

# International Expansion

A case study of how a state-owned enterprise expands internationally

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**Abstract:** The purpose of this single-case study is to investigate how state-owned enterprises internationalize. This is a perplexing phenomenon as state-owned enterprises face the constant threat of changing political opinions which makes long-term strategic planning difficult. A qualitative study has been conducted on a Swedish state-owned enterprise and empirical data has been collected from a range of sources.

The results indicate that a financially strong owner who encourages internationalization enables the enterprise to expand simultaneously to many markets, contrary with the Uppsala model. Moreover, state-owned enterprises are more willing to create a permanent presence in areas which are regionally integrated, through institutions such as the European Union, than areas which are not. State-owned enterprises exploit markets with changing institutions, if they can predict the direction of the change however they do prefer markets with little government turbulence. This is because political turbulence is harder to predict and makes the development of appropriate connections difficult. Furthermore, state-owned enterprises want to establish themselves as large players on markets and obtain full control of acquired companies as it incites the domestic market's government to engage in cross-governmental discussions with the host country's government. Finally, state-owned enterprises choose to apply the domestic organizational structure on the acquired companies so that the owner can maintain control over its subsidiaries.

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**Key words:** State-owned enterprise, government-owned enterprise, internationalization, international expansion, strategy

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# 1. Introduction

Whether or not states should be company owners has long been subject for debate, and scholars argue their case through performance evaluations of state-owned enterprises. The finding in this area tends to be contradictory (Meyer, 1975; Mann, 1970; Moore, 1970). However, what research does clarify is that state-ownership involves a complex and dynamic relationship between the owners and the enterprise (Hafsi, 1985). Pre-elected politicians influence the enterprises' strategies and are often tempted to use the enterprises as a tool to achieve sociopolitical goals (Kole & Mulherin, 1997). In turn this diversified target structure influences the strategies deployed by state-owned enterprises. In some cases these targets are quite contradictory and become the foundation of heated public debate.

When a state-owned enterprise expands internationally the enterprise can be used to advocate political values and/or strengthen international relations. However, this double edged political sword has to be used with care, as contradicting goals can undermine foreign politics. With that said, state-owned enterprises can still remain successful in the economic sense of the word.

It is clear that there is a tremendous complexity of state-ownership and, what becomes an interesting area of study is the actual impact state-ownership has on the formulation and implementation of strategy. Although state-ownership can most likely be traced as far back as the origin of the state the research on the implications of state-ownership on strategy is scarce (Vernon, 1979). Moreover, international expansion in state-owned enterprises is a field that has not been studied in-depth. This is because state-owned enterprises have traditionally been very protected by the state, and have therefore not been exposed to competition. Moreover, foreign markets have not been accessible in modern times, as state-owned enterprises had the purpose of serving the domestic market. During the 1980s and 1990s the deregulation waves in Europe led to the introduction of competition and opportunity of entering foreign markets. Consequently, we have decided to investigate what strategies state-owned enterprises use when expanding internationally.

## ***1.1 Background***

In the early 1990s, the Swedish state-owned electric utility company, Vattenfall AB, henceforth referred to as Vattenfall, decided to expand their enterprise internationally. Vattenfall initiated their expansion when they acquired a Finnish electricity distribution company in 1996. Germany and Poland followed in 1999 and 2000 respectively. Today, Vattenfall owns power generation plants in the foreign markets: Germany, Poland, the Netherlands, Great Britain, Denmark, Norway and Finland (Vattenfall Annual Report, 2009). In our study, we have decided to investigate the international strategy used by Vattenfall when expanding abroad.

## ***1.2 Purpose and research question***

The purpose of our study is to examine how a state-owned enterprise expands internationally. More explicitly, we intend to study the practical impact that state-ownership has on international expansion strategy in a state-owned enterprise. We wish to study the geographic market choice, degree of market adaptation and market entry mode. Thus, the following research question has been formulated and will be answered through the study:

*How does a state-owned enterprise expand internationally?*

In order to create a wholesome understanding of the phenomena at hand and comprehensively answer our research question, the study will include two sub-questions. Firstly, we will examine why state-owned enterprises decide to pursue international markets. This part will encompass a consideration of where and by whom the decisions to expand are made. Secondly, we will investigate the challenges state-owned enterprises face as a result of their expansion abroad, both in their domestic and foreign markets. This will facilitate a partial understanding for the changes in the international expansion strategy across time. After the sub-questions have been answered, the strategy employed will be investigated, and thus our main research question will be answered.

The following two sub-questions have been formulated:

- i. *Why do state-owned enterprises choose to pursue international markets?*
- ii. *What are the challenges faced by a state-owned enterprise as a result of foreign market presence?*

### ***1.3 Objective***

The objective of this study is to make additional contributions to the research of internationalization strategies, by which we imply international expansion strategies, of state-owned enterprises. Our extensive literature search demonstrates that there are established theories on internationalization within the field of international business. However, these theories are to a great extent based on studies of private enterprises. We, therefore, desire to depict this phenomenon for state-owned enterprises through a case study, by which we hope to contribute to the current research on internationalization strategies for state-owned enterprises.

### ***1.4 Delimitations***

Given the objective and the purpose of this study we have chosen the following delimitations to allow for an in-depth analysis of the phenomena. We will study one state-owned enterprise in order to allow for a focused investigation of the problem area. In order to provide a detailed analysis of the international expansion we have delimited the period to encompass the years from 1996 to 2009. This is because our pre-study indicated that for the selected enterprise, the periods prior to this included little structured international expansion. Moreover, it is important to realize that the intention of the research question is not to capture all the strategic choices a state-owned enterprise makes when it decides to pursue international markets; instead we have decided to include and investigate the following parameters: geographic market choice, degree of market adaptation and market entry mode.

### ***1.5 Disposition***

In the next chapter, chapter 2, the theories required to understand the research area will be presented. In chapter 3, methodological choices and their implication will be discussed. Chapter 3 will also introduce the interview subjects and the selected company. Chapter 4 will present the empirical data collected throughout the study, including both interviews and external documents, such as annual reports. This chapter serves as the foundation for chapter 5, where the analysis is conducted. Chapter 6 will present the conclusions, and will explicitly answer the research question and sub-questions. The final chapter will discuss the general implications of the analytical findings of the study. Moreover, limitations and suggestions for further studies will be presented.

## **2. Theory**

The following chapter will draw upon previous research for international expansion in order to give the reader a perspective on the existing studies that can be found. Since the literature in the area of internationalization and state-owned enterprises is rather limited the idea is to supplement the literature for private enterprises with that of state-owned enterprises in order to give the reader a more comprehensive theoretical background. This chapter is structured in the following way: the first part will define the central concepts that will be used throughout the study. The following part will describe what motives governments have for acquiring enterprises. The final part will provide insights on why companies pursue international markets, what challenges they face and how they expand abroad.

### ***2.1 Definitions***

In order to provide the reader with sufficient knowledge about the terminology that will be used this section will define the most crucial concepts. Therefore, the purpose of this section is to define the following: strategy, internationalization and state-owned enterprise.

#### ***2.1.1 Strategy***

There are various definitions of a company's strategy but usually these definitions describe strategy as the general direction which the company is planning to follow in order to reach its goals (Anthony & Govindarajan, 2006). Furthermore, in order for a business strategy to be successful it must take into account both internal factors, such as skills and resources, and external factors, such as opportunities and threats. This implies that strategy can be defined as a company's linking procedure between internal factors and external factors (Grant, 1991). It is also important to recognize that strategy contains both market and non-market components, where the market components include the setting in which the company operates and the non-market components include institutions, information and interests. Hence, a successful strategy needs to be congruent with the firm's capabilities and goals but also with the market- and non-market components of the environment (Baron, 1995).

Based on this discussion we have defined strategy as the plan the organization intends to pursue in order to achieve the organizational goals. Plan is defined as the specific actions that lead to achieving the goals and goal is defined as the aim the company intends to achieve.

#### ***2.1.2 Internationalization***

Internationalization can be described as a process by which companies gain new market power by exploiting opportunities. Hence, increased internationalization can be a way to leverage existing market shares (Tallman & Fladmoe-Lindquist, 2002). More broadly, internationalization can be described as the process by which a local industry expands from the domestic market to national or even international markets (Porter, 1986). Another alternative classification defines internationalization as the enlargement of a company's trading countries, traded commodities or international technology sharing (Kemp & Shimomura, 1999). Internationalization in this context ultimately implies a movement from one nation to another (Myers, 1995). This definition requires that the boundaries between nations are defined. The boundaries are in this sense often the boundaries of a homogenous area, such as a specific country. It is essential to note that it may not always be easy to distinguish one area from another and sometimes there are greater in-country differences than across countries (Hollander, 1970).

We have chosen to define internationalization as the process by which a company expands their business outside the national borders. Internationalization will therefore be used interchangeably with the term international expansion.

### *2.1.3 State-owned enterprise*

Garner (1970) has defined state-owned enterprises as legally autonomous entities which are owned by the government and operate in commercial lines. As governments in democratic societies eventually become replaced through elections, their impact on the governance of institutions is small. States on the other hand “*embody values and legal orders that tend to persist over time*” (Murtha & Lenway, 1994, p. 114). Consequently, although the government governs the enterprise their management will be predetermined by the values and the legal orders, such as social expectations, institutions and organizational structure of the enterprise (Murtha & Lenway, 1994).

In line with Garner’s (1970) definition, we will use the definition that state-owned enterprises are legally autonomous entities which are owned by the government and operate in commercial lines.

### **2.2 A government’s motives for acquiring enterprises**

Generally, scholars agree that state-owned enterprises are governed by more than purely economic goals. These multiple goals include socio-political goals, such as pursuing a political agenda, by for instance increasing employment. This phenomenon can be captured through public choice theory where both voters and government officials try to maximize their own personal utility. Therefore, government officials will support policies and set up goals for an enterprise which can help them advance their political career and maximize their own personal utility (Backhouse, 2002). However, the extent to which each goal is present and decisive for an enterprise’s management has been disputed (Murtha & Lenway, 1994; Vernon, 1979; Ravi & Ramamurti, 1987). One important question that needs to be answered is: why do governments choose to own enterprises in the first place? Vernon (1979) discusses five categories of motivation that can lead governments to engage in state-ownership. It is important to note that state-ownership can be driven by more than one category and that the motives that the government has when acquiring an enterprise can change over time. The five categories are: fiscal agent, national champion, mobilizer of national monopoly and monopsony power, official agent in bilateral trade arrangements, and agent of industrial policy.

*Fiscal Agent:* The government might sell at high monopoly or buy at low monopsony prices to levy taxes. The same result can be achieved through subsidies or direct taxes, but through state-ownership the process is less complicated.

*National Champion:* There are instances when the private sector is reluctant to enter certain areas because of high risk, or little experience. Moreover, private enterprises might be unable to defend their position against foreign competitors. Therefore, the government assumes control over certain industries that they believe need to be controlled so that the economy can be managed properly. The purpose of state-ownership is thus to create domestic market dominance.

*Mobilizer of National Monopoly and Monopsony Power:* Rather than to introduce tariffs and the like, the government can use the enterprise to improve the terms of trade by controlling state-trading entities. Similar to when the government acts as a fiscal agent, the process of improving the terms of trade through an enterprise is less complicated than through for example tariffs.

*Official Agent in Bilateral Trade Arrangements:* In order to encourage or maintain a two-way trade balance between countries, governments can assume ownership. By assuring a balance of trade, a country does not risk being dominated by a stronger counterpart.

*Agent of Industrial Policy:* Governments might believe that certain sectors or regions are falling behind levels that the government considers desirable. State-ownership is then assumed to improve these levels. However, the government might take control over an enterprise to ensure that development does not occur too rapidly for the enterprise's own good as a result of pressure from international competition. Finally, governments might assume control to ensure that prices do not ascend above acceptable levels.

### ***2.3 Why do enterprises pursue international markets?***

The literature on the internationalization pressures can be grouped into three main categories: increasing profits, exploiting competitive advantage or improving competitive disadvantage, and changing institutions. More than one category can determine why companies choose to internationalize. This section will explore these categories.

#### *2.3.1 Internationalization as a means to increase profits*

There is an inclination in research to suggest that state-owned enterprises are reluctant to expand internationally. Vernon (1979) and Mascarenhas (1989) argue that international expansion is contradictory to the goals of state-ownership. However, the broad range of socio-political and economic goals in state-owned enterprises suggests that there are factors which could induce internationalization.

New markets offer companies new opportunities to increase their profits, which can be useful if sales are declining or the domestic market demand is saturated. Enterprises might wish to benefit from first-mover advantage when seeking sources of profits on new markets or it might be a competitive response. The enterprise might simply imitate competitor trends to avoid a situation where they have a competitive disadvantage relative to their competitors (Porter, 1986). Internationalization offers new possibilities to sell products to an expanding consumer base. It also offers a possibility to prolong the life-cycle of a product. If there is a time lag between markets, internationalization enables firms to sell products that the domestic market no longer demands on new markets. On the supply side, overproduction or excess capacity can be the drive for international expansion as products can be pushed to new markets. Beyond that, the expansion may facilitate economies-of-scale. Enterprises can thus reduce their unit costs by expanding the output, which leads to a profit increase (Czinkota, 2004).

Consumers may be demanding a more diversified product range, which is particularly applicable to state-owned enterprises as they tend to have a very narrow product line (Mascarenhas, 1989). Therefore, the enterprise can expand by diversification, where the internationalization offers an opportunity to expand the product portfolio (Tallman & Fladmoe-Lindqvist, 2007). Thereby consumer satisfaction can be preserved.

Arguably, whatever the driver for internationalization, the net present value of the investment should be positive for a firm to pursue it, if the firm is economically rational. Brealy et al. (2006) state that if all else is equal, managers prefer running large enterprises to small ones. Therefore, this managerial ambition to build an empire can lead companies to make investments that will not necessarily generate positive net present value.



Conclusively, internationalization is a means by which companies can increase their profits. However, internationalization can also be driven by the managerial ambition to create an empire, which does not necessarily lead to increased profits.

