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INTERNATIONALIZATION AND INTERNALIZATION THEORIES AS TOOLS FOR ASSESSING THE EFFECTS OF COMPANIES' INTERNATIONALIZATION

The research problem in this article is the phenomenon of companies internationalization in the foreign direct investment context. This issue becomes more important due to markets openness and globalization. The theories describing the determinants of foreign investments are also the tools for assessing the phenomenon of enterprises internationalization and they can be blended into two groups: theories of internationalization and internalization. The article explains their use in understanding the conditions for direct foreign investment process.

Keywords: internationalization; internalization; foreign direct investments.

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ТЕОРІЇ ІНТЕРНАЦІОНАЛІЗАЦІЇ ТА ІНТЕРНАЛІЗАЦІЇ ЯК ІНСТРУМЕНТИ ОЦІНЮВАННЯ РЕЗУЛЬТАТІВ ВИХОДУ КОМПАНІЙ НА ІНОЗЕМНІ РИНКИ

У статті описано феномен виходу компанії на іноземні ринки шляхом зовнішнього інвестування. Ця проблема стає більш актуальною через зростаючу відкритість ринків та глобалізацію. Теорії, що описують пряме іноземне інвестування, можна поділити на дві великі групи – теорії інтернаціоналізації та інтерналізації. Описано різницю в їхньому розумінні умов та процесу прямого іноземного інвестування.

Ключові слова: інтернаціоналізація; інтерналізація; пряме іноземне інвестування.

Рис. 1. Літ. 13.

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ТЕОРИИ ИНТЕРНАЦИОНАЛИЗАЦИИ И ИНТЕРНАЛИЗАЦИИ КАК ИНСТРУМЕНТЫ ОЦЕНИВАНИЯ РЕЗУЛЬТАТОВ ВЫХОДА КОМПАНИЙ НА ИНОСТРАННЫЕ РЫНКИ

В статье описан феномен выхода компании на иностранные рынки путём внешнего инвестирования. Данная проблема становится всё более актуальной в связи с возрастающей открытостью рынков и глобализацией. Теории, описывающие прямое иностранное инвестирование, можно разделить на две большие группы – теории интернационализации и интернализации. Описана разница в их понимании условий и процесса прямого иностранного инвестирования.

Ключевые слова: интернационализация; интернализация; прямое иностранное инвестирование.

Introduction. The research problem undertaken in this article is the phenomenon of companies internationalization in the context of foreign direct investment. The issue becomes more serious and important due to market openness and globalization, as the identification of determinants of foreign investment undertaking by businesses has not only a theoretical but also a practical perspective.

Theories describing the determinants FDI, being also the tools for assessing the phenomenon of enterprises internationalization can be blended into two groups: internationalization and internalization theories.

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This article aims to conceptualize and explicate the theories of internationalization and internalization, and in particular their use in understanding the conditions for FDI.

The theory of internationalization. Literature focused on the issues of internationalization clearly states that internationalization occurs when a company enters the relationship with a party outside the country of origin. The concept of internationalization is based on the assumption that company operations at a local market differ from its activities at foreign markets (Fonfara et al., 2011).

The aforementioned statement finds its confirmation in Z. Pierscionek's definition. The internationalization of company relates to any form and scope of business relationship with foreign markets (Pierscionek et al., 2003).

M. Gorynia has a different approach to the issue of internationalization. One may consider internationalization if at least one product or service in the portfolio is related to activities at foreign markets (Gorynia et al., 2007).

Subject literature often draws attention to the process-oriented nature of internationalization. M.K. Nowakowski points out that internationalization of a company can be understood as the development of a company and interpreted both as a process or a change of its sphere of activity (Nowakowski et al., 1999).

Internationalization as a process is also defined by P. Pietrasienski who states that globalization is a process based on: export of products, and increasingly also on transfer of production to foreign countries (Pietrasienski et al., 2005). Sales of products at foreign markets often requires from a company to adopt a number of changes. J. Johnson and J.-E. Vahlne state that company's internationalization is a consequence of gradual adaptation to a changing business environment, both external and internal (Johanson, Vahlne et al., 1997).

