distributors or partnership with local staff.

Motivation gap. The work force had not much tradition to take initiative or responsibility.

Compared with Western business conditions, other authors emphasize that the main differences have included the weak concept of market regulation. Weak property, exchange and contract laws, no valid price structure, inadequate accounting and managerial skills, poor communication and transportation infrastructure, and lack of familiarity with democratic processes [2] have been present. Despite of the political changes governments still play a major role in the business sector compared with Western countries.

Culture includes every part of life and marketers and investors need knowledge of marketing and business consequences of cultural differences. Foreign marketers need a cultural scheme in studying country attractiveness and market potential of foreign markets. An anthropologist approach, that can be a useful framework for foreign marketers, determines the meaning of culture by the following elements:

1. Material culture including technology and economics [3];
2. Social institutions including social organizations, education and political structure;
3. Humans and the universe, including beliefs systems;
4. Aesthetics including graphic and plastic arts, folklore, music, drama and dance;
5. Language.

The above gaps represent identification of the basic differences in material culture, e.g. technology and economics, as well as in the field of organizational and individual behaviour. According to Usunier's view cultural approach in international marketing includes two principal approaches, e.g. a cross-cultural approach and an inter-cultural approach [4].

A *cross-cultural approach* includes proceeding by comparison of national marketing systems and trade practice in different countries. It has the objective to mark off both the universal part and the specific part of the local culture. This approach is necessary for designing and implementing marketing strategies. An *inter-cultural approach* is focused on studying different interactions. It is important to study interactions between business people (and organizations) that have different cultural bases as well as interactions between products of different cultures (e.g. their physical and symbolic attributes and their national image) and customers having different culture. These approaches are of great importance in the preparatory stage to enter a foreign market and designing strategy as well as in the stage of evaluation of results.

2. Motivations and Opportunities

Before analyzing in details the special motivations of foreign marketers as well as the expectations of ECE countries, a global approach of motivations has to be mentioned. According to certain views international market entry strategies are sometimes motivated by *search for strategic equilibrium in oligopoly type of markets* [5]. International firms may enter a new market motivated by the fact that competitors are already present in these markets. Certain firms would find equilibrium by entering other markets instead. GE's investment in Hungary, for instance, was incited by the need to compensate the loss of US market share. By the acquisition of the Hungarian light bulb manufacturer Tungsram, GE has bought European market share. The same reasons have motivated the investment of Suzuki in Hungary. It had opted for investing in Hungary because it found competitors too strong on other markets.

Literature is almost unanimous in the opinion that despite of the explained gaps, former socialist economies represented both *a marketing and a low cost manufacturing opportunity* for Western investors [6]. On the

other hand, ECE countries have expected, without exemption, obtaining industrial and managerial know-how in order to upgrade their manufacturing facilities and infrastructure. Hungarian economists have anticipated capital import to cover shortage in capital and to promote economic growth, technology transfer as well as transfer of management skills, and the contribution of foreign capital to the improvement of export capabilities [7]. One may assert that also these expectations have reinforced opportunities and encouraged Western firms to profit here from the opportune moment.

Marketing opportunities in the ex-socialist countries have been marked by a long list of industrial products needed for developing economies: such as computers and telecommunications, machine tools, electronic process control, packaging and processing equipment, environment pollution control equipment. The list can be continued by other product categories, such as chemicals, pharmaceuticals, medical equipment, agricultural machinery, construction equipment, project management assistance, and so on. Significant opportunities have been open for the service industries such as financial service, auditing, tourism, hotels, and so on [8]. The demand of financial services has been important due to the need to support Western marketers and investors, as well as to work together with government organizations in privatization of state owned firms.

As far as consumer products are concerned, they have required minimal adaptation for sales in Eastern Europe. A great majority of customers have been familiar with Western brand names, so they could be retained. Marketers have found that customers can afford not only the less expensive products in the line. A new upper class has an important demand for quality products as well as for luxury goods and services.

However, one should not forget that opportunities in product markets and the pace of progress toward market economy differ from one country to the other. CEC countries can be devised at least into two groups: those that are adjusting more rapidly to market economy (Hungary, Czech Republic, Poland) and the rest of the region that is adjusting more slowly. Hungary remained the country most favourably disposed to foreign investment.