### *2.3.2 Internationalization as the result of competitive advantage or competitive disadvantage*

Collis & Montgomery (1995) have defined competitive advantage as the ownership of resources that enables an enterprise to perform superiorly to its competitors, thus offering their consumers greater value. Tallman & Fladmoe-Lindqvist (2007) argue that competitive advantage is created through capabilities, or the unique combination of resources, rather than the resources in themselves, as these can simply be imitated by competitors. Regardless of the exact definition, it has been argued that internationalization can be encouraged by a firm's belief that it possesses a competitive advantage or that such a competitive advantage could be created by international expansion (Caves, 1982). Firms can exploit technological advantages or exclusive information, benefit from lower time-to-market, or leverage capabilities abroad and thus create a competitive advantage. Closer proximity to consumers can for instance increase the speed by which products reach the end-consumers or it can increase the understanding of consumer needs and thus increase the value delivered. Consequently, consumers will be willing to pay a premium for the additional value (Kotler et al., 2005). In turn consumers can benefit from lower prices or other values which justify higher prices. Therefore, state-owned enterprises may internationalize if they have competitive advantage or can gain one by doing so.

Occasionally, enterprises have a competitive disadvantage, which means that there is a gap between the enterprise and the leading enterprises. An international expansion enables companies to close that gap by obtaining necessary resources or capabilities, rather than creating a unique competitive advantage. State-owned enterprises can acquire technological and brand assets (Child & Rodrigues, 2005) by tapping into competitive clusters in other countries (Tallman & Fladmoe-Lindqvist, 2007). However, the asset might not only be missing in the enterprise, it might be missing from the entire domestic market. This implies that the competitive disadvantage is that of the enterprise but also that of the country. Therefore, the government can see the expansion as a means to obtain assets for the country. Mazzolini (1979) argues that state-enterprises can also expand abroad to obtain control over natural resources that the home country does not have. In this case, the lack of resources is not necessarily a competitive disadvantage for the enterprise in relation to other enterprises; however, it may be of significant competitive disadvantage for the home country in relation to other countries. In conclusion, the possession of a competitive advantage or disadvantage can lead to internationalization.

### *2.3.3 Internationalization as the result of changing institutions*

North (1990) has defined institutions as humanly devised constraints structuring political, economic and social interaction. He distinguishes between formal institutions, laws and rules, and informal institutions, values and norms. However, institutional political economists would argue that institutions not only constrain but also enable interaction (Chang, 2002). In view of the fact that institutions “*promote a certain outcome in a particular context*” (Goodin, 1998, p. 18), institutions can be designed to either encourage or discourage entrance of foreign firms, and encourage or discourage the international expansion of domestic firms.

The purpose of institutions is to reduce uncertainty (North, 1991), and therefore stable institutions in the host country are argued to encourage internationalization. However, unstable institutions do not necessarily discourage internationalization. This volatility presents companies with an opportunity to exploit barriers of entry (Slack & Lewis, 2008). Firms can engage in

institutional entrepreneurship in order to consciously shape the institutions by creating relationships with the host country government and employ other non-market strategies. In turn, a previous barrier of entry or source of uncertainty can be exploited to create barriers of entry for competitors. Whether or not firms will be persuaded to enter new markets based on the stability of the institution will be highly dependent on how risk prone they are. Additionally, state-owned enterprises, just like most international firms, are not only affected by national institutions but also global institutions, which can create more favorable or unfavorable expansion conditions.

State-owned enterprises are often considered risk-averse, implying a preference for stable institutions (Mascarenhas, 1989). However, at times state-owned enterprises' internationalization is more risk prone than justified by expected returns. For instance, state-owned enterprises do invest in countries which have high political risks (Mazzolini, 1979). Arguably, this could be driven by purely economic goals. On the other hand, expanding into countries with unstable institutions also offers an opportunity to create cross-country relationships where the enterprise can help to nurture political ties (Mazzolini, 1979). Others would go further and argue that governments can take advantage of poor institutions to establish a presence in the host country and are therefore able to determine the institutional developments. This is a form of economic imperialism, which allows the government to gain control of and insight in the foreign market by means of shaping the institutions so that they are favorable (Backhouse, 2002).

Summarizing whether or not the enterprise decides to expand for economic or socio-political goals, changes in national and international institutions which increase or reduce stability can be a reason for state-owned enterprises to expand internationally.

## ***2.4 What are the challenges companies faces in their host markets?***

When entering new markets, companies will encounter unfavorable barriers of entry compared to local enterprises. These challenges are specific for the foreign companies and are often viewed as liabilities. However, there are also certain situations where the same challenges can represent unique opportunities. The purpose of the following chapter is to introduce some of the most common challenges companies face when entering foreign markets and their implications. The challenges which will be discussed are recontextualization and liability of foreignness, and legitimacy.

### *2.4.1 The challenge of recontextualization and liability of foreignness*

This section will investigate the challenges described by Brannen (2004) and focus on the discussion around recontextualization and liability of foreignness. Recontextualization implies that the company's assets, once transferred to the host market, will have a different meaning and implication. Hence, it becomes important for companies to realize that all societies have different kinds of political, historical and cultural contexts which each give rise to different interpretations of the company's assets.

A term related to recontextualization is foreignness and this is another challenge companies face on international markets. Foreignness is defined as the differences between the home and host countries and is normally viewed as a liability for the expanding company. Broadly, there are three dimensions that determine foreignness: the level of internationalization, host country experience and institutional distance. The greater the institutional distance the poorer the strategic fit. Additionally, foreignness can be translated into representing different kinds of costs that a foreign company has but a domestic company does not have. Examples of these costs are transportation costs and costs resulting from host country reception which are costs such as lack

of legitimacy of foreign firms and economic nationalism. Although foreignness constitutes a challenge for companies, there are ways to mitigate some of the negative effects. Experience from international expansions is one of the foremost factors that can aid in mitigating the liability of foreignness. Another way of mitigating the liability of foreignness is to be aware of the cultural differences and work towards diminishing potential misunderstandings. Foreignness does not necessarily need to be a liability and there are situations in which it is considered an asset. An example of such a situation is when the local companies have been overprotected by the government and lost legitimacy. Relative to the foreign company the expanding company can therefore appear legitimate from the very beginning.

#### *2.4.2 The challenge of developing and maintaining legitimacy*

In order for a company to be successful in their new host environment it is extremely important that they learn how to develop and maintain legitimacy. Kostova and Zaheer (1999) have defined legitimacy as the acceptance that a company receives from its environment. Legitimacy is a phenomenon that is socially constructed, which implies that a company is perceived as legitimate as long as its operations follow the social values, norms and expectations that exist within a given country. Hence, legitimacy will always be problematic in one way or the other since social expectations and values often tend to contradict each other and change across time. This makes it difficult for companies to operationalize them (Ashforth & Gibbs, 1990). When companies enter foreign markets each of their subunits will face different kinds of institutional environments. Therefore, there are different kinds of legitimacy aspects that the company as a whole must fulfill. Consequently, each subunit will face the task of establishing and maintaining both external legitimacy, host environment legitimacy, and internal legitimacy, company specific legitimacy (Kostova & Zaheer, 1999).

Additionally, it has been stated that *“legitimacy has to do with the way the exercise of power is perceived”* (Boddeyn, 1995, p. 151). In this context Boddeyn (1995) points out that a company needs to consider if their operations are, firstly, in accordance to the host governments’ legal requirements and secondly, if their actions will be congruent with the local customs. Only when a company fulfills the obligations of the host environment will it gain complete legitimacy.

### ***2.5 How do companies pursue international markets?***

There are many different ways for an enterprise to expand abroad. When the internationalization decision has been made the enterprise needs to start formalizing a strategy that will make their international expansion successful. The following section will describe how enterprises expand into foreign markets by considering their geographic choice of market, the choice of market entry strategy and the degree of market adaptation.

#### *2.5.1 Geographic market choice*

When a company decides to look for expansion opportunities in the global arena, one of the strategic decisions the company makes is to decide which geographic areas it will pursue. According to Barkema et al. (1996) there are three models that describe the internationalization process of enterprises. In the product life cycle model the internationalization of an enterprise is determined exclusively by cost considerations. However, this theory lost much of its validity due to new arguments presented to the model, claiming that in terms of market conditions and factor costs, the differences among countries decline. The second category of models, known as innovation-adoption models, claim that *“firms stay in the vicinity of their past practices and the routines which govern them”* (Barkema et al., 1996, p. 152). These focus on small- and medium-sized

companies and on categorizing the internationalization process into stages, but no attention has been paid to explain the international expansion patterns.

The third model is the Uppsala stage model, which attempts to identify the pattern of internationalization. This model predicts that companies begin to pursue markets that are geographically near the domestic market. As knowledge from foreign markets is obtained, markets which are located further away geographically are pursued. This method of expansion offers a possibility to reduce the risk. Expansion, according to this model, is further distinguished by a careful and gradual process that is the result of incremental and concurrent local learning (Forsgren & Hagström, 2007). The model assumes that firms incrementally increase their involvement in a country through four successive stages. In the first stage, the company has no regular export activities. In the second stage, the company begins to export its products through independent agents. In the third stage, the company constructs an offshore sales subsidiary. In the fourth and final stage, the company has acquired enough knowledge to set up a production facility (Barkema et al., 1996).

The Uppsala stage model has received mixed support (Forsgren & Hagström, 2007) and as a result of this mixed support the model has been modified. The modification assumes that countries expand to areas which are not necessarily geographically near, but near in psychic distance. Psychic distance is represented by political, cultural and institutional factors, factors which explain societal values, norms and preferences in each specific country. These factors can further disrupt the information flow between a company and a potential foreign market especially if the psychic distance is large (Barkema et al., 1996). To reduce the possibility of disruptions, companies will show a tendency to enter those markets where the psychic distance is the smallest. Therefore, larger investments will be made in culturally, institutionally or politically near markets compared to culturally, institutionally or politically distant markets (Hosseini, 2008). As psychic distance is a modification of the Uppsala stage model, companies will incrementally expand to areas which are further away in psychic distance as they accumulate knowledge of foreign markets, similar to the Uppsala stage model. Additionally, scholars argue that the learning process in the Uppsala model can accelerate if the firm acquires competencies or mimics the behavior of others rather than learns by doing, or in this case learns by expanding. Therefore, internationalization can occur at a much quicker pace than the Uppsala model originally suggests (Forsgren & Hagström, 2007).

Psychic distance is a form of barrier of entry as it consists of political, institutional and cultural factors which can obstruct entry into a market. Therefore, if one of these factors is encouraging it will reduce the barrier of entry. Furthermore, international governmental relationships between countries can facilitate state-owned enterprises to enter specific countries where these relationships smooth the process of internationalization. The political and institutional factors may be encouraging as a result of the international relationship (Mascarenhas, 1989).

### *2.5.2 Mode of entry*

Depending on the situation, such as the risk associated with host markets, and the specific company characteristics there are different means by which one can enter new markets. A few of the most prominent ways of entering new markets is by export, joint-ventures, wholly-owned direct investments in foreign markets, acquisitions, and licensing (Malhotra et al., 2003).

*Export:* Through exports the company does not physically establish a presence on a new market; rather it sells its products or services from its home base and transports it to the host market. Through exports the core competencies of a company are retained in-house. Exports offer a low-

risk and often low-cost strategy of expanding. One of the disadvantages is the distance to local consumer tastes (Johanson & Vahlne, 1990).

*Joint venture:* This mode of entry involves two companies entering a business arrangement in which both have equal control. Commonly this arrangement is chosen when the venture is risky. When expanding abroad, two companies from the same country can create a joint venture and pursue international markets. Another possibility is that a company can create a joint venture with a company from the host country, and can thus tap into local know-how and reduce the risks presented by internationalization. Moreover, a joint-venture with a host country company can also be the result of regulations on foreign ownership imposed by the host country (Malhotra et al., 2003).

*Wholly-owned direct investment in foreign markets:* This is when a company sets up facilities in the host market. Direct investment in foreign markets is believed to be a high-risk entry strategy especially if the company has little knowledge of foreign markets. However, it also offers the company a possibility to retain know-how and other core competencies in-house (Malhotra et al., 2003).

*Acquisition:* In an acquisition, the company simply takes over a host country company and its tangible and intangible assets such as know-how, brand and customer relationships. Acquisitions offer the company a fast track to local tastes and customs. As well as acquiring assets, the acquisition also implies that the company acquires liabilities and risks of the acquired company (Malhotra et al., 2003).

*Licensing:* When a company desires to enter a new market it can do so by licensing products, rights, technologies or the like to another company. This gives the licensee the permission to sell the product under an agreed set of terms, in their home market. Licensing can be a result of regulation that prohibits the licensor to sell the product in the foreign market. Beyond this, licensing implies that the company does not need to face the risks and cost of physical presences. The disadvantage is that the license can be abused and the brand name damaged (Alon & McKee, 1999).

There have been disagreements regarding the risk-propensity of state-owned enterprises. Vernon (1979) argues that state-enterprises are risk prone as they are not subjected to the risk of bankruptcy as the government will assist the enterprise if that would become necessary. On the other hand, Mazzolini (1979) argues that state-owned enterprises are for most part risk-averse. Therefore, it is difficult to determine state-owned enterprises' generic risk-propensity and use this to deduct the type entry mode. However, what can be established is that state-owned enterprises display a tendency to engage in business relationships with other state-owned enterprises (Mascarenhas, 1989; Vernon, 1979). Moreover, state-owned enterprises display a reluctance to create a permanent presence abroad (Mascarenhas, 1989; Mazzolini, 1979). This increases the risk of internationalizing as state-owned enterprises have little experience from abroad. However, this risk decreases as the state-owned enterprise accumulates knowledge from international markets. Moreover, it should be noted that state-owned enterprises are encouraged by the government to increase exports (Vernon, 1979).

### 2.5.3 Degree of market adaptation

Kostova & Zaheer (1999) state that when companies decide on expanding their business internationally it is important that they adapt to their new host environment in order to become a successful international player. Based on the levels of market adaptation they identify three types of enterprises: geocentric, polycentric and ethnocentric enterprises.

*Geocentric:* This enterprise develops a global orientation that is not connected to the domestic identity. Thus, this type of company will create global practices and structures that are not connected to any country or culture in particular.

*Polycentric:* Rather than using one worldwide identity a polycentric enterprise develops multiple orientations, each reflecting the cultural differences in the countries where the company is present. Market adaptation becomes a quite smooth process as the enterprise can adapt to different local environments and institutional requirements.

*Ethnocentric:* Enterprises that are ethnocentric strongly connect their identity to the domestic market, and do not adapt to local orientations. This can cause great difficulty due to the differences in local practices.

