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CHOICE OF FOREIGN MARKET ENTRY STRATEGY: BASED ON THE CASE STUDY OF LETRIM OÜ

Master's Thesis

Advisor: Associate Professor Rünno Lumiste
Co-Advisor: Lecturer Bernd Hofmann

Tallinn 2015

Hereby I declare that this master’s thesis,
my original investigation and achievement,
submitted for the master degree at Tallinn University of Technology
has not been submitted for any other degree or examination.

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The chairman of the defence committee:
Permitted to defence
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(position, name, signature, date)

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ACKNOWLEDGEMENTS

Many people contributed to this thesis and I would like to thank all of them. To begin with, I would like to thank my supervisor, Rünno Lumiste, for his guidance during this period. To add, I would like to thank the co-supervisor, Bernd Hofmann, who provided me with information relevant for this thesis about French market. I would also like to thank my partner Peep Põlluäär, the CEO of Letrim OÜ, whose competence and experience in the field of furniture production and marketing added significant value to this paper. Finally, I would like to thank my family for their patience and understanding during the writing period.

ABSTRACT

In the situation of increasing globalization, many firms attempt to expand their sales into foreign markets. International expansion provides opportunities for the growth of the company, helps to increase competitiveness and facilitates access to new product ideas. However, providing a lot of opportunities, internationalization for a firm is a process associated with many risks, and without clear strategy the internationalization is unlikely to be successful. There are many important questions that need to be solved before entering a target market, including foreign market entry strategy selection. When entering a foreign market, a market entry mode should be selected, which is a vitally important decision for a small sized company.

This is also the reason why the author decided to write this thesis over the foreign market entry strategy selection. In this case, the author chose a market entry strategy to France for the company Letrim OÜ. Letrim is the author's family company that is engaged in furniture marketing and has been operating in Central European markets for 7 years. One of the strategic goals of the company is to enter and operate in French market. France is a huge market with a number of opportunities when it comes to ready-to-assemble pine wood furniture. Nevertheless, the market appears to be highly competitive and facing economic difficulties. This is why it was very important to choose a right entering method for the company in order not to waste resources.

The research method used in this paper was case study. To answer the research question the author used a qualitative research method by providing secondary data analysis. Author conducted PESTLE analysis.

By carrying out the analysis the author found that in order to lower the logistic costs and the costs related with manufacturing, the indirect export mode would be the most appropriate one for French market as the local wholesalers usually buy bigger quantities than the retail stores usually do. Also, the local wholesalers know the local trends and inquiries.

There have been many papers written about the selection of export target countries, but how to choose a foreign market entry mode is a field that has not received enough attention. This research provides a highly practical value for the company Letrim OÜ but is also beneficial for all the companies wishing to internationalize by providing information and analyses on market entry methods. The paper is also useful for all furniture manufacturers who intend to

enter French market as it provides information about the political, economic, etc. conditions of the market.

Internationalization, export mode of entry, risks and uncertainties, small- and medium sized enterprises.

INTRODUCTION

Estonian timber furniture sector has long traditions but the local market is very small and price sensitive. This is the reason why Estonian furniture manufactures are very dependent on foreign markets. The main export markets for Estonian furniture have mainly been the neighbouring countries Finland, Sweden and Norway. But the recession in Europe has created many challenges for the Nordic countries, which is why the competition in the furniture market of these countries is very high. Accordingly, the author has chosen to study export opportunities for wooden furniture in France.

The work is based on the company, Letrim OÜ. The company is specialised in marketing solid wood pine furniture.

The main activities of the company are:

- Solid wood pine furniture purchase and sale
- Purchase and sale of furniture components
- Marketing assistance and technological consultancy for small Estonian furniture manufacturing companies
- Furniture production

The company is active in B2B market and the main strategic goal is to find new export markets.

This study is searching for an answer to the following question:

What is the best export strategy for Letrim OÜ to enter and operate in the French furniture market?

The **research subjects** are export methods as well as the specifics of the target market.

The **main aim** of the thesis is to find out which entering method is best for Letrim OÜ.

To achieve this objective the author has set the following **tasks**:

- Describe the export methods and analyse their strengths and weaknesses
- Analyse target market conditions, risks and opportunities
- Analyse the competitive advantages of Letrim OÜ

In order to find the right export strategy, the author has decided to carry out a PESTLE analysis of the target market to analyse the political, economical, social, technological, environmental and legislative conditions to find out the opportunities and risks that are related with the market entry. Also, the author attempts to propose methods for reducing these risks. The author is also planning to analyse the capabilities of Letrim OÜ.

The first chapter of the thesis explores the nature of the European wooden furniture market by presenting the key numbers. This chapter also provides an overview of the capabilities of Letrim OÜ and gives a short description about the Estonian timber furniture industry with an emphasis on the opportunities and constraints the Estonian furniture sector faces.

The second chapter of the present thesis provides a theoretical framework by summarizing relevant market entry theories. The author provides an analysis of different export methods and explores the factors which influence the choice of the market entry mode.

In the third chapter the author carries out a PESTLE analysis. The author will finish this chapter with an analysis and brings out the findings of this study.

The theoretical part of this thesis is mainly based on the following authors: S. T. Cavusgil, S. Hollensen, F. Root, K. A. Miller, G. Osland, C. Taylor, S. Zou, F. Root, J. Sutherland, D. Canwell, P. W. Beamish, J. W. Lu, R. J. Brown, C. S. Dev, Z. Zhou, S. Agarwal, N. Ramaswami.

The method used in this paper is case study. The author uses qualitative research method: secondary data analysis (company documentation, media publications, statistical databases, websites of different organizations).

The paper should answer the question, what market entry method is best for Letrim OÜ to enter and operate in French market. The paper also attempts to identify the risks and opportunities which are related with the market entry.

1 FURNITURE SECTOR

1.1 The impact of globalization on international trade

Since international business involves all commercial transactions — private and governmental — between parties of two or more countries (Daniels, et al. 2007), then globalization refers to global economic, social and political integration and interdependence between nations, which occurs through flows of capital, goods, information, ideas, people, forces as well as environmental changes (Al-Rodhan and Stoudmann 2006). There have been many attempts to define the concept and various opinions have been brought to debate, but despite different views, there is only one conclusion: the definition of this term is anything but easy as globalisation is not a single concept that can be defined and encompassed within a set time frame, nor is it a process that can be defined clearly with a beginning and an end (Al-Rodhan and Stoudmann 2006). According to Daniels (2007), the term globalization refers to the on-going social, economic and political process that deepens a relationship between and broadens the interdependences amongst nations — their people, firms, organizations and governments. Daly (1999) defines globalization as global economic integration of many formerly national economies into one global economy, mainly by free trade and free capital mobility, but also by easy or uncontrolled migration. It is the effective erasure of national boundaries for economic purpose.

These factors are, of course, all interrelated and combined, they are now changing the world in a way mankind never has seen before, where distances are subjective and relative. To change the world in such a way requires strong forces. According to Daniels (2007), there are seven factors fuelling globalization:

- Vast improvements in transportation and communications technology
- The removal of restrictions on international trade and foreign investments
- The reduction of risks of doing business internationally by available services provided by governments, banks, insurance companies, etc
- Consumers have higher demands as there is much more variety of service and goods on local markets, as well as better access for the consumer for other foreign markets.

That has led to higher quality and lower prices, as the competitors have to respond to these higher demands

- As the domestic market is now flooded with imported goods and services due to increased global competitions, firms need to enter into international markets to sell their goods and to maintain their operational flexibility and competitiveness
- The political situation of the world is changing. With the rise of China as an economic giant and the improvements in national infrastructure and the provision of trade-related services by governments, the world trade pattern is changing, resulting in increased trade and investment levels between those countries and the rest of the world
- Cross-national co-operation is increasing with cross-national treaties and agreements, receiving a helping hand from international organizations such as the United Nations, the International Monetary Fund, the World Trade Organization and the International Bank for Reconstructions and Development

Due to these factors, there has been an explosive growth in international trade in recent years as can be seen on chart 1. Though there was a drawback in the year 2009, the indication is for continuing growth of exports. In fact, after the drawback of the year 2009 and the global economic crisis that the world was facing, 2010 saw a record high annual change in the world trade market, so the loss of the year 2009 was gained back. This means that despite of the global financial crises the international trade continues to rise and an increasing number of countries is involved in this process of globalization.

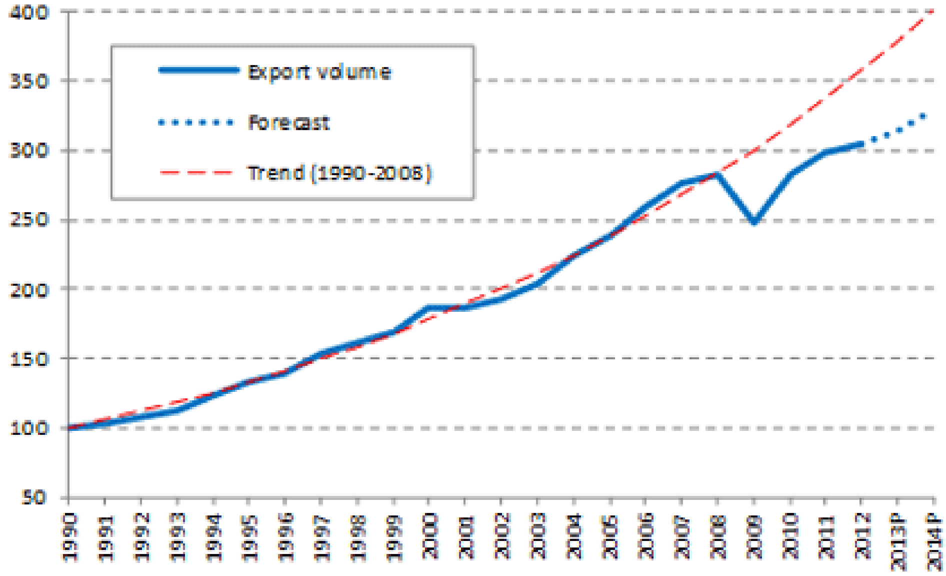

Chart 1. Volume of world merchandise exports, 1990-2014 Indices, 1990=100

Source: (WTO Secretariat, 2013)

When speaking about the international furniture sector, an increasing number of goods have being traded internationally and more countries are significant participants in this trade. In particular, low wage developing countries in Asia and other parts of the world are making their presence felt as exporters amongst industrialised countries. As it is very hard for the industrialised countries to compete with lower prices of Asian companies, the nature of competition has changed from price to a range of other issues, including quality, delivery reliability and flexibility. To add, it is becoming more important for the companies to grasp the global developments and understand the opportunities and risks the globalization entails. For example, the financial crisis of 2008 had a devastating effect on global furniture market. Many manufacturers went bankrupt or had to change their field of action. In addition, the welfare of construction industry and the fluctuations in raw material prices are also affecting the global furniture market. The bubbles in housing markets have usually a positive effect on furniture demand but they can also influence furniture sector negatively as the prices of raw materials rise and the furniture manufacturers are no longer competitive. The above mentioned factors mean that the furniture industry is an unstable one in which manufacturers must be well aware of changes in global trends and demand.

Economic globalization is particularly important for small countries like Estonia as they depend heavily on foreign trade. Growth and development of the export sector play a key role for economic growth and higher living standards for these countries. It is important that the economic and business environment is built in the way that it supports and encourages local companies to take advantage of the opportunities offered by globalization.

1.2 Overview of the European furniture sector

In this section the author analyses the European Union wooden furniture market, observing its main producers, importers and exporters by presenting main statistical numbers to understand the overall situation in the European furniture market.

To begin with, the furniture sector of the EU has managed to maintain its position as a major global player, not just due to its size, but also because of its role to influence international fashion and design trends. Even if with the presence of fast growing consumption areas at the global level and the recession, the EU market still accounts for around one quarter of world furniture consumption and production (Tracogna 2013).

The most important countries which consume and produce furniture in the European Union are the UK, Germany, Italy, France and Spain. During the recession, the EU wood furniture consumption fell from euro 43.2 billion in 2007 to euro 34.4 billion in 2009 (Global Wood 2014). As furniture is a discretionary product then during the recession consumers tend to postpone purchases of discretionary items. As can be seen on the chart 1.2, the overall furniture consumption in Europe has not regained the pre-crisis level and after a small rise in the 2010, the overall consumption has fallen again.

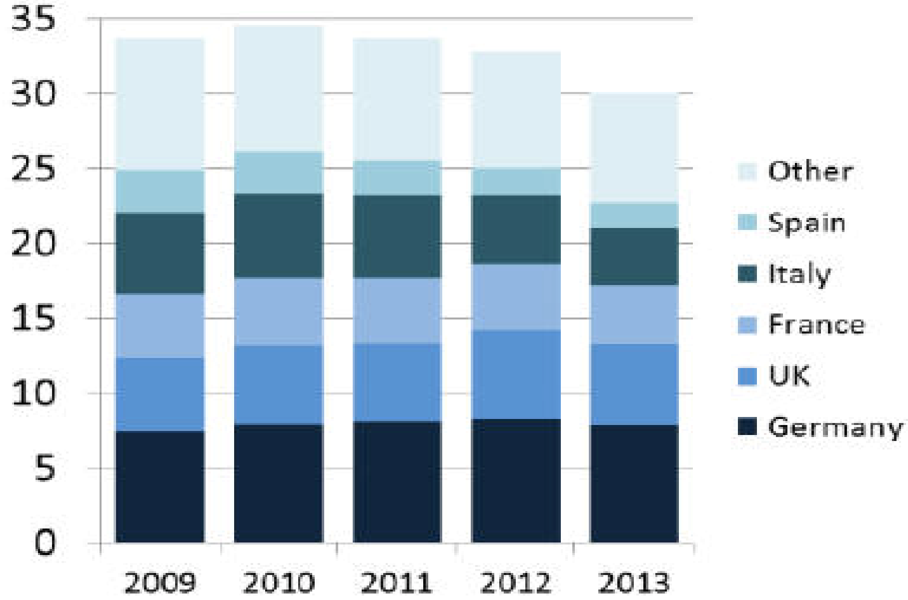

Chart 1.2. EU-28 wooden furniture consumption (billion euro)
Source: (Global Wood 2014)

As can be seen on the chart 1.2, there has been a recovery in Germany, consuming euro 8.1 billion of wood furniture in 2011, up from euro 7.4 billion in 2009 (Global Wood 2013). In year 2012, the furniture consumption of Germany stayed stable but decreased again in 2013 from 8.27 billion euro to 7.81 billion.

Italian wood furniture consumption increased from euro 5.5 billion in 2009 to euro 6.8 billion in 2011 (Global Wood 2013). In 2012, Italian wooden furniture consumption fell again to euro 4.57 billion and decreased 15% more, to euro 3.88 billion in 2013 (Global Wood 2014).

In the UK and France, wood furniture consumption was quite stable between 2009 and 2011 at around euro 5 billion and euro 4.4 billion respectively. In 2012, the UK furniture consumption increased to 5.94 billion and decreased again by 8% to euro 5.49 billion in year 2013. After a slow year of 2012 in France the furniture consumption suffered a further 11% decline to euro 3.90 billion in 2013 (Global Wood 2014).

The import of wooden furniture in the EU has been quite modest over the years, accounting for 12% of total supply in 2013, down from 13% of the previous year and the peak level of 14% recorded in 2010 (Global Wood 2014) though the exports have been rising. At the beginning of 2011, the EU net trade in wood furniture was close to zero, with both imports and exports averaging close to euro 500 million per month. However, by the end of 2013, the EU had a trade surplus in wood furniture of around euro 350 million per month. Average monthly imports of wood furniture into the EU had fallen to euro 350 million while exports had risen to just over euro 700 million per month (Global Wood 2014). It can be concluded that the EU external trade in wood furniture is relatively small compared to total consumption, which is about euro 50 billion per year (or euro 4200 million per month). There is much reliance on domestic manufacturers. Only about one quarter of wood furniture consumed in the EU countries ever crosses a national boundary. According to Global Wood (2014), the total internal trade in wood furniture between EU countries averages around euro 1,200 million per month.

The charts 1.3 and 1.4 illustrate the total supply of wooden furniture and the share of value by supply source into the EU, including imports.

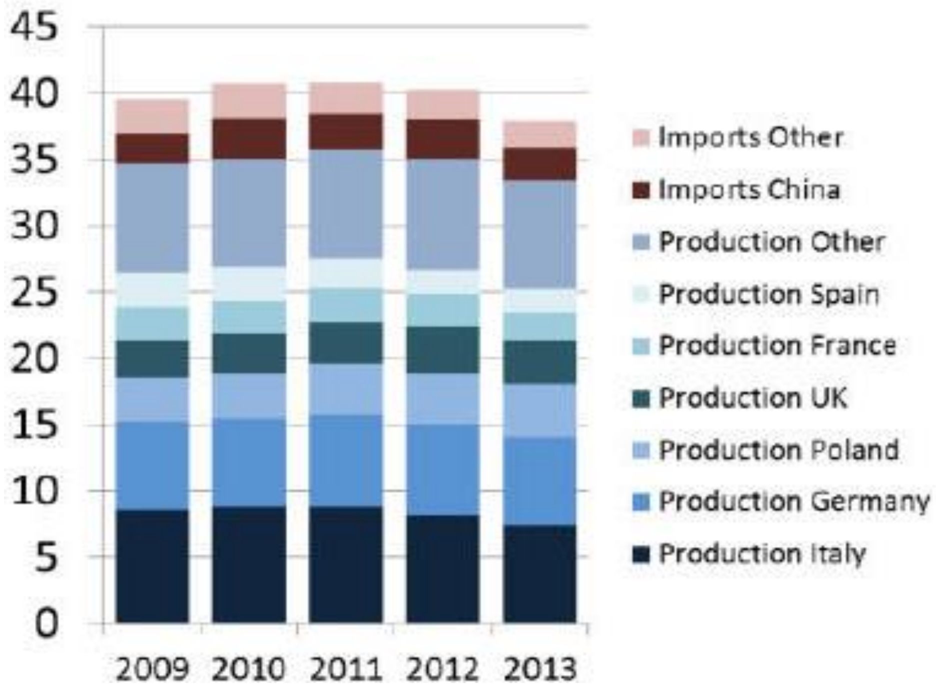

Chart 1.3. EU-28 wooden furniture supply (billion euro)
Source: (Global Wood 2014)

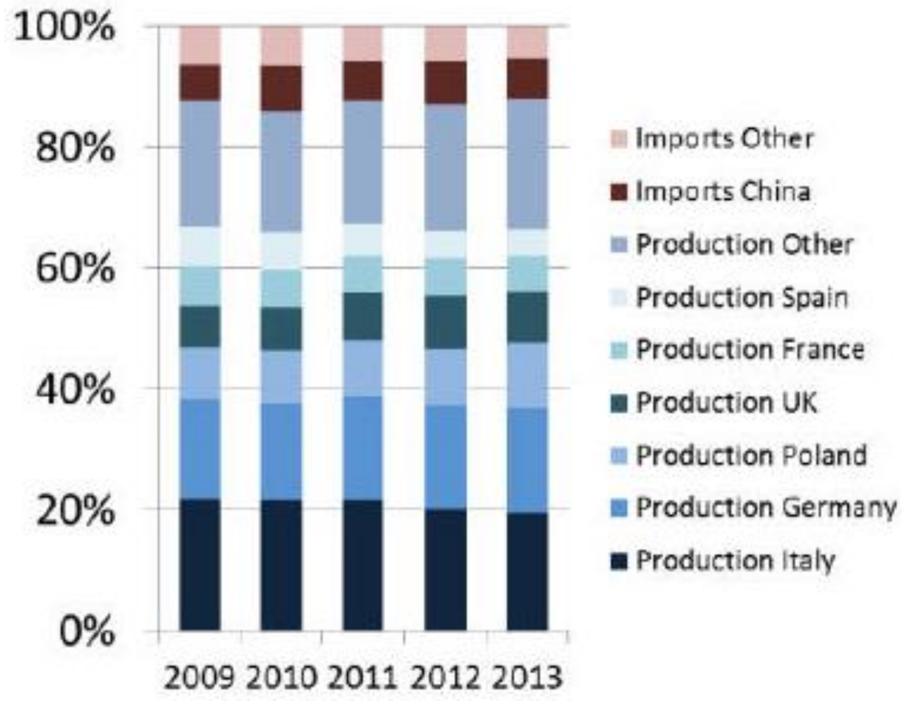

Chart 1.4. Share of value of EU-28 wood furniture supply by source (%)
Source: (Global Wood 2014)

Over the years 2009-2013, a rising share of wood furniture imported into the EU has been destined for just three countries, the UK, Germany and France. In 2012, the import of UK accounted for 1.6 billion euros, in Germany 956 million and in France 827 million euros. In the year 2013, the share of imports decreased in all these countries, accordingly 11% in the UK, 12% in Germany and 23% in France. As been discussed earlier, the overall consumption also decreased.

