

Louvain School of Management

What are the common characteristics for a typical good internationalization process, from a capital structure and strategic point of view?

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Abstract

This thesis examines the impact of capital structure on firm's internationalization process. The main objective of the case study is to determine the optimal internationalization process for a growing company from a financial perspective, without forgetting the entry's strategy. The case study uses four financial indicators including, the ownership of the company, the net debt to equity ratio, annual EBITDA and stock price at the end of each year. These indicators will help us to understand their impact on the company efficiency and his globalization process.

Four companies have been selected for this case study and one interview has been made to understand strategic and financial decisions made during the internationalization process of the company.

The results show that there is a link between the capital structure and the internationalization process's success. There is also a link between capital structure and ownership. Finally, the results show that knowledge of the targeted new market is the key to succeed in the internationalization process.

The case study recommends the company to find the best net debt to equity ratio with the minimum cost to maximize the financial performance. Indeed, an internationalization process is costly, even if the debt is cheaper, the company has to find a good balance between net debt and equity to finance the process. The firm has to take into consideration that too much debt will lead to an increase in direct cost with an increase in interest rate but also indirect cost such as financial distress cost. Moreover, the company has to take into consideration that an exceed of equity will lead to a loss of ownership and increase the cost of capital. Finally, the company has to raise enough money because, with a lack of fund, the whole internationalization process might be compromised.

With a strategy point of view, the case study recommends the company to have as much knowledge as possible of the targeted market and been as close as possible to the new targeted client by acquisition or being on the field.

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1. Introduction

For the last few years, internationalization has been one of the most debated subjects in economy. Companies have evolved to the multinational market boom. Saarenketo (2002) suggests that a growing number of small companies are participating and are linked to foreign markets, which means that even the smallest enterprises must face the pressures of internationalization.

I have been really interested in international business and especially small businesses' internationalization. It began by exploring the framework of books and publications on company's internationalization. There are several studies about the subject, and it was difficult to find a place I could fill for my work. I do require my thesis that I will have cases that support theoretical analysis. I needed to see how each other's theory and interpretation interact.

I considered a truly fascinating point of view to research internationalization mechanisms when I was interested in the internationalization of concepts. Throughout my research, I wanted to address the ideas of internationalization of several well-known scientists. Several paths and methods exist, and the field is researched extensively.

Oviatt & McDougall (1994) emphasize that when learning about foreign companies, not just major multinational firms hold important role. An individual with capital can work by telecommunications, internet and digital technologies anywhere in the world. You will move around the globe in one day by using today's digital technologies. This encourages small businesses with limited capital to reach beyond their domestic countries for market prospects. Axinn & Matthyssens (2002) suggest the clarification of internationalization is now difficult. Today's internationalized businesses are more diverse, and their pace is comparatively quicker than before. In several cases, businesses become multinational and use diverse approaches. Trade liberalization has led to businesses spreading to adjacent countries and thus turning them into global economies. For most sectors internationalization is not a new phenomenon today but is a regular feature of corporate routines.

The internet has brought in a new movement on the markets. Consumer knowledge is more readily accessed through the Internet and the presence of collaborators and interactions are also encouraged. There is also support for small and medium-sized businesses with no established network. Indeed, if an organization has no current network on new markets, it can create a network and manage these communications with the Internet.

Moreover, the theory of capital structure and its relationship with a firm's performance has always interested me. Indeed, capital structure is a key parameter in a company's success, it is a necessary condition but not sufficient for a successful performance. In addition, since the Modigliani and Miller theory (1958) argue that under the perfect condition of a capital market which assumes that the value of this firm is independent of the capital structure and therefore the expected cash flow was the only variable which defined the firm valuation., it had been a puzzling problem in corporate finance and accounting literature. Many models have been developed since then to describe a company's financial structure.

1.1 Research question and objective

The objective of this case study is to point out capital structure's effects on a growing company that want to enter a new market. Indeed, after taking into account the existing theory, the analysis of cases and the interview with Pierre Boël, the goal is to find recommendations for an efficient internationalization process from a capital structure and strategic point of view.

That is why my research question is:

“What are the common characteristics for a typical good internationalization process, from a capital structure and strategy point of view?”