State-owned enterprises are often created with the purpose to dominate domestic markets and hence they normally have limited internationalization experience (Mascarenhas, 1989). Therefore, state-owned enterprises that have little experience from abroad will have tailored their process and strategies for the domestic market and will tend to apply their domestic strategy on the international market. As the state-owned enterprises experience increases, its strategies and process will become better adapted to foreign markets (Mazzolini, 1979).

### 3. Research method

The purpose of this chapter is to discuss the methodological choices made and thus provide the reader with insight in the research process.

#### 3.1 Choice of method

Within social sciences, research papers can only have a practical significance if they are based on a theoretical construction. The theoretical construction will enable concepts to be formulated comprehensively which will further facilitate a logical elaboration of the empirical data (Weber, 1949). Therefore, it is important to establish the relationship between theory and knowledge. The two classical approaches within the field of social sciences are *inductive* and *deductive* methods. If a deductive method is applied, the researcher uses established theory to formulate a hypothesis. Empirical data is then collected and the hypothesis is tested. If an inductive method is applied the research process moves in the opposite direction to deduction. The researcher begins with gathering empirical data and then deduces the implication the findings have on theory (Bryman and Bell, 2007). An alternative and third method is the *abductive* method. This method encompasses attributes from both the inductive and deductive methods. The abductive method therefore requires the researcher to alternate between theory and empirical findings (Alvesson & Sköldbberg, 2008).

The theoretical foundation for this study is the field of internationalization. The available research has enabled us to identify a relatively unexplored phenomenon: internationalization of state-owned enterprises. However, much of this research has been conducted on private enterprises. International expansion of state-owned enterprises is a phenomenon which cannot be understood and explained entirely through the existing theoretical research. Therefore, theory and empirical data will be alternated in an attempt to complement the theory with our findings. The existing literature has therefore set the premises for this research; as the theory cannot singlehandedly explain the empirical findings. Conclusively, the abductive method is the most suitable as it falls into the continuum of inductive and deductive methods (Bryman & Bell, 2007).

Based on the chosen relationship between theory and research, the choice of research area and the research question, it has been established that a *qualitative* rather than a *quantitative* research strategy is better suited to answer the research question: *how does a state-owned enterprise expand internationally?* Therefore, a qualitative research strategy has been chosen. Quantitative research is often portrayed as the collection of numerical data and processing collected data in order to describe a phenomenon. Qualitative research, on the other hand, emphasizes the process, patterns and social context of the studied phenomena, which gives the reader an intrinsic insight to the field (Bryman & Bell, 2007).

Within the field of qualitative research there are various approaches which can be selected such as case studies and archival analysis. Each approach can be used for explanatory, exploratory or descriptive purposes, which is why the purpose is not a good discriminator between alternatives. However, one way to successfully distinguish between the various alternatives is to take into consideration three conditions and discriminate on the basis of the distinctive characteristics of the studied phenomenon. These conditions are:

- The type of the research question
- The amount of control the investigator has on behavioral events
- Whether the event is contemporary or historical

(Yin, 2003, p. 5)

The research question is: *how* does a state-owned enterprise expand internationally? As investigators we have no control over the behavior of the firm or its employees. Moreover, a contemporary event is being studied although it is analyzed from an historical perspective. A dead past would imply that we would have to rely on secondary data; because this is not the case we are thus studying a contemporary event. According to Yin (2003) the nature of the research thus indicates that a case study is the most suitable approach.

After establishing that a case study is the most appropriate research approach a case-study design must be chosen. The two basic designs are *single-case* and *multiple-case* (Yin, 2003). Multiple-case studies are an extension to the single-case study design (Bryman & Bell, 2007). There has been considerable debate as to which approach is more suitable. Eisenhardt (1989) argues that a multiple-case study is more powerful because of its comparative nature. Dyer and Wilkins (1991) argue that a single-case study is not inferior to a multiple-case study. In fact a single-case study allows for focused research in one and the same organizational setting. This enables a complete contextual insight, which is lost in a multiple-case design. Clearly there are trade-offs between the methods, and no method can be deemed superior. However, in our case a single-case study is considered to be the most appropriate, as our scope has been limited to one company. Moreover, a single-case study will allow for a thorough insight into the studied phenomenon.

Case studies can further be divided into three subcategories, *exploratory*, *descriptive* and *explanatory*, depending on the research purpose. Exploratory cases explore and provide insight into a phenomenon from a new perspective (Yin, 2003), which is the purpose of the thesis. Therefore, an exploratory case has been selected. Summarizing, an abductive method and a qualitative research strategy have been chosen. Based on the purpose and delimitations, a single-case study which is exploratory in its nature has been selected.



Figure 1: Overview of the selected study approach

### 3.2 Data collection

As “no single source has a complete advantage over all the others” (Yin, 2003, p. 85) a valuable case study will combine sources in an attempt to develop converging lines of inquiry; this will be discussed under the section quality of research. This section will give an account of the sources used.

#### 3.2.1 Selection of company

Before data can be collected, a suitable company for study needs to be selected. Vattenfall was selected because it fulfills the criteria of being state-owned. Moreover, the company accounts for almost half of the total annual turnover of the Swedish state-owned companies (Swedish Government Offices, 2006). Approximately 60% of Vattenfall’s operating profit comes from its non-Nordic markets, which makes it increasingly interesting (Vattenfall Annual Report, 2009). Finally, as the enterprise is owned by the Swedish government, and the research is conducted in Sweden, it allows for proximity to the phenomenon as well as facilitating interviews with government representatives, supplementing the case with the owner perspective.



### 3.2.2 Theory

Theory can be defined as “an explanation of observed regularities” (Bryman & Bell, 2007, p.7). However, the purpose of the theoretical section goes beyond explaining observed regularities; it serves as the foundation for the thesis and empirical inquiries, and strengthens the credibility of the findings. The theory provides a deeper understanding of the empirical phenomena. Moreover, our thorough theoretical research not only explains the empirical findings but it also facilitates in our interview preparations.

It has been argued that articles are a better source for theoretical research as these are published quicker. However, books have the advantage of providing established and recognized theories (Patel & Davidson, 2003). Therefore, a combination of books and articles has been used to present a balanced theoretical background. The secondary sources have been found through the databases at the Stockholm School of Economics. Because there are many terms for state-ownership, we used combinations of the terms that are found in the categories: ownership type, business entity and strategy. Each search term from one category was combined with another term from the other two categories. For instance one combination of search term was “state-owned”, “firm” and “internationalization”. The table below illustrates the three categories:

Ownership	Business Entity	Strategy
State-owned	Enterprise	Internationalization
Government-owned	Corporation	International Expansion
State	Business	Expansion
Government	Firm	
	Entity	

Table 1: Most used search terms

It became apparent that there was not much literature that was tailored to the specific ownership type that we wished to study. Therefore, we also conducted a literature search where the ownership term was abandoned from the search terms. At that point the literature search became much more fruitful. This is one of the main reasons as to why we chose an abductive method.

### 3.2.3 Interviews

In qualitative research one of the most prevalent sources of data are interviews (Merriam, 1994). Interviews give the “investigator an agile instrument with which to capture how the respondent sees and experiences the world” (McCracken, 1988). Therefore, six interviews were conducted. We were recommended by our instructor to contact Jan Greisz, Head of Group Strategic Management at Vattenfall, for an orientation interview, which we did. We also contacted a former employee in charge of HR at Vattenfall, who suggested that we speak with three additional co-workers. Two of these co-workers currently work at Vattenfall, and one of the co-workers is currently retired. An advantage of contemporary study is that it includes interviews with people involved in the studied event (Yin, 2003). Therefore, it is very valuable that these subjects worked at the company during its most expansive phase and had a role in Vattenfall’s internationalization strategy.

Further, we contacted the Ministry of Enterprise, Energy and Communication, henceforth referred to as the Ministry, and were directed to Magnus Fernström, special adviser and official at the Ministry who is responsible for Vattenfall. Having interviewed subjects from Vattenfall and the Ministry we were able to get a deeper insight into state-owned enterprises. It was important that the owners were represented, as ownership is one of the most prevalent features distinguishing state-owned enterprises from private enterprises. Having interviewed the special adviser and official at the Ministry it became evident that some questions were better suited for

politicians, which is why we contacted the former Minister of Energy and Enterprise, Thomas Östros. We were directed to his former Political Advisor, Ola Pettersson, with the inquiry for an e-mail interview. As Ola Pettersson was Political Advisor between the years 2004 to 2006, a period where Vattenfall's previous acquisitions received considerable public debate, we considered him an appropriate subject. Currently, it is election year in Sweden, therefore we opted for an e-mail interview, so that the Political Advisor could find some time to answer the questions at his discretion. Moreover, the purpose of this interview was to supplement the previous interviews, which is why we felt that an e-mail interview would be suitable. After conducting the six interviews the value added by an additional interview was considered limited, since empirical findings tended to converge. Interviewee details follow:

Name	Position	Short Description	Date & Time	Location
<b>Jan Greisz</b>	Head of Group Strategic Development at Vattenfall	Has worked for Vattenfall for over 20 years at various positions and on various geographic locations.	2010-04-26 60 min	Stockholm office
<b>Magnus Fernström</b>	Special Adviser and Analyst at the Ministry of Enterprise, Energy and Communications	Has worked for the Ministry since 2008, prior to that he worked at Ernst and Young. Vattenfall is one of the companies for which he is responsible	2010-04-27 60 min	Stockholm office
<b>Bosse Andersson</b>	Head of Public Affairs Nordic at Vattenfall	Has worked on and off for Vattenfall for 20 years, prior to working with public affairs at Vattenfall he worked with market research.	2010-04-30 60 min	Räcksta office
<b>Alpha (fictive name)</b>	Current Employee at Vattenfall	Anonymous	2010-05-03 60 min	Secret Location
<b>Beta (fictive name)</b>	Former Employee at Vattenfall	Anonymous	2010-05-11 60 min	Secret location
<b>Ola Pettersson</b>	Former Political Advisor for Thomas Östros	Worked as Political Advisor between 2004-2006, when Thomas Östros was Minister of Enterprise, Energy and Communications	Questions sent: 2010-04-29 Reply received: 2010-05-10	E-mail

Table 2: Interviewee details

The subjects, with the exception of the Former Political Advisor, were contacted via e-mail with a short description of our thesis and asked if they would be willing to participate in a one-hour interview. Five short questions were sent in advance to give the interviewees an opportunity to prepare, as this was believed to increase the quality of the interview material. However, to avoid biased and overly prepared answers generalized questions which only set the outline for the interview were sent. Before the commencement of each interview subjects were asked if they desired to be anonymous and if we were permitted to record the interview. Two of the subjects decided that they would prefer to be anonymous. To emphasize the different point of views we have chosen to use the subjects' position rather than names in the thesis as the positions are more informative. For the anonymous subjects we cannot refer to their position as their positions could disclose their identity. Further, all of the subjects authorized us to record the interviews under the premises that a transcribed version would be sent for approval before the material was analyzed and used in the essay. This method was selected to allow for the subjects to be free-spoken and not fear repercussions if they were to say something incriminating. With the exception of the former employee and current employee, who made minor spelling amendments, interview subjects made no amendments.

There are three fundamental types of interviews: *guided conversations*, *focused interviews* and *survey interviews*. Guided conversations are open-ended conversations, where the interviewer can inquire about both facts and opinions. Focused interviews can be open-ended, however a certain set of questions are inquired about. Survey interviews, are the most structured and are aimed at producing quantitative data (Yin, 2003). As the respondents were only interviewed once and for a

short time, we chose to conduct focused interviews that were semi-structured. After an extensive review of the theory used in the research we designed three interview guides, with a set of standardized questions that were open enough to provide varying answers, one for Vattenfall, one for the Ministry and one for the Former Political Advisor. The interview guides have been included in the appendix. The reason for asking standardized questions was to facilitate triangulation. These questions were unobtrusive in nature, to ensure that the answers reflect the respondents' view of the phenomena (McCracken, 1988).

#### *3.2.4 Documents*

Documents are highly advantageous sources as they are non-reactive, that is they have not been created for the purpose of the research (Bryman & Bell, 2007). The documents that have been reviewed in the thesis include Government Bills, reports from the Swedish National Audit Office, annual reports from Vattenfall and the Government Office, and Vattenfall's internally circulated pamphlets. These documents were examined before the interviews for the purpose of creating focused interview guides. Applicable documents have also been presented in the empirical data so that they can be analyzed.

### **3.3 Data analysis**

There is no established praxis of how to analyze case study evidence which makes it a difficult process. However, one way to collect the evidence is to create a case study database which noticeably increases the reliability of the case study (Yin, 2003). For that purpose we created such a database where both documents and interviews were included. Firstly, the documents were added into the database as those were read prior to the interviews. The main points were summarized, placed into the case-study database and cross-referenced with the original documents. Secondly, the interviews were included in the database after they had been transcribed. Each interview and every document could thus be analyzed separately and in conjunction, which facilitated the process of pattern recognition, and strengthened the study's internal validity (Yin, 2003). Bearing in mind that data should be presented in a way that enables the reader to make his or her own analysis (Eisenhardt, 1989) empirical findings include quotations and illustrative examples.

### **3.4 Research quality**

In order to assess the research quality the reliability and validity of the research needs to be evaluated.

#### *3.4.1 Reliability*

The reliability of a study determines whether or not the results are repeatable (Bryman & Bell, 2007). Reliability thus increases with the transparency of the study. In a qualitative research concerns with reliability arise as it is "*impossible to freeze a social setting*" (Bryman & Bell, 2007, p. 410). However, because the expansion is studied from a historical perspective the setting is already frozen. Detailed information about the research process has been included to increase the reliability, as the research method section provides a comprehensive account of the procedure. The reliability was further enhanced as, with the exception of two subjects, interview subjects agreed to disclose their names, which means that a researcher that wishes to conduct the same study has the possibility to interview the majority of the same subjects. To increase reliability we also attempted to standardize the data collection process (Holme & Solvang, 1997). The focused interviews, with the exception of the e-mail interview, were always conducted in Swedish, two-to-

one; they were recorded and transcribed. Any misinterpretation could be eliminated as the interview subjects had an opportunity to correct for ambiguities. Three separate interview guides were created, with open-end questions, and several stakeholders were interviewed to further strengthen the development of converging lines of inquiry. Although three interview guides were created applicable questions coincide across the guides to strengthen triangularity across stakeholders. Moreover, the empirical data section is unbiased in nature, and provides a detailed and transparent account of the findings. We have striven to maintain a chain of evidence in the presentation of our case, to assist the external observer when he or she traces the evidence that lead to the conclusions (Yin, 2003). Conclusively, a number of measures have been taken to increase the reliability of our study.