The chart 1.5 outlines 10 of the largest furniture importers in EU in 2012. The chart 1.5 includes imports from both inside and outside the EU.

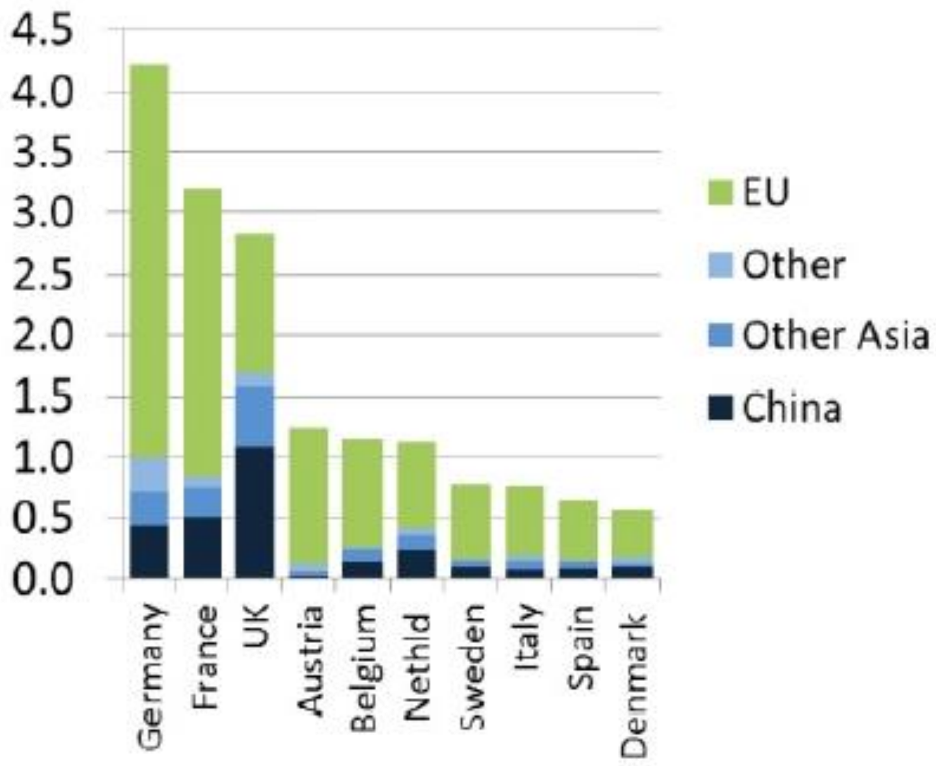

Chart 1.5. 10 largest wood furniture importers in the EU in 2012 (billion euro by region of origin)
Source: (ITTO 2012)

The following chart 1.6 indicates a very high variability in Member State dependency on wood furniture imports from outside the EU — ranging from close to 60% in the UK to less than 10% in Austria. The UK is losing the most of its market share to Chinese products. Due to that it is much harder for the European manufacturers to be competitive in the UK market. The furniture production sector in the UK itself is also suffering because of the high proportion of Chinese products in the market.

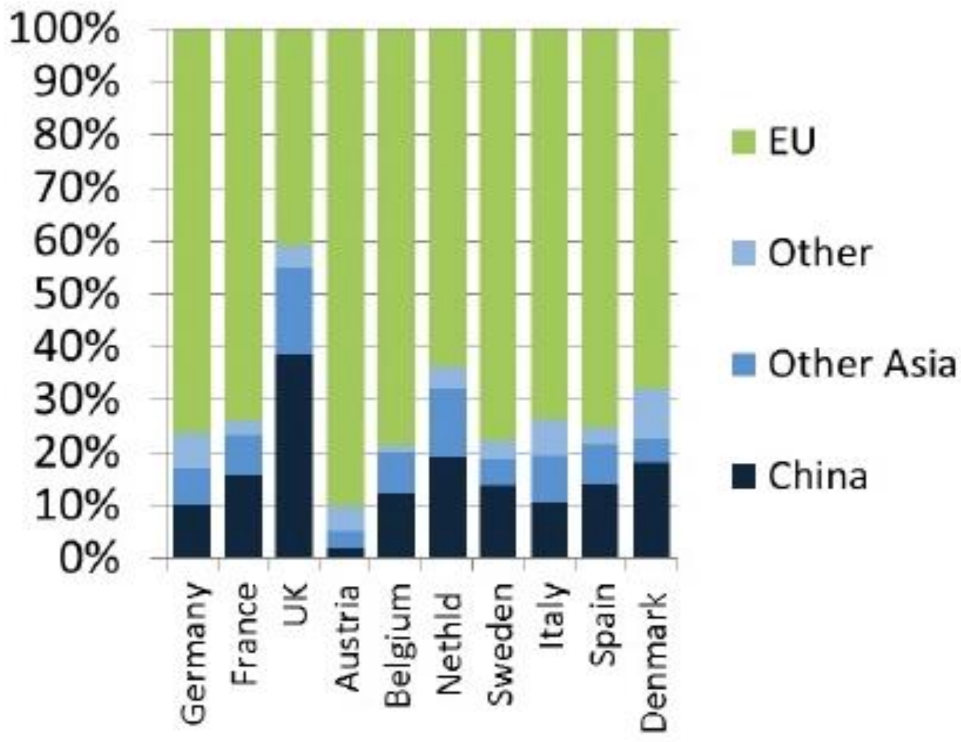

Chart 1.6. Regional share of wood furniture imports by the EU countries in 2012 (% euro value) Source: (ITTO 2012)

The variation between the member states can be due to a number of factors:

- The presence of very large domestic manufacturing furniture sectors in some countries (particularly in Italy, Germany, Poland);
- Proximity to manufacturers elsewhere in the EU (most other Central-European countries also source a very large proportion of furniture from Italy, Germany and Poland);
- The level of loyalty to domestic furniture brands (a major factor behind low levels of imports into Italy);
- Extent of consolidation in the retail sector — external suppliers have had more success developing markets for furniture products in countries with relatively large consolidated retail networks (such as the UK, Benelux countries, Germany and France) than in countries with more fragmented retail networks such as in Italy (ITTO 2013)

The importance of China cannot be ignored in the EU furniture imports as its lower priced products compete with the higher prices of the European manufacturers. Nevertheless, the long distance and lower quality level are the reasons why the share of Chinese products in European markets has been rather modest. But the threat for European manufacturers to lose the market share to Chinese products is still there and depends heavily on the prevailing economic situation. The chart 1.7 highlights the extent to which China has come to dominate the EU imports of wood furniture products.

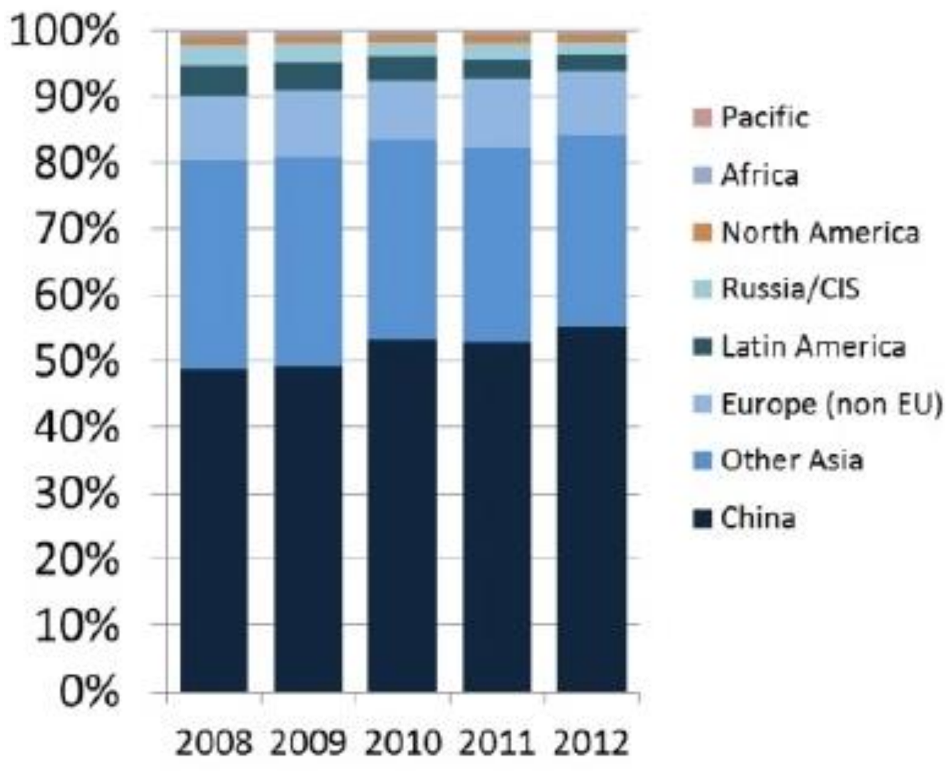

Chart 1.7. Regional share of EU-27 wood furniture imports (% euro value)

Source: (Fordaq Furniture 2013)

During the period of 2008-2012, the share of China in the EU import value increased from 49% to 55%. During the same period, the share of other Asian countries fell from 32% to 29% and the share from Latin America fell from 4% to 2%. The share of imports from the CIS region, Africa and North America have been negligible during this period. However, the non–EU European countries maintained the share of around 10% import value throughout the 5-year period (ITTO 2013). This means that the Chinese share in the European furniture market is slowly rising, although the total import share in Europe is still quite modest and the majority of the furniture consumed in EU is still produced inside the European Union.

To discuss further, Europe is not only an important consumer of wooden furniture but also an important manufacturer. However, the share of furniture production of the EU has contracted over the last decade and the value of furniture production in 2012 was almost at the same level as ten years ago. But, even if the value of furniture output produced in European plants is stable, the trend is counterbalanced by furniture production that takes place in plants run by European companies outside the EU (Tracogna 2013). This means that the European companies continue to play a leading role in the global market.

Lower prices of Asian furniture resulting from lower labour costs are pressuring European plants to find ways how to compensate their relatively high cost of labour. This is possible by investing into the machinery and product development that has reduced the relative contribution of labour to overall costs, and placed a premium on technical, design and market knowledge. European manufactures have also exploited other advantages. Increasingly important factors in wood furniture marketing include quick supply on demand, rapid response to changing tastes and the provision of customers with support services, including guarantees for customers wanting to return products.

Around 85% of the European furniture producing companies are micro enterprises with less than 10 employees (Tracogna 2013), but there are also a number of very large companies. Europe is home to 84 of the world’s top 200 furniture manufactures. These companies are mainly located in Germany, Italy, Sweden, France, the UK, Poland, Finland, the Netherlands, Austria, Denmark, Lithuania, Spain and Romania. The 100 largest companies in Europe have a total turnover of 20 billion euros. Together these 100 companies account for around 20% of the EU furniture sector turnover. Their productive presence now includes numerous plants outside the EU, notably in China, Russia, Ukraine, Belarus and USA (Global Wood, 2014). Because of the financial crisis, the large European furniture companies have been forced to adopt new strategies in order to enhance their competitiveness. These include downsizing, outsourcing and increasing of the production efficiency. This means more investments in machinery, improvement in work efficiency and the efficient use of the operating positions. European furniture manufactures have also focused strongly on brand development.

Inside the EU, the role of the manufacturing sector varies from country to country. Comparative advantages relate to the low cost labour, the presence of raw materials, technological endowment and investments into the sector. Long traditions in furniture making is another comparative advantage (Tracogna 2013).

While external trade forms only a small part of the furniture sector of the EU, it is becoming much more relevant for the European furniture manufacturers. During the recession, manufacturers have become more focused on improving competitiveness related to manufacturers in other countries, particularly China. With consumption static in domestic markets, European furniture companies are seeking to increase sales in other parts of the world. This more outward looking strategy seems to be working for the EU manufacturers. As illustrated on the chart 1.8 exports of wood furniture are rising, particularly to Russia, North America, China and the Middle East.

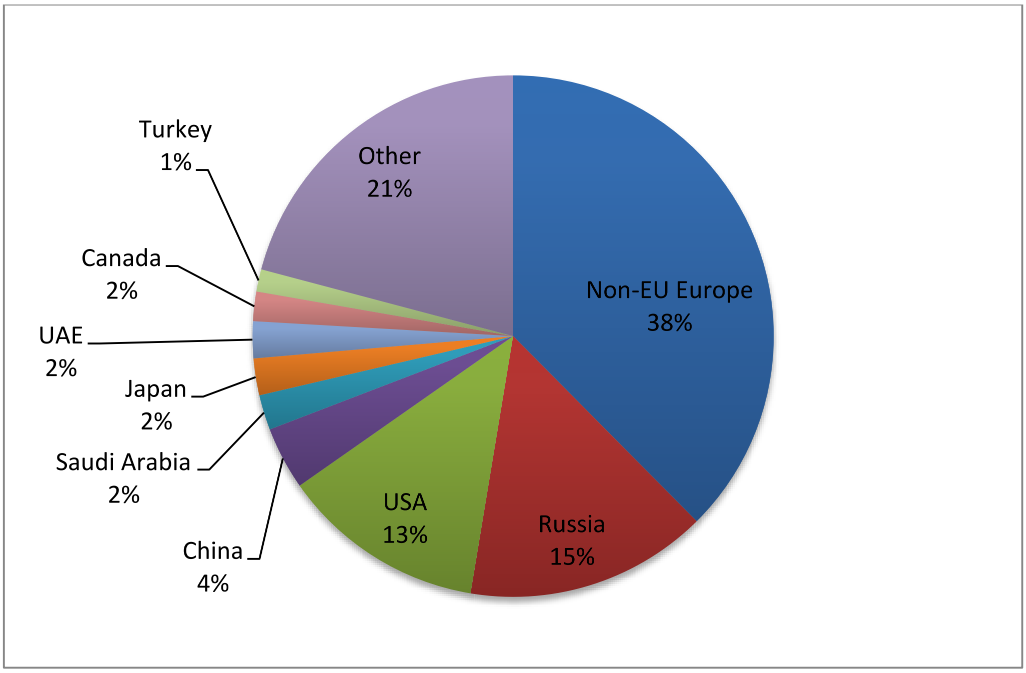

Chart 1.8. EU-28 exports of furniture in 2012 (see Appendix 1)

Source: (Eurostat 2012)

The rise in exports has been led by the manufacturers in Italy, Germany and Poland (Global Wood 2014). Germany is the most important performer in the furniture sector at world level, it ranks second for furniture exports and it is the third world's largest furniture producer after China and the USA (Tracogna 2013). Between years 2012 and 2013, German wooden furniture production has fallen by 5% from euro 6.91 billion to euro 6.57 billion. Between these years the export has decreased by 14% from euro 2.65 billion to euro 2.28 billion (Global Wood 2014).

With 20,000 companies, mainly SMEs, Italy used to be the first furniture manufacturer in Europe until 2012 (Tracogna 2013). Years 2013 and 2014 have been difficult for the Italian economy and the wooden furniture production has fallen by 8% to euro 7.45 billion in year 2013. The exports decreased by 1%. CSIL estimates that as the international trade is recovering, the export of Italian companies is starting to grow again (Colautti 2014).

The furniture production also declined both in the UK and France by 10% and 7% respectively.

Over the years, Poland has reinforced its position at an international level, becoming the world's 7th largest manufacturer and the 4th largest furniture exporter after China, Germany and Italy. Poland recorded a 7% increase in furniture production value from euro 3.81 billion in 2012 to euro 4.01 billion in 2013. The rise of production was mainly due to growth in the local market. The wooden furniture exports of Poland remained stable at around dollar 3.35 billion in both year 2012 and 2013 (Global Wood 2014). There are almost 24,000 companies in Poland that declare furniture production to be their main activity. Polish furniture industry has achieved the highest position among all Polish manufacturing industries. Poland is also an important producer of furniture materials and components which means that Poland has got plenty of raw wood reserves. Also, the technology used in woodworking is quite modern (Wiktorski 2014).

Wooden furniture production has continued to rise not only in Poland but also in other Eastern European countries during the year 2013. For example, Romania is the second largest manufacturer in Eastern Europe after Poland. Wooden furniture production in the country increased 4% to euro 1.05 billion in 2014. Romanian exports of wooden furniture were euro 783 million in 2013. It is important to notice that Romanian economy is weakening and there are reports of shortages of wood for furniture manufacture in the country. This means that Romanian furniture sector may face challenging times ahead (Global Wood 2014).

Wooden furniture production in Lithuania has also increased. For example in the year 2013 furniture production increased 3% from euro 766 million in 2012 to euro 788 million. The majority of this is being exported. The value of wooden furniture production in Lithuania has increased by around 65% in the last 5 years by producing mainly for the furniture giant IKEA (Global Wood 2014).

In Slovakia the wooden furniture production increased by 7% to euro 442 million and was stable in Czech Republic (euro 337 million), Estonia (euro 224 million), Hungary (euro 287 million) and Slovenia (euro 163 million).

To conclude, the European wooden furniture market is an important global player and still accounts for around one quarter of world furniture consumption and production. Major factors of competitiveness for the sector consist of the following factors: research and innovation, skills and quality, design and added value, knowledge and know-how together with better access to the export markets.

1.3 The drawbacks and opportunities of Estonian furniture sector

The previous section sought to develop a picture of the wooden furniture sector in Europe. The focus was on understanding the nature and special location of import, production and trade in the sector. In this section the author is going to analyse the opportunities and challenges the Estonian furniture manufacturers face.

To begin with, furniture industry in Estonia is a sector with long traditions and accounts for approximately 4% of the country’s total value of production. According to Statistics Estonia there are altogether nearly 600 companies active in the furniture manufacturing sector today. This number has increased in recent years. To compare, in 2005 there were about 400 companies in the sector.

As can be seen on the chart 1.9 there are many micro enterprises in the sector that are important employers in rural areas. In 2012 there were 482 companies that employed less than 10 employees.

There are also large companies in the sector, though in 2012 there were only three enterprises employing more than 250 employees. According to the statistics of year 2012, the biggest furniture manufacturing companies are the upholstered furniture manufacturer AS Bellus Furniture, office furniture manufacturer AS Standard and furniture component producer Flexa Eesti AS.

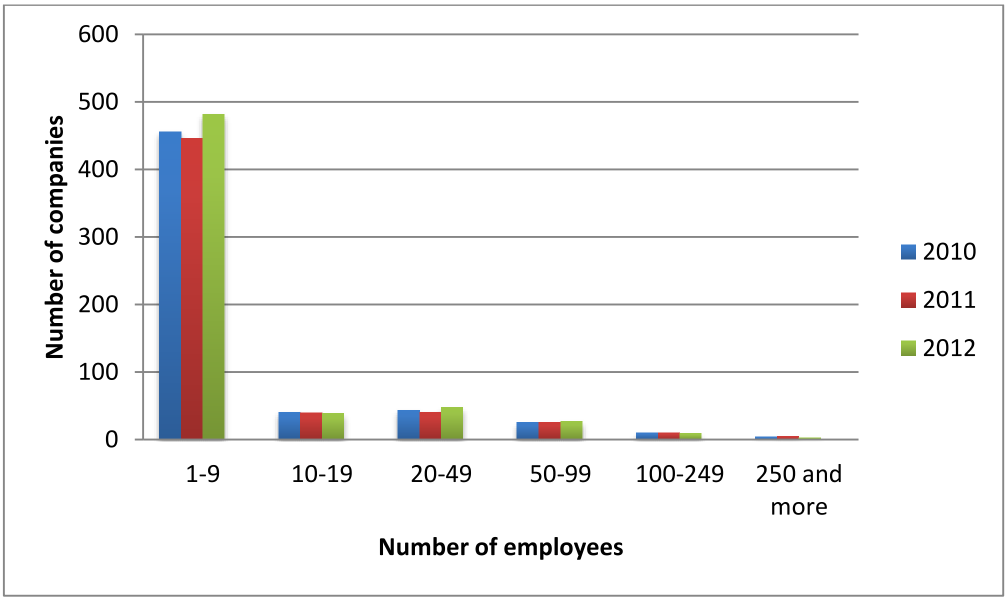

Chart 1.9. The number of employees in the furniture manufacturing companies (see Appendix 2)

Source: (Composed by author based on data of Statistics Estonia)

The total number of employees in the furniture sector has significantly decreased over the years. According to the Statistics Estonia, in 2012 there were about 7,500 employees in the furniture manufacturing sector compared with the year 2005 when there were about 10,000 employees in the sector.

It is important to notice that even if the number of employees has decreased, the chart 1.10 shows that the industrial output per employee has grown: in 2005 it was 31,416 euro per employee but in 2012 it was 52,619 euro per employee. It shows that work efficiency of the furniture producing companies has risen.