The origin of the internationalization theory is derived from the concepts directly related to international business, primarily focusing on explaining international flows of goods and services. Among the first researchers of the problem we should mention Smith, Ricardo and Ohlin. They pointed out which effects international trade has, and which goods would be subject of such trade (Gorynia, Jankowska et al., 2007).

Most popular among the concepts of internationalization is the so-called Uppsala model, created by 3 employees of the University of Uppsala. The authors of this model are Johnson, Wiedersheim-Paul and Vahlne. They noted that the proceedings of companies engaged in overseas expansion are characterized by 3 facts:

1. Expansion is preceded by a success at the internal market and is a result of various decisions taken in the company.
2. Expansion usually starts with markets located close by and afterwards covers additional markets – the concept of psychic or cultural distance between markets has been introduced, defined as a set of factors hindering bilateral flow of information. This distance is the factor of language, culture, politics etc.
3. Companies entering foreign markets often start with export activities, later they decide to engage themselves into more demanding activities (Gorynia, Jankowska et al., 2007).

The main thesis of the Uppsala model is that internationalization process is sequential, phased, evolutionary or gradual – this set of terms is suggesting a reason-

able non-random sequence of events, a process developing over time (Gorynia, Jankowska et al., 2007).

The Uppsala model identifies 4 stages in internationalization:

1. Irregular export activity – sporadic export.
2. Export through independent intermediaries (agents).
3. Establishing of a subsidiary, sales branch.
4. Establishing of a subsidiary, production branch (Johnson, Wiedersheim-Paul et al., 1975).

The Uppsala model is presented graphically in Figure 1.

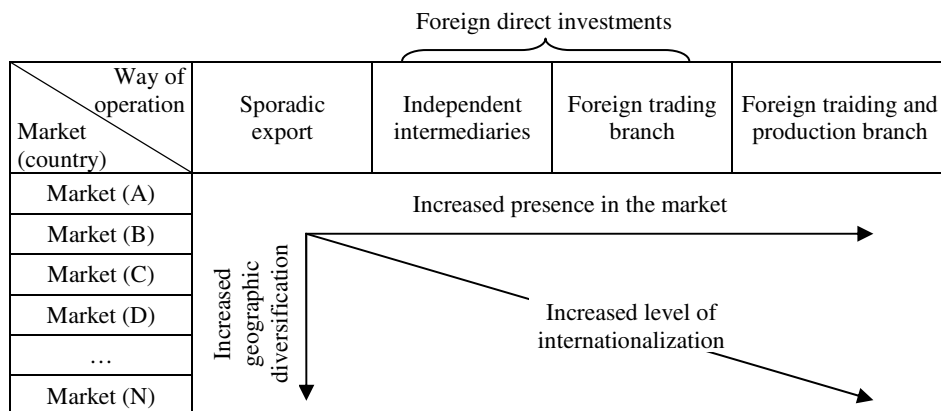


Figure 1. **Business internationalization – Uppsala model** (Hollensen et al., 2011)

During the first stage there is no regular export, the company does not engage resources abroad, but also hardly obtains any information about the market. Export through independent agents indicates that the company is entering into the initial phase of resource engagement and obtains information on the factors affecting the ability to sell at a given foreign market. At the third stage of internationalization the company forms a sales subsidiary abroad. The company is far more interested in obtaining knowledge on sales determinants and necessary commitment of resources at the market. The last stage of the evolutionary process of internationalization is to build its own production facility abroad. This stage requires relatively greatest knowledge about the expansion and is associated with extensive commitment of resources by the company abroad (Gorynia, Jankowska et al., 2007).

The last two stages are essential for company expansion and are also a symptom of another important phenomenon which is foreign direct investment (FDI).

The sequence of steps in the Uppsala model has been defined by the authors as chain establishment (Gorynia, Jankowska et al., 2007). It should be noted, that the creators of the model did not give it an extremely deterministic character, realizing that not always all these steps will come into play in the proposed order (Gorynia et al., 2007).