### 3.4.2 Validity

The validity of a study concerns the integrity of the conclusions produced through the research (Bryman & Bell, 2007). There are three main types of validity: *construct validity*, *internal validity* and *external validity*.

*Construct validity* is concerned with “*establishing the correct operational measures for the concepts being studied*” (Yin, 2003, p.34) and thus reduce the subjectivity of the research. Relying on one source of evidence can considerably reduce the construct validity. Therefore, one of the measures taken was to use multiple sources, interviews as well as published documents. The use of non-reactive sources in combination with reactive sources strengthened the construct validity. As previously mentioned, the standardization of data collection further strengthened the construct validity. Additionally, the structure of this study seeks to establish a chain of evidence, where we have attempted to ensure that original evidence has not been lost through carelessness or bias, which further strengthens the construct validity (Yin, 2003).

*Internal validity* refers to whether or not causality can be established and inference can be made (Yin, 2003). One potential threat to the internal validity is that the interview subjects were not selected randomly, but selected on the basis of past experiences and positions. To increase the internal validity a number of subjects were interviewed and were asked the same questions. In order to reduce subjective inferences of the interview data, quotes which have been approved by the interviewees have been used to a great extent. Additionally, the interviewees' disregard for anonymity could be a potential threat to the internal validity. The subjects might have felt uncomfortable disclosing potentially controversial information especially since Vattenfall, during the time this was written, was present in various media and political discussions. To reduce this problem we interviewed two subjects that preferred to remain anonymous. We hope that the willingness of the interviewees to participate, their cooperative spirit as well as interviewing various stakeholders, will counterbalance the potential problems of naming some of the interviewees.

*External validity* establishes if the findings are generalizable beyond the particular context (Bryman & Bell, 2007). Therefore, it could be problematic to use a single-case study. However, the external validity can be increased if the purpose of the case is to “*generalize a particular set of results to some broader theory*” (Yin, 2003, p. 37). Inasmuch as we acknowledge that the external validity is negatively affected by the use of a single-case study, the study serves as starting point for further research, where the study can be repeated. Moreover, it provides an extension to an established theory, rather than creating a new theory.

## 4. Empirical Findings

In order to give the reader a thorough background of the implications of Vattenfall's internationalization, the empirical chapter will be divided into four main sections. The first section will provide background information about the state-owned enterprise Vattenfall. The following section presents information on the decision-making structure and division of responsibility for Swedish state-owned enterprises. The third section will describe the foremost institutional changes that took place in Europe during 1996 to 2009. The final two sections will provide information on Vattenfall's internationalization process.

### *4.1 Background to the case*

Vattenfall is a Swedish state-owned limited liability company that has approximately 40,000 employees; out of these approximately 80 percent work outside the Swedish borders (Head of Public Affairs Nordic). In 2009 Vattenfall was the number one producer of heat and the fifth largest generator of electricity in Europe. Their vision is to become a leading European energy company. Vattenfall started their international expansion in 1996 and has since then continued to enter new markets abroad. In 2009 Vattenfall operated in eight countries: Finland, Denmark, Poland, Germany, the Netherlands, Belgium, Great Britain and Sweden. Vattenfall's product portfolio consists of heat, electricity and gas. The value chain of these products can be broken down into sales, production, transmission, generation and distribution. In heat Vattenfall is active in sales, production and distribution. In electricity they are active in all parts of the value chain, while in gas they are only active in production and sales. Vattenfall's production portfolio includes nuclear power, hydro power, fossil-based power, biomass-based power and wind power (Vattenfall Annual Report 2009).

### *4.2 Overview of state-ownership in Sweden*

This section will describe the state-ownership structure in Sweden. The first subsection will provide a background of state-ownership, followed by an identification of the two types of categories that the Swedish state-owned enterprises have been divided into. Thereafter, a subsection with the state's goals and objectives for Vattenfall will be addressed. The following subsections describe the ownership structure and division of responsibilities for state-owned companies. The final subsection identifies the cornerstones of Vattenfall's strategy formulation.

#### *4.2.1 Background to state-ownership in Sweden*

In Sweden there are 54 enterprises that are either wholly or partially state-owned. Out of these companies three are listed: Nordea Bank, SAS and TeliaSonera (State-owned Companies Annual Report 2008, p. 108). According to the special adviser and analyst at the Ministry "*these companies are in total worth approximately 500 billion SEK.*" The total net turnover for the state-owned enterprises was 347 billion in 2008 of which Vattenfall accounted for approximately 47 percent (State-owned enterprises Annual Report 2008, p. 1).

Historically, the aim of state-owned enterprises has been to serve the national market, although the exact objectives varied across the enterprises. However, this began to change when Sweden joined the European Union, as Sweden became compelled to enable international competition in previously protected sectors. Therefore, it was no longer needed or in some cases even possible to manage the state-owned enterprises in a way that protected national interests (Verksamhetsberättelse för företag med statligt ägande 1999, p. 9). As a result, the goal formulation for state-owned enterprises has evolved from serving the national market to creating

value. Value is created by maximizing the return of the state's equity or fulfilling specific societal interests, determined by the state (State-owned companies Annual Report 2008, p. 8).

#### 4.2.2 Categories of state-ownership in Sweden

Prior to 2000 the government acknowledged that state-owned enterprises had varying degrees of commercialism, ranging from enterprises with societal interests and no commercial operations to fully commercial enterprises with no societal interest. Regardless of the degree of commercialism, all state-owned enterprises had the mission to minimize the cost of capital by optimizing the capital structure (Verksamhetsberättelse för företag med statligt ägande 1999, p. 9). In the years that followed the objective of state-owned enterprises started to take a clearer form. In 2000 companies were separated into two distinctive categories: *companies operating under market conditions* and *companies with special public interest*. The goal of the state-owned enterprise became determined by the category to which the enterprise belonged (Special adviser and analyst at the Ministry).

State-owned enterprises that operate with special public interests are subjected to direct state control and operate under special conditions. These companies can be wholly or partially owned without competition but they can also be fully competitive; this is reflected in the required rate of return. 24 of the state-owned enterprises belong to this category. The 30 state-owned enterprises that belong to the category companies operating under market conditions have clearly identified economic targets, such as required rate of return. The state has a determining influence and can also set other targets than financial ones (State-owned companies Annual Report 2008, p. 39).

#### 4.2.3 Goals and objectives for Vattenfall

Vattenfall has previously been a governmental-owned company (*affärsverk in Swedish*). A governmental-owned company is an organizational form which is a juridical body within the state and is controlled and governed similarly to a government authority. The governmental-owned companies have complete obedience in relationship to the state (Regeringen, 2010). One of the reasons why Vattenfall was formed by the government was "*the will to fulfill the industrial demand for infrastructure*" (Special adviser and analyst at the Ministry). As a government-owned company Vattenfall prided itself in contributing to the modernization and welfare of Sweden. However, the company was also used to control the energy policies of Sweden (Former Employee).

Following a resolution from the Swedish Riksdag (Parliament) in 1991, the governmental-owned Statens Vattenfallsverk was reformed into two separate units, Vattenfall AB and the new governmental-owned company, Svenska Kraftnät which had the responsibility of running the national electricity grid (Svenska Kraftnät, 2007). With the resolution Vattenfall became a state-owned limited-liability enterprise (Verksamhetsberättelse för företag med statligt ägande 1999, p. 58). After becoming a state-owned enterprise "*disorientation occurred as the company was no longer sure of its role*" (Former Employee). As a result, Vattenfall's goals were redefined. Today, one of the official aims is that Vattenfall is to become one of the leading European companies and a global energy partner (Special adviser and analyst at the Ministry). Through the years environmental and societal aims have been written into the articles of association. In 2000 Vattenfall had an environmental objective stating that the company should reform their operations into one that integrated societal, environmental and sustainable aspects into their day-to-day activities (State-owned companies Annual Report 2000, p. 119).

Vattenfall belongs to the category of companies operating under market conditions. The Swedish government has explicit financial objectives for Vattenfall. For 2002, these were a 15 percent return on equity and a single A-credit rating (State-owned companies Annual Report 2002, p. 58).

Currently, the government only has financial goals for Vattenfall. As long as profitability is preserved additional aims are encouraged through the articles of association, such as “*to be leading in the transformation process of the Swedish energy supply system*” (Special adviser and analyst at the Ministry). However, Vattenfall’s aims and the role of the government are subjected to political debate. The Political Advisor of Thomas Östros argues that the state should use its influence to govern Vattenfall more actively, so that the company helps to set the standards and serves as a role model for the energy industry as well as other industries. Moreover, he argues that Vattenfall, beyond supporting the basic industries, should offer Europe’s lowest electricity prices.

#### *4.2.4 The state ownership policy and the organizational structure of state-owned enterprises*

Before 1999, the responsibility for the different state-owned enterprises fell on several different ministries. The responsibility for a company was related to the political responsibility within each industry block. In 1999 this structure was changed and replaced with specific ownership units within the Government Offices (Verksamhetsberättelse för företag med statligt ägande 1999, p. 9). The Ministry of Enterprise, Energy and Communications is responsible for providing the state-owned enterprises with a template for the articles of association. The template is structured around the regulations and policies that the state-owned enterprises need to follow; these are the state ownership policy, the Swedish Code of Corporate Governance, and the Companies Act (State-owned companies Annual Report 2008, p. 14). The state-ownership policy for 2009 can therefore be described as having the Swedish Code of Corporate Governance and the Companies Act as building blocks together with the Riksdag decisions, the Government’s administration mandate and the administration that is separated from the regulatory framework (State-owned companies Annual Report 2008, p. 12).

*The Riksdag and the Government:* When it comes to the organizational structure of the state-owned enterprises it is the Riksdag that is responsible for deciding the framework within which the company should operate, which includes defining the general business goals. In regards to the organizational structure of Vattenfall “*it is important to remember that it is ultimately the Riksdag that decides the mission for the company*” (Special adviser and analyst at the Ministry). The Riksdag gives the government a mission, which is “*to actively manage the state’s assets in order to achieve the best long-term development of value*” (State-owned companies Annual Report 2008, p.9). This implies that the government has access to the Riksdag’s funds and other assets. In situations that can lead to significant changes, the government needs the Riksdag’s approval. Significant changes include actions which could change capital contributions, the ownership structure and the general direction of the enterprise (State-owned companies Annual Report 2008, p.9). Additionally, the Riksdag is responsible for appointing the board of directors (Special adviser and analyst at the Ministry).

*The Government Offices, the Ministry of Enterprise, Energy and Communication and the Division for State Enterprises:* The Government Offices is an integral authority that assists the Government in its work and consists of the Prime Minister’s Office, the Office for Administrative Affairs and the twelve ministries (Swedish Government Offices 2008, p. 8). The areas of responsibility for the Ministry of Enterprise, Energy and Communication are, among others, state-ownership, energy, and transport and infrastructure (Swedish Government Offices 2008, p.13). Vattenfall as a state-owned enterprise thus falls under the responsibility of the Ministry of Enterprise, Energy and Communication and the Division for State Enterprises.

*The Ownership Unit and the Swedish National Audit Office:* The auditors, normally appointed by the Shareholders' meeting, have the responsibility of examining the accounting practices and annual accounts of an enterprise. In addition they should observe the work done by the chief executive officer and the board of directors (The Swedish Corporate Governance Code 2010, p. 12). In the case of Vattenfall, the Ministry of Enterprise, Energy and Communication has an ownership unit that is represented by politically neutral officials which examines the operations of the company. Beyond that, the Swedish National Audit Office makes continuous revisions of Vattenfall *"seen from the perspective of the intentions of the owners, but guarding both the Riksdag and the government's interests"* (Head of Public Affairs Nordic).

*The Annual General Meeting, the Board of Directors and the CEO:* The highest decision-making body for enterprises in general is the shareholders' meeting which has *"a sovereign role over the board of directors and the chief executive officer"* (The Swedish Corporate Governance Code 2010, p. 9). As mentioned earlier, for state-owned enterprises the board of directors is appointed by the Riksdag and it is central that the right competences are found during the board nomination process. According to the Former Employee at Vattenfall, *"the people being recruited always get a specific mission with them"*. Furthermore, it is important that the board of directors can vouch for the owners' demands and the mission of the company (Special adviser and analyst at the Ministry). The board of directors at Vattenfall decides the strategic objective for the company and in addition to this the company has *"discussions with the Ministry of Enterprise, Energy and Communications regarding what the strategic aims should be"* (Head of Group Strategic Development). The strategic objective for Vattenfall is further updated once a year and this procedure follows a model that has been created by the board of directors (Head of Group Strategic Development). When it comes to the day-to-day management of an enterprise these activities fall under the chief executive officer's responsibility. The board of directors may instruct the chief executive officer on how to decide and manage certain issues or activities (The Swedish Corporate Governance Code 2010, p. 11).