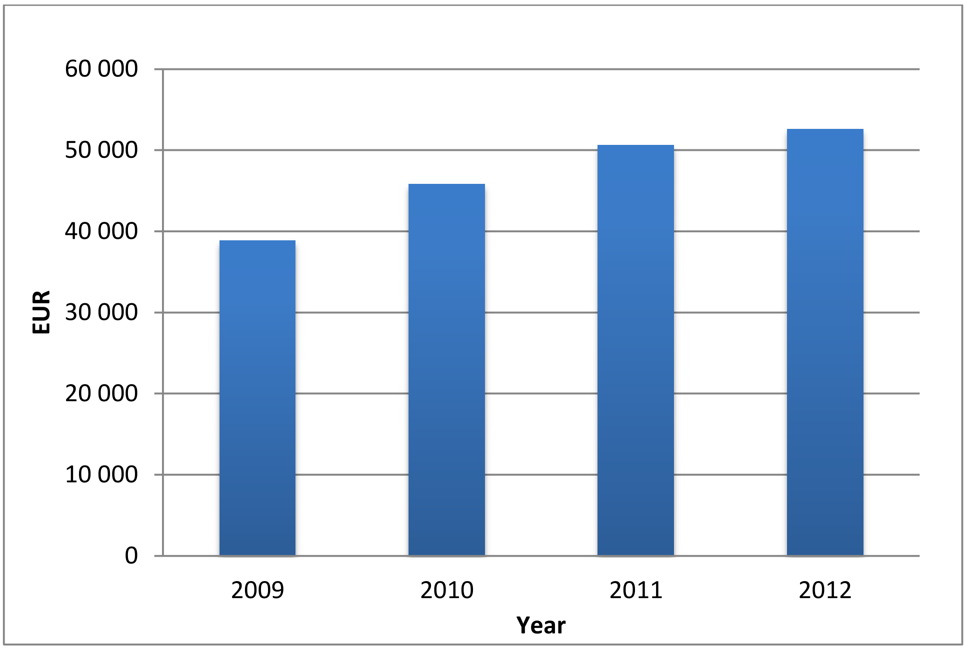

Chart 1.10. Industrial output per employee (see Appendix 3)

Source: Composed by author based on data of Statistics Estonia

Furniture production in Estonia has been associated mainly with subcontracting but there are also manufacturers who use designers and develop their own collections.

As the Estonian domestic market is very small and price sensitive, then selling to foreign markets is very important. Export share in sales revenue of furniture in 2010 was 69%, 2011 68% and 2012 66%. As shown in the table 1, furniture sales revenue and export have both increased but the export share of sales revenue has decreased by 3% in 2012 compared with the year 2010. It means that domestic consumption has grown faster than exports but exports still accounts for a large part of the furniture production.

Table 1. Furniture sales of Estonian companies in current prices

	Sales revenue (million EUR)	**Export (million EUR)**	**Export share of sales revenue**
2010	355	245	69%
2011	394	268	68%
2012	413	272	66%

Source: (Composed by the author based on data of Statistics Estonia)

The following chart 1.11 shows the foreign trade balance for furniture sector in Estonia, which has been strongly positive in the recent years.

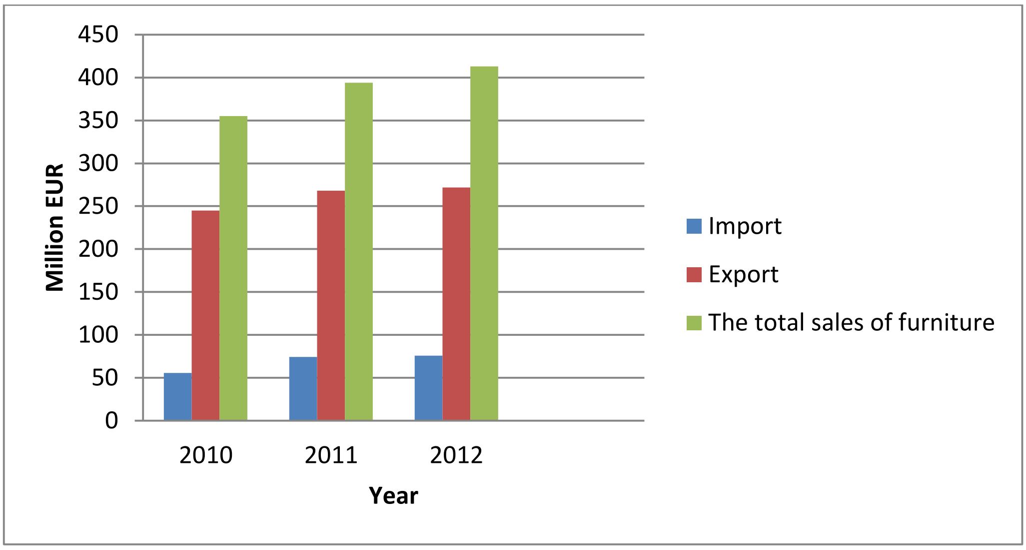

Chart 1.11. Foreign trade balance of Estonia (see Appendix 4)

Source: (Composed by the author based on the data of Statistics Estonia)

The main countries of destinations for Estonian furniture have been the Nordic countries. In 2012, the main furniture export country was Finland accounting for 27% of the total exports. For years, Finland has been the main export country for Estonian furniture and most likely it is also the case in the near future. Sweden and Norway accounted for 15%, Germany 9%, UK 6% and France 5% of the total exports as shown in the chart 1.12.

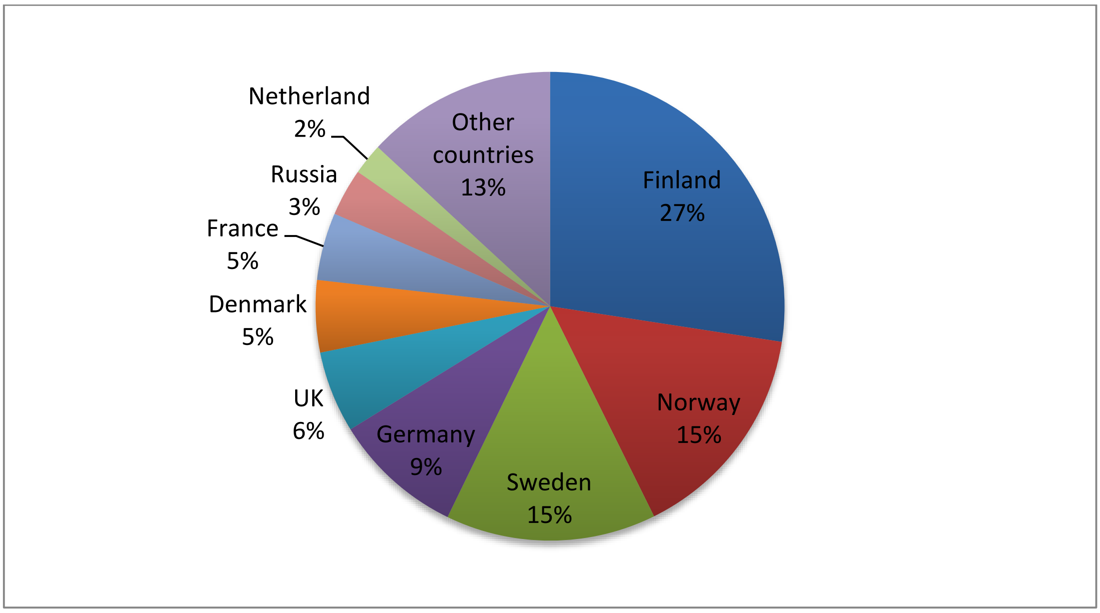

Chart 1.13. Furniture export in Estonia by country in 2012 (see Appendix 5)
Source: (Composed by author based on the data of Statistics Estonia)

The chart 1.14 shows the main commodity groups being exported by Estonian furniture manufacturers. According to the Statistics Estonia, in 2013 the main export article of Estonian furniture has been seats. Unfortunately, the exact contents of this product group has not been given but it can be concluded that in a large extent it includes upholstered furniture.

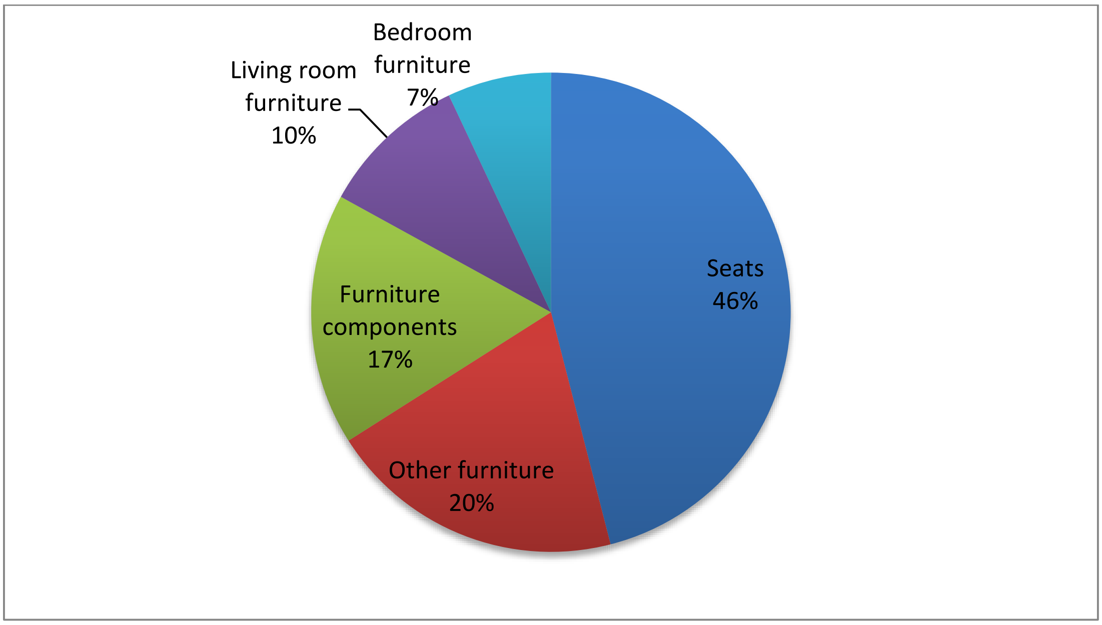

Chart 1.14. The export revenue distribution of Estonian furniture production by main commodity groups in 2013

Source: (Composed by author based on the data of Statistics Estonia)

As nearly 70% of the furniture produced in Estonia is sold for export, it is important to analyse the export related problems and advantages. In Estonia, the furniture manufacturing companies are mainly small enterprises whose export capabilities are limited. There are many reasons behind this, for example the lack of resources, limited marketing and sales skills. The Estonian Furniture Industry Association conducted a survey amongst its members in 2011 to find out the main obstacles to export.

The following chart 1.15 illustrates the findings of this survey and as can be seen, the most mentioned reason was the small size of the business. This leads to the other mentioned problems like marketing experience, work efficiency, required production capacity, etc.

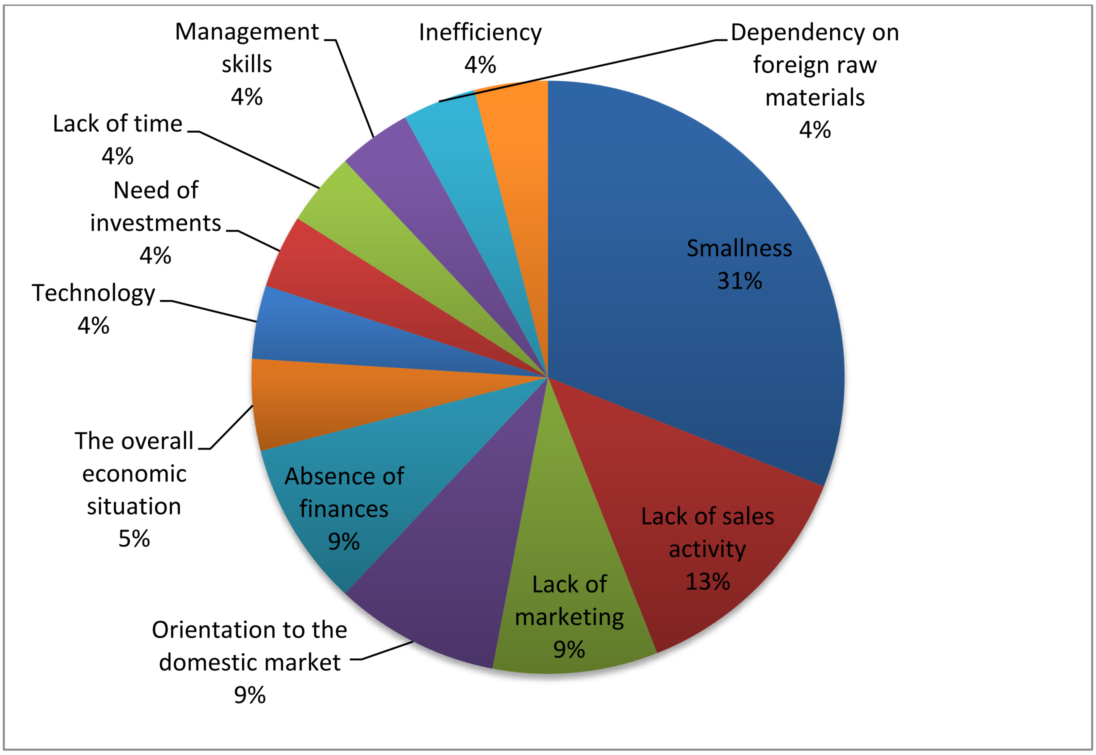

Chart 1.15. The main obstacles for Estonian companies to start export

Source: (Estonian Furniture Industry Association, 2011)

To add, in 2010 the Estonian Chamber of Commerce and Industry carried out a survey which also examined the export-related problems and opportunities that Estonian furniture manufacturing companies face. The author finds it important to analyse some of the findings pointed out in this survey.

To begin with, the study revealed that speed, quality and flexibility are seen as their primary competitive advantages by the furniture producers themselves. As the production processes are less automatic than in big mechanized plants as for example in China or Poland, the possibilities to make different kinds of high quality products are easier. This means it is possible to produce products that need more handiwork and to provide smaller order sizes. Also, as the production processes are less automatic, it makes it possible to react more quickly to the changing demand.

One of the biggest problems brought out in the survey was the high price of logistic services (Eesti Kaubandus-Tööstuskoda 2010). This reveals the importance of Nordic markets because the product prices of Estonian manufacturers compared with the local producers are lower and the logistic costs are also not so high due to near proximity of the market.

Additionally, it was brought out that one of the disadvantages of Estonian producers, which is related with logistic costs, is the absence of intermediate warehouses (Eesti Kaubandus-Tööstuskoda 2010). However, it depends on the product — for knocked-down wooden furniture the presence of intermediate warehouses is not so important as the transportation costs are not so high compared, for example, with upholstered furniture.

The additional drawbacks of Estonian manufactures are similar to the findings of Estonian Furniture Industry Association and include limited marketing skills, poor knowledge of foreign markets, limited network of contacts and poorly protected property rights (Eesti Kaubandus-Tööstuskoda 2010). The problems of different companies vary and depend on size, export experience and capital structure. It appears that the foreign-owned companies have been more successful in export markets than the companies based on Estonian capital. One of the reasons is the wide contact network of the owners and better understanding of foreign market business culture.

The main advantages of Estonian manufactures brought out in the survey are outlined below in the order of importance (Eesti Kaubanudus- Tööstuskoda 2010):

- Quick responding to the changes in demand
- High quality of products
- The presence of know-how
- Long export experience and personal contacts abroad
- High quality of labour
- Good language knowledge
- High quality products with competitive price level
- Contemporary technology
- Sufficient capacity

One of the biggest advantages of Estonian manufacturers is definitely the lower wage level compared with the Western and Central European countries. This enables to provide a competitive product price. The availability and closeness of raw material is also a huge advantage that helps to speed up the manufacturing process and make it cheaper. The price of raw material is dependent on the construction and energy sector or more precisely on the extent these sectors are using wooden material. For example, during the economic boom the prices of wooden material significantly increased and lots of furniture manufactures were forced to close down.

To conclude, the competitiveness of Estonian furniture manufactures is dependent on the welfare of other economic sectors, the overall wage level and economic development. The drawbacks of international competitiveness are the steadily rising prices of raw materials and wage level. But it is important to notice that at the same time the work efficiency and technology level of the Estonian furniture companies is steadily rising that enables to keep product price competitive and increase the production volumes.

1.4 Competitive advantage of Letrim OÜ

One of the most important trends in industrial organization of the past quarter century has been the growth of collaboration between independent companies. These inter-firm alliances involve cooperative relationships that are not fully defined either by formal contracts or by ownership. The term strategic alliance has been used to refer to such alliances where the parties maintain autonomy but are bilaterally dependent to a non-trivial degree. Strategic alliances embrace a diversity of collaborative forms, such as supplier-buyer relationships, outsourcing agreements, technical collaboration, shared new product development, shared manufacturing agreements, etc. (Grant; Baden-Fuller 2004). Letrim OÜ, established in 2008, is a fast developing family company that is engaged in marketing of furniture. This knowledge-based company is using subcontractors for production and different partners for other services, such as accounting, transportation, constructional work and design. As subcontractors, the company uses different medium and small sized Estonian furniture manufacturers. On the part of resale, Letrim collaborates with various wholesalers who are taking care of the marketing by supplying furniture to Central European markets. Through these strategic alliances it is possible to run the company efficiently and profitably.

There are two employees active in the company today: manager and sales manager.

The main aim of the company is to offer high quality furniture with competitive price. Furniture sales (100% export) accounts for 90% of the company’s turnover, other 10% comes from service provision. The main export markets of the company are located in Central Europe, for example Denmark, Germany and Switzerland.

The product range of Letrim OÜ consists of different furniture:

- Living room furniture: chests of drawers, cupboards, display cases, coffee tables
- Bedroom furniture: beds, cupboards, chests of drawers, bunk beds
- Hall furniture: shoe cupboards, shelves
- Bathroom furniture: sink cabinets, shelves
- Kitchen furniture: dining tables
- Other furniture: e.g., chests for clothes

Figure 1. Letrim OÜ Products

Source: (Letrim OÜ Catalogue)

All products are manufactured of solid wood pine and product development is carried out in cooperation with the customer. From among the order inquiries sent to the company, the company attempts to select the products which are most profitable to manufacture.

The main risk associated with products and services is the quality risk as there can be problems with the quality of raw material, treatment of material or handling.

The current supply chain is presented below on chart 1.16.

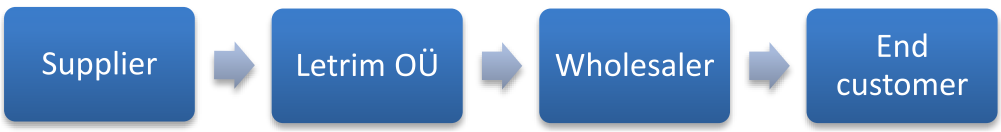

Chart 1.16. Supplier chain

Source: (Composed by author)

The supply-chain of the company is order-based as the company does not want to take additional risks by keeping the products in stock. Delivery time is 6-8 weeks. Minimum quantity the company is ready to supply is 50 pieces per product. This is necessary to keep the price of delivery costs reasonable and the prices of products competitive.

According to the Export Plan (2013) of the company, the author is bringing out the main internal and external uncertainties of Letrim OÜ:

- Financial crisis
  Economic recessions in target markets can lower furniture demand. As the company is selling lower-priced furniture that can be classified as commodity product in the big Central-European markets, it is unlikely to occur that the demand is going to decline drastically.
- Price rise of raw material
  Lowers the ability to offer competitive price.
- Supplier risk
  There is a possibility that main suppliers can go bankrupt. It is possible to lower the risk by widening the supplier network.
- Solvency of the customer
  Financial risks resulting from new clients cannot be predicted. It is possible to lower the risk by using different kind of insurances.
- Entering barriers in different markets
  There is a high competition in the markets that makes it difficult to enter the markets. It is possible to use local agents, distributors and wholesalers to facilitate the entry.
- Price competition

  The cheaper prices of Chinese and Polish furniture manufacturers are making it hard to stay competitive. Higher prices can be compensated with higher and more stable quality than the Chinese or Polish producers can offer. To add, the higher prices can be compensated by offering wider selection of products and services. The trend in recent years also shows that there is a demand for changing the product range more often. Also, technological and constructional consultancy in case of developing new products is an advantage in front of the other competitors.

As defined by Sutherland and Canwell (2004), a core competency is a deep proficiency that enables a company to deliver unique value to customers.

The core competences of Letrim are as follows:

- Know-how

  One of the company's key success factors is connecting supplier opportunities and client demands. This enables to find most suitable supplier for every client and product and consult producers in all aspects that concern the quality, production efficiency, construction, etc.
- Good business relations with clients and suppliers

  Business relations with clients and suppliers are meant to last for years. Therefore it is very important that everyone's interests have been taken into account. For example, price negotiations where it is important to offer satisfactory price for both the client and the supplier.
- Flexibility

  Readiness to offer required product batches with different treatments. By combining different producers it is easier to meet client's wishes (different treatments, more complex products, constructional consultancy, etc.).
- Reliability

  Adherence to deadlines (delivery and volumes)
- Quality

  Readiness to guarantee the required quality level. Company is doing cooperation only with the producers who can guarantee required quality level.