The Uppsala model raises many controversies and significant criticism based on other experiences, which indicated that internationalization as a process may be carried out either evolutionary, or incrementally. Some corporations actually gradually

overcome operational barriers at foreign markets and learn how to reduce the psychological distance (Fonfara et al., 2011).

Undertaking various forms of parallel actions at the market or commencing from their higher level may be observed in recent period. It is often explained by growing homogenization of markets, higher level of international education and more experienced staff, development of international consulting and information technology facilitating access to multiple markets (Fonfara et al., 2011). It is also important to note the issue of the so-called "born global", i.e. high-tech companies that produce unique products which already at the early stages of development aim to be international. The phenomenon of "born global" is undoubtedly a major challenge to traditional theories of internationalization (Fonfara et al., 2011).

It is also important to look at the phenomenon of foreign direct investment, however, neglected for years, placed closely as one of the last stages of enterprises internationalization considered as extreme or final. Only in the last 40 years FDI have become increasingly important should be (Rymarczyk et al., 2004).

The issue of enterprises internationalization is also important to clarify using the macro- and microeconomic theories.

Internationalization theory as an microeconomic attempt to explain FDI.

Economic literature on foreign direct investment shows two traditional research perspectives: micro and macro.

In the first case, an enterprise is the basic unit of observation, assuming that international economic activity is actually implemented at the company level.

In the macroeconomic perspective, the focus is on the aggregated amounts of direct investment on the country – country level, often divided into different sectors (Gorynia et al., 2007).

In this article we would like to focus on the microeconomic perspective of internationalization.

At the microeconomic foundations, a number of theories to explain the issue of FDI were formed. The theory of monopolistic advantage, the theory of oligopolistic reaction, also called international oligopoly, location theory, Vernon's product life cycle theory, the ownership advantage theory, appropriation theory and the theory of internalization, which is the main subject of our further deliberations.

Internalization theory has many fathers. Each of them made a significant contribution to the above theory. Such names as R. Coase, A. Rugman, E. Heidhues, P.J. Buckley, M. Cassone, O.E. Williamson, testify to the significance of the issue of internalisation in international expansion.

The point of company's activities internalization consists in the acquisition by it of certain features that were carried out against it by independent partners. If they are based in different countries, this process leads to the formation or growth of international business. This means, therefore, internationalization through internalization (Rymarczyk et al., 2004).

This theory shows that the basis for international expansion of companies is primarily a performance condition defined as savings. It is similar to the theory of international oligopoly in the sense that deficiencies at the market are also the explanatory variables. In this case, however, the main issues are the so-called Williamson's cognitive imperfections of transaction costs (Gorynia et al., 2007).

Genesis of this concept in terms of internal rather than international has its origins in the works of R. Coase. The author stated that company's market operations involve some costs. In its activities, the company can use internal market and so the operation takes place within the company and external market, which relate to transactions with suppliers and customers (Gorynia et al., 2007).

Coase's statements were adapted and expanded into a new Oliver Williamson's theory.

According to Williamson transaction costs are the result of imperfect information and vary depending on institutional market type chosen by the company. Relative costs of internal and external market influence the selection of a market (Gorynia et al., 2007).

With further research the importance of the issue of transaction costs was noted as well as their impact on individual investment decisions. The company will become internalized if due to market imperfection transaction costs at external markets will increase to such an extent that it may proceed with cheaper transaction when it's at both sides of the market at the same time, which means it carries out transactions by itself. In other words, it replaces the external market by interior semi-market (Rymarczyk et al., 2004).

Competition generally leads to choosing the most effective market institutions. Internalization depends on the fact that external market is a substitute for internal market, which results in a hierarchy and centralization of resource allocation (Teece et al., 2007).

In the case of internalization special attention is paid to wide-ranging information, which is also an important issue to look at the changing face of company's internationalization.