Foreign investors had to adapt their strategies to the situation they found in the countries they enter. Motivations of investors in Hungary are shown in the *Table 1.*

3. Market Entry Strategies

Market entry strategies have included three basic elements that are related to three questions: What form of market entry has been chosen? What was the timing strategy? What form of participation has been preferred? The main entry forms included exporting, licensing contracts, joint ventures and subsidiaries.

Table 1. Motivations of foreign investors in Hungary

Motivations/intensity of motivations	some	few	medium	important	decisive
- Entry to the Hungarian market					x
- Entry to the Eastern European market			x		
- Closeness of the Western European market		x			
- Cheap labour force				x	
- Developed infrastructure		x			
- Labor force of quality		x			
- Cheap raw material	x				
- Government subsidies such as taxation advantages, etc.		x			
- Developed Hungarian bank system		x			
- Importance of privatization supply				x	
- Political stability				x	
- Other*				x	

*Personal contacts for investments of smaller size.
Source: ÁRVA, L. (1997) p. 1012. [9]

Exporting included various industrial products and services as well as consumer products that are mentioned above, among marketing opportunities. The weakness in hard currency in the target countries has constituted the principal obstacle to exporting. On the other hand, some restrictions on advanced technology exports from West to East remained from the so called COCOM list whose origin goes back to the Cold War epoch. Due to the hard currency problem some companies have chosen countertrade and have imported goods against exported goods. A kind of countertrade has been used by other companies, too, who extracted and repatriated profit in the form of goods that were produced in these countries. Anyway, the availability of local products has limited the countertrade and export opportunity, too. A third opportunity is to invest export revenues in local businesses.

A considerable number of technology licensing have been contracted with ECE countries. Franchising can be cited as one of the preferred forms of licensing contracts especially in the service industries like fast food sector among others. *Joint ventures* have been particularly popular in these markets as for foreign investors, as for local organizations or governments. The latter prefers the entry form of joint venture because it involves the transfer of managerial and technical know-how as well as sharing of risks. Improvement of productivity and product quality will enable ECE countries both to satisfy domestic demand and to increase export. As far as foreign

investors are concerned, their choice between three forms of market entry, e.g. licensing or joint venture, or fully owned subsidiary has depended on factors such as contact to local market or information about market, or the need to safeguard technology and product quality. The privatization process in ECE countries offered an extraordinary occasion of acquisitions for foreign investors that occurs not very often in history. Especially a price mechanism not functioning normally and overestimated profit expectations of foreign investors constituted considerable risk factors.

Large multinational companies established in Europe have been the *first to enter* and exploit business opportunities in ECE. They had some advantages that most small companies did not enjoy. They could cope with the difficulty of extracting hard currency and arranging countertrade. They could decide to expand in ECE without concern for repatriating profits in the near future [10]. Previous business experiences with these countries as well as the availability of government founds constituted other advantages for entering CEC countries. A great number of entrepreneurs in ECE have searched for Western partners and inversely. Government agencies have been created to help matching Western and local partners to make business together. Many expatriates of ECE countries living in the West have had advantages to trade or make business with ECE entrepreneurs. Other participation opportunities for small industrial businesses lie in the licensing and commercialization of ECE inventions.

4. Impacts of Foreign Marketers and Investment

The problem of *excessive demand and scarcity* of goods inherited from the planned economic system has been solved very rapidly. An opposite tendency has emerged: now marketers have to face decreasing consumption and demand in the majority of these countries. The consumption rate dropped by 40–60 per cent during the first half of the nineties [11]. Besides the drastic fall of the average real incomes that causes the fall of the demand, there is an increasing black or grey market sector in these countries including Hungary [12]. Lower prices in these markets – even if products are of lower quality – attract a considerable number of the population.