As mentioned before, the furniture production and sales is a very competitive sector. The main competitors in addition to the European manufacturers are the Chinese and Brazilian producers whose price level is much lower compared to Letrim. It is important to emphasise that in China and Brazil the quality level of manufactured products is often very low. To add, delivery deadlines are very long and refund for poor quality products is not possible. Therefore, the main competitive advantages of Letrim are the balance between price, quality, security of supply and speed of delivery or, in other words, high quality products with a competitive price.

Table 1.2. Summary of the SWOT analysis of Letrim

STRENGHTS	**WEAKNESSES**
• The company has got all the competences required for furniture production and export • Ability to offer more complex products with different treatments and high quality	• It takes time to run in new sales channels • Inability to offer very large quantities
OPPORTUNITIES	**THREATS**
• To grow with the market	• Tight competition in export markets • Weaker than expected growth in the market demand • Economic downturn can weaken demand and lower the prices • Price rise of raw material

Source: (Letrim OÜ Export plan)

2 THEORY

2.1 Internationalization of SMEs

Internationalization, an increase in international operations and international linkages between firms in various geographical areas has become an everyday reality for contemporary firms. The interconnectedness between customers and marketing partners has increased due to major advances in information, communication, transportation and technologies (Elo 2005). It can be said that geographic expansion is one of the most important paths for firm growth. By broadening customer bases through entering into new markets, firms are able to achieve a larger volume of production, and grow. Manufacturing and service companies may enter international markets for several reasons, but the most important impulse behind entering to foreign markets is the prospect of profit on immediate sales (Root 1994; 1).

In the book *A Framework For International Business* Cavusgil brings out five different characteristics that are associated with international expansion:

1. Push and pull factors serve as initial triggers
   Push factors include unfavourable trends in the domestic market that compel firms to explore opportunities beyond national borders, such as declining demand, growing competition at home market, and arrival at the mature phase in a products life cycle. This is the case for the wooden furniture market in Estonia. Pull factors are favourable conditions in foreign markets that make international expansion attractive, such as the potential for faster growth and higher profits, foreign government incentives, or increased opportunities to learn from competitors.
2. Initial international expansion can be accidental or unplanned
   For example, unexpected foreign customer without any deliberate export activity.
3. Risk and return must be balanced
   Risk-averse managers prefer entering safe markets using conservative entry strategies by targeting markets with a culture and language similar to the home country.
4. Internationalization is an ongoing learning experience

Internationalization exposes managers to new ideas and valuable lessons they can apply to the home market and to other foreign markets.

5. Firms may evolve through stages of internationalization
   With growing experience and competence, the firm will target increasingly complex markets by using more challenging entry strategies such as FDI and collaborative ventures.

The prominence of the internationalization phenomenon has captured the interest of researches in strategic management, international business and entrepreneurship for many years, though the focus has mainly been on large, well-established firms. But the internationalization of micro, small and medium-sized enterprises also deserves more attention as they play a central role in the European economy and are major source of entrepreneurial skills, innovation and employment. According to the European Commission the SMEs represent about 99% of all enterprises in the European Union (Beamish, Lu 2001). Numerous definitions strive to clearly define SMEs, yet there is no consensus up to now. Researches broadly agree that various quantitative and qualitative characteristics determine SMEs. Qualitatively, SMEs often join ownership, liability, management and risk in one person. Quantitative classification relate to turnover, profit, total assets and the number of employees. The European Commission defines SMEs as firms with less than 250 employees, a sales volume of up to 50 million euros, and total assets of maximum 43 million euros (Eiche 2010).

As mentioned before, the concept of international business refers to the performance of trade and investment activities by firms across national borders. Firms organize, source, manufacture, market and conduct other value-adding activities on an international scale. They seek foreign customers and engage in collaborative relationships with foreign business partners. Firms exchange many physical and intellectual assets, including products, services, capital, technology, know-how, and labour (Cavusgil 2013; 2). As a result, it seems that anyone can start up an international company and export to distant countries. In theory that can be true but in real life this is not so simple and multiple factors should be considered. Entry strategy for international market is a comprehensive plan. It sets forth the objectives, goals, resources, and policies that will guide the international business operations of a company over a future period long enough to achieve sustainable growth in world markets. Without an entry strategy for a product or target market, a company has only “sales” approach to foreign markets (Root 1994; 2). The following table 2 outlines the differences between the sales and entry strategy approach.

According to Root (1994), the sales approach is not viable in a world of international competitors who plan and act to create foreign market position for long run success.

Table 2. Entry strategy approach versus "sales" approach to international markets

	"Sales" approach	**Entry strategy approach**
Time horizon	Short-run	Long-run
Target markets	No systematic selection	Selection based on analysis of market/sales potential
Dominant objective	Immediate	Build permanent market position
Resource commitment	Only enough to get immediate sales	What is necessary to gain permanent market position
Entry mode	No systematic choice	Systematic choice of most appropriate mode
New product development	Exclusively for home market	For both home and foreign markets
Product adaption	Only mandatory adaptions of domestic products	Adaption of domestic products to foreign buyers preferences, incomes and use conditions
Channels	No effort to control	Effort to control in support of market objectives/goals
Price	Determined by domestic full cost with some adjustments to specific sales situations	Advertising, sales promotion, and personal selling mix to achieve market objectives/goals
Promotion	Mainly confined to personal selling or left to middleman	

Source: (Root, F. 1994)

Before undertaking an international venture, launching a new product in foreign markets the firm should conduct a formal assessment of its readiness to internationalize. When assessing the readiness of the company to internationalize, it has to assess the quality of skills, capabilities, and resources available for internationalization. An evaluation of organizational capabilities is useful for both the firms which are new to international business and to those with considerable experience (Cavusgil 2013; 161).

It is equally important to assess the products or services suitability for foreign markets.

The essential and often the hardest task for most firms is to identify the best country for export. Population, income, demographic characteristics, government stability, and nature of the general business environment can help to determine which markets are growing and which shrinking. There are different questions firm's managers should answer before going international:

- What is the market demand or possible potential for the product of the company
- How is the competition
- What is the sale price for the product
- Are there entry barriers (customs, quotas, property rights, other barriers or political or economical risks)

These questions are just few that need to be answered.

There are also other methods that provide important information about target market. For example:

1. Porter's five forces

In his book, M. Porter identified five competitive forces that shape every single industry and market that can be seen on the chart 2 below.

Chart 2. Porter's five competitive forces

Source: (Harward business review, 2008)

The mentioned five forces are, to begin with, the threat of new entrants. Intense competition on the market can make the market entry for a new firm very difficult. Additionally, different market entry barriers can limit the number of entrants. The second force is the power of suppliers. This measures how much pressure suppliers can place on businesses within the industry. The larger and the more dominant the supplier, the further it can squeeze the businesses margins and profits. The power of buyer measures how powerful are the customers and what pressures they can apply to the firm. The larger and more reliant customers are, the more likely they are to be able to affect the margins and volumes of business. Threat of substitute products measures how likely it is that buyers will switch to a competing product or service. Businesses should be aware that similar products, if not exact substitutes, may tempt the buyer to switch to another supplier and this is a serious threat for a firm. The last force is a competitive rivalry that measures the degree of competition between existing businesses in an industry (Sutherland 2004).

2. PESTLE

The PESTLE analysis is the analysis of the environment as a whole in which a business operates or tends to offer its trade. These are systematic factors that are beyond ones control and businesses need to chart out strategies keeping the results in view to peacefully coexist and keep on gaining revenues despite the concurrent situation. It covers political, economic, social, technological, legal and environmental factors that should be analysed because they can differ from country to country.

The political factors analyse the political temperament and the policies that a government may put in place for some effect, for example, the fiscal policy, trade tariffs and taxes. The economic factors take into view the economic condition prevalent in the country, which include the inflation rates, foreign exchange rates, interest rates etc. All these can affect the supply and demand cycle and can result in major changes of the business environment. Social factors have to do with the social mind-set of the people that live in a certain country. This sums up the aspect of culture, age demographics, gender and its related stereotypes. Technological factors take into consideration the rate at which technology is advancing and how much integration does a company needs to have with it. Legal factors have to do with all the legislative and procedural components in an economy. Also, this takes into account certain standards that the business might have to meet in order to start production/promotion. Environmental factors have to do with geographical locations and other environment related factors that may influence the trade. For example, agri-businesses hugely depend on this form of analysis (Makos 2014).

3. SWOT

A SWOT analysis is a structured planning method used to evaluate the strengths, weaknesses, opportunities and threats involved in a business venture. The analysis can be carried out for a product or business and it involves specifying the objective of the business venture and identifying the internal and external factors that are favourable and unfavourable to achieve that objective. The following chart 2.1 illustrates the elements of the PESTLE and SWOT analysis.

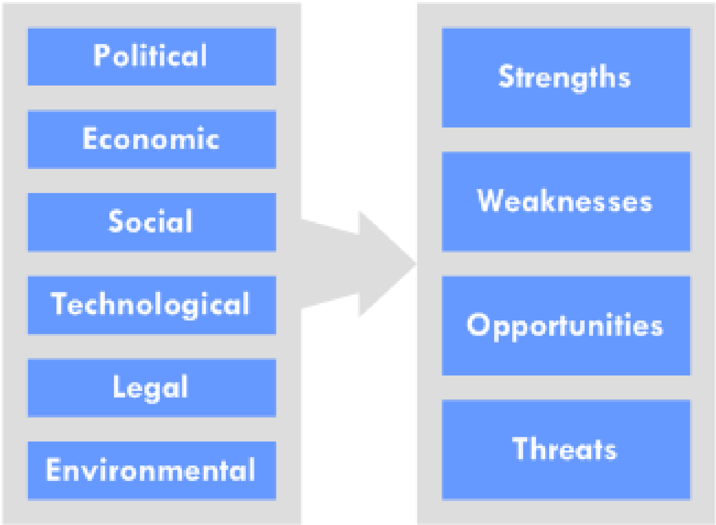

Chart 2.1. Elements of PESTLE and SWOT analysis
Source: (Infonet, 2008)

Some firms target countries that are psychically near — that is, countries similar to the home country in language, culture, legal environment, etc. As managerial experience, knowledge, and confidence grow, firms expand into more complex and culturally distant markets. Other firms are more venturesome and target non-traditional, higher risk countries. The information necessary for country screening varies by product type or industry (Cavusgil 2013; 164).

It is also important to examine the external business environment by studying opportunities and threats in the markets where the firm seeks to do business. Aside from having to develop new resources and capabilities on foreign entry, an internationalizing firm faces heightened political risks as well as the operational risks stemming from the foreignness of the new environment (Beamish, Lu 2001).

2.2 Approaches to foreign market entry mode selection

Firms interested in servicing foreign markets face a difficult decision with the regards to the choice of an entry mode. The key assumption underlying in international business literature is that the best entry mode is the one that aligns the entrant's strengths and weaknesses with the local markets environment as well as with the firm's structural and strategic characteristics (Brown 2003). When selecting an entry mode, the management must identify underlying motivation of the firm for venturing abroad. The motivation for internationalization can be divided into two — internal and external. Albaum, Strandskov and Duerr (1998) have divided internal and external factors into reactive and proactive factors. For example, following major customers abroad is a reactive mode, in contrast seeking high-growth markets abroad is a proactive mode (Cavusgil 2013).

There are different distinct market entry strategies to choose from. The options available to a firm include direct and indirect exporting, licencing, joint venture and strategic alliance as illustrated on the chart 2.2.

Chart 2.2. Global market entry strategies

Source: (Composed by the author)

Each of these strategies has its advantages and disadvantages, and each places specific demands on the managerial and financial resources of the firm (Agarwal 1992). The motives of companies that launch exporting, licencing, or franchising ventures are usually straightforward.

They typically seek to maximize returns from investments they have made in products, services and know-how by seeking a larger customer base in foreign markets. In contrast, FDI and collaborative ventures are riskier and usually flow from more complex motivations (Cavusgil 2013). Therefore, the entry mode selection is very important, if not a critical strategic decision.

When undertaking foreign market entry, the management should consider numerous factors, including (Cavusgil 2013):

- Goals and objectives (profitability, market share, competitive positioning)
- Degree of control the firm wants to maintain
- Resources and capabilities available to the firm
- Degree of risk the management is willing to take
- Characteristics of the product or service to be offered
- Target market conditions (legal, cultural, economic etc.)
- Competition in the target market
- Availability of partners in the market
- Long term strategic importance of the market
- The value adding activities the firm is willing to perform itself in the market

All the above-mentioned factors are extremely important to consider before choosing an entry mode. An important factor to analyse is the degree of control the firm wants to maintain over venture. Control is the ability to influence the decisions, operations, and strategic resources involved in the foreign venture (Cavusil 2013). The next chart 2.3 illustrates the foreign market entry strategies based on the degree of control.

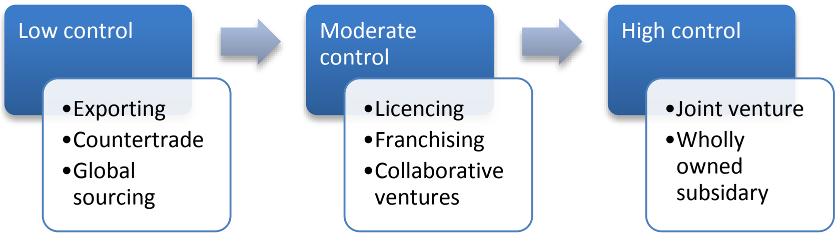

Chart 2.3. A classification of foreign market entry strategies based on degree of control
Source: (Cavusgil 2013)

As seen on the chart 2.3 above, low-control strategies are exporting, countertrade and global sourcing. They provide the least control over foreign operations because the firm delegates considerable responsibility to foreign partners, such as distributors or suppliers. Moderate control strategies are contractual relationships such as licencing, franchising and project-based collaborative ventures. High-control strategies are equity joint ventures and FDI, as in this case firm attains maximum control by establishing a physical presence in the foreign market (Cavusgil 2013; 180).

2.2.1 Export as an market entry mode

Exporting is the entry strategy responsible for the massive inflows and outflows that constitute global trade and generates substantial foreign exchange earnings for nations. Export is also the most common mode for SMEs to enter foreign markets. This is because exporting is very flexible entry strategy. The exporter can enter and withdraw from markets fairly easily, with minimal risk and experience. This is why the author is investigating the export method more thoroughly than other entry methods. Osland, Taylor and Zou (2001) claim that competitive issues are very important factors associated with the use of exporting. They found that exporting is the most appropriate entering method for the very competitive target market, where the competitor's products are very similar and easily substitutable by customers. There is no need for using the high control mode that requires a high level of resources because in case of easily substitutable products the customers are very price sensitive. They also claim that exporting is the quickest method for entering foreign markets and it helps to prevent competitors from claiming first-mover advantages in the new foreign market.

Export can be divided into direct and indirect export which are distinguished by how the exporting company carries out the transaction flow between itself and the host country buyer. The decision between direct and indirect export mode depend on the control desired by the exporting companies:

- Direct export occurs when an exporting company sells directly to an importer or a buyer in a foreign market
- Indirect export occurs when the exporting company uses independent organizations that are located in the host country. For example, agents, resellers etc

The main difference between these two export modes is the involvement of the exporting companies in the global marketing process. For example, companies who choose direct exporting can build up overseas contacts, do market research and can be involved in the design of the marketing mix strategies (Hollensen 2007).

Hollensen (2007) has constructed a table for the two different types of export. The table 2.1 shows both the advantages and disadvantages of the two types of entry modes.

Table 2.1. Advantages and disadvantages of different export modes

Export modes	Advantages	Disadvantages
Indirect exporting (e.g., export buying agents, export management company)	• Limited resources and investment required • High degree of market diversification is possible as the company utilizes the internationalization of an experienced exporter • Minimal risk • No export experience required	• No control over marketing mix elements other than the product • An additional domestic member in the distribution chain may add costs, leaving smaller profit to the producer • Lack of contact with the market • Limited product experience (based on commercial selling)
Direct exporting (e.g., distributor or agent)	• Access to local market and contacts to potential customers • Shorter distribution chain • Market knowledge acquired • More control over marketing mix • Local selling support and services available	• Little control over market price because of tariffs and lack of distribution control • Some investment in sales organization required • Cultural difference • Possible trade restrictions

Source: (Hollensen 2007)

Indirect exporting may be a good way for a firm to enter a foreign market as it demands little if any foreign market knowledge on the part of the manufacturer. A company that wants active penetration of international markets should choose the direct export channels. However, direct exporting has higher start-up costs, greater information requirements and higher risks than indirect exporting. Direct exporting relies on two principal channels: the foreign agent/distributor channel and the foreign branch or subsidiary channel. The third channel can be considered the direct contact between the manufacturer and final buyers in the target market, such as mail-order exporting. Direct export channel is therefore an element of the full marketing channel and its selection. Facilitating agencies provide services to the manufacturer, for example the services of sales agents, transportation companies, but they do not engage in export sales transactions or control the marketing effort as do channel members in case of indirect export (Root 1994; 59).

In addition to the direct and indirect export there are also cooperative export modes or, in other words, export marketing groups. Export marketing groups are frequently found among SMEs attempting to enter export markets for the first time. Many firms do not achieve sufficient scale economies in manufacturing and marketing. One of the most important motives for SMEs to join with others is the opportunity of effectively marketing a complementary product programme to large buyers.

For example:

Manufactures A, B, C have their core competences in the upstream functions of the following complementary product lines:

A- living room furniture

B- dining room furniture

C- bedroom furniture

Together they form a broader product concept that could be more attractive to a buyer in a furniture retail chain, especially if the total product concept targets a certain lifestyle of the end costumers. The cooperation between manufacturers can be tight or loose. In loose cooperation the separate firms in a group sell their own brands through the same agent, whereas a tight competition often results in the creation of a new export association. Even if such groups have many advantages for SMEs there is not many of those that are actually running. One of the reasons could be that the firms have conflicting views and many of them want to obtain their independence (Hollensen 2007; 323).

Experienced managers use a systematic approach to successful exporting by assessing potential markets, organizing the firm to undertake exporting, acquiring appropriate skills and competences, and implementing export operations. On the chart 2.4 there are highlighted necessary steps for exporting.

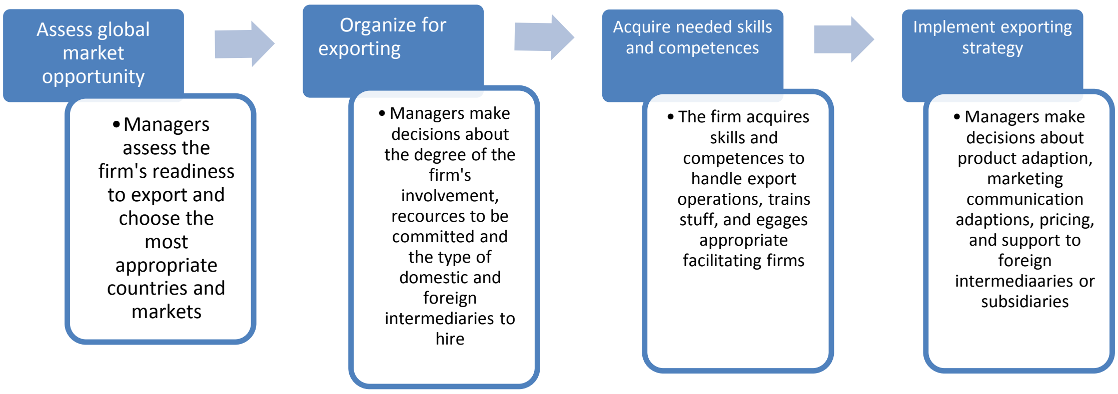

Chart 2.4. A systematic approach to exporting

Source: (Cavusgil 2013)

As a first step, the management of a firm assesses the various global market opportunities available to the firm. It analyses the readiness of the firm and its products to carry out exporting, screens for the most attractive export market, identifies qualified distributors and other foreign business partners and estimates industry market potential and company sales potential (Cavusgil 2013; 186).

Next, managers ask what types of managerial, financial and productive resources the firm should commit to exporting. Export transactions require specialized skills and competences in areas such as product development, distribution, logistics, finance, law, and currency management. In the final stage, the firm implements its export strategy (Cavusgil 2013; 188).

2.2.2 Foreign direct investment and collaborative ventures

Foreign direct investment is an internationalization strategy in which firms establish a physical presence abroad through direct ownership of productive assets such as capital, technology, labour, land, plant and equipment. According to Beamish and Lu (2001), FDI can require a greater level of resource commitment in foreign countries than exporting and is more difficult to reverse. It is also less flexible in coping with investment hazards, such as political instability and fluctuating market conditions in host countries.