But what is a “good” internationalization process? Indeed, “good” in a very approximative indicator without tangible conditions to decide if the internationalization is a success or not. As said before, the goal of this case study is to provide general recommendations. But each internationalization process is unique because each company and market are different. Moreover, each company has different goals during an internationalization. For example, some companies just want to enter a new market to continue their growth. The goal of these companies' internationalization is to be profitable to continue their growth. But for some companies such as Carrefour, their main goal is to be the market leader in every market.

From an investors point of view, their goal is to make money. To achieve that, the company's value has to increase, and the company should become profitable so they receive more dividend and they will make an added value when they will sell their shares.

From a chief or the company point of view, they may have different goals (such as being a market leader) but the choice of capital structure is important to reduce costs of capital and therefore increasing profit. Moreover, in the long term, the goal of a company is to be profitable.

Therefore, in this master thesis, a “good” internationalization process is to be profitable on the long term because at the beginning, it is difficult to be directly profitable with all the costs at the beginning of the process, but on the long term, to make the company in the new market sustainable, it must be profitable. Profitable means that the difference between earnings and cost is positive. That is why one of my financial indicators is the earnings before interest, tax, depreciation and amortization (EBITDA). It is an indicator reflecting company performances and it is difficult to be manipulated.

1.2 Research limits

It was not easy to measure and compare the impact that the capital structure has on the company's internationalization process. I think I discovered several interesting aspects thanks to my interview. However, I do not think that general conclusions from my thesis can not be applied to all firm in all sectors.

First of all, I know that creating reliable and effective surveys involves several skills that I had not learned before my master thesis. Therefore, although I have designed my questionnaires to be as accurate as possible based on my theoretical knowledge on surveys and information I needed to compare with other companies, someone with greater qualitative surveys expertise might be able to get more useful information than I did with a more precise survey.

Second, all companies are different in many aspects. It will influence the impact of the capital structure on the internationalization process. Indeed, all companies have different cost of capital therefore, each optimal capital structure is different. Moreover, strategy can be different for some companies like Tesla. Indeed, Tesla is a unique firm with his founder Elon Musk who can influence the whole company just with some tweet.

Third, another limitation is the sample size of the analyzed companies. Due to the limited number of companies analyzed, we have probably missed some aspects of the internationalizations process.

Fourth, strategy and capital structure are not the only two variables which impact the internationalization process. Indeed, there are multiple factors which have an impact on companies' performance. Therefore, this case study gives recommendation but there are definitely not sufficient conditions to have a successful internationalization process.

Finally, even if I have chosen to do a general analysis and conclusion, it is impossible to cover all firm and sectors. That is why, they are just recommendations. And alternatives can be found without affecting performance and internationalization process.

2. Related literature

2.1 Capital Structure

Let's start this related literature with the capital structure of a company. Indeed, all firms have a capital structure and we will see what it is and how it is affecting the company. If any field of finance theory has gained the most attention and created the largest debate, it is undoubtedly the theory of capital structure and leverage and its effects on the efficiency of any business. The topic of capital structure and its effects on company performance can be traced back to the paper of Modigliani & Miller (1958), which argued that under some hypotheses it can be demonstrated that the combination of debt and equity does not affect firm value whilst the only variable affecting firm value is its future expected cash flow.

Since Modigliani & Miller began to publish their research about capital structure in 1958, it has been a significant subject in literature. Capital structure is an extraordinary subject, it has been studied at both academic and corporate level since a company's financing decisions are absolutely crucial for its operational and investment activities. It is basically referred to how a company mixes debt and equity in order to finance itself. Even though there are many hypotheses that analyze it in different ways, there is still a very heated discussion about the nature of an ideal capital structure and how it influences firm efficiency, and vice versa.

Modigliani & Miller (1958) created a hypothetical tax-free universe without transaction costs, bankruptcy costs, growth opportunities, asymmetric knowledge between internal and external stakeholders and risk disparities between various companies and people. It is under these ideal terms that it has been shown that financing is meaningless to shareholder capital, therefore there is no optimal debt-to-equity ratio. Nonetheless, subsequent literature has also challenged the set of simplifying assumptions. There are three basic assumptions that can be made from these: (1) the tax benefits of gearing, (2) the cost of bankruptcy and (3) asymmetric information. And the four main theories of capital structure are based on these hypotheses: (1) trade-offs, (2) pecking order, (3) market timing, and (4) free cash-flows. As stated by Lew (2012), the trade-off theory is built on the tax benefits of gearing and bankruptcy costs and asymmetric information leads to the pecking order, free cash-flow and market timing theories. However, real-world taxes do exist and have a great influence on the capital structure of a company and the value of the firm. In general, there are also incentives for debt instead of equity because the cost of capital is higher. The tax deduction permitted for interest payments would reduce the

after-tax debt expense significantly, which will decrease the net cost and raise the valuation of the business.