The organizational communication from company to owner goes through the board of directors via the chairman of the board. In order to prevent confusion *"it is very important that the formal structure is kept intact even if the information naturally flows between the links"* (Special adviser and analyst at the Ministry). The formal structure and the fact that Vattenfall is a limited liability company operating under market conditions leave no official room for political influence (Head of Group Strategic Development). However, occasionally attempts are made to use the company for political purposes. Head of Public Affairs Nordic believes that Vattenfall *"has probably been a political tool during its entire existence"*

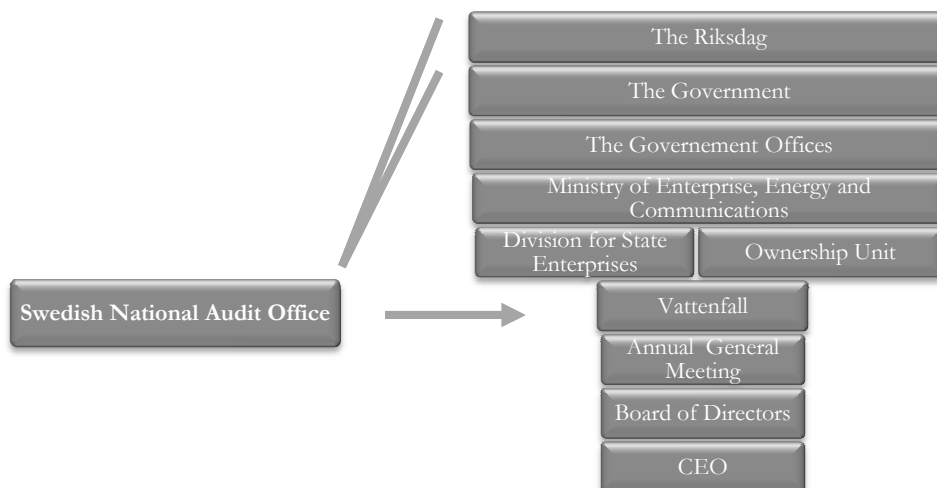


Figure 2: Vattenfall's formal organizational structure



#### *4.2.5 The cornerstones of Vattenfall's strategic formulations*

Vattenfall's energy production strategy can be illustrated by a triangle, where three factors need to be considered and weighted against each other. These factors include cost, secure supply and environmental sustainability. Cost and environmental sustainability are self-explanatory, secure supply implies the ability to continuously provide consumers with energy. Vattenfall's strategic formulation takes these factors into concern, and throughout times the importance of factors relative to one another has changed. Environmental sustainability has increased in importance relative to cost and secure supply (Head of Public Affairs Nordic).

### **4.3 Institutional changes**

The period 1996 to 2009 is signified by political ideologies that instigated institutional changes on a national and international level. Throughout this period Europe faced deregulation waves, regional integration and increased climate awareness.

#### *4.3.1 Thatcherism: a political influence encouraging deregulation*

The 1979 elections in Great Britain marked the beginning of a new era for the country. After the Keynesian markets failed, Margaret Thatcher, the leader of the Conservative Party, emerged as the first female Prime Minister. She was a strong proponent of neo-liberal politics and thus believed that the economy could be restored by decreasing the role of the state and encouraging freer markets. This is why her period in office, 1979 to 1990, is distinguished by a series of privatizations and deregulations on the British market. Thatcherism as it came to be known was a political ideology that spread beyond the borders of Great Britain and seeped through to influence European politics (Leitner et al. 2007).

#### *4.3.2 Deregulation of the Swedish electricity market*

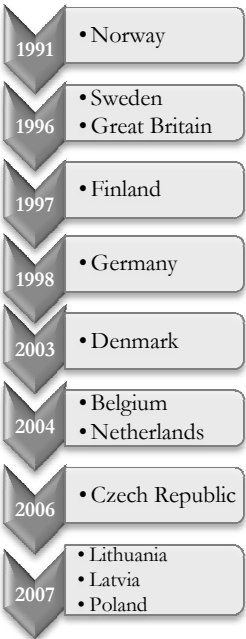
In Sweden it has been ascertained that the deregulation process of the electricity market began with the corporatization of Vattenfall (Bergman, 2002). In 1992 the government proposed a government bill that was to increase the competition on the electricity market by rationalizing pricing, increasing the possibility to export and import electricity by foreign and domestic players and decreasing monopoly pricing possibilities (Proposition 1991/1992, p.18). This proposition was passed and put into effect on the first of July 1996 (Bergman, 2002). Along with this proposition a new electricity law was passed which divided the local electricity companies into two distinctive components: generation and sales. In effect two markets were established, one for wholesale electricity and one for retail electricity (SOU 2002:7 p.6). Prior to the deregulation and the new electricity law *"the entire industry was very physical"* (Current Employee). These institutional changes led to *"inconceivable changes in the commercial environment in the electricity industry"* (Current Employee).

#### *4.3.3 Regional integration and deregulation of the European electricity market*

Up to the mid-1990s the deregulation on the European electricity market was to a great extent by driven national politics, after this period the European Union was an additional force driving the deregulation process. The founding countries of the European Union include Germany, France, Italy, the Netherlands, Belgium and Luxembourg. In 1973 Denmark, Ireland and Great Britain joined the European Union, followed by Greece in 1981 and Spain and Portugal in 1986. Sweden and Finland did not join the Union until 1995, considerably later than their Danish neighbors. Poland, Lithuania, Latvia and the Czech Republic all joined simultaneously in 2004 (Archick,

2008). The official task of the European Union is to establish “a common market and an economic and monetary union by implementing common policies (...) by promoting a high degree of competitiveness and convergence of economic performance” (Treaty Establishing European Community, Article 2). Therefore, increased membership in the European Union has “increased the integration of the electricity market as the electricity market underwent a Europeanization” (Current Employee). One of the purposes of integrating the European electricity market was to enable the pooling of resources and creating a more reliable and secure electricity system (Head of Public Affairs Nordic).

In 1996 an EU electricity market directive was passed, with common regulations for the internal electricity market. The directive took effect in 1999 with the aim to secure free mobility and strengthen the competitiveness of the electricity market. In 2003 a new directive was adopted and amongst other things it included 2007 as an end date for the full opening of the electricity markets in Europe (RiR 2004:18, p. 12). The Swedish deregulation was more far-reaching than the directives from 1996 and 2003, and had already been completed in 1996 (Bergman, 2002). The wave of deregulations spreading in Europe was believed to offer Vattenfall a paramount of opportunities (Vattenfall Annual Report 1997, p.5). Therefore, Vattenfall was actively working at both the European and national level to push for deregulation during this period (Current Employee). “Dialogs with the national authorities were held (...) with the hope to influence” (Head of Group Strategic Development). At a European level Vattenfall opened a representation office in Brussels, where Vattenfall continuously worked with the EU commission (Current Employee).



The Current Employee clarifies that “the deregulation process was the fastest in Northern Europe”. Norway, Sweden, Finland, and Great Britain were among the first European countries that separated a previously vertically integrated value chain, and had all completed the deregulation of their respective electricity markets by 1997 (Bergman, 2002). Germany opened their markets for competition in 1998, the same year in which Poland began the process of deregulation. Denmark was less speedy than its Scandinavian neighbors and completed their deregulation in 2003. Belgium and the Netherlands both concluded the deregulation process in 2004 (EU Internal Market Fact Sheet, 2007). In Eastern Europe, Poland finished deregulation in 2007, a year later than their Czech neighbors and “not as soon as originally anticipated” (Head of Group Strategic Development). The latecomers Lithuania and Latvia did not finish deregulating their electricity markets until 2007 and the deregulation of their gas markets was postponed to 2010 (EU Internal Market Fact Sheet, 2007). The deregulation of the electricity market in countries where Vattenfall has been or is present is illustrated in figure 3.

Figure 3: Deregulation of the electricity market in countries where Vattenfall has been or is present  
 Source: EU Internal Market Fact Sheet, 2007

The deregulation of the electricity markets implies that power generation is separated from sales; an assumption is that this is achieved as a result of privatization. The process of deregulation however takes different forms in various countries. In Norway “a bill was presented to further strengthen public ownership of electricity” (Vattenfall Annual Report 1998, p. 11) in 1998. Moreover, to the present day “the Norwegian legislation does not make private and foreign ownership of Norwegian hydroelectric power possible” (Head of Group Strategic Development). In France the process of deregulation had proceeded at the minimum pace required by the European Union (Bergman, 2002). In Latvia, the conflicts between the government and other stakeholders made it a

hazardous area to expand to (Current Employee). However, regardless of the pace and exact structure of the deregulation, the EU membership states agreed in a summit in Barcelona in 2002 that the electricity market for both households and non-households was to be fully deregulated by 2007 (Bergman, 2002).

#### *4.3.4 The three pillars determining the European Union efforts in the energy sector*

The European Union's climate attitude can be mirrored in the directives and regulations passed. In 2007 it was established by the European Council that three pillars are to determine the efforts in the energy sector. These include: *environmental sustainability*, *economic efficiency* and *increased security of supply*. Increased economic efficiency and supply is to be achieved mainly through increased use of renewables (2001/77/EC) and reduction of carbon dioxide emissions by increasing end-use efficiency (2006/32/EC). The 2006/32/EC repeals the 93/76/EEC and sets specific targets rather than general goals. As a result of 2006/32/EC the Swedish government has assumed the goal to ensure that the energy intensity in the Swedish economy is to be reduced by 20% by 2020.

#### **4.4 Internationalization: Early experimentation**

Vattenfall's internationalization can be divided into two main phases: early experimentation and internationalization at the turn of the century. During the 1950s the advance of electric generation and electric grids was considered the cornerstone of Swedish modernization (Schön, 2000, p. 387). Hydroelectric power was expanded and an extensive nuclear program was issued. In 1965 the first nuclear power generation plant was built, Oskarshamn 1. The 1970s were considered the breakthrough decade for nuclear power and in 1973 two nuclear power reactors were exported to Finland. Sweden remained one of leaders within power technology development, an esteemed position held since the breakthrough of the industrialization in the 1850s (Schön, 2000, p. 387). The state used its influence and decided that Vattenfall should conduct research projects, although Vattenfall's employees were not always sure of the projects' contribution (Former Employee). As society modernized the domestic demand began to reach a saturation point, consequently the building of power generation plants declined in terms of volume. At that point, most power producing companies, including Vattenfall, were in possession of overcapacity and engineers. Moreover, the power companies operated in terms of commission (Current Employee).

In the late 1980s Vattenfall began to look at possibilities to use their overcapacity in other industries. Vattenfall entered a number of facility projects, such as building bridges and rebuilding sewage disposal plants (Current Employee). The enterprise also looked outside Europe for opportunities in Thailand, Laos and Bolivia (Head of Group Strategic Development). Some would argue that the purpose of the early expansion was to build and rebuild facilities for profit (Current Employee). Others would argue *"that the sentiment of the industry was that you had to eat or be eaten"* (Head of Public Affairs) and that Vattenfall *"was too small to be large and too large to be small"* (Head of Group Strategic Development). However, much of the activity in South America and Asia were aid projects, on commission from SIDA, the Swedish International Development Cooperation Agency, and inasmuch as they offered an opportunity to learn, the financial contribution to Vattenfall's profit was limited (Former Employee).

Head of Public Affairs describes the international expansion in the early 1990s as *"taking a world map and throwing a dart, you ended up where you ended up (...) having small investments here and there"*. The Current Employee believes that local connections were important in determining the expansion, as it was important to know the political and legislative structures. He *"remember[s] it as a period where you were out meeting people, it is not like you had a hundred projects and selected the best"*. Moreover, the

electricity sector was and remains highly influenced by politics. Vattenfall's expansion in Latvia and the Czech Republic was for instance obstructed by political conflicts. At the turn of the decade Vattenfall divested or swapped the South East Asian and South American projects, as well as their operations in the Czech Republic, Lithuania and Latvia, as *“creating leverage with the existing knowledge was more difficult than expected, the distance had a larger impact than originally anticipated and Vattenfall reached a point where it wanted to be more than just a financial investor”* (Head of Group Strategic Development).

#### ***4.5 Internationalization: At the turn of the century***

This section will be divided into five subsections, providing empirical data about the internationalization at the turn of the century. The first subsection will provide empirical findings on the geographic choice; this section is followed by a description of the choice of the production mix and market entry. The fourth section will describe the market adaptation and the final section will list the challenges faced during the internationalization.

##### *4.5.1 Geographic market choice*

Around the year 2000 Vattenfall decided to concentrate their efforts geographically. Moreover, they decided to narrow their focus to acquiring production technologies and facility projects. Physical geographic distance was an important factor in determining which markets should be penetrated. At the early stages electricity which was not physically available was considered valueless as it could not be used (Current Employee). Considering the knowledge about the neighboring markets, and the smaller cultural and physical distance, it is believed that expansion to adjacent markets can facilitate economies-of-scale and the transferring of competence (Head of Group Strategic Development). When selecting a suitable market, prior projects in a country are considered a valuable factor because they increase the know-how of a market. For instance the SwePol link, a submarine cable connecting Sweden and Poland, increased Vattenfall's experience of doing business in Poland (Head of Public Affairs). The discrimination between markets is further affected by the size and growth of a market, as Vattenfall has *“chosen a strategy where we [they] want to belong to the top three players on a market because we [they] want to have impact on the market”* (Head of Public Affairs).

##### *4.5.2 Production technology mix*

From the year 2000 onwards, *“the foremost value-creating strategy of the European energy companies has been growth”* (Special adviser and analyst at the Ministry). Therefore, the large European players have grown mainly through acquisitions (Vattenfall Annual Report 2003, pp.26-27). To a large extent Vattenfall acquires the existing production mix of the market which they enter. This implies that if a production mix of a country for instance includes gas Vattenfall will purchase companies which have gas production technologies (Current Employee). One motivation for acquiring the existing production is that *“there has been very little choice”* (Current Employee). However, acquiring parts of a market's production mix is also considered to have *“been beneficial from a risk perspective”* (Head of Group Strategic Development). Moreover, this strategy allows Vattenfall *“to feed on knowledge from other markets”* (Head of Public Affairs). The Head of Public Affairs exemplifies this with Vattenfall's entry to Denmark where they tapped into the Danish companies' knowledge on wind power which was far greater than Vattenfall's.

#### 4.5.3 Market entry choice

When acquiring companies, Vattenfall “*has decided that it wants to be an industrial owner, with managing control and majority ownership in the acquired companies*” (Head of Group Strategic Development). Vattenfall buys varying percentages of a company’s shares and gradually increases their ownership. The speed of assuming managing control is affected by both the sellers’ reluctance to sell everything at once and Vattenfall’s inability to “*swallow such large prey in one bite*” (Current Employee). The acquisition of Nuon was, for instance, affected by the Dutch municipalities’ request that the purchase took place incrementally. As a result acquisitions often extend over time and require a lot of work before full ownership can be attained. Therefore, the speed of the acquisitions has varied over time and across markets. However, Vattenfall has not only acquired companies single-handedly, in the 1990s Vattenfall shared their offices in Poland, Lithuania and Latvia with IVO, currently Fortum, as there was no competitive relationship between the firms (Current Employee). However, with tougher laws on competition and changing competitive relationships between companies the ability to share the risks with other companies has decreased. Thus, variations in market entry form have changed and decreased across time (Head of Group Strategic Development). Vattenfall acquires companies either through swaps or cash payments as mergers and stock payments are not made possible given the ownership structure (Current Employee).