An international collaborative venture is a cross-border business partnership in which collaborating firms pool their resources and share costs and risks of a new venture. Here the focal firm partners with one or more companies to pursue a joint project or other business venture. International collaborative ventures are also sometimes called international partnerships or international strategic alliances (Cavusgil 2013; 201). SMEs often face constraints deriving from the internal shortages of information, capital and experience. Such deficiencies impose constraints on internationalization. Alliances have been suggested as one important means of overcoming resource and capability deficiencies and enhancing the likelihood of success for internationalization of SMEs. Alliances can have several benefits, such as minimization of transaction cost, increased market power and shared risks. Alliance partners can help SMEs to overcome shortages of capital, equipment and other tangible assets through resource sharing between two or more separate firms engaged in the alliance. There can be partners from the host country, from the home country or firms from the third country (Beamish, Lu 2001).

The ultimate goal of FDI and international collaborative ventures is to enhance company competitiveness in the global marketplace. As seen in the chart 2.5 below there are three types of reasons why managers choose FDI or collaborative ventures for going on a foreign market.

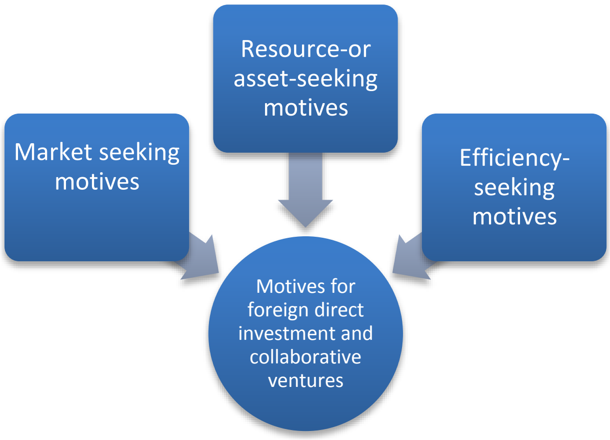

Chart 2.5. Firms motives for foreign direct investment and collaborative ventures

Source: (Cavusgil 2013)

There are three main market-seeking motives: to gain access to new markets or opportunities, follow key customers and compete with key rivals in their home market. To add, firms frequently want to acquire production factors that are more abundant or less costly in a foreign market. For example, firms in oil industries have a little choice but to go where the raw material is situated. Efficiency-seeking motives are seen as the intention of the firm to avoid tariffs and other trade barriers which usually apply only to exporting (Cavusgil 2013; 204).

2.2.3 Contractual strategies

Contractual entry strategies in international business are cross-border exchanges in which the relationship between the focal firm and its foreign partner is governed by a contract. There are two common types of contractual entry strategies: licencing and franchising. Licensing is an arrangement in which the owner of intellectual property grants another firm the right to use that property for a specified period of time in exchange for compensation. Franchising is an advanced form of licencing in which one firm allows another the right to use an entire business system in exchange for fees.

Cross-border contractual relationships share several common characteristics (Cavusgil 2013; 222):

- They are governed by a contract that provides the focal firm a moderate level of control over the foreign partner
- They typically include the exchange of intellectual property and services
- Firms can pursue them independently or in conjunction with other foreign market entry strategies
- They provide dynamic choice
- They often reduce local perceptions of the focal firm as a foreign enterprise
- They generate a consistent level of earnings from foreign operations

Contractual strategies are fairly common in international business and allow companies to routinely transfer their knowledge assets to foreign partners. For example different fast food, retailing, car rental, etc. rely on licencing and franchising agreements.

2.3 Factors influencing the choice of the entry mode

In the previous chapter the author described different market entry methods and analysed their strengths and weaknesses. In this chapter the author is looking more closely different factors that influence the choice of the market entry mode.

Entry strategy for international markets is a comprehensive plan. It sets forth the objectives, goals, resources, and policies that will guide the international business operations of a company over a future period long enough to achieve sustainable growth in world markets (Root 1994; 2). The choice of the entry mode of a company for a given product or target country is the net result of several, often conflicting forces. For the next, F. Root (1994) has brought out several factors that influence the choice of and entry mode.

In the previous chapter there were explored several entry modes for international markets, but how should managers decide on the right entry mode for a given product and given target market?

According to Root (1994), there are three different decision rules for entry mode selection:

- Naive rule

  Managers follow the naive rule when they consider only one way to enter foreign market. Statements such as "We only export" or "We only licence" are examples of the naive rule. Commonly, this rule is implicit in the behaviour of managers rather than explicit in a policy statement. This rule ignores the heterogeneity of the individual foreign markets and entry conditions.
- Pragmatic rule

  Most firms appear to start their international careers by using the pragmatic rule. In this case the decision maker uses a workable entry mode for each different foreign market. In the early stages of exporting the firm typically starts doing business with a low risk entry mode. Only if the particular initial mode is not feasible or profitable will the firm look for another workable entry mode.
- Strategy rules

  The strategy decision rule- use the right entry mode- is more difficult for managers to follow than the pragmatic rule, because it demands systematic comparison of alternative modes, but it guides manager to better entry decisions. This approach requires that all alternative entry modes are systematically compared and evaluated before any choice is made. An application of this decision rule would be to choose the entry mode that maximizes the profit.

Many SMEs use the pragmatic or even naive rules.

There are many factors that influence foreign market entry mode decision. Seen from the perspective of the manufacturer the market entry modes can be classified into three groups:

1. Export modes: low control, low risk, high flexibility
2. Intermediate modes (contractual modes): shared control and risk, split ownership
3. Hierarchical modes (investment modes): high control, high risk, low flexibility

Hollensen (2007) brings out next factors that should affect the choice of a foreign market entry mode.

Internal factors:

- Firm size

  Size is an indicator of the availability of the resources of the company. Increasing resource availability provides the basis for increased international involvement over time. SMEs are more likely to enter foreign markets using export modes because they do not have the resources necessary to achieve a high degree of control or to make these resource commitments. As the firm grows, it can use the hierarchical model.

- International experience

  Another firm-specific factor influencing mode choice is the international experience of managers and thus of the firm. International experience reduces the cost and uncertainty of serving market, and in turn increases the probability of firms committing resources to foreign markets. In developing their theory of internationalization, Johanson and Vahlne (1977) assert that uncertainty in international markets is reduced through actual operations in foreign markets rather than through acquisition of objective knowledge. They suggest that it is direct experience with international markets that increases the likelihood of committing extra resources to foreign markets.

- Product/service

  The physical characteristics of the product or service, such as its value/weight ratio, perishability and composition, are important in determining where the production is located. Products with high value/weight ratios, such as for example expensive watches, are typically used for direct exporting, especially where there are significant production economies on scale, or if management wishes to retain control over production. Conversely, in the soft drinks and beer industry, companies typically establish licencing agreements, or invest in local bottling or production facilities, because shipment costs, particularly to distant markets, are prohibitive. The nature of the product affects channel selection because products vary so widely in their characteristics and use, and because the selling job may also vary markedly. For instance the products with high complexity may require service both before and after sale and in this case the hierarchical mode is used.

External factors:

- Sociocultural distance between home country and host country

  Socio-culturally similar countries are those that have similar business and industrial practices, a common or similar language, and comparable educational levels and cultural characteristics. Sociocultural differences between the home country of the firm and its host country can create internal uncertainty for the firm, which influences the mode of entry desired by that firm. The greater the perceived distance between the home and host country in terms of culture, economic systems and business practices, the more likely it is that the firm will shy away from direct investment in favour of joint venture agreements. This is because the latter institutional modes enhance the flexibility of the firm to withdraw from the host market. To summarize, if all other factors are equal and the perceived distance between the home and host country is great, firms will favour entry modes that involve relatively low resource commitments and high flexibility.
- Country risk/demand uncertainty

  Unpredictability in the political and economic environment of the host market increases the perceived risk and the uncertainty of demand experienced by the firm. In the case of high country risk, firms will favour entry modes that involve relatively low resource commitments (export modes).
- Market size and growth

  Country size and market growth are key parameters in determining the mode of entry. The larger the country and the size of its market, and the higher the growth rate, the most likely the management of the company is to commit resources to its development, and to consider establishing a wholly-owned sales subsidiary or to participate in a majority owned venture. Retaining control over operations provides management of the company with direct contact and allows it to plan and direct market development more effectively. Small markets, on the other hand, especially if they are geographically isolated and cannot be serviced efficiently from a neighbouring country may be best supplied via exporting or a licencing agreement.

- Direct and indirect trade barriers

  In case of tariffs or quotas on the import of foreign goods or other trade barriers in the host country encourages company to consider a joint venture or other contractual arrangements for entering the market. The local partner helps in developing local contacts, negotiating sales and establishing distribution channels, as well as diffusing the foreign image.

- Intensity of competition

  When the intensity of competition is high in a host market, firms will do well to avoid internationalization, as such markets tend to be less profitable and therefore do not justify heavy resource commitments. The greater the intensity of competition in the host market the more the firms will favour entry modes that involve low resource commitments (export modes).

- Small number of relevant intermediaries available

  In such a case the market field is subject to the opportunistic behaviour of the few export intermediaries, and this will favour the use of hierarchical modes in order to reduce the scope for opportunistic behaviour.

Desired mode characteristics:

- Risk averse

  If the decision maker is risk averse they will prefer export modes or licensing because they typically entail low levels of financial and management resource commitment. A joint venture provides a way of sharing risk, financial exposure and the cost of establishing local distribution networks and hiring local personnel. However, modes of entry that entail minimal levels of resource commitment and hence minimal risks are unlikely to foster the development of international operations and may result in significant loss of opportunity.
- Control

  Mode-of-entry decisions also need to consider the degree of control that management requires over operations in international markets. Control is often closely linked to the level of resource commitment. Modes of entry with minimal resource commitment, such as indirect exporting, provide little or no control over the conditions under which the product or service is marketed abroad. In case of licensing and contract manufacturing management needs to ensure that production meets its quality standards. Joint ventures also limit the degree of management control over international operations and can be a source of considerable conflict where the goals and objectives of partners diverge. Wholly owned subsidiaries provide the most control, but also require a substantial commitment of resources.
- Flexibility

  Management must also weigh up the flexibility associated with a given mode of entry. The hierarchical modes are typically the most costly but the least flexible and most difficult to change in the short run. Intermediate modes limit the ability of the firm to adapt or change strategy when market conditions are changing rapidly.

Transaction-specific factors:

- Tacit nature of know-how

  The difficulties and cost involved in transferring tacit know-how provide an incentive for firms to use hierarchical modes. Investment modes can better facilitate the intra-organizational transfer of tacit know-how.

So it can be concluded that the company has to take into account several, often conflicting forces. Also, changes in the external factors in the foreign target country may encourage or force a company to revise its entry mode. Therefore, it is vital that a company continually monitors the external factors in the target country and is prepared to revise its entry mode in order to sustain or strengthen its market position (Root 1994; 18). As mentioned above, it is very important know the risks that are related with the market entry. In the next chapter the author is analysing the different type of risks and uncertainties that the companies face when entering the foreign markets.

2.4 Export related uncertainties and risks

Managing risks is one of the primary objectives of firms operating internationally, but the field of strategic management lacks the generally accepted definition of risk. The major uses of the term are in reference to unanticipated variations or negative variations in business outcome variables such as revenues, costs, profit, market share and so forth. Managers generally associate risks with negative outcomes. In some cases risk is defined as an uncertain event which may negatively impact the achievement of goals. The term uncertainty as used in strategic management and organization theory refers to the unpredictability of environmental or organizational variables that impacts corporate performance (Miller 1992). If the firm plans to go international, it faces several risks that need to be mitigated.

Kent Miller in his study “A framework for integrated risk management in international business” identifies a number of uncertain components that the companies face in international markets. Uncertainty about organizational variables reduces the predictability of corporate performance, that is, increases risks. Miller has divided the uncertainties into tree groups:

- Environmental uncertainties
- Industry uncertainties
- Firm Uncertainties

The division of environmental and organizational components into these three levels does not mean that managerial perceptions of the uncertainty of these components necessarily vary across the three levels of analysis. That is, not all the firms have homogeneous perceptions of the general environmental uncertainty nor are the industry uncertainties similar to all firms in a given industry. Managerial perceptions of the uncertainty of each factor can vary with individual and firm characteristics. General environmental uncertainties correspond to factors that affect the business context across industries. The chart 2.6 summarizes the general environmental uncertainties and provides a list of examples within each category.

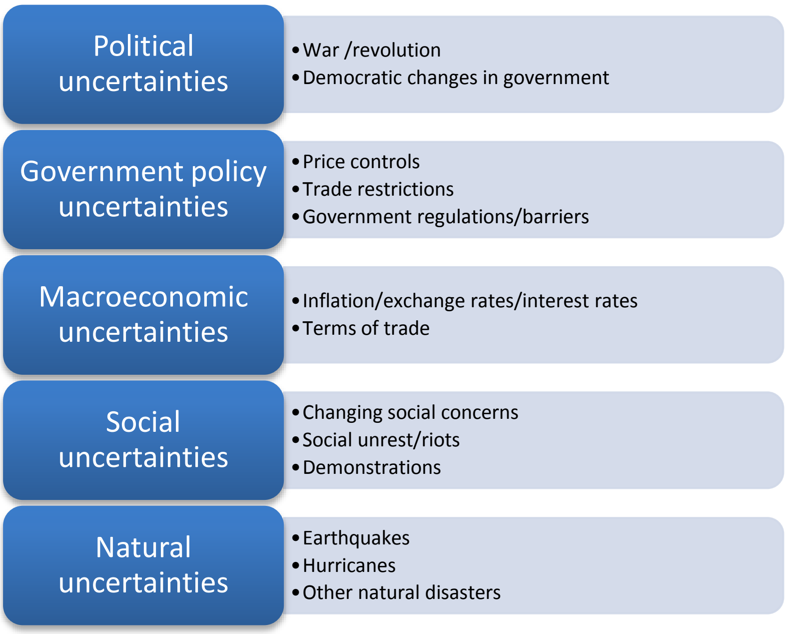

Chart 2.6. Environmental uncertainties

Source: (Miller 1992)

Political uncertainty is generally associated with major changes in political regimes that can affect the business community. Some authors do not distinguish political and policy uncertainties and use the term political risk to encompass both of these uncertainties. The most relevant policy uncertainties are fiscal and monetary reforms, price controls, changes in the level of trade barriers, etc. Macroeconomic uncertainty is a broad concept encompassing fluctuations at the level of economic activity and prices. Social uncertainty follows from the beliefs, values, attitudes of the population that are not reflected in current government policy or business practice. The fifth general environmental uncertainty factor is natural uncertainty which includes natural phenomena that impacts economic output.

The extent to which general environmental uncertainties impact firms functioning in different countries depend on the political, economic and social systems of the countries (Miller 1992).

Industry dynamics involve three major classes of uncertainties: input market uncertainty, product market uncertainty and competitive uncertainty. The chart 2.7 below summarizes industry uncertainties.

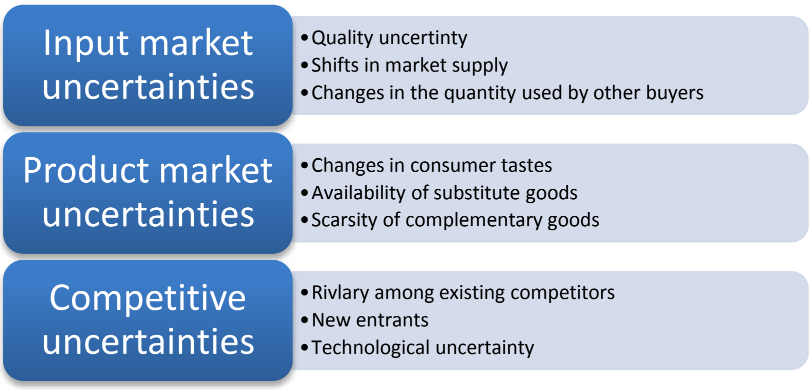

Chart 2.7. Industry uncertainties

Source: (Miller 1992)

Input market uncertainty refers to the industry level uncertainties surrounding the acquisition of quantities and qualities of inputs into the production process. It may arise from either shifts in producer supplies or fluctuations in other users demand for the input. In the international environment input uncertainty, for example political instability affecting the production process. In wooden furniture sector the political situation in Russia can affect the raw material availability. Product market uncertainty refers to unexpected changes in demand for and industry's output. Such shifts may be due to changes in consumer tastes or the availability of substitute products. Competitive uncertainty is a broad category covering the uncertainties associated with rivalry among existing firms and potential entrants into the industry (Miller 1992).

The third set of uncertainties the international firm faces is associated with firm-specific factors. Chart 2.8 below presents an overview of firm-specific uncertainties.

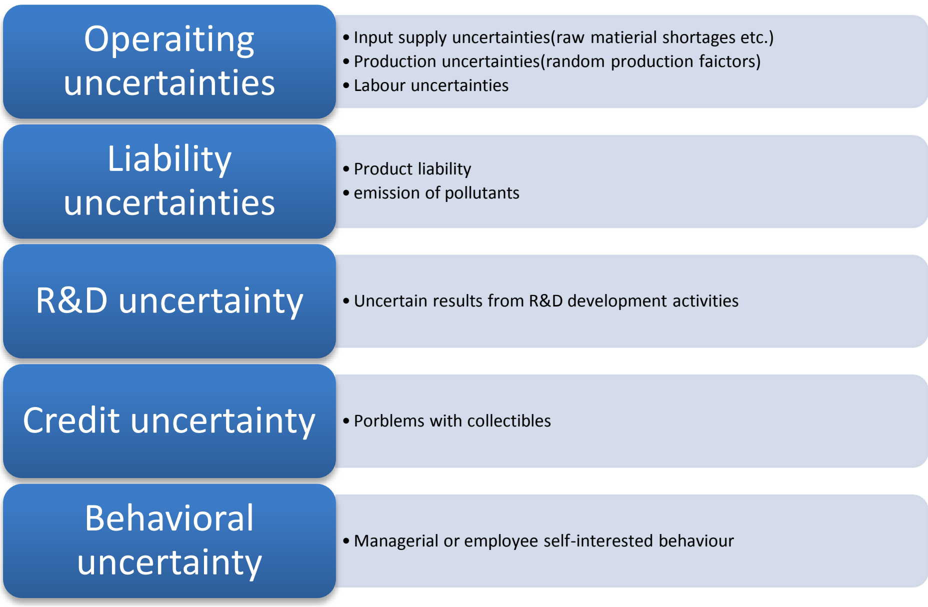

Chart 2.8. Firm-related uncertainties

Source: (Miller 1992)

Uncertainty regarding specialized labour or other inputs is rather firms-specific rather than having an effect to the industry in general. Raw material shortages, quality changes in inputs are also examples of firm operating uncertainties. Input supply uncertainties tend to be greatest when a single supplier provides critical input for the firm. Production uncertainty includes variations in output due to, for example, machine failures (Miller 1992).

Product liability uncertainty relates to unanticipated negative effects associated with the use of a product that can result in legal action against the producer. In addition to technological uncertainty at the industry level, individual firms investing in research and development, encounter uncertainty about the relation between their R&D investments or new product or process outputs. Credit uncertainty involves problems with collectibles. The failure of the customers to pay their debts to the firm can be a direct cause of variations in the income stream of the firm. The final category of firm-related uncertainties is associated with the agency relationship within a firm. Jensen and Meckling define an agency relationship as a contract under which one or more persons engage the agent to perform some service on their behalf, which involves delegating some decision making authority to the agent. (Miller 1992).

All the uncertainties mentioned above are the relevant dimensions of uncertainty faced by small and big firms operating internationally. It is important that the company understands the uncertainties and risks that appear in different target markets and looks for a method how these risks can be minimized or allocated.

Miller (1992) brings out various organizational uncertainty responses which are shown on the table below:

Chart 2.9. Organizational response to uncertainties

Source: (Miller1992)

The principal financial risk reducing technics are purchasing insurance and buying and selling financial instruments. A futures or forward contract requires the seller of the contract to make delivery of a pre-specified quantity of goods or assets some fixe time in the future. The ability to lock in a fixed price is the key risk-reducing feature of futures and forward contracts for both the buyers and sellers (Miller 1992).

There are a number of strategic moves that can mitigate the risks associated with uncertainties. Uncertainty avoidance occurs when management considers the risk associated with operating in a given product or geographic market to be unacceptable. Examples of control strategies include political activities or gaining market power. Vertical integration is an attempt to control input or demand uncertainties (Miller 1992).

Cooperative strategies for reducing uncertainty include long-term contractual agreements with suppliers or buyers, alliances or joint ventures, franchising agreements or technology licencing agreements (Miller 1992).