The weakness in *distribution* has included weak infrastructure, much lower number and average size of retail stores compared with Western countries. This weakness has been followed rapidly by improvements thanks to liberalization of small enterprise regulations and the proliferation of retail stores. More significant improvements were achieved by the intensive expansion of international retail chains in the territory of these countries. In Hungary, for instance their sales volumes may soon reach an upper limit since the offer of consumer goods is becoming excessive in relation to solvency. Additionally, their expansion may lead soon to the same problem that exists in

the developed market economies, especially in Europe. Smaller independent retailers shall fail and sales points will be unavailable for certain groups of the population. Weakness in *advertising* infrastructure and efficiency has been resolved relatively rapidly. International advertising agencies are present in these countries, too, and media opportunities have developed considerably.

Foreign direct investment (FDI) has always been viewed as a huge contributor to the economic transition. It has been suggested that FDI may contribute directly, supplying capital, raising employment, by transferring technologies, management and labor skills, and marketing channels, and by fostering a market based business culture.

Table 2. Transition indicators, country risk ratings and levels of FDI

Country	Average transition indicator in 1995 (4 is advanced transition)	Country risk rating, 1 is low risk (number of raters in brackets)	Cumulative FDI inflows 1989–95 (mn US $)	Cumulative FDI inflows per capita 1989–95 (US $)	Number of projects in sample
Czech Republic	3.44	1.11 (99)	5.481	532	23
Hungary	3.44	1.28 (95)	11.466	1.113	21
Poland	3.33	1.44 (99)	2.423	63	27
Slovakia	3.22	1.76 (80)	623	117	5
Estonia	3.22	2.05 (73)	637	413	4
Slovenia	3.11	1.49 (57)	505	253	3
Lithuania	2.78	2.25 (71)	228	61	1
Croatia	2.78	2.73 (44)	251	53	2
Kyrgyzistan	2.78	3.14 (21)	143	32	1
Latvia	2.67	2.18 (73)	409	164	5
Bulgaria	2.56	2.70 (71)	302	36	5
Russia	2.56	3.07 (74)	3.100	21	31
Romania	2.44	2.68 (77)	879	39	5
Ukraine	2.22	3.16 (61)	581	11	10
Kazahstan	2.11	2.95 (39)	1.831	110	1
Turkmenistan	1.11	3.22 (23)	215	54	1

Sources: EBRD Transition Report, 1995, survey data, IMF and EBRD estimates. Cited by LANKES and VENABLES (1996) [13]

According to LANKES & VENABLES (1996) and the *Table 2* transition indicators in the different ECE countries can be used to grade progress in the dimension of the factors of structural reforms. This includes the extent of privatization, enterprise restructuring, the scope and openness of markets, progress in financial sector reform and in the creation of legal and institutional framework supporting private sector activity. Indicators range progress from 1 (little progress) to 4 (advanced progress). Risk factors

represent assessment by respondent of a survey where 1 refers to a relatively low risk while 4 refers to an unacceptably high level of risk. As risk factors, regulatory and legal risk, transfer risk, risk of macroeconomic instability, expropriation risk and labor force unrest had been rated. A close negative correlation has been found between progress in transition and perceived country risk. Three main motives had driven foreign investors: being close to customers, low cost manufacturing, and access to the local markets.

Evaluations of the impacts of FDI in Hungary usually represent more disappointment from a macroeconomic point of view than from that of individual companies. Disappointment is mainly related to expectations. According to ÁRVA (1997), companies that were fully or partially owned by foreigners in 1995 produced 57 per cent of the manufacturer sector sales. Thus these companies were dominant in the Hungarian economy.

Table 3. Impact of different foreign investment types on the host country's economy

Type of investment	Domestic supplier relations	Effect on the balance of trade	Transfer of developed technology
1. Colonial type investment	none	negative	none
2. Export promotion investment	medium or strong	negative on short period of time, strongly positive on longer period of time	strong
3. Import substitution investment	weak or medium	negative	weak or medium
4. 'Best-buy' market development investment	strong in the beginning, weak later and becoming stronger once again	rather negative in a short period of time, and strongly positive in a longer period of time	not significant in a short period of time and medium or strong in a longer period of time

Source: ÁRVA, L. (1997) pp. 1007–1018

However, these companies became more and more responsible for the trade balance deficit. Their responsibility is related to their investment motivations. They have preferred market penetration to other motivations and prefer foreign suppliers to Hungarian ones. They find that Hungarian

suppliers are not flexible enough, usually do not respect delivery conditions and the quality of their products is objectionable. That is why they often replace Hungarian suppliers by foreign ones. The *Table 3* shows impacts of the different types of investment.