#### 4.5.4 Market adaptations

Vattenfall applies its management control models to the newly acquired companies, implying that it divides the organization in accordance to the value chain. The organization therefore includes a wholesale, sales, production, distribution and, in some cases, transmission division (Head of Group Strategic Development). Normally, a temporary Swedish manager is appointed to the acquired company. The acquired company’s management is trained into Vattenfall’s management philosophy for example by participating in the ongoing management training programs, along with managers from other acquired companies (Former Employee). The process of retraining employees can be very difficult: “*some countries are more difficult than others; in Poland it has been difficult to gain acceptance of Vattenfall’s way of working*” (Former Employee). However, “*it’s not like we [Vattenfall] force the Germans to be Swedish*” (Current Employee).

During the consolidation process in mid-2000 foreign acquisitions obtained the Vattenfall brand, because it was believed that the acquired companies “*should act and be recognized as Vattenfall. From an internal and external perspective having a number of brands does not look so good*” (Head of Group Strategic Development). Moreover, Vattenfall hopes to be able to leverage the brand on the end-consumer, enabling them to charge higher prices than their competitors. However, this is not something which they to date have been able to do (Head of Group Strategic Development).

First and foremost Vattenfall follows the national laws of the individual markets they enter; in Sweden Vattenfall follows Swedish laws, in Germany they follow German laws and so on. However, Vattenfall does “*consciously act to be ahead of the legislator*” (Head of Group Strategic Development). The Swedish state requires Vattenfall to follow the laws and regulations applicable in each country they operate in. It is believed that applying Swedish laws and regulations on a foreign market could become increasingly unprofitable because it might not be consistent with the enterprise’s commercial targets (Special adviser and analyst at the Ministry). However, many of the legislative developments start in Brussels where new EU directives are issued. These directives are applied to all markets with local modifications (Head of Public Affairs). *Figure 4*, illustrates Vattenfall’s foreign activity on the European market between the years 1992 to 2009.



Figure 4: Vattenfall's expansion in Europe  
Source: Vattenfall's Annual Reports 1997 to 2009

#### 4.5.5 Challenges

When Vattenfall enters various foreign markets, Sweden and Swedish values are highly esteemed (Head of Public Affairs). Head of Strategic Development “believe[s] that Sweden, and via Sweden Vattenfall, has an image abroad of being innovative and having a green profile, especially on the British market”. There are considerable benefits with being state-owned: “there is no risk that the company will default (...) the company also receives greater credibility relative to its consumers and suppliers” (Former Employee). Despite that, Vattenfall's activities abroad have been monitored over the years, most likely due to the size of the company and because electricity is one of the central sources for the economy as a whole (Current Employee). Special adviser and analyst at the Ministry believes that Vattenfall, on its foreign markets, is associated with the Swedish government to a greater extent than private companies. The Current Employee agrees that this is the case in discussions involving governments and other authorities; however he believes that the foreign end-consumers are unaware of the fact that Vattenfall is state-owned. Although employees at Vattenfall and the

Ministry disagree, some believe that one of the challenges for the Swedish government is that the credibility of its environmental and energy policy “*is affected negatively*” (Former Political Advisor) if the international expansion is not consistent with the Swedish values.

Vattenfall has among other companies acquired state-owned companies. In these instances Vattenfall had to struggle with communicating the importance of the connection between revenues and investments. This represented a challenge since the companies were accustomed to get finances for their investment and hence found it hard to see that investments needed to be financed somehow (Current Employee). Head of Group Strategic Development says that in the acquisitions at the beginning of 2000 “*what we could have done better is understanding the need the acquired company had for clear communication*”. He, however, believes that the early acquisitions were very educative in this aspect and have enabled Vattenfall to improve considerably in the area of communication. Communication with various interest groups is difficult. The Head of Public Affairs ascertains that communication between Vattenfall and the acquired companies is not the only time communication has failed. For instance, the first acquisitions in Germany led to a number of demonstrations in the local community as the public feared that the brown coal operation would be shut down. Today, Vattenfall still faces demonstrations, but from different interest groups, such as Greenpeace, where they want Vattenfall to shut down the brown coal operations. The Head of Public Affairs believes that Vattenfall could have improved their way of communicating their intentions and should work continuously with communications.

## 5. Analysis

This chapter will analyze the empirical findings. Firstly, the analysis will answer the two sub-questions. Section one will determine why state-owned enterprises choose to pursue international markets, and section two will establish the challenges faced by a state-owned enterprise as a result of foreign market presence. Secondly, the analysis will examine how state-owned enterprises expand internationally, which will provide an answer to the main research question.

### *5.1 Why do state-owned enterprises choose to pursue international markets?*

This section will be divided into three parts, and these are the main categories into which internationalization pressures can be grouped. These groups are: increasing profits, exploiting competitive advantage or improving competitive disadvantage, and changing institutions.

#### *5.1.1 Internationalization as a means to increase profits*

One of the drivers for internationalization was the saturation of the Swedish markets. The Swedish energy market had practically been fully developed, therefore Vattenfall tried to enter new product markets. However, it was difficult to grow efficiently and establish a presence this way given the need for connections to receive contracts. At the same time Vattenfall was in possession of overcapacity and internationalization offered an attractive possibility to employ this overcapacity (Czinkota, 2004). The fact that Vattenfall's competitors grew through international acquisitions means that Vattenfall's expansion to some extent was a competitive response. They did not desire to fall behind their competitors (Porter, 1986). In order to survive on a deregulated market, they could only defend their position if they chose to be small enough, to protect a niche territory or large enough, to defend themselves against internationalizing energy companies.

However, inasmuch as Vattenfall might have responded to competition, the owners had quite high ambitions for Vattenfall. The government-owned Vattenfall, was an agent of industrial power as well as a national champion, driving the modernization and electrifying Sweden. Once Vattenfall became a state-owned limited liability company the ambition of being a national champion remained, however now it extended beyond the Swedish borders. Moreover, with the deregulations, the state could no longer protect Vattenfall against competition. If Vattenfall did not act they faced the risk of being acquired by a larger and more powerful company. Therefore, the government's ambition to build an empire was a contributing factor to Vattenfall's international expansion (Brealy et al., 2006). Moreover, one could argue that Vattenfall's willingness to expand internationally is contradictory to the theory claiming that state-owned enterprises are reluctant to establishing a permanent presence on foreign markets (Mascarenhas, 1989; Vernon, 1979). However, as a result of European integration, through the European Union, it is highly likely that governments have redefined their domestic borders. This would imply that European state-owned enterprises are today willing to expand beyond their domestic markets but unwilling to expand beyond the EES countries, as the EU has developed a regionally integrated electricity market. Therefore, with modifications, this would support the established theory. Moreover, international expansion is not contradictory with the goals of state-ownership (Mascarenhas, 1989; Vernon, 1979) if the goal is to create a national champion outside the domestic market.

#### *5.1.2 Internationalization as a result of competitive advantage or competitive disadvantage*

Vattenfall had a considerable competitive advantage of working on deregulated markets, partly because the Swedish market had been deregulated very early relative to its European counterparts. But also because local companies on some foreign markets, like for instance



Poland, have been overprotected by the government. The regulated markets led the local companies to lose their legitimacy as they operated more like government authorities than companies (Brannen, 2004).

In some markets, Vattenfall believes it has benefitted from its brand value and empirical findings suggest that Vattenfall has had an advantage from being associated with Sweden. Now whether or not that association is a result of state-ownership or due to brand value can be discussed. Clearly, the investments made in the brand and the size of the company can lead to the company being connected to its domestic market, in a similar fashion to the IKEA brand. However, during the early acquisitions the enterprise's brand could not have been well known even on the domestic market. Moreover, in the early acquisitions in Germany, the acquired companies were almost triple the size of Vattenfall; without additional legitimacy it could have been difficult to manage these companies credibly. Therefore, it is very probable that type of ownership provided Vattenfall with a competitive advantage. The company was directly connected to a powerful and creditworthy owner, but more importantly the ownership form strengthened the association to Sweden. Being connected to Sweden was a considerable advantage especially since Swedish values were highly esteemed and Sweden was also considered one of Europe's leading countries in developing power technologies. Therefore, it was the owners rather than the brand that led to Vattenfall's association with Sweden. This in turn represented a considerable competitive advantage.

However, simultaneous to offering a competitive advantage, state-ownership has presented a considerable competitive disadvantage. The active ownership implies that Vattenfall has to be responsive to political influence. Goal incongruence between owners and management is not an uncommon occurrence in companies. However, every four years Vattenfall faces a potential change of owner that has the power of changing the institutional framework under which the company operates. Beyond the change of owner, political ideologies change over time. Political parties do not have the same political ideologies today as they had ten years ago, for instance. In the case of private ownership, the change of owners might induce a new way to work, but most often the aim is the same: maximize profits. With state-owned companies the change of aims is often connected to individual party politics. Moreover, the government appoints the board of directors and writes the articles of association and in effect it can control every step the company takes. Therefore, state-ownership is a considerable potential competitive disadvantage, as it can cause disorientation. Another reason as to why the ownership is a competitive disadvantage is because it limits the choice of entry mode.

Mazzolini (1980) argues that state-owned enterprises expand abroad to obtain control over natural resources that the home country does not have. Sweden's access, to for instance gas is limited, however, Sweden has a safe energy supply because of its access to natural resources and nuclear power plants. Therefore, acquiring control over natural resources has not been necessary to maintain the energy production. Child & Rodrigues (2005) argue that state-owned enterprises internationalize to obtain technological assets. Truly, Vattenfall has acquired production technologies that are not present on the Swedish market, which enables Vattenfall to be in the vanguard of the energy sector. It also offers Sweden the ability to retain the prestigious title of belonging to Europe's leading countries in developing power technologies.

### *5.1.3 Internationalization as the result of changing institutions*

Vattenfall has not waited for institutional changes to occur instead, they have been actively engaged in discussions with politicians. This institutional entrepreneurship has allowed Vattenfall to direct the process of deregulation. In Sweden this means that the Swedish market was

deregulated when the enterprise had received considerable time to prepare and was finally ready to be exposed to competition. Through the Brussels office Vattenfall has been able to influence European politics. To what extent this has been successful is unclear. Inasmuch as changing institutions have offered an opportunity to exploit new markets, Vattenfall has been prevented from entering adjacent markets at the speed they desired because the process of deregulation did not happen fast enough or because it was limited. Nonetheless, Vattenfall entered many markets long before they had been deregulated. This is because being among the first on the market they could create barriers of entry by building relationships with the society and politicians.

Summarizing, Vattenfall's international expansion was driven by a number of factors, and assessing their relative importance is difficult. However, without the deregulations Vattenfall would not have been able to expand internationally through the energy sector. Moreover, internationalization was driven by both ambition and pressure.

## ***5.2 What are the challenges faced by a state-owned enterprise as a result of foreign market presence?***

When a state-owned enterprise enters a foreign market it will meet challenges that are company specific. Hence, a state-owned enterprise might find difficulties as a result of its ownership structure. The following section will analyze the specific challenges Vattenfall faced as a state-owned enterprise when expanding abroad. The section includes an analysis of the general challenges, recontextualization and legitimacy.

### *5.2.1 Challenges in general*

When Vattenfall expanded abroad most of the acquisitions were not acquisitions of equals. The acquired companies during the late 1990s were often much larger in size. It therefore became a challenge for Vattenfall to establish itself as superior, as the acquired companies found it inferior due to its smaller size. In time Vattenfall's acquisition objects have been smaller relative to Vattenfall and Vattenfall no longer faced the same difficulties resulting from size. Given that acquisitions imply that the acquired company becomes a part of the acquiring company, assimilating the organization and mindset has been challenging. This is a problem that Vattenfall faced both on the Polish and German markets. Additional challenges have been economic nationalism faced in regulated markets, and as a result of institutional distance. It appears that the challenge regarding institutional distance was so great, that the solution to it was to leave the markets that presented this challenge. Therefore, Vattenfall left Latvia, Lithuania and the Czech Republic.

### *5.2.2 Recontextualization*

When it comes to recontextualization theory suggests that the host market will interpret the foreign enterprise given their local context (Brannen, 2004). The case of Vattenfall has also proven that the home market can interpret the domestic company through the context of the foreign market. To specify, the domestic market of Vattenfall has interpreted the company's operation through their foreign market operations. This implies that Vattenfall's operations in the German market have influenced the company's operations in Sweden. For a state-owned enterprise it implies that the host country can interpret the politics of a country through the state-owned enterprise. Additionally, these will be interpreted from a local context. The challenge is thus for the state-owned enterprise to overcome, prevent or, if possible, make use of the shift and changes of meanings in different cultural contexts.

Another aspect that has been confirmed in this case is that the challenge of recontextualization and that it changes over time. When Vattenfall started their international expansion they became associated with Swedish values. Once abroad Vattenfall faced positive recontextualization issues, their operations were interpreted as representing the best of Sweden. However, as Sweden has continued to push for environmental sustainability foreign markets have interpreted this as these values should be projected through Vattenfall. But Vattenfall follows the local conditions where they operate and have thus not yet been able to entirely channel the Swedish environment focus into some of their foreign markets. What previously had not been a recontextualization problem now is.

### *5.2.3 Legitimacy*

During the beginning of Vattenfall's internationalization the company gained acceptance from its environment and hence faced few challenges in regards to achieving legitimacy as theory has suggested (Kostova and Zaheer, 1999). In recent years Vattenfall's challenge in regards to legitimacy can be divided into two aspects, one internal and one external. Following the internal aspect, Vattenfall encountered legitimacy challenges when the objectives of the company started to change. In their strategy triangle this is represented by a shift from a balance point close to secure supply and cost to a new point closer to environmental sustainability. When this shift was not clearly reflected in Vattenfall's international operations the company's legitimacy started to decrease. It is noteworthy that Vattenfall's strategy triangle is very similar to the three pillars adopted by the European Union, which suggests that European Union has a crucial influence in Vattenfall's strategy.

The external aspect is connected to the politics of the home country and how these are reflected through the state-owned enterprise. Sweden is characterized as an environmentally friendly country, constantly working to improve the technologies towards an industry free from pollution. Vattenfall on the other hand needs to consider the local conditions in their host countries. Thus, Vattenfall's legitimacy decreases both in the home and host country when they, for instance, maintain their brown coal operations in Germany and yet continue to position themselves as an environmentally friendly company. Therefore, in order to gain and maintain legitimacy it becomes important for state-owned enterprises to keep a credible political stance when going abroad since their actions will be perceived as representing the home country government's politics.