The theory of internalization for companies' internationalization and foreign direct investment focuses on the information on a specific advantage of a company (knowledge, technology, market, organization of management, marketing etc.) over its competitors (Gorynia et al., 2007). Although the concept of internalization includes all types of market failures such as natural and resulting from government interference, however, the main focus is on intermediate goods, market imperfections, and particularly knowledge (Buckley, Cassone et al., 2007). Market knowledge is imperfect, bearing difficulties in estimating the value of knowledge and prices determination (Gorynia et al., 2007). Knowledge itself is rarely exposed for sale, the company would always recognize specific knowledge as one of the greatest competitive advantage. Many companies makes huge investments in protecting their knowledge. For these reasons, the use of internal knowledge within the enterprise market is often the most effective solution (Gorynia et al., 2007).

This is another argument favoring internationalization. Important is also the problem of gigantic expenditures on research and development, for example, Samsung in 2012 spent on R&D 9 bln USD. And as we can see the amounts spent on R&D are significant even for global companies but the sale of knowledge generated by these investments is not meaningful due to imperfect nature of the market.

The concept of internalization includes the dynamic aspect of company's activity aimed at preventing the spread of knowledge it possesses (Gorynia et al., 2007).

It should be noted that in addition to the desire to avoid costs and risks of transactions the internalization motifs include also the desire to monopolize knowledge and know-how (Rymarczyk et al., 2004).

Moving to the issue of expenditure on research and development of innovation it should be noted also that the so-called S.P. Magee's appropriation theory is similar. We can say that the appropriation theory is present within the theory of internalization. The author of this theory emphasized the advantages of innovative enterprises, which due to large input in research and development, develop their technical knowledge and refine their production technology (Gorynia et al., 2007).

Internalization theory is the theory often used to describe international investment activity of enterprises. Let us take a different look at the issues of information and knowledge. It brings the concept of transaction costs to the activities of international undertakings analysis, realizing the need to minimize the level of these costs as the motive for internationalization activities.

Concluding considerations it's worth mentioning that internalization is always beneficial, if external market costs are too high or if you do not find an appropriate external market. Choosing a new form of organization of certain transactions under these conditions is beneficial not only for a company but also for international sphere, where applicable, as by partial replacement by international markets the company usually increases the efficiency of the market system functioning. Reduced operating costs of international companies leads to lower prices for their products and services, which in turn positively affects the demand (Rymarczyk et al., 2004).

Summary. This article is a short presentation of the internationalization and internalization theories as a way of understanding international investment activity of enterprises. The overview of these theories gives the opportunity to respond to many important theses such as the need to have specific knowledge, the desire to reduce transaction costs, the creation of a specific internal market, the reluctance to share the knowledge which is a strategic competitive advantage.

According to the Uppsala model of progressive internationalization business activity is associated with greater assets commitment, thus leading to more risky forms of international expansion, conditional to having more comprehensive knowledge of market expansion (Gorynia, Jankowska et al., 2007).

It is worth mentioning that with the progress of internationalization and gaining experience by researchers of this phenomenon come numerous modifications of internationalization. The theories of Bilkey, Tesar, Czinkot, Cavusgil alter the shape and the scope of this issue, thus criticizing the classical approach. The critics point to the increasingly significant influence of such factors as innovation, experience or being "born global".

The internalization theory gives a new perspective on information, specific knowledge, as a condition of international investment activity. Internalization creates an image of the company avoiding seeking alternative transaction costs at the internal market.

It is necessary, however, to mention that none of the presented theories is universally applicable regardless the type of a company, industry or country, stage of a life cycle etc. It is necessary to distinguish between internationalization processes occurring in the sectors of manufacturing industry and services, in multinational or global

companies, and what is important in large or small companies (Gorynia, Jankowska et al., 2007).

Regarding the theory of internalization we can take the risk to claim that this theory is not in obvious contradiction with other approaches, and is so general that perhaps the results of the research on other microeconomic approaches could be used to complement it, which in turn would provide further development of the coherent theory. So far, such attempts have not been taken.

The most important is the fact that recent research seems to seek to establish a compromise position, which could mean that in future we may witness the creation of a universal theory addressing international investment activity of enterprises.

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Стаття надійшла до редакції 2.02.2015.