This was an introduction to the capital structure to show that under certain hypotheses, it does not affect companies' performances but in reality, it does. Now, the conception of capital structure, capital structure components, and cost of each component will be clarified in this chapter.

2.1.1 Capital Structure Definition

Several attempts have been made to describe capital structure, most definitions describe the sort of securities and proportionate quantities that compose capitalization. It is the combination of multiple long-term assets such as equity shares, preference shares, debentures, long-term loans, and retained profits. One of those definitions is by Gangeni (2006), about the analysis of capital structure, which tries to explain the combination of securities and sources of finance used by corporations to finance real investments. In order to at least stay in the market, a company needs to make investments, to demonstrate some progress and differentiation. Companies may use internal sources of financing such as retained profits and selling public securities to fund such acquisitions or use external resources such as loans or bonds.

According to Parmasivan & Subramanian (2009), the term capital structure relates to the relationship between the various long-term sources of finance such as equity capital, preferential share capital and debt capital. Financial structure is the company's ongoing funding, mainly by long-term leverage and equity, so agreeing on the correct capital structure is the financial management's essential decision as it is directly linked to the firm's valuation. Gitman and Zutter (2012) described the corporation's capital structure as a combination of long-term debt and equity.

While the actual total combination of the firm's perpetual long-term funding, defined by debt, preferred stock, and common stock equity, may change significantly over time, most companies are seeking to maintain their finance balance close to a target configuration. The key aim of the capital structure, according to Ehrhardt & Brigham (2011), is to contain the optimum balance of debt and equity. A firm's decision on capital structure involves selecting an optimal capital structure, the total maturity of its debt and the different forms of funding it chooses to raise at

any given time. As with business decisions, executives will take decisions about the capital structure intended to increase the performance of the company.

The capital structure can be defined based on the last definitions as the combination of financial sources to fund the activities of the firms. Financial channels may involve the debt and equity which the companies will use.

Now that we have tried to define the capital structure and we know that in reality, it affects companies' performances, we will try to find the optimal capital structure.

2.1.2 Optimal Capital Structure

The cost of the capital structure must be considered at the lowest point to increase the inherent value of the company. This implies that the optimal capital structure is reached upon hitting this level. Parmasivan & Subramanian (2009) describe optimum capital structure as the capital structure or mix of debt and equity leading to the firm's ultimate valuation. Optimum capital structure is the financial structure that minimizes the Weighted Average Cost of Capital (WACC) and thereby maximizes the value of the company.

Choosing the appropriate capital structure is a key economic management choice, since it is directly linked to the firm's valuation. Capital structure is the firm's ongoing funding, mainly by long term debt and equity. Asaf (2004) states that "Optimal capital structure means having the right balance of debt and equity financing in the business" For most corporations, new debt choices affect combining a series of tradeoffs involving costs, liquidity, maturity choices, and the basis and regularity of interest rate resets.

Since a company's valuation is equivalent to the current value of the potential cash flows as in the formula, it assumes that the company's valuation is maximized as capital expenditures are minimised. In other terms, once the discount rate (the cost of capital) is at its lowest, the current value of potential cash flows is at its highest. By using this equation Gitman and Zutter (2012, p.535) identified the firm's value, V , as follows on the next page:

$$V = \frac{EBIDA \times (1 - T)}{WACC}$$

Where:

EBIT = Earnings before Interest and Taxes

T = tax rate

WACC = Weighted Average Cost of Capital

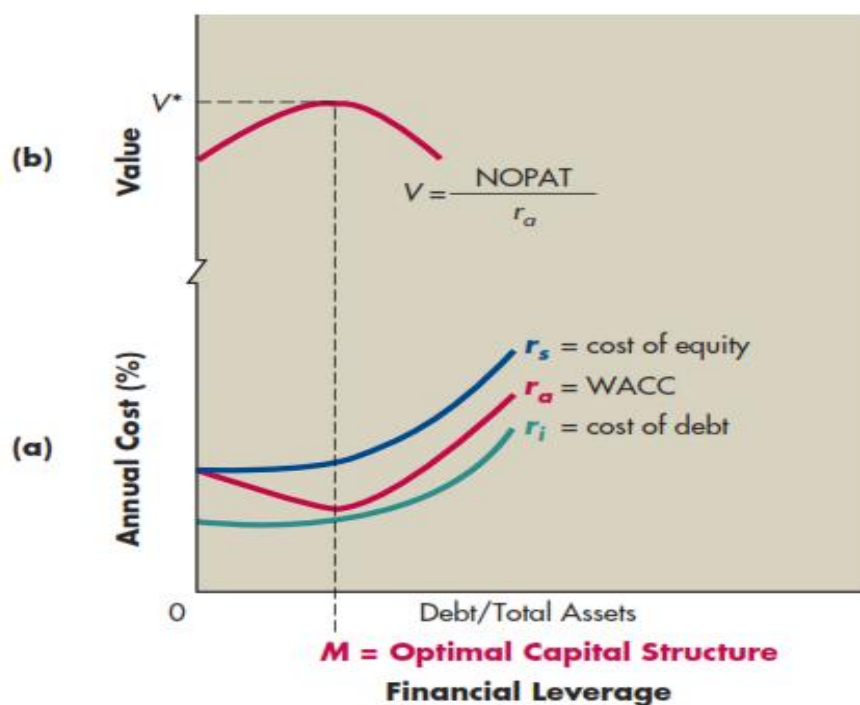
Obviously, if the numerator is supposed to be stable, the firm's value, V , is optimized by decreasing the WACC. There are three cost functions from figure 1 on the next page: debt cost, equity cost, and the WACC as a function of the financial leverage determined by the debt ratio (debt to total assets). The debt rate, r_i , stays small due to the tax shield, but it increases gradually as the leverage rises, to compensate borrowers for increasing risk. The cost of equity, r_s , is higher than the cost of the debt as the stockholders expect a greater yield to cover for the increased financial risk. The r_a emerges from a weighted average of the company's debt and equity capital costs. When debt is supplemented by equity and the leverage ratio rises, the WACC decreases as the cost of the after-tax leverage is smaller than the cost of equity ($r_i < r_s$). Within this context, the increased debt tax gains outweigh the interest costs further. Nevertheless, if the debt level begins to increase, the debt and equity costs inevitably lead the WACC to increase (after point M in Figure a).

2.1.3 Graphical View of Optimal Structure

Since benefit maximization, V , is accomplished when the total cost of capital, r_a , is at the lowest point (see Equation), the ideal capital structure is when the r_a is optimized. In Figure 1, point M defines the minimum WACC as the maximum financial leverage point and hence the maximum capital structure for the company.

The graph (b) plots the value of the company resulting from the replacement of cost graph (a) to the zero-growth valuation model in Equation for different levels of financial leverage. As seen in graph (b), the valuation of the company is maximized at V^* which represent the optimal capital structure, point M. Generally, decreasing the WACC enables management to pursue a larger range of successful projects, thus increasing the firm's value.

FIGURE 1: Cost function and value capital cost and the optimal capital structure



Source: Gitman and Zutter (2012, p.536)

Nonetheless, as a general rule, there is no way to quantify the optimum capital structures suggested by Figure 1. Since it is either difficult to determine or to stay at the exact optimal capital structure, according to Gitman & Zutter (2012), companies usually seek to work within a framework that puts them close to what they consider as the optimal capital structure. Companies typically tend to reach the maximum value with a target capital structure from the last calculation by having a mix of equity and debt at the lowest cost.

Now that we have seen that companies have to mix debt and equity to find the lowest WACC, we will analyze the two components.

2.1.4 Components of Capital Structure

2.1.4.1 Equity Financing

Within financial system elements equity capital represents the company's investment capital. It is the ultimate money, which can not be removed during the firm's existence. Owners are the true bearers of threats, but they gain incentives as well. Their liability is limited to contributing capital.