According to Aaker and Mascarenhas, strategic flexibility may be defined as the ability of the organization to adapt to substantial, uncertain and fast-occurring environmental changes that have a meaningful impact on the performance of the organization. The most widely cited example of flexibility in the strategy literature is product or geographic market diversification. This reduces the risk of the firm through involvement in various product lines or geographic markets. Flexible sourcing of materials is a mean of limiting the risks of a form associated with the dependence on a single supplier. Flexibility is also described in terms of the speed of design and volume changes in manufacturing operations. To conclude, flexible firms are able to take advantage of the opportunities presented by short-term movements in the price of inputs and products (Miller 1992).

To continue, the effective risk management process includes the following factors:

- Risk identification
- Risk assessment
- Risk control
- Risk administration

It is important for the management to identify the specific risks that are related with the particular export activity. Some risks are fairly obvious and others take a little more thought to fully understand the potential risk. Risk assessment requires the identification and gauging of risk exposures that the company may be subjected to in an export environment. Assessing the level of risk as well as estimating the probability of the event occurring and its magnitude is extremely important to risk avoidance. Implementing a system of on-going monitoring of the risks provides the necessary protection against the risk avoidance. By implementing these risk management procedures, there are many benefits that can be achieved, some of which include:

- More effective strategic export planning
- Better business cost control
- Increased knowledge and understanding of exposure risks
- A systematic, well-informed and thorough method of decision-making
- Minimizing business disruptions
- Better utilization of available resources
- Strengthening in-house business culture for continued future improvements

To summarize, before taking a decision to export, apart from assessing the market potential of the target countries, there is also a need to evaluate the different types of risks associated with exporting to particular territories. Successful management requires developing an understanding of the political and legal context abroad, and understand the extent and nature of trade and investment barriers abroad.

2.5 Entry mode selection approaches and stages

According to Young, Hamill, Wheeler and Davis (1989), making the right entry mode selection requires a systematic analysis of all the entry mode alternatives as well as the overall purpose and goal of the company. Also, the entry and development strategies have to be developed for each product and each market since no market is alike. The authors further suggest three approaches to establish the most appropriate foreign market end development mode:

1. The economic approach
2. The stages-of-development approach
3. The business strategy approach

The economic approach is a selection of foreign market entry that emphasizes rational behaviour. The approach focuses on the cost and benefits of the entry mode alternatives and identifies which alternative that will maximize the profits on the long run. The economic approach is based on a transaction cost analysis and aim at helping managers with selecting the most the most appropriate mode measured on the terms of risk and return of investment. According to the authors for both risk and return of investment the most important determinant is control. Entry modes with high control will increase the return and the risk, and low control entry modes, on the other hand, reduce resource commitment and therefore also the risk, and this often at the expense of the return of investment. Therefore, the selection of entry modes becomes a trade off for companies, they can trade different levels of control for a reduction of resource commitment hoping for a reduction in risk and an increase in return.

The stages-of-development approach to the decision of foreign market entry and development mode is based on the incremental mode of internationalization. According to the authors, the incremental model is described as an evolutionary process where companies gradually develop their commitment to foreign market over time with an increase in international experience and foreign sales. There are several major entry mode options available for companies in each stage of their international expansion. According to the authors, the decision regarding which foreign entry mode to choose is taken incrementally and also with a shift to other entry modes. This is only done after the previous entry modes have become inadequate. Entry modes can become inadequate because of lack of profits or because of previous success for example shifting from exporting to more involvement in the market (Young, Hamill, Wheeler and Davis 1989).

The business strategy approach differs from the other two approaches which both assume rational decision making. The business strategy approach focuses on the pragmatic approach instead. This is because of the external uncertainty and political nature of decision making, especially in the context of international markets servicing decisions. Companies have several objectives for expanding abroad and conflict between these objectives is likely to occur. Because of the need to combine the objectives and the uncertainty of the company, it is difficult to adopt a rational-analytic approach, this is especially true for SMEs because of their limited resources (Young, Hamill, Wheeler and Davis 1989).

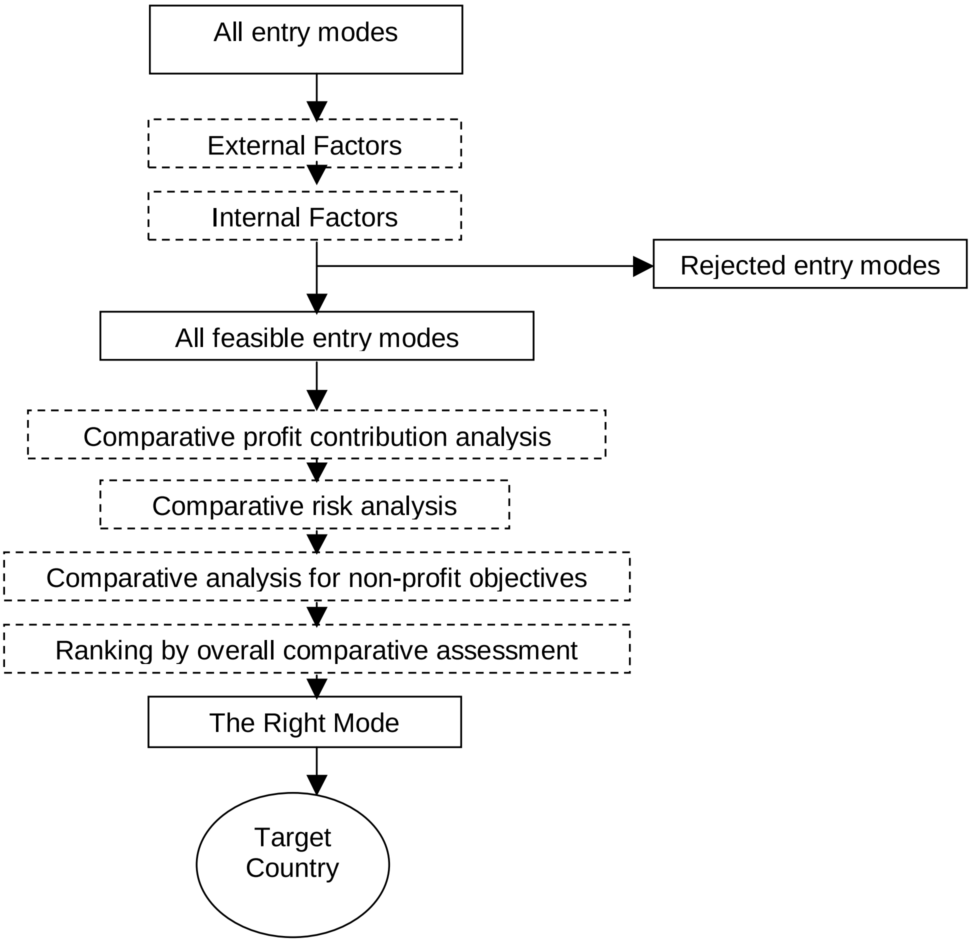

Chart 2.10. Deciding the ideal market entry and development strategy

Source: (Young, Hamill, Wheeler and Davis 1989)

As can be seen on the chart 2.10 above, for choosing the entry mode the companies have to conduct a feasibility screening of the entry mode alternatives in order to reject those alternatives that are not possible to use, taking into consideration the resources of the company and the external factors, such as market size, competition, etc. The estimated profitability of the alternative entry mode should be calculated and compared. Finally, the companies have to rank the entry mode alternatives taking in considerations the net profits, political risk and the companies non-profit objectives (Young, Hamill, Wheeler and Davis 1989).

3 ANALYSIS OF THE RESEARCH QUESTIONS

3.1 PESTLE analysis

3.1.1 Political system

Country: Republic of France

Area: 551,695 km^2 (metropolitan France)

Language: French

Religion: Roman Catholic, Protestant, Jewish and Muslim

Time zone: GMT +1

Population: 63,460,768 (INSEE 2012 estimate, metropolitan France)

Neighbours: Andorra, Belgium, Germany, Italy, Luxembourg, Monaco, Spain and Switzerland.

Capital City: Paris

Primary Port: Marseille

Primary airport: Charles de Gaulle (Paris)

Currency: Euro (EUR)

The French Republic is a sovereign unitary state comprising of the territory in the Western Europe and several overseas regions and territories. France is a semi-presidential republic. The institutions of governance of France are defined by the Constitution. The head of the state and head of the executive is the President. As of May 2012, the president of France is *François Hollande*. The current prime minister, as of March 2014, is *Manuel Valls*. In 2014, France is governed by the *Socialist Party* and the allies.

The main political parties are:

- **On the righ**t: The Popular Union Movement (UMP - *Union pour un Mouvement Populaire*),
- **Centre right:** the New Centre (*Nouveau Centre*), and the Union of Democrats and Independents (launched in 2012) *l'Union des démocrates et indépendants,*
- **Centre:** The Democratic Movement (*Mouvement Démocratique*, MoDem)

- **On the left:** the Socialist party (*Parti Socialiste*, PS) – as of June 2012 the party in power. The French Communist Party (*parti Communiste Français* - PCF).
  The Green Party (*EELV - Europe Ecologie Les Verts*)

The political environment of France is stable. According to the World Bank, the average value of the political stability index of France between the years 1996-2013 is 0.56 points with the minimum of 0.18 points in 2003 and the maximum of 0.85 points in 2002 (scale: -2.5 to 2.5).

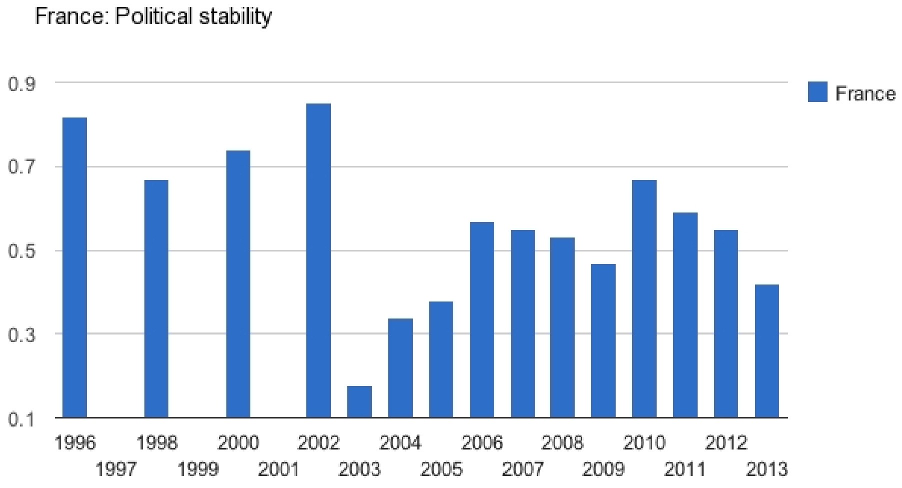

Chart 3. France's political stability index
Source: (The World Bank 2014)

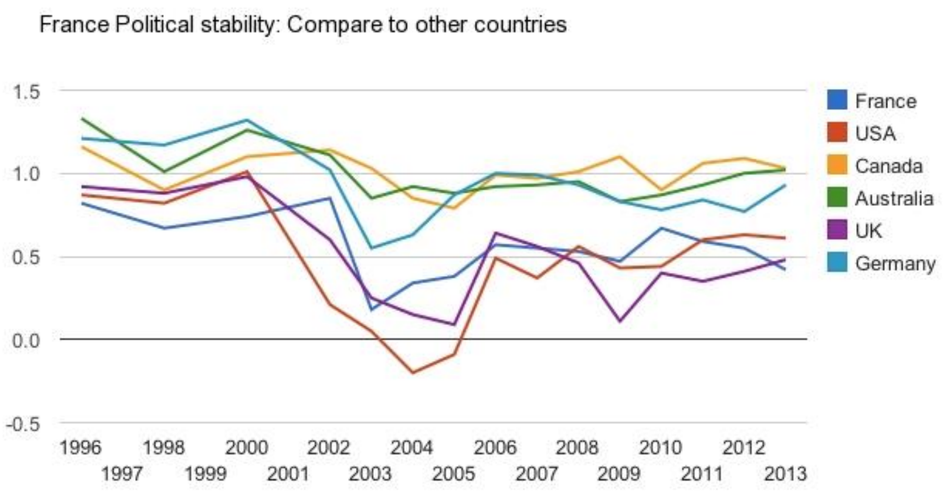

Chart 3.1. France's political stability compared with other countries
Source: (The World Bank 2014)

The estimated control of corruption value for France in the year 2012 is 1.42 (scale: -2.5 to 2.5). Compared with the previous year, the control of corruption value for France has fallen 6.56% (The Global Economy 2012). This indicates that there is a slight corruption in France but the overall corruption level is low.

Estimated government effectiveness value for France is 1.33 (scale: -2.5 to 2.5). Compared with the previous year the estimated government effectiveness value for France has fallen by 3.14% (The Global Economy 2012).

The 2009 global downturn hit the economy of France hard, leading to a deterioration of the labour market and an inflated fiscal deficit. The French government is still under a lot of pressure and facing difficult times — there is a strong need for the implementation of structural reforms of its social systems and labour markets. However, there is too much opposition within Hollande's Socialist Party to implement the necessary reforms. The new government has implemented strategies that are not beneficial for the economy of the country, for example the overall tax take has risen from 44% of the GDP in 2011 to 47% in 2014 (The Economist 2014).

The further priority of the government according to the Stability Programme of 2014-2017 is to achieve faster growth and a sustainable increase in private sector jobs. This is the best way of enhancing the purchasing power of households.

The communication and transport infrastructure of France is one of the most developed in Europe.

France faces an elevated risk of terrorism and social or inter-community tensions, although the security services have been largely effective at mitigating these risks in recent years (IHS 2014).

3.1.2 Economical system

Centrally located within the European Union, there is a strong competition for market share in all French industrial and service sectors. Exporters to France generally face more competition from European companies than from Asian ones. Positioned at the heart of the world's largest market, France offers a favourable economic environment to potential exporters. With a GDP of approximately $2.8 trillion, France is the world's fifth-largest economy (2013). France has substantial agricultural resources, a large industrial base, and a highly skilled workforce. While manufacturing has declined from 16% of GDP in 1999 to 12.5% in 2013, a dynamic services sector accounts for an increasingly large share of economic activity and is responsible for nearly all job creation in recent years.

France is the second-largest trading nation in Western Europe (after Germany). In 2013, the country ran an dollar 84 billion trade deficit of goods based on total trade of dollar 1.2 trillion (Collette 2014). More detailed data is presented on the table 3.

Table 3. Trade and external account indicators

	2011	2012	2013	2014	2015	2016	2017	2018
Exports of Goods (US$ bil.)	588.1	565.2	576.7	587.4	571.5	597.6	651.2	699.0
Imports of Goods (US$ bil.)	695.1	655.8	660.5	672.2	660.6	688.8	748.6	803.0
Trade Balance (US$ bil.)	-107.0	-90.5	-83.8	-84.8	-89.1	-91.2	-97.4	-104.0
Trade Balance (% of GDP)	-3.7	-3.4	-3.0	-3.0	-3.4	-3.3	-3.2	-3.3
Current Account Balance (US$ bil.)	-49.8	-56.5	-37.7	-39.5	-28.6	-27.2	-27.7	-26.7
Current Account Balance (% of GDP)	-1.7	-2.1	-1.3	-1.4	-1.1	-1.0	-0.9	-0.8

Source: (IHS 2014)

The majority of the trade of France (58.7 percent) was with EU-27 countries. The main trading partners of France are Germany, Belgium, Italy, Netherlands, United Kingdom and Spain. The more detailed information about the trading partners of France can be found from the table 3.1 below.

Table 3.1. Major trading partners of France in 2013

EXPORTS			IMPORTS		
Country	Billions of USD	Percent Share	Country	Billions of USD	Percent Share
Germany	94.2	16.6	Germany	130.2	19.6
Belgium	44.6	7.8	Belgium	75.9	11.4
Italy	40.8	7.2	Italy	50.5	7.6
United Kingdom	39.9	7.0	Netherlands	49.6	7.5
Spain	39.0	6.9	Spain	45.2	6.8
United States	33.1	5.8	United Kingdom	32.9	4.9
Netherlands	23.5	4.1	China	32.2	4.8
China	19.1	3.4	United States	25.5	3.8
Switzerland	16.9	3.0	Switzerland	19.1	2.9
Russia	9.2	1.6	Russia	13.2	2.0

Source: (IMF 2013)

France is a member of the G-8 (and initiator of the G-20), the European Union, the World Trade Organization and the OECD, confirming its status as a leading economic player in the world.

There are, of course, reasons for caution as well, GDP growth in France was in 2013 0.4% (table 3.2) and according to IHS (2014) predictions the GDP growth will remain modest in subsequent years.

Table 3.2. Economic growth indicators in France

	2011	2012	2013	2014	2015	2016	2017	2018
Real GDP (% change)	2.1	0.4	0.4	0.4	0.8	1.4	1.7	1.6
Real Consumer Spending (% change)	0.4	-0.4	0.3	0.1	0.7	1.5	1.7	1.7
Real Government Consumption (% change)	1.0	1.7	2.0	1.4	0.3	1.0	1.1	1.2
Real Fixed Capital Formation (% change)	2.1	0.3	-0.8	-2.1	0.1	1.8	2.6	2.5
Real Exports of Goods and Services (% change)	7.1	1.2	2.4	2.5	2.9	3.4	3.2	2.8
Real Imports of Goods and Services (% change)	6.5	-1.2	1.9	2.1	1.3	2.7	3.4	3.4
Nominal GDP (US$ bil.)	2,861.6	2,685.8	2,808.0	2,835.9	2,625.6	2,782.4	3,030.8	3,200.6
Nominal GDP Per Capita (US$)	45,258	42,274	43,987	44,185	40,693	42,904	46,501	48,870

Source: (IHS 2014)

The inflation rate was recorded at 0.5% in October 2014 and according to IHS (2014), the inflationary pressures should remain muted due to a high employment and weak demand levels.

The budget deficit of France has grown steadily and it accounted for a 4.3% of GDP in 2013. For 2015, experts predict it will climb to 4.7 percent (Pabst 2014).

The unemployment rate in France is also growing and has reached 10.1 % by the second quarter of 2014 (IHS 2014). Data about unemployment rate of previous years is presented on the chart 3.2.

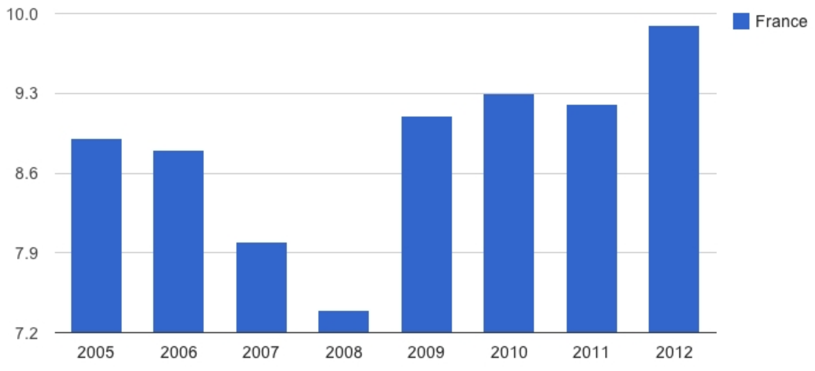

Chart 3.2. France unemployment rate

Source: (The World Bank 2013)

The labour market situation is expected to remain difficult as a result of weak activity levels and low confidence. Measures which are being implemented to lower labour costs will help boost employment once the recovery is more established. Tax credits and payroll tax cuts entering into force from 2015 should help reduce labour costs, which are among the highest in the EU. Very low corporate profit margins — which fell during the second quarter of 2014 to their lowest level since 1985 — are also likely to weight on job creation.

Low interest rates may also provide an incentive for firms to replace labour with capital when possible.

According to IHS (2014) experts, the economic conditions of France will remain challenging over the medium term. Tighter fiscal policy, dysfunctional labour market and extremely low profit margins of companies will keep output growth under pressure. The large fiscal deficit has resulted in a sharp increase in government debt, close to 100% of GDP as presented on the chart 3.3 below that puts the economy in a vulnerable situation. Interest rates have remained low and the debt structure of France is solid.