## ***5.3 How does a state-owned enterprise expand internationally?***

As explained in the delimitations section, all aspects of how a state-owned enterprise expands internationally will not be discussed. Therefore the following parameters will be analyzed: geographic market choice, degree of market adaptation and market entry mode.

### *5.3.1 Geographic market choice*

In the early experimentation phase Vattenfall explored both culturally and geographically remote markets. The years following 2000 were signified by a geographic concentration, adjacent markets were penetrated and non-adjacent markets were vacated (*see figure 5*). This pattern of expansion is diametrically opposed to the predictions made by the Uppsala model. Moreover, it seems to contradict the idea that state-owned enterprises are risk-averse (Mascarenhas, 1989). However, as the expansion is further scrutinized it appears that Vattenfall has generally expanded in line with the Uppsala model, despite the fact that they have had the support of a powerful owner (Vernon, 1979).

The early expansion in Asia and South America were relatively risk-free as these escapades were aid projects initiated and financed largely by SIDA. At the same time, conducting business in these areas offered access to potentially lucrative future markets and enabled relationships to be built, though more importantly it enabled Vattenfall to accumulate knowledge of how it was to conduct business overseas. Most likely it was the difficulties faced with realizing synergies and the experience of the complex cultural matching, which induced Vattenfall to pursue geographically neighboring markets. As of the late 1990s the expansion has continued to geographically close markets, despite nearly 20 years of foreign presence.

The empirical data shows that Vattenfall wanted to enter geographically near markets and then continued their expansion entering adjacent markets. In the late 1990s, geographical proximity was a prerequisite for market penetration as electricity needed to be transferable to the domestic market otherwise it had little value. However, this does not explain why Vattenfall first entered and then chose to leave Latvia, Lithuania and the Czech Republic. Lithuania and Latvia are separated from Sweden by the Baltic Sea, in similar fashion to Poland, and Poland has been penetrated. Moreover, Lithuania and the Czech Republic are both neighboring countries of Poland. The early entrance into various Baltic states and a couple of markets in Eastern Europe was a risk diversification strategy. These former Soviet states offered considerable growth potential, with their outdated production facilities that ran inefficiently. They all had bright prospects of upcoming modernization, which in turn would require the development of the electricity sector. With a powerful owner, Vattenfall could enter these markets simultaneously.

However, Lithuania, Latvia, Poland and the Czech Republic also presented considerable political risks and as political winds are difficult to predict Vattenfall entered a number of potentially politically volatile markets to diversify the political risk exposure. In time Lithuania, Latvia and the Czech Republic proved to be extremely politically turbulent. This made it virtually impossible for Vattenfall to establish the proper connections that would enable them to establish themselves on these markets. Lithuania, Latvia, the Czech Republic and Poland all became membership states of the European Union simultaneously and finished deregulating their markets almost concurrently. However, relative to the others, Poland was more politically stable. Furthermore, Vattenfall had established connections in the country which made it a market that was less risky and thus more attractive than the others. Moreover, Poland is larger than all the other three markets combined; therefore, leaving the other markets allowed Vattenfall to concentrate their effort on one market.

Another contributing factor to the choice of market is the opportunity for Vattenfall to leverage their competitive advantage. As Sweden deregulated its markets quite early, one of Vattenfall's competitive advantages has been their experience in this process. Interestingly, with the exception of Norway and Great Britain, Vattenfall has entered markets which were deregulated subsequently after Sweden. In addition to growth potential of a market, Vattenfall wishes to be among the top three players on the markets they enter, so that their institutional entrepreneurship can become more fruitful. Vattenfall has in the past been engaged in governmental discussions; trying to shape the deregulation process on the markets on which they were present. However, it is important to keep in mind that the pace of deregulation largely dictated the ability and speed with which Vattenfall presence could be established on markets. For instance, although Denmark was a desirable market as a result of its geographic location, it was a complicated market because Vattenfall's ambition was limited by the country's regulation. Vattenfall did, however, attempt to influence the pace. Therefore, the changing institutions in Europe offered Vattenfall an opportunity to use their competitive advantage to benefit from a first mover advantage and to engage in institutional entrepreneurship. Though, changing institutions have also confined

Vattenfall's expansion. Clearly, the choice of markets has been an incremental process, though the Uppsala model does predict that, with increased international presence, a company will expand beyond its comfort zone. Yet Vattenfall has continued to expand to adjacent markets. It could be argued that this is because they have not accumulated sufficient international experience. However, this strategy is employed to create a strong foothold in Northern Europe. Resources can be pooled across markets, and synergies are more easily realized.

Unlike Mascarenhas (1989) predicts Vattenfall does not display a preference for stable institutions. Vattenfall seems to have acted in line with Mazzolini's (1979) argument and invested in countries with high political risk, when that political risk is defined as unstable institutions. Vattenfall exploits unstable institutions, which might be difficult to understand given their preference for political stability. However, as a state-owned company it is possible that Vattenfall has considerable experience from continuously changing institutional frames. In a period of five years Vattenfall went from a government-owned enterprise to a state-owned enterprise, and faced deregulations on the Swedish market. Therefore, they have considerable experience from changing institutions. Moreover, since the direction of the deregulations had already been pointed out, it was considered a matter of time before the European countries followed suit. Political turbulence is more difficult to predict and Vattenfall did not have much experience from working under such conditions. Conclusively, there are various categories of political risk. One category is characterized by changing institutions and another is characterized by governmental turbulence. Vattenfall finds the former desirable and the latter undesirable.

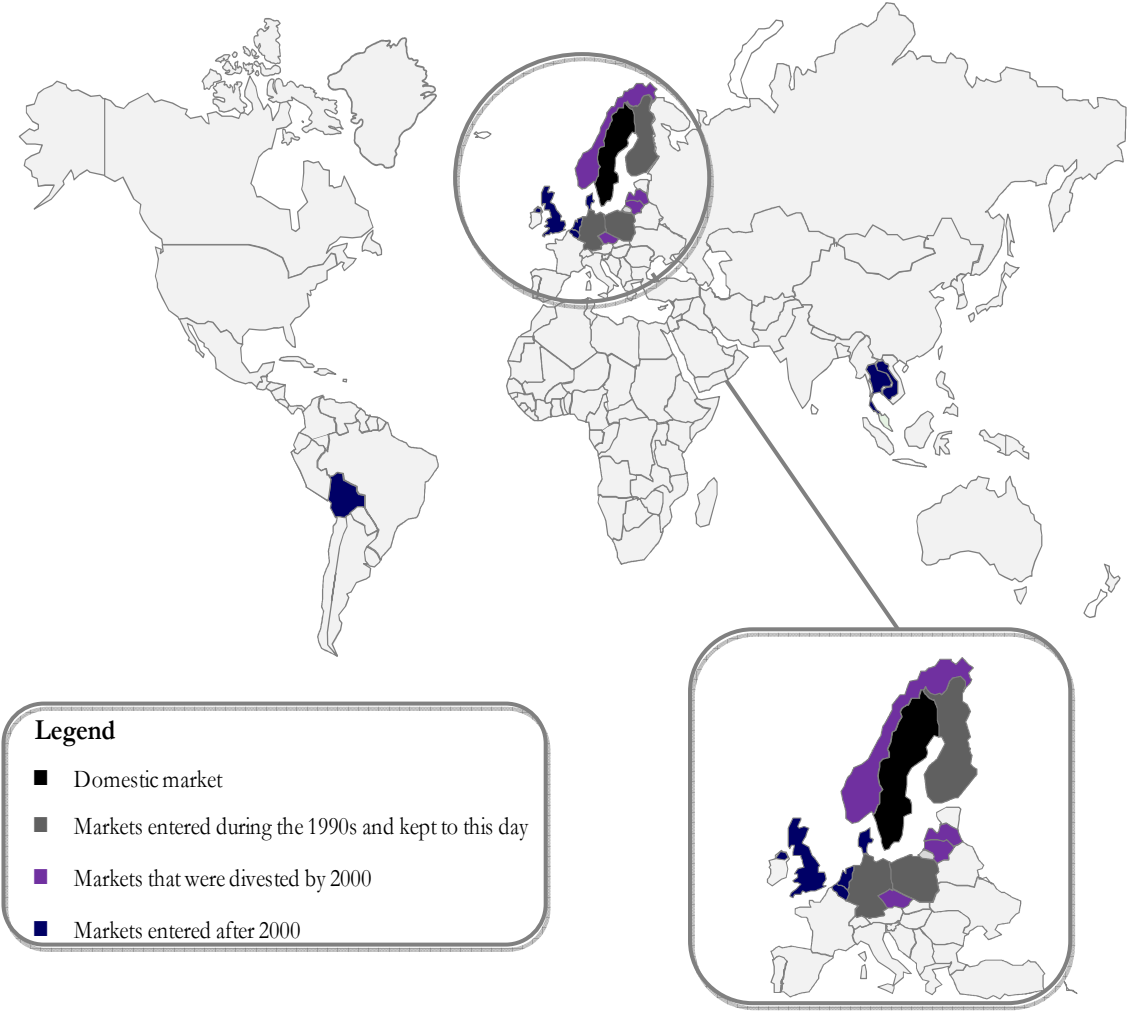


Figure 5: Vattenfall's international expansion

Summarizing, the factors determining Vattenfall's choice of market include lack of choice, unfavorable or favorable institutional conditions, growth potential of a market, the likelihood of successfully establishing themselves as a powerful actor, and cultural distance. However, the most decisive factor seems to be geographic proximity. Geographic proximity is not only a less risky alternative than geographic distance, but more importantly it enables Vattenfall to create a strong foothold in Northern Europe and realizing economies-of-scale. Additionally, Vattenfall does not favor stable institutions over unstable institutions.

### *5.3.2 Market entry mode*

Beyond predicting which markets companies will enter, the Uppsala model also suggests that firms incrementally increase their involvement in a country (Barkema et. al, 1996). Vattenfall has entered new European markets in a number of ways, however never through mergers as those are not possible given Vattenfall's ownership structure. Before entering a new market, prior connections in a country are considered a decisive factor. Between the years 1990 to 1997 Vattenfall set up representations offices in Poland and Germany, and entered a joint venture in Germany to nurture the connections previously established. The only acquisition in this period was made in Finland. After 1997, a joint sales company was formed in Denmark and shares were purchased in companies in Europe. Over time Vattenfall either increased their shares in acquired companies and joint ventures or left the markets where they could not increase their influence. This pattern suggests that involvement has increased in line with the Uppsala model. However, one must take into consideration that the market conditions determined the speed with which Vattenfall entered new markets and the type of influence exercised.

As competitive relationships evolved, joint venture with other players was prevented because of competition laws. However, it is clear that Vattenfall desires to gain full management control in the companies they acquire. Therefore, joint ventures were voluntarily abandoned. Conversely, with the appearances Vattenfall has not followed the Uppsala model's four-step process of involvement because they want to reduce risk, but because of regulations they have not been able to acquire full control immediately. Before the deregulation of the electricity market, Vattenfall's choice of entry was restricted. Therefore, they desperately tried a number of ways to establish their presence. During the process of deregulation host governments dictated the pace in which companies were sold off. However, in some cases Vattenfall has not had the ability to attain full control immediately simply because of the size of the acquisitions. Noteworthy is that this forced incremental involvement has enabled Vattenfall to learn which could also be a reason as to why Vattenfall chose to penetrate some markets and exit others.

The question that remains is why Vattenfall wants to have complete control over the acquired companies. One of the reasons is that it will make the acquired company an integrated part of Vattenfall, and thus it indirectly becomes a Swedish state-owned company. As a result the Swedish government will have increased interests in the development and progress of the acquired company. Along with the market dominance, Vattenfall's desire for complete ownership implies they can influence society to a larger extent. Moreover, being a dominant player will induce cross-governmental conversation between the host and domestic market, which can create favorable business conditions for the company (Mazzolini, 1979). Furthermore, the owners might demand full control to enable the government to influence the acquired companies.

It has been suggested that state-owned enterprises are more prone to enter business relationships with other state-owned enterprises (Mascarenhas, 1989; Vernon, 1979). While this has been partially confirmed by Vattenfall's activities in Laos, Thailand and Bolivia, though the expansion in Europe rejects this theory. Vattenfall has not displayed a will to enter business relationships

with state-owned enterprises to a larger extent than with private enterprises. Vattenfall has purchased previously state-owned enterprises because of the way deregulation has been shaped in some countries, rather than because they discriminate against private enterprises. Conclusively, Vattenfall has tried various modes of entry because of the restrictions placed by regulations. They do not display a desire to engage in business relationships with state-owned enterprises to a larger extent than private enterprises. Even though the entry mode has been incremental, it has not been so by choice. Aside from facilitating management control, full control is required to allow the state-owned enterprise to draw benefits from their owners, as the owners can engage in political negotiations on the enterprise's behalf.

### *5.3.3 Degree of market adaptation*

The empirical findings on market adaptation can be divided into three separate categories: organization, regulation and production technologies.

*Organization:* Vattenfall has adopted an ethnocentric approach to the structure of their organization, meaning that Vattenfall's domestic organization is applied on the foreign markets. Mazzolini (1979) argues that the strategies and processes of state-owned companies have been tailored for the domestic market. Therefore, increased international presence should increase market adaptation. However, the organizational structure has not followed this pattern. This is not because Vattenfall considers its organization superior to its competitors; rather it is the ownership structure that demands that the organizational structure is kept intact. If the organizational structure were to change, the Swedish government's influence on Vattenfall's subsidiaries could be reduced. Because of the consequences Vattenfall's action can have on the political debate, the state needs to retain considerable control, which it can through the organizational structure. It is that the frame for the organizational setup is transferred when expanding abroad; however, the management of each foreign company is kept. It could be argued that one reason for keeping the management intact is to tap into local tastes. More importantly, in an industry where connections are crucial for success, the local employees have already established these connections. Therefore, it is important to retain key personnel.