It is common to have stock securities in the investment community. Through equity funding by common stock, by selling or buying common stock to/from one or more individuals or institutions in exchange for a defined sum of capital, you can minimize or maximize your ownership percentage in your business. The common equity reflects the sum spent in a company by all common shareholders. More notably, it requires the common shares' worth itself. It also combines remaining profits, though, and extra paid-in cash.

According to Nawaz, et al. (2011), capital is composed of two types : (1) Contributed capital, which is the money initially spent in the firm in return for equity or ownership rights, and (2) Retain earnings, which reflect income from previous years that the organization has retained and used to improve the balance sheet, finance growth, acquisitions or company growth.

If a company doesn't want to use debt financing, it is referred as an unlevered company. It brings in what is called market risk, which is described as the danger that the common stockholders of a firm would face if the company did not have any debt (Ehrhardt & Brigham, 2011). In other words, it is the potential risk in the operations of the company which emerges from uncertainties about potential operating profits and needs of capital. If a corporation will not use debt, then the return on capital spent would be determined by return on equity. That clearly means that a leverage-free firm's market risk would be calculated by its standard return on equity (ROE) deviation.

2.1.4.2 Debt Financing

Within a company's financial structure, the debt capital corresponds to borrowed money by working in the company. The cheapest form is usually called long term debt since, according to Nawaz, et al. (2011), the company has years to come up with the balance, if not decades, while charging interest only in the interim. In financial structure elements, debenture debt is a portion of lending money; the debenture holders are the company's shareholders. For the convenience of creditors, different forms of debentures are provided. Organizations are also eligible to receive long- to medium-term loans from banks and other financial institutions. Public deposits may be used as bond financing; public deposit means all funds that a non-bank firm collects from the public by way of investment or borrowing, including staff, clients and business owners rather than in the form of shares and debentures.

If a company wants to use financial leverage for its activities, it involves financial risk, and is pointed to as a leveraged firm. Ehrhardt & Brigham (2011) defined financial risk as the added risk that the decision to finance with debt placed on the common stockholders. Financial risk is the likelihood the company's earnings will not be as estimated due to the financing method. Therefore, the financial burden emerges because debt typically has a fixed - rate commitment in the form of interest that must be paid as the liability comes due before the shareholders can share in the remaining income. The amount of debt (financial leverage) appropriate to one company or industry, in another one, it may be extremely risky, since different sectors and business have different operational characteristics (Gitman & Zutter, 2012).

2.1.4.3 Pecking order theory

According to Chen, L. J., & Chen, S. Y. (2011), in his empirical study of 305 electronic listed firms, profitability and growth opportunity are important variables which influence the capital structure of the company. Profitability impacts capital structure negatively therefore businesses prioritize internal funding. Companies are using internal money to fund innovative ideas. In the case of lack internal capital, companies purchase debt, as a last resort, the equity is issued.

Now that we have describe the two component of the capital structure and we know that we have to minimize their cost, first we have to know what their cost are.

2.1.5 Cost of Capital

Capital is composed, as explained above, of two factors: one is debt and the other is equity. If a company funds its business with loans, it borrows money from an investor with a commitment to return the money including its interest within a given amount of time. The lender receives interest payments upon the loan in return. With equity investment the shareholders buy stock in the company, they become investors and receive a percentage of the company net profit in return. Price of capital in general, reflects the varying expenses added to an organization's multiple sources of funding.

2.1.5.1 Cost of Debt

The business may raise debt for a given amount of time at a certain interest rate in a number of forms that include borrowing funds from financial institutions or from public debt in the form of bonds (debentures). (Wakida, 2011)

The firm will use different bonds, loans and other types of leverage, and this calculation is helpful to provide an indication of the average cost the company is paying by using debt financing. The metric will also provide creditors a sense of the company's riskiness relative to others, as riskier companies typically have higher debt costs.

Another cost is the agency costs of debt. It is generally defined as a substitute for properties. The future differences between shareholder claimants and debt claimants encourage investors to utilize the assets of debt holders by engaging in new projects which are riskier than the ones already pursued by the firm. In this situation, much of the revenue is gained by shareholders, that is, because they carry for high risk ventures, and most of the risks are carried by debt holders. (Jensen and Meckling, 1976 and Fama and Miller, 1972).