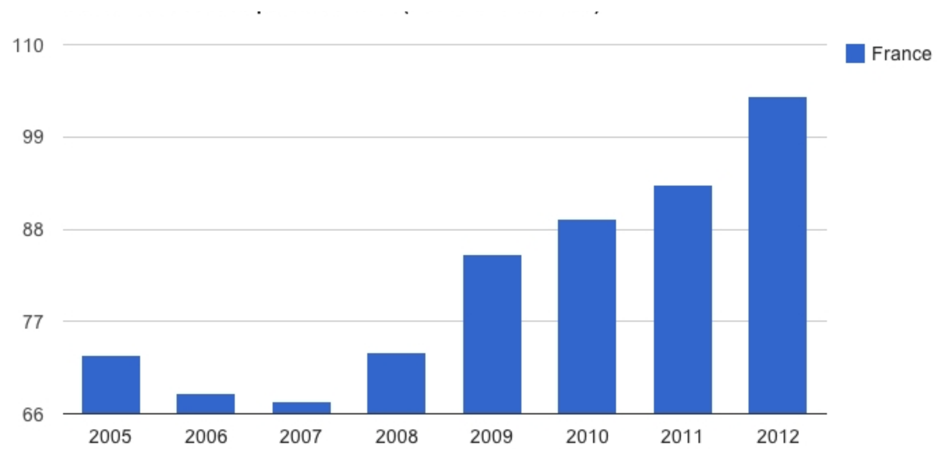

Chart 3.3. Government debt as percentage of GDP

Source: (The World Bank 2013)

The investment environment is also expected to remain difficult. Government measures aimed to improve the business environment and increase the competitiveness of the economy have failed to boost confidence. Decreased demand and low profit margins will weigh down on business investment. The profit margins of companies remain low as a direct result of rising input costs, higher taxes, and a competitive domestic environment since the start of the crisis.

Low margins provide a strong disincentive for investment, although there can be expected the positive trend in margins to continue over the medium term (IHS 2014).

The financial system of France is very well developed, with financial services, banking and insurance activities making up around 30% of countries annual GDP. France has several very large international banks including the Banque Nationale de Paris, Credit Agricole, Credit Lyonnais, etc.

Economical conditions of the furniture market (Euromonitor 2014):

- Compared with 2012, the indoor furniture sales declined by 0.9% in 2013, resulting in sales of 10.6 billion US dollars. Between the years 2008-2013 this number has remained largely the same. According to the predictions of Euromonitor (2014), there is no sign that the sales volume will decrease or increase drastically
- In France wood furniture consumption was quite stable between 2009 and 2011 at around euro 4.4 billion respectively. After a slow year of 2012 in France the furniture consumption suffered a further 11% decline to euro 3.90 billion in 2013
- In 2012 the import of furniture of France accounted for 3.31 billion euros. In 2013, the total import of furniture in France has decreased by 9.4% compared with the year 2012
- The main import partners of furniture are China, Italy, Germany, Spain and Poland
- In 2013, the export of furniture in France has decreased by 2% compared with the year 2012 accordingly 1 and 1.02 billion euros
- The main export partners of furniture for France are Germany, Switzerland, Belgium, USA and the UK

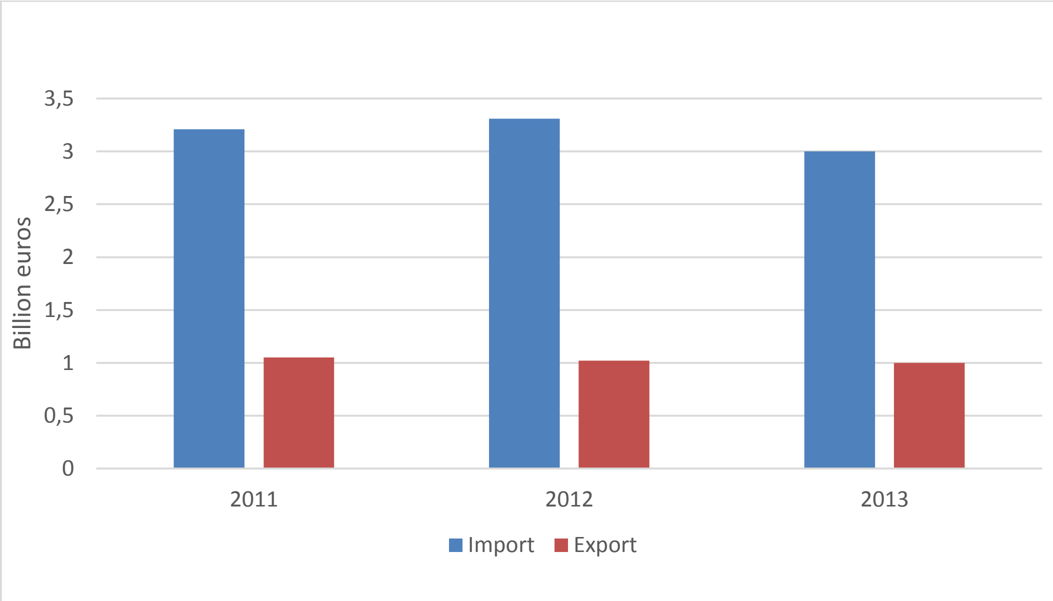

Chart 3.4. Total export and import of furniture in France (see Appendix 6)
Source: (ITC 2014)

- The eco-tax increases pressure on an already unsettled category, eco-tax stands to dampen the growth prospects, resulting in an increase in unit price that will have a negative impact on sales, representing the biggest threat to growth. Manufacturers and retailers will need to adjust their commercial strategy in order to minimise its impact. Small retailers are more likely to suffer as a result of this tax, as bigger retailers are more able to absorb price rises and are also able to have stakes in the Eco-mobilier organisation
- IKEA France Snc (Meubles) is the leading player in France in 2013 with a 13% value share. Its low prices continued to appeal to French consumers looking for good value for money and easy-to-build furniture
- Despite the leadership of IKEA, the domestic players active in home furnishings are enjoying a strong position in the French market but these players are mainly retailers, such as Alinéa and Fly from Groupe Rapp
- The real estate market, reaching a low point in 2013 with a decline in transactions, was a factor contributing to the decline in value sales for home furnishings. Compared with 2012, the total constructional output declined by -0.9% in 2013.

- Tougher competition between retailers also led to a decline in unit price in 2013 for the home furnishings market
- As a result of small living spaces, the need for “clever storage” is becoming greater and manufacturers are seeking to innovate in this category
- Bedroom furniture and home office furniture both posted a 2% current value decline in 2013, with the categories suffering from a fall in volume sales and in unit price. Retailers sought to combat this by offering high discount rates, reflecting tightening competition in these categories in France
- Homewares and home furnishing stores were also the preferred channels for sales of indoor furniture, accounting for 90% of value sales in 2013
- Home furnishings sales are expected to recover over the course of the forecast period, if the general economic situation brightens in France. The home furnishings category, being mature, relies not only on innovation to drive growth but also on consumer confidence in the economy, as it is a product area where it is easy for consumers to lower their expenditure in a gloomy economic context. Consumers will expect prices to either adjust accordingly or they will look for cheaper alternatives, thereby also threatening further growth

3.1.3 Social system

France has a very large and skilled labour pool, which has undergone significant structural change. The chief source of jobs growth has been in the service sector, where around 68% of the French labour force is now employed.

France is not highly unionized in comparison with other industrialized nations, but its unions are extremely powerful and frequently use their strong position to force the hands of the government over the policy. This is why hiring and firing of staff in France is extremely difficult. The nature of the relationship between the state and trade unions is complex, with the latter usually heavily involved in the construction of welfare policy as well as nationwide wage bargaining and working-condition agreements (Euromonitor 2014).

Population growth rate for France is 0.53% in 2013 and it has been stable for 5 years. Demographics of France represent a major challenge for the future. Despite the fact that France is currently experiencing larger fertility rates, the aging of the population will lead to a declining working-age population and this is a threat to public finances. Life expectancy at birth total is 82.57 years (2012). And this is expected to grow (Euromonitor 2014).

When doing business in France the following aspects should be taken into account (Passport to Trade 2014):

- Punctuality is treated very casually in France
- France is a highly stratified society, with strong definition and competition between classes
- The French handshake is brief and is accompanied by a short span of eye contact.
- The French have a great respect for privacy. Knocking and waiting before entering into a room is demanded. Additionally, it is not polite to "drop in" unannounced.
- Business can be conducted during any meal, but lunch is best
- It should be avoided drinking hard liquor before meals or smoking cigars between courses. The French believe this permeates the taste buds, compromising the taste of the meal
- Gift giving is left to the discretion of the foreigners. Good gifts to present include books or music, as they demonstrate interest in intellectual pursuits

Furniture distribution in France is dominated by specialists. It is characterized by concentration in large furniture chain stores and household good stores, which sell furniture next to audio equipment, household equipment and electronics. Within the furniture chains the *jeune habitat* with large stores in the out of town shopping centres is rapidly increasing. This trend towards fewer, but bigger outlets has an important impact on how exporters from developing countries can access the French furniture market.

There are many furniture agents and distributors in France, but their influence is decreasing as more retailers buy straight from manufacturers.

Some importers specialise in particular type of furniture, whereas other general importers suffer from growing competition from large retailers. Nevertheless, importers, wholesalers, agents, remain the most interesting trade channels for exporters from developing countries. Some of the agents and importers may work on a regional basis (CBI).

Furniture agents may be found: Federation of Agents- http://www.comagent.com/

For finding a suitable partner in France there is a number of ways:

- To contact the main trade associations

- Follow by trade affairs, which tend to feature a list of exhibitors, many of whom may be potential partners
  Meuble Paris — http://www.maison-objet.com/paris/pages/meuble-paris/
- In addition to the sources, there are a number of general or specific information portals that will be useful
  The French Furniture Portal — http://www.ameublement.com/
  The French Chamber of Commerce — http://www.cci.fr/

The most important ways to develop business relationships is either to exhibit at one of the major furniture trade fairs or to make direct approach to wholesalers or major retailers. It is important to have a professionally designed website because the business partners can make an evaluation based on that.

3.1.4 Technological system

According to Euromonitor (2014), France boasts one of the largest telecom markets in Western Europe with high levels of competition, expanding 4G networks and rapid growth in the uptake of applications such as mobile gaming and m-commerce. Investment in fiber optics is increasing to facilitate next-generation broadband connectivity, with speeds in excess of 30.0Mb/s. The e-commerce segment is extremely dynamic and the country is one of the most advanced globally in terms of e-government development.

France had 54.3 million Internet users in 2013 (85%), a 23.5% expansion over 2008. This has put the country in the third position in terms of total Internet users in Western Europe in 2013, ahead of all other countries except Germany and the UK. The Internet user base is expected to increase to 66.3 million by 2030, a growth of 19.1%.

French businesses are avid technology users and engage extensively with consumers through various mediums to promote their brands and enhance revenues. In 2013, 99.4% of businesses used computers and 99.1% used the Internet, compared to 97.7% and 95.2% respectively in 2008.

The share of the online medium has been rising steadily over the period 2008-2013 alongside a fall in the share of print ad spend from 28.6% in 2008 to 23.4% in 2013. With businesses devising strategies to connect with consumers online aided by growing 4G coverage and high smartphone penetration, the share of online ad spend is expected to grow further.

E-commerce market by Segment Share in 2013 can be seen on the chart 3.5.

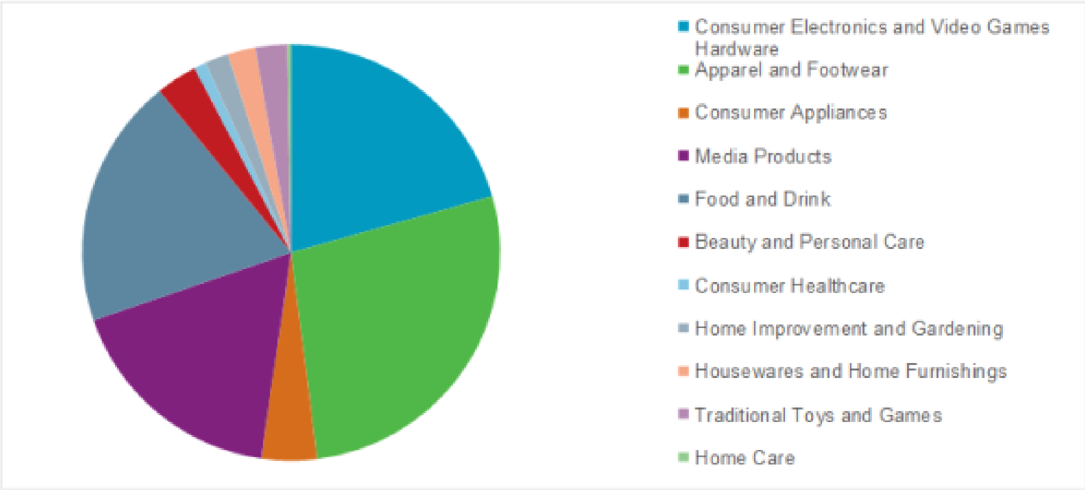

Chart 3.5. E-commerce market by Segment Share in 2013

Source: (Euromonitor 2014)

France is one of the fastest growing e-commerce markets in Western Europe. The total value of Internet retailing stood at euro 22.7 billion (US dollar 29.9 billion) in 2013, an expansion of 118% in real terms over 2008. At 282%, traditional toys and games registered the fastest growth in real terms over 2008-2013, followed by media products at 81.7% (IHS 2014).

The continuing rapid growth of e-commerce segment is showcased out by data from the European Commission, which shows that in 2012, 57.0% of the French population shopped online compared to the 45.0% average of the EU. Moreover, 17.0% engaged in cross-border transactions from other EU retailers, above the EU average of 11.0%. In the table 3.3 the most visited Internet pages in France can be seen.

Table 3.3. Ten most visited internet sites by reach (May 2014)

Web page	Description	Ranking (out of 100)
Google.fr	French search engine	1
Google.com	Search engine	2
Facebook.com	Social Network	3
Youtube.com	Video-sharing	4
Wikipedia.org	Online encyclopedia	5
Yahoo.com	Internet portal	6
Leboncoin.fr	Online classifieds portal	7
Amazon.fr	E-commerce portal	8
Orange.fr	Telecom company website	9
Free.fr	Telecom company website	10

Source: Alexa 2014

Internet retailing is forecast to grow by a relatively healthy 65.0% in real terms over the period 2014-2018, despite the maturity of the market and high e-commerce take-up among the population. This real growth rate is, however, lower than that of Luxembourg (119%), Belgium (115%) and Spain (72.8%) but ahead of Germany (57.2%), Netherlands (30.0%) and the UK (19.5%) (IHS 2014).

3.1.5 Legal system

The basis of the French legal system is laid out in a key document originally drawn up in 1804 and known as the *Code Civil* or *Code Napoléon*, (Civil code or Napoleonic code) which laid down the rights and obligations of citizens, and the laws of property, contract, inheritance, etc. France has a dual legal system, one branch, known as *Droit public*, or Public law, defines the principles of operation of the state and public bodies. This law is applied generally through public law courts, known as *les Tribunaux administratifs*. The other system, known as *Droit privé*, or private law, applies to private individuals and private bodies. Private law, *le droit privé* is the basic law of the land. It is administered through the judicial courts (Cave 2012).

There are two judicial channels (Cave 2012):

- Channels dealing with civil litigation
- Channels dealing with criminal offences

Basic civil litigation concerning private individuals is dealt with by a local court or by a regional or departmental court, depending on the importance of the case. Commercial and business law is administered through institutions known as *Tribunaux de commerce*. These are known as "first degree courts" (Cave 2012).

Appeals are heard in a Court of Appeal, a "second degree court". In France, there is a fundamental right of appeal in all cases. In exceptional circumstances, judgments of the Appeal Court can be contested at the highest level, the French Supreme Court in matters of private law (Cave 2012).

There are growing numbers of international corporate law firms established in Paris, Lyon, Toulouse and other big cities.

Legal aid is easier to obtain and cheaper in France than in many other countries.

3.1.6 Environment

On 1 January 2013, the state approved the new Eco-Tax that is intended for all firms conducting business in France, in order to organize the collection, recycling and recovery of household furniture.

This eco-contribution scale covers the following three categories: seating, bedding and furniture. The tax should be calculated by the importer in order to be added to the price and invoiced in addition to the product price, in the same manner throughout the distribution chain, from the manufacturer/importer to the end customer, in a legible manner for the latter.

This eco-contribution shall be determined by product weight. The tax can be up to euro 4 for a sofa bed, less than euro 1 for a chair and euro 6 for a wardrobe, for example. All producers of furniture who place their products onto the French market are obligated to pay this tax. In this case the producers can be defined as (Eco-Mobilier 2014):

- Manufacturers
- Retailers
- Importers
- Online retailers

Foreign distant sellers making sales directly to end-users are also obligated to pay this tax. There are no thresholds, therefore the company is obligated from the first piece of furniture placed on the market. Obligated companies must join one of the two compliance schemes to offset the majority of their obligations. The handling of private household furniture has been entrusted to Eco-mobilier, while Valdelia is responsible for the professional sector. Membership of Eco-mobilier is currently mandatory for business selling furniture directly to customers (B2C). Valdelia will oversee the recovery and recycling of business furniture (shops, cafes, restaurants, etc.). More information can be found:

- Valdelia — http://www.valdelia.org/anglais/
- Eco-Mobilier — http://www.eco-mobilier.fr/international

3.2 France as a target market

In this last section of this paper the author provides an analysis that should answer the research questions set at the beginning of this thesis: what is the best export strategy for Letrim OÜ to enter and operate in the French furniture market? To answer this question the author conducted a PESTLE analysis of the target market to find out the opportunities and risks the company faces by entering the French market.

Before it is possible to go on with an analysis, there is one more question that needs to be answered, why the company has chosen France as a target market? As said at the beginning of this paper, the main markets for Estonian furniture have been our neighbouring countries Finland, Sweden and Norway. The competition in those markets is very tight and has gone even tighter in the previous years because of the difficult economic conditions. Letrim has concentrated on marketing solid wood pine furniture. Pine is a traditional material that is appreciated in certain markets, for example Finland, Norway, Germany, France and the UK. On the contrary, in Sweden, for example, furniture made of birch is appreciated more. So, the company must concentrate on markets where pine wood furniture is appreciated among the customers. In Germany the pine wood furniture has been popular for many years and this is why the sales of the company to Germany has not decreased even during the crisis. Germany is a stable market and concentration to that market during the financial crisis has been a strategically right decision.

The strategic goal of Letrim for the next four years is to find new export markets. The potential export markets are the UK and France: these markets are large and pine wood furniture is popular there. In the first chapter, it became apparent that a very large amount of furniture imported into the UK originates from China. This makes it extremely difficult for the producers inside the EU to enter and operate in the market of UK. Exporting products from China has influenced the overall market conditions where the consumers are accustomed to consume cheaper products. This situation has also affected the producers of the UK as the sector continues to suffer from loss of market share to Chinese products in the domestic market. So, to enter and operate in UK means that Letrim has to find ways to lower the product prices or find partners who are ready to provide a lower price level than existing partners do.

When speaking about France, positioned at the heart of the European Union market, there are several opportunities for businesses around the world. This is a big market with much potential. In France the solid wood pine ready-to-assemble furniture is also very popular and the mid-range products are experiencing an increasing demand. The market as a whole is divided into two categories: basic and luxury. Basic has simple design, proven materials and shapes.

The environmental issues and the related life cycle consideration are also gaining more importance and influencing the finishing techniques. For example, water-based treatments (lacquers, paints) are becoming more and more popular. Natural materials are as important. Because of the high competition, the market is price sensitive and because of the lower price level, pine wood furniture is much more popular than other wood furniture. Pine is a traditional material that has found its place in contemporary interior design.

Environmentally friendly and sustainable forest management is also very important to French customer. And because of that the existence of FSC® certificate is also gaining more popularity. The aim of the certificate is to support the environmentally friendly, socially equal and financially viable management of world forests.

As the furniture business is a very competitive one, then every aspect listed above has a great importance when choosing a target market. The competences of Letrim meet the requirements of French market: the company owns the FSC® certificate, providing environmentally friendly treatment materials and ready-to-assemble products made of natural material. This is why the company has chosen France as a target market and is searching an entering method for this particular country.

3.3 Finding the right export strategy

One of the most complex decisions for internationalizing companies is the choice of an effective entry mode. Each mode of entry has its advantages and disadvantages, therefore the selection of a strategy is highly influenced by a range of sometimes conflicting forces.

The entry mode selection for a company is very important, as without a clear strategy the company will not be able to maximize its profits and faces too many uncertainties.

As discussed in the previous chapter, then according to Root (1994) there are tree different rules for selecting an entry mode strategy: the naive, pragmatic and strategy rule. As SMEs typically use naive or pragmatic rule where the same workable entry mode strategy is used for all the markets then the author is choosing a strategy rule by comparing the all the alternative entry modes before making a choice.

According to Hollensen (2007), there are groups of factors that are believed to influence the entry mode decisions. These are divided into internal and external factors. The author is going to analyse each factor separately in order to find a right entry strategy for Letrim OÜ to French market.

To begin with, the author is going to analyse the internal factors. The first factor that should be taken into consideration is the size of the company. As Letrim is a small company with limited resources, it is reasonable to choose a low cost method for entering, as higher cost methods need more resource commitment.