*Regulations:* Vattenfall's approach to regulations has been polycentric, i.e. they have adopted multiple orientations. This means that Vattenfall has abided by national regulations, although they pride themselves on being one step ahead of the regulators. Kostova and Zaheer (1999) suggest that this orientation makes market adaptation a quite smooth process. In Vattenfall's case it has caused considerable friction, as they are often scrutinized by various global stakeholders. Through time Vattenfall has applied a more geocentric orientation, however not as a result of will, but regional integration.

*Production technologies:* Vattenfall has acquired the production technologies that various markets have offered as part of a risk-diversifying strategy. As a result of deregulations, energy companies can no longer diversify their risk by controlling various parts of the value chain. Therefore, Vattenfall has diversified both geographically and through production technologies. Again it has been suggested by Kostova and Zaheer (1999) that adapting to local norms and making use of local resources would ease the process of adaption, though this has not always been the case. Although the initial entrance into Germany, for instance, was welcomed particularly because the local resources were used, in time the consequences of applying a polycentric approach have been troublesome. The reason for this is that Vattenfall has moved to developing a global orientation. These production technologies fall under the global brand, Vattenfall. As a result the acquired companies are to a greater extent connected to Swedish values and political sentiments and some of the acquisitions are contradictory to these.

## 6. Conclusions

This chapter will answer the sub-questions and the main research question of the paper.

### *6.1 Why do state-owned enterprises choose to pursue international markets?*

There are a number of factors that made Vattenfall expand internationally. The saturation of Swedish energy markets made a change in strategy necessary. Moreover, companies in the energy sector began pursuing international markets and as a competitive response Vattenfall replied with imitating the competition. Vattenfall has not expanded abroad in order to obtain control over natural resources that are not present in Sweden, rather they have expanded abroad to obtain control over production technologies that are missing from the Swedish market. This has enabled Sweden, via Vattenfall, to retain the prestigious position of being one of Europe's leading countries in developing power technologies. Furthermore, Vattenfall's competitive advantages have encouraged internationalization. These competitive advantages include experience from deregulated markets and the advantage of being a foreign firm in markets where the local companies had lost their legitimacy as a result of regulation.

Moreover, Vattenfall has had a considerable advantage of being state-owned as it implies having a strong owner behind them and it has also increased the association with Sweden. Additionally, the findings show that state-owned enterprises do not display a reluctance to create a permanent presence abroad (Mascarenhas, 1989; Vernon, 1979) this is because increased regional integration has led to a redefinition of the domestic market. The Swedish government formulated the vision of making Vattenfall a national champion, not only in Sweden but in Europe. Consequently the government's ambition to create an empire has further encouraged internationalization. Therefore, international expansion is not contradictory (Mascarenhas, 1989; Vernon, 1979), with the goals of state-ownership if the goal is to create a national champion. However, being state-owned has also been a competitive disadvantage, because it has resulted in goal incongruence, but more importantly it has obstructed long-term strategic planning as the potential change of owner or ideologies is constantly looming.

### *6.2 What are the challenges faced by a state-owned enterprise as a result of foreign market presence?*

Vattenfall has faced a number of challenges as a result of their foreign market presence. These include communication problems with both the host country's employees as well as the societal interest groups. They have also suffered problems with recontextualization. Vattenfall's foreign markets interpret the enterprise through their actions on the domestic market. However, simultaneously Vattenfall's domestic market interprets the enterprise through its actions on the foreign market. Given that foreign markets and domestic markets have different expectations on how the company should behave, this has been problematic. Additionally, the fact that values have changed over time makes recontextualization difficult; what had not been a recontextualization problem previously now is. When values shift on the domestic market and are not reflected in Vattenfall's international operations, the legitimacy decreases. The study has found that in order to gain and maintain legitimacy it is important that state-owned enterprises retain a legitimate political positioning. This is because the state-owned enterprise's actions are perceived as representing the home country government's politics. If these are not aligned, the enterprise will suffer problems with legitimacy.



### ***6.3 How does a state-owned enterprise expand internationally?***

This section will answer the research question through the previously presented case. The parameters investigated are geographic market choice, degree of market adaptation and market entry mode.

#### *6.3.1 Geographic market choice*

When determining which market to enter, Vattenfall takes into consideration factors such as institutional conditions, growth potential of a market, the probability of establishing themselves as a powerful actor, and cultural distance. However, one of the most important prerequisites is geographic proximity, as this enables Vattenfall to create a strong geographical foothold in Northern Europe. Although the Uppsala model predicts that neighboring markets are chosen to reduce the risk in the initial phases of expansion, Vattenfall has not chosen these markets to reduce risk. In the energy sector it is crucial to realize economies-of-scale, and expanding through clusters enables the pooling of resources required to realize these. The reason why these clusters are neighboring is because when Vattenfall began to expand through acquisitions of production technologies it was vital that electricity could be transferred to the domestic market.

Contrary to popular belief (Mascarenhas, 1989), state-owned Vattenfall has not displayed a tendency to prefer stable institutions over unstable institutions and have thus not chosen markets on basis of stability rather on the basis of instability. Though, when it comes to the institutional instability exploited by Vattenfall, deregulation, the direction had already been pointed out; first, by political influence, and second, by the European Union. Therefore, given Vattenfall's competitive advantage, institutional instability offered a considerable opportunity. Markets with governmental turbulence, however, were divested. This is because political turbulence is hard to predict and, therefore, makes the development of appropriate connections increasingly difficult.

#### *6.3.2 Market entry mode*

Vattenfall have entered new European markets in a number of ways. It appears as Vattenfall expands in accordance to the Uppsala model's four-step process of involvement but they have not done so with the intention to reduce risk. The market entry mode is rather a result of restrictions. They desperately tried to penetrate the markets which appeared attractive. The goal, however, has always been to obtain full control and to be one of the top three players on a market. Full control incites the domestic market's government to engage in cross- governmental discussions with the host country's government.

#### *6.3.3 Degree of market adaptation*

Vattenfall adopts an ethnocentric approach when applying their organizational structure to the acquired companies. In the early expansion phase it could be argued that this was the case because as a state-owned enterprise the strategies and process had been tailored for the domestic market (Mazzolini, 1979). However, maintaining the organizational structure has been crucial for maintaining the Swedish government's influence on its subsidiaries. Vattenfall have nonetheless chosen to maintain the local management, in order to tap into local know-how. Vattenfall's approach to regulations has been polycentric, however they have been one step ahead of regulators. As a result of increased regional integration Vattenfall have adopted a more geocentric approach to regulations. The enterprise has diversified their risk by purchasing a market's production technologies, and thus adopted a polycentric approach. However, this has resulted in considerable legitimacy problems.

## 7. Discussion and Research Limitations

This chapter will provide a discussion of the findings. It will also discuss the limitations and provide suggestions for further research

### *7.1 Discussion*

This study shows that, for state-owned enterprises, it does not necessarily need to be managerial ambition that drives internationalization; it can also be the government's desire to create a large and powerful enterprise. This will be particularly evident when the ambition is to create an enterprise that is a national champion (Vernon, 1979). In that case, internationalization will be launched to accentuate the strength of the enterprise or even the country as a whole. It can also be assumed that if the owner encourages international expansion, the owner will appoint a board of directors that will pursue this strategy. Moreover, they will assign the CEO the mission to expand, ensuring that the management of the firm will have the same ambition as the owner. This implies that the government in effect controls the entire internationalization strategy of a state-owned enterprise. If the owner has the ambition to internationalize they will also be more willing to provide financial assistance if required. Even if the owner does not provide any actual financial backing it seems unlikely that if the state encourages international expansion it will allow for its company to go bankrupt if the investment decisions turn out to be unprofitable. Therefore, it will allow the state-owned enterprise to be less cautious in the initial steps of the expansion compared to if the owner opposes expansion. Moreover, the credit ratings increase considerably for state-owned enterprise, because of its rich owner, which will provide the finances needed to enter multiple markets in a capital-intense sector. That will mean that state-owned enterprise can expand more aggressively to new geographical markets. They can enter several markets simultaneously, spread their risk and increase the speed of incremental learning.

Because the government controls the strategy of its companies, long-term internationalization strategies for the enterprises become impractical. As the owners can be replaced or ideologies changed every four years, a government supporting internationalization can be replaced with one that does not. Moreover, government officials will set up strategies and goals for the enterprise which will advance their political agenda (Backhouse, 2002). As internationalization is often a long-term strategy it can cause considerable difficulties in predicting the political winds. For instance in the election 1998 the Green Party (Miljöpartiet) received 4.5% of the votes in the general elections. Today, it is a substantial possibility that they will get seats in the government. 12 years ago their position today could not have been predicted by many, and it illustrates the difficulty that state-owned companies face when they decide their long term strategies. Given that political sympathies change it becomes increasingly difficult to maintain legitimacy on the markets where state-owned enterprises operate. Initial expansion occurs under one political ideology, and future ideologies might condemn this. However, it does not necessarily mean that the host markets are critical about the behavior, because of different political influences.

State-owned enterprises are not risk-averse when it comes to geographical choice as they have a strong owner behind the decisions they make. Moreover, state-owned enterprises do not display a preference for stable institutions. If the state is weak it can therefore be presumed that the companies will be more risk-averse. Regardless of the strength of the state, state-owned enterprises will prefer countries with stable governments, so that international relationships can be nurtured, and influential political discussions held. Especially in industries where political ties are crucial for the establishment on a market, which is the case for the energy sector, state-owned enterprises are inclined to obtain full control over their acquired companies. This is so that the government can exercise its influence over the acquired company. Moreover, it enables the owner to make decisions singlehandedly, without consideration of other individual interests.

Conclusively it can be established that state-owned enterprises can operate on market conditions, despite goal incongruence, providing that the government wants it to operate on market conditions.

## ***7.2 Limitations of the research***

The reliability and validity has been discussed under the research method chapter of this study. In order to put the findings into perspective we would like to restate some of the main points and hence put the concluding results within the context of possible limitations.

To get a high *reliability* we have followed as standardized procedures as possible in order to mitigate external factors from influencing the results of the interviews. The interviews were conducted two-to-one, recorded, transcribed and then sent to the interview subject for approval thus giving the interviewee a possibility to correct any misinterpretations. Additionally, three sets of interview guides with coinciding questions were used and we strove to avoid leading questions that might have made the answers biased.

The *construct validity* was enhanced in this study by the fact that multiple sources have been used, ranging from non-reactive to reactive sources. Hence, the study has relied on both primary data, in the form of interviews, and secondary data. The construct validity could have been even further improved if the interview subjects had been selected randomly.

The *internal validity* is strengthened by having coinciding questions asked to several interview subjects. Additionally, in order to mitigate subjective inferences, quotes have been used to as large an extent as possible. Most of the interviewees chose not to be anonymous which might decrease the internal validity since it may contribute to manipulation of the answers. However, it is also important to note that it is a politically sensitive area. Two of the interview subjects responded that they wanted to be anonymous when they were contacted once again with the transcribed interview material. Hence, the internal validity loses strength due to the fact that the interviewees did not feel comfortable with discussing the problem area no matter whether they were anonymous or not.

The *external validity* of this study is rather low due to the fact that it has used a single case study which lessens the possibilities to draw general conclusions. This could have been strengthened if the study had been extended into investigating two or more companies. Furthermore, this study has been conducted within the energy industry and it is possible that other results would occur in another industry. Hence, some of the findings might not be applicable in a different setting.

In conclusion we would argue that the findings have high reliability and construct validity. The study has a lower external validity and the internal validity is reduced mostly due to the external problem of political sensitivity. Nevertheless, we hope that the readers of this study will perceive the findings useful and insightful as a starting point for studying the area of the internationalization of state-owned enterprises.

### ***7.3 Suggestion for further research***

There are many interesting areas which this study leaves open to further investigate. One possibility could be to include several companies in order to increase the ability of making general conclusions. In addition, some of the companies could come from the energy industry, as in the case of Vattenfall, and others might come from a different industry. Taking several companies representing two different industries will make the findings trans-boundary and hence more generalizable. Another option would be to make a study including both private- and state-owned companies in order to enable the findings to be contrasted and compared. In such a study it will be clearer where the exact differences are when it comes to the international expansion of state-owned enterprises. Finally, this study is focused on a state-owned enterprise operating on a competitive market; it would also be interesting to change the market setup to include non-competitive markets and partly competitive markets and see how the findings will change. By studying different market setups the credibility of the findings will be enhanced.

Consequently, there are opportunities within this problem area that can be further investigated and by following the above alternatives there will be enhanced possibilities to transfer the conclusions to different industries and find more general patterns on how state-owned enterprises expand internationally.

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## **Interviews:**

**Jan Greisz**, Head of Group Strategic Development at Vattenfall, 2010-04-26

**Magnus Fernström**, Special Adviser and Analyst at the Ministry of Enterprise, Energy and Communications, 2010-04-27

**Bosse Andersson**, Head of Public Affairs Nordic at Vattenfall, 2010-04-30

**Alpha (fictive name)**, Current Employee at Vattenfall, 2010-05-03

**Beta (fictive name)**, Former Employee at Vattenfall, 2010-05-11

**Ola Petterson**, Former Political Advisor for Thomas Östros, 2010-05-10



## 9. Appendix-interview guides

### ***9.1 Interview guide one: former political advisor***

1. Why is Vattenfall state-owned?
2. Aside from purely economic objectives, what other aims and objectives, does the state have for Vattenfall?
3. In what way is the credibility of Swedish environmental and energy politics affected if the international expansion of Vattenfall is inconsistent with the values and environmental responsibility that guides Sweden?
4. What is the purpose of Vattenfall's international expansion, from an owner perspective?

### ***9.2 Interview guide two: special advisor***

Includes:

- Questions 1-4 from *interview guide one*
1. How is the strategic decision-making process for international expansion in Vattenfall designed?
  2. What role do the owners have in the strategic decision-making process?
  3. What should Vattenfall take into consideration before acquiring foreign firms?
  4. What risk appetite do the owners have?

### ***9.3 Interview guide three: current and former employees at Vattenfall***

Includes:

- Questions 1-4 from *interview guide one*
  - Questions 1-4 from *interview guide two*
1. Why has Vattenfall decided to pursue international markets?
  2. What strengths and weaknesses have Vattenfall had when expanding?
  3. What challenges have Vattenfall faced when internationalizing and how have these changed over time?
  4. How does Vattenfall select geographic markets?
  5. How does Vattenfall establish themselves in a new geographic market?
  6. Which entry mode has Vattenfall selected and why?