Other research and evaluations suggest that activity of foreign marketers and investors has brought about important changes in company capabilities and policies in Hungary, especially in the field of marketing orientation and strategy. A research [14] on the impacts of foreign investment shows that the improvement of company capabilities is more related to production and customer policy. But in the field of functional achievements, such as new product development, market research, relation with suppliers and intermediaries fewer changes have occurred thanks to foreign investment.

Significant differences have been found between companies in which foreign investors have different shares or status. Four types of companies have been distinguished: (1) companies belonging exclusively to Hungarian owners, (2) companies privatized with participation of foreign investors, (3) joint ventures and (4) green field investment of foreign capital. According to the range from (1) to (4) marketing attitude is increasingly important. Marketing attitude involves the orientation toward long term market development and increase of market share, an aggressive increase of sales as marketing objective, as well as a higher positioning of products, services and prices on the markets. Among factors of competitive advantage prices take the first place, while brand image and company image take the second for all of the company categories. Product quality plays a leading role only in the case of green field investments and joint ventures. Research findings have proven the hypothesis concerning the principal motivation of foreign investment, e.g. to profit from advantages related to domestic labor force.

Foreign investors have had a stimulating influence on marketing activity at Hungarian companies [15]. Especially marketing know-how plays an increasing role. Increased marketing activity is expressed in an important growth of advertising expenditure from the beginning of the nineties. However, this expenditure stabilized and did not increase by the second half of the decade. Research finding shows that both external and internal marketing environment have been stabilized that may allow the assumption that a general stabilization has occurred and the period of transition might be over. Companies have escaped from their earlier constraints and their development does not depend more on these constraints. Companies are able to find their own strategies based on models such as Porter's model of competitive advantage.

The influence of Western business culture on CEC economies has resulted in a very specific management consequence at companies remaining properties of local investors. HOVÁNYI [16] reports that a great number of Hungarian companies had to introduce a series of measures in order to achieve a 'slimming cure' thanks to the increased competition with Western

firms on national markets, as well as to the collapse of other markets. This drastic slimming cure has led to give up from 50 to 70 percent of their outputs and to dismiss their employees in the same percentage. Managers of downsized companies had to apply a new kind of management, a so called 'low flame management technique' in order to run their firms.

5. Motivations and Impacts of EU Investment

Motivations and impacts of foreign investment from the European Union (EU) have not been different from the average western motivations [17]. Investment in form of joint venture has been motivated by the intention to profit from differences in labor force cost, advantage of local manufacturing that permits to penetrate into local markets, access to local markets and closeness to Western Europe. The latter is an important advantage in relation to Asian countries, for instance. However, the former advantages are rather of medium run. In a shorter time foreign investors usually prefer other more flexible market entry forms, such as subcontracting.

Advantages for CEC economies are those of a longer run. Foreign investment may contribute to the increase of management and technological competence of the local personnel. Local partners can profit from the distribution experience of Western firms. Investment in key sectors, such as automobile manufacturing for example, may contribute to emerging of a competitive advantage. Working together with small and medium enterprises multinational firms may promote the increase of their competence as well as help them to enter international markets. These advantages can be illustrated by some data. In 1995 in Hungary more than 50 per cent of the export was performed by foreign firms. This share has reached near 80 per cent in certain industries. 45 per cent of foreign firms have realized at least a quarter of their sales by exportation (OECD, 1995).

Disadvantages must not remain without attention. A macroeconomic advantage of foreign investment is generally the stimulation of employment and economic growth. But in the CEC countries the acquisition of companies by foreign investors led initially to an important loss of jobs, due to the introduction of new management. Another disadvantage is that foreign firms may oust local manufacturers from their market position. These consequences might lead to unfavourable attitude toward foreign investors. Despite of the increase of exchange between Western countries and CEC from the beginning of the nineties, one may ask the question, whether there is yet any growth potential, or, to the contrary, a slowdown is assumable.

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