Another firm-specific method is international experience that reduces the cost and uncertainty of serving the market. For example, developing their theory of internationalization, Johanson and Vahlne (1997) assert that uncertainty in international markets is reduced through actual operations in foreign markets rather than through the acquisitions of objective knowledge. The company has over 20 years of international competence which is the most important competitive advantage of Letrim. The company has exported to Germany, Netherlands, Denmark and Switzerland. Therefore, it can be concluded that the competence is strong but includes mainly indirect exporting through different partners (agents, distribution and wholesale companies, etc.). As a result, the company has got limited marketing experience as marketing has been so far made by partners abroad. By choosing the hierarchical entry mode the company has to invest more into marketing by improving the marketing skills. In case of exporting or through strategic alliances the marketing will be still made by partners abroad and the company can continue with the activities it is more experienced in.

According to Hollensen (2007), the nature of the product also affects the selection of the channel because products vary so widely in their characteristics and use. Letrim is producing solid wood pine furniture that is a lower priced commodity product. The furniture is ready-to-assemble that enables to transport larger quantities and does not necessarily need an on-the-spot storage. All products are tightly packed into the package so that they would take a minimum amount of space. The minimum quantity the company is ready to provide is 100 pieces per product to keep the production as efficient as possible and provide reasonable transportation costs. The on-spot storage could help the company to serve a wider client network by offering smaller quantities, but this is also connected with higher risks and with huge investments. As it turned out in the PESTLE analysis, the French market is facing rough times and is extremely competitive. So it seems unreasonable to enter a foreign, unknown, diminishing and competitive market through huge investments. By using the wholesalers as partners, it is possible to lower the transportation costs as wholesalers are buying bigger quantities than the retail shops do.

In furniture business the after-sales service is also important. This includes supplying spare parts in case of missing or defective product parts. As firms often need a on-spot office to handle this process, then in furniture business this process can be handled by using local partners who take care of the after service. The distance between Estonia and France is short enough to send the spare parts by mail.

The uncertainty related with knowledge, what kind of products the market requires or the clients prefer also confirms the need to find a local a partner or distributor who knows the local trends and requirements and helps to allocate the product related uncertainty.

The external factors affecting the international market entry mode are, to begin with, the sociocultural distance between home and host country. Such sociocultural differences can create an internal uncertainty as the differences between industrial practices, language and cultural characteristics can be very large. Some of the cultural distinctions that businesses most often face in France include differences in business styles, attitudes towards the development of business relationships, punctuality, negotiating styles, gift-giving customs, greetings, significance of gestures, meanings of colours and numbers and customs regarding titles. The cultural distinctions between the Estonians and French are not so large, and can be overcome by learning the main customs the French people appreciate. Although the English language is widely taught in schools in France, the knowledge of French in business relationships is recommended. As the knowledge of French language in the company is incomplete, a local partner would be appreciated. Though, by acquiring the sufficient experience or experiential knowledge by getting the necessary business contacts in the market, the uncertainty can be reduced and extra resources can be directed to the market through more hierarchical entry modes.

The unpredictability in the political and economic environment of the host market increases the perceived risk and demand uncertainty experienced by the firm (Hollensen 2007). France is a politically stable country and the only uncertainty associated with the political environment is the risk of terrorism and social or inter-community tensions. Though these risks have been successfully allocated by the corresponding institutions and should not constitute any harm for local businesses or reflect a demand of the household products.

According to Hollensen (2007), the size of the country and rate of market growth are the key parameters in determining the mode of entry. The larger the country and the size of its market, and the higher the growth rate, the more likely management will be to commit resources to its development and to consider establishing a wholly-owned sales subsidiary or to participate in a majority-owned joint venture. France with the area of 551,695 km^2 and the population of 63 million people is one of the biggest economies in the European Union. The GDP of France is approximately 42 billion (2013) US dollars and the sales of furniture totalled to 10.6 billion US dollars in 2013. All this can lead to the understanding that France is a huge market with lots of opportunities. Nevertheless, the country is facing difficult times and so is the furniture sector. The employment rate is increasing by being one of the highest in the European Union, the overall consumption is decreasing, because of the economic uncertainty of people. The furniture consumption is also decreasing. Compared with 2012, the import of wooden furniture in France has decreased for 23% in 2013 and the established eco-tax increases pressure on an already unsettled category. In this point of view it looks like there are no prospects for new entrants in the market. But if discussed further, France is still a strong economy with a huge market and a lot of export potential. During the crises people stop buying luxury goods and prefer medium-priced products instead. As the company produces lower cost good quality furniture then it is expected that the demand for the lower-priced furniture should stay the same. The predictions of Euromonitor (2014) also indicate that the demand of the indoor furniture is expected to remain at the same level. Also, there is a pressure for the importers in France to start looking for a better price. This can mean that the share of existing import partners will shift in favour of lower-cost producers or partners. Of course, there is a risk that this share will be taken by Asian firms. Though the share of Asian manufacturers in total furniture imports is only around 25% and is quite low compared with the UK, Netherlands and Denmark. Also, according to the European Commission (2014), the furniture import from China to France has decreased in recent years.

When speaking about possible trade barriers, then all the trade barriers inside the European Union are restricted. The only tariff France has established is the eco-tax but as it applies to all the furniture manufacturers and sellers equally then this cannot be considered as a trade barrier.

As ready-to-assemble furniture is not connected with brand loyalty or with the tendency “buy national”. there is no need for a national company to diffuse the foreign image though there could be a need for a local partner to help to develop local contacts, negotiating sales and establish distribution channels.

According to Hollensen (2007), when the intensity of competition is high in a host market, firms will do well to avoid internationalization, as such markets tend to be less profitable and therefore do not justify heavy resource commitments. The greater the intensity of competition the more the firm will favour entry modes that involve low resource commitments. French market is very competitive. By being the second-largest market in the European Union, France attracts the exporters all around the world, although the major share of imports comes from inside the European Union. Because of the difficult economic situation, the competition inside France is becoming even tighter. Because of that the market entry method preferred due to competition is direct or indirect export.

In French market there are many furniture distributors, retailers and agents that prove to be good partners for exporters from different countries.

The entry mode selection is in a large extent connected with the manager’s willingness to take the risks or the extent to which managers are ready for resource commitment. As Letrim is a small company with limited resources, the management is not likely to be ready for a high level of resource commitment. Therefore, the methods like indirect and direct exporting are more suitable for market entry.

The control level is often linked with the resource commitment. As there is no brand reputation or image at stake, the company does not wish to maintain a high control over the products marketed abroad. The flexibility is also very important for the company as the competition in the market is very high and the overall economical conditions are also tough. In this case the hierarchical modes are difficult to change and limit the ability of the company to adapt or change the strategy quickly when needed.

The last characteristics that the author will analyse are related to the transaction-specific factors. There are several costs that are related with the market entry and for minimization of these costs firms often integrate vertically, that is search local partners. According to Hollensen (2007), the transaction costs can be divided into different forms of costs related to the transactional relationship between buyer and seller.

Search costs include the cost of gathering information about the foreign market. As in this case the author is conducting an analysis herself, there is no cost related with that matter. By using the local export intermediaries, there may be costs related with agreements between the seller and buyer. For example, when using the services of local agents, the commission fees will be added to the product price. There are several partners the firm can use. The most common practise is to use an agent. The agents usually take commission from sales turnover, this is a certain percentage that is agreed between the exporter and agent. Using an agent is the most cost efficient method for entering the foreign market, as the costs appear only if the actual sales take place. But in case of long-term partnership and in case the turnover of the company grows, using an agent becomes an additional cost that cannot be removed. After some time the company also acquires competences and does not need an agent anymore, so in long-term perspective using an agent is losing an advantage in front of direct exporting.

By using a local wholesaler there are no extra costs related but the pressure to the price is stronger. It is much harder to be competitive as the wholesaler is adding its percentage to the existing price. Although it is a good opportunity for a small company for entering the market, as the local distributor is familiar with the local needs and tastes. Also, the logistic costs can eventually be smaller. As wholesalers usually buy bigger quantities than local supermarkets do, as they are selling for several department stores, then transaction costs related with logistics are smaller.

By selling straight to the local department stores there can be several costs included. As discussed above, the logistic costs can be bigger as the destinations of goods are different. The quantities can be small and this can eventually lead to a need for a warehouse or even a local warehouse.

The costs related to product development should also be added to the product price in case of direct exporting. As big department stores usually tell themselves what kind of products they want, then smaller shops usually expect the exporters to have their own product portfolio. The costs related to marketing should also be added as the products may be left in storage.

The costs may also include costs related with monitoring the agreements to ensure that both buyer and seller fulfil their obligations, for example, different insurances. To add, enforcement costs that are related with sanctioning of a trading partner who does not perform its contractual obligations. For example, penalties related to delayed delivery or poor of quality.

When speaking about firm-specific know-how, then in this particular business there is no such know-how since the furniture design and technology can be very easily copied.

3.4 Findings

The prior analysis shows that there are several factors that influence the foreign market entry mode selection. By analysing all these factors, it became apparent that small size and limited resources of Letrim are the factors that most influence the decision of the entry mode. Due to that Letrim should enter this French market by using exporting as the company does not have the necessary resources to achieve a high degree of control. The product itself does not also require high control method as there is no need for an on-spot storage or office and the sales of the product can be managed from distance.

The greater the perceived distance between the home and host country in terms of culture, economic systems and business practices, the more likely it is that the firm will shy away from direct investment in favour of joint venture agreements. Although the cultural distance between Estonia and France is not big, the knowledge of French is highly appreciated. This also refers that Letrim should prefer export modes or joint venture as there is no knowledge of French in the company.

The PESTLE analysis revealed that France is a huge market with many opportunities but also a highly competitive one where the market entry opportunities can take place at the expense of someone else. This may occur for different reasons: bankruptcy of the existing partner, problems of supply or the need for bigger volumes that the current partners are unable to fulfil. This means that entering the market is difficult. The theory claims that the greater the intensity of competition in the host market, the more the firms will favour entry modes that involve low resource commitments. This suggests that the most appropriate choice for entry would be through exporting because of the high competition in the market.

The risk averse nature of the manager, the desire of control and flexibility are also important factors that decide the foreign market entry mode. As the manager of Letrim does not want to take additional risks in the form of huge investments, the most appropriate way for entering the market would be through exporting.

To conclude, by using the hierarchical entry mode there will be many additional costs which include marketing, logistics, investments, etc. For an SME, there are too many uncertainties related with these costs. This is why the best choice for Letrim by taking into consideration all the above mentioned factors would be exporting. As has been discussed in the previous chapter, in order to lower the logistic costs and the costs related with manufacturing, the indirect export mode would be the most appropriate one for French market as the local wholesalers usually buy bigger quantities than the retail stores usually do. Also, the local wholesalers know the local trends and inquiries.

Finally, the author can draw a conclusion out of this study concerning the best entry mode for Letrim OÜ to French market:

- The author found that because of the tight competition and the resulting uncertainties in French market the low-control method should be preferred
- Because of the small size of the firm and the limited resources, the low-control method should be preferred
- Because of the poor skills of marketing and the manager’s will to avoid huge investments, the low-control method should be preferred
- The author found that the most appropriate market entry method for Letrim OÜ would be indirect exporting

CONCLUSION

The phenomenon of internationalization has captured the interest of researches in strategic management, international business and entrepreneurship for many years. The concept of international business refers to the performance of trade and investment activities by firms across national borders. Firms organize, source, manufacture, market and conduct other value-adding activities on an international scale. They seek foreign customers and engage in collaborative relationships with foreign business partners. Firms exchange many physical and intellectual assets, including products, services, capital, technology, know-how and labour. For internationalization, firms need an entry strategy, but choosing an entry strategy for international market is a comprehensive plan. It sets forth the objectives, goals, resources and policies that will guide the international business operations of the company over a future period long enough to achieve sustainable growth in world markets. There are a number of factors that the company should analyse before deciding which entry strategy to choose.

The purpose of this study was to find what market entry strategy is best for Letrim OÜ to enter and operate in the French market. To answer this question, the author focused on the competences of Letrim OÜ and analysed the specifics of the target market by conducting a PESTLE analysis. The author also analysed the overall situation of the European Union furniture market to understand the nature and special location of import, production and trade in the sector. This was also important to find out who are the main competitors of Letrim OÜ. It revealed that the European furniture market is very competitive one and the most important furniture consuming and producing countries are the UK, Germany, Italy, France and Spain. The import of furniture has been modest and the majority of the furniture consumed in the EU is produced inside the EU. The major import partner of the EU is China but because of the long distance and volatile product quality the amount of furniture imported into EU is rather modest. The main competitors for Estonian furniture manufacturers are Polish, Chinese, German, Italian and Spanish companies.

As Letrim is using Estonian small and medium sized companies for manufacturing its products, then it was important to analyse the export problems that the Estonian companies face. The author based her research on the surveys conducted by the Estonian Furniture Industry Association and the Estonian Chamber of Commerce and Industry and analysed the major findings of these studies. The biggest advantages of Estonian manufacturers appeared to be the lower wage level that enables to provide a competitive product price and the availability and closeness of raw material that helps to speed up the manufacturing process and make it cheaper. The discussed drawbacks of international competitiveness were the steadily rising prices of raw materials and wage level. The competitive advantage of Letrim OÜ coincides in many aspects with the competitive advantages of Estonian manufacturers participating in these two studies. Good quality level, willingness to provide greater variety of more complex products and know-how are the competences of Letrim OÜ and were also mentioned in these two studies the author analysed.

For finding the best export strategy, the author concentrated on the theory of Hollensen and Root by analysing the major internal and external factors that influence the market entry strategy choice. It appeared that for a small sized company with limited resources, the low-control methods are the most suitable ones. To add, high competition in the French furniture market also confirms that the company should favour low-control methods. These include direct exporting and indirect exporting through different partners. The study revealed that for the company Letrim OÜ the indirect export mode is the most appropriate one. Local distributors and wholesalers usually buy bigger quantities than local retail shops do and know the local trends and requirements. By using different partners it is possible to operate with lower costs and keep the risk level low. Through indirect exporting the possibilities of the company to control the marketing processes are lower, but as the marketing knowledge in the company is limited, then this aspect should not be a problem.

To conclude, it is a huge step for a small firm to enter a new foreign market and that involves a great deal of resources. Choosing an entering method for each target market separately helps to save resources, such as costs, time and human resources.

KOKKUVÕTE

Rahvusvahelistumine on olnud strateegilise juhtimise ja ettevõtluse uurimisobjektiks juba mitmeid aastaid. Mõiste „rahvusvaheline äri“ viitab kaubandusele ja investeerimistegevusele, mis leiab aset erinevatest riikidest pärit ettevõtete vahel. Ettevõtted organiseeruvad, hangivad, toodavad, turundavad, otsivad välispartnereid pikaajalisteks koostöösuheteks, juhivad teisi väärtust lisavaid tegevusi rahvusvahelisel tasandil. Rahvusvahelise äri käigus vahendavad ettevõtted füüsilisi ja intellektuaalseid varasid, sealhulgas tooteid, teenuseid, kapitali, tehnoloogiat, oskusteavet ja tööjõudu. Edukaks rahvusvahelistumiseks vajavad ettevõtted turule sisenemise strateegiat. Sisenemismeetodi valik on aga keerukas plaan, mille käigus tuleb arvestada nii sihtturu spetsiifikat kui ka konkreetse ettevõtte iseärasusi. Välisturule sisenemise strateegia käigus tuleb ettevõtte jätkusuutlikkuse ja kasvu tagamiseks püstitada eesmärgid, leida ressursid, määrata poliitika, millest juhindutakse pika ajaperioodi vältel. Erinevaid tegureid, mida igal ettevõttel tuleb enne välisturule sisenemise strateegia valikut analüüsida, on palju.

Käesoleva töö eesmärgiks oli selgitada välja ettevõtte Letrim OÜ Prantsuse turule sisenemise strateegia. Uurimisküsimusele vastamiseks analüüsis töö autor ettevõtte kompetentse, teostas sihtturu analüüsi PESTLE´i meetodil. Lisaks uuris autor Euroopa Liidu mööblituru spetsiifikat, et selgitada välja Euroopa Liidu peamised mööbli eksportijad, importijad ning tootjad, kes on ühtlasi ka ettevõtte Letrim OÜ peamisteks konkurentideks Prantsuse mööblituru. Töö käigus selgus, et Euroopa mööbliturg on ülimalt konkurentsitihe ning peamiseks mööbli tarbija- ning tootjariikideks on Suurbritannia, Saksamaa, Itaalia, Prantsusmaa ja Hispaania. Import on pigem tagasihoidlik ning enamik Euroopa Liidus tarbitavast mööblist on toodetud Euroopa Liidu riikides. Euroopa Liidu peamiseks impordipartneriks on Hiina, kuid pika vahemaa ja sellest tuleneva aeglase transpordi ning ebaühtlase kvaliteedi tõttu moodustab see tarbitavast mööblist suhteliselt väikese osa. Analüüsist selgus, et peamiselt pakuvad Letrimile konkurentsi Euroopa Liidu, sealhulgas Prantsusmaa turul Hiinast, Poolast, Saksamaalt, Itaaliast ning Hispaaniast päris tootjad.

Kuna Letrim teeb mööbli tootmiseks koostööd erinevate Eesti keskmise- ja väikese suurusega ettevõtetega, pidas autor vajalikuks uurida ka Eesti mööblitootjate peamisi eksporditakistusi ja -võimalusi. Autor kasutas Eesti Mööblitootjate Liidu ning Eesti Kaubandus- ja Tööstuskoja poolt läbi viidud uuringute tulemusi. Uuringute kohaselt olid Eesti mööblitootjate peamisteks eelisteks madalamad tööjõukulud, mis võimaldab pakkuda konkurentsivõimalist tootehinda, tooraine lähedus ning kättesaadavus, mis aitab kiirendada tootmisprotsessi. Peamiste puudustena olid välja toodud nii toormaterjali hinnatõus kui ka palgataseme kasv. Letrim OÜ konkurentsieelised langevad paljuski kokku uuringus osalenud ettevõtete konkurentsieelistega, milleks on hea tootekvaliteet, valmisolek pakkuda laia valikut tehniliselt keerukamaid tooteid ning pikaaegne kogemus.

Parima ekspordistrateegia leidmiseks analüüsis autor peamisi firmasiseseid ja –väliseid faktoreid Hollenseni ning Root'i teooria põhjal. Autor jõudis järeldusele, et väikese, piiratud ressurssidega ettevõtte jaoks on kõige sobilikumaks madala kontrolli meetodid. Tihe konkurents Prantsusmaa mööbliturul kinnitab samuti seisukohta, et ettevõte peaks eelistama madala kontrolli meetodeid, milleks on otsene ja kaudne eksport. Autor leidis, et ettevõttele Letrim OÜ on Prantsusmaa mööbliturule sisenemiseks kõige efektiivsemaks meetodiks kaudne eksport läbi sihtriigis asuvate partnerite. Sihtriigis asuvad hulgimüüjad ostavad harilikult suuremaid koguseid kui kohalikud jaekaubandusketid ning on kursis ka kohalike trendide ning tarbijate vajadustega. Kasutades kohapealseid partnereid on võimalik opereerida madalamate kuludega ning hoida riskid kontrolli all. Kuna turundusalane kompetents on ettevõttes piiratud, ei ole vähene kontroll kohapealse müügitegevuse üle ettevõtte jaoks probleemiks.

Lõpetuseks tõdeb töö autor, et väikese ettevõtte jaoks on uuele sihtturule sisenemine suur samm, mille jaoks on vaja väga palju ressursse. Valides igale sihtturule sisenemiseks kõige sobilikuma meetodi on võimalik säästa suurel hulgal raha, inimressurssi kui ka aega.

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APPENDIXES

Appendix 1. EU-28 export of furniture in 2012

Country	2012
Non-EU Europe	2881
Russia	1154
USA	971
China	299
Saudi Arabia	167
Japan	175
UAE	175
Canada	140
Turkey	106
Other	1601

Appendix 2. The number of employees in the furniture manufacturing companies

No. of Employees	2010	2011	2012
1-9	456	446	482
10-19	41	40	39
20-49	44	41	48
50-99	26	26	27
100-249	10	10	9
250 and more	4	5	3

Appendix 3. Industrial output per employee in Estonian furniture manufacturing companies (euros)

2009	2010	2011	2012
38,837	45,778	50,592	52,619

Appendix 4. Foreign trade balance of furniture in Estonia

	Import	Export	Total sales of Furniture
2010	56	245	355
2011	74	268	394
2012	76	272	413

Appendix 5. Furniture export in Estonia by country in 2012 (mln euros)

Total	782	100%
Finland	191	27.4
Sweden	123	15.3
Norway	123	14.5
Germany	76	9.0
UK	43	5.6
Russia	42	5.0
Denmark	38	4.7
France	30	3.3
Netherlands	14	2.2
Other Countries	97	13.1

Appendix 6. Export and import of wooden furniture in France (bln euros)

	2011	2012	2013
Import	3,21	3,31	3
Export	1,05	1,02	1