To shield itself from risk changes, bondholders typically include securing arrangements and control devices. Pacts dealing with new financing, distributions, or rentals and mergers, for example, are fairly straightforward mutual agreements. However, it is far more difficult to track and enforce arrangements that restrict managers' abilities for participating in negative NPV projects. If such debt costs increase, the interest-holding rate will rise. Conflicts of interest among shareholders and bondholders thus contribute to higher debt costs.

Regardless of the fact that lenders face the least risk of long-term capital contributors, the cost of the loan is also smaller than the cost of other sources of financing. In addition, the tax deduction of interest payments significantly reduces the company's debt costs.

2.1.5.2 Cost of Equity

If investment money is allocated to the company, investors are entitled to potential returns as members of the business that can not be decided at the outset, Wakida (2011). Businesses have an internally retained profit alternative to collect money. The return on dividends paid by shareholders is the opportunity cost of the remaining earnings and the cost of foreign equities is a minimum rate of return provided by the shareholders of the funds supported by new stock investments in order to avoid the present market price decline of the equity share. (Wakida, 2011)

In contrast to the debt capital, which the company will eventually pay back, the company continues to invest in equity capital indefinitely — it has no termination date. The two main equity resources are (1) preferred shares and (2) common shares, which contain both common

stocks and retained earnings. Usually, the common stock is the costliest equity type, followed by retained earnings, and then preferred stock. Moreover, a company that significantly increases leverage utilization can see its debt costs increase when lenders start to care about the ability of the company to repay its debt. Gitman & Zutter (2012) pointed out that if the company borrows more or too little it is often true that the demands of common stockholders are more volatile than the claims of the borrowers.

Now that we have describe and analyze components of the capital structure, we will understand how it is really affecting companies' performances.

2.1.6 Firm Performance and Capital Structure

2.1.6.1 Corporate Performance

The capital structure is one of the key factors affecting the company's performance. Because insolvency problems happen, more use of debt in order to benefit from tax deductions leads to declining results. Therefore, there is an adequate capital structure that meets the total tax-related gains of the incremental substitution of debt with equities, so this rises in bankruptcy cost. There are two kind of bankruptcy cost: the direct and indirect one. Direct costs include the expense to lawyers and accountants, the amount of the administrative time spent on bankruptcy proceedings and other professional charges. Indirect costs include missed sales, missed revenues and, with exception to particularly expensive terms, the company's failure to secure credit or to issues securities (Warner, 1977). The companies are able, by the management of the correct capital structure or the optimum capital structure, to optimize their efficiency and reduce their financing expense.

Nonetheless, as mentioned in an earlier paper, it may cause companies to have more capital structure leverage than they would if they underestimate the cost of bankruptcy or reorganization or the shared interest of both management and shareholders. The high debt rates in the capital structure will therefore decrease the company's efficiency according to Zeitun (2006). However, it is not only the company leverage, but also its debt maturity structure, that is affecting performance and failure of the company. In other words, choosing a debt arrangement will influence the performance of all companies and the probability of failure. In addition to the capital structure, there are additional variables, according to Zeitun (2006), that

affect corporate performance, such as corporate size, age, expansion, risk, tax rate, economic activity variables and macro-economic factors.

Since the key goal of an organization is to make money, during the past thirty-five years of corporate finance study, profitability was analyzed as the most significant framework. In Chathoth's view (2002), researchs attempting to establish connections among the environment, plan, structure and corporate performance, the critical problem that needs to be addressed concerns the definition of the variables reflecting the corporate performance system.

In short, the performance of a company could be influenced by the choice of the capital structure and debt maturity structure. In fact, the tax rate will also affect the value of a company as seen in the numerator of the equation. The analysis of the impact of capital structure on the performance of a company therefore the following section will describe performance.

2.1.6.2 Performance Measures

The concept of performance is wide because of its multi-dimensional significance and lead to a controversial issue in finance. Organizational success study is focused on corporate theory and strategic strategy. According to Tudose (2012), the selection of alternatives to approached performance (whether operational or financial) depends on the goals outlined; therefore, the evaluation of firm performance using financial indicators must be accompanied by an analysis based on non-financial indicators; at present, there is a trend to evaluate performance based on value creation, still listed on the sustainable growth target.

Financial results such as profit-maximization, maximization of profits on investments and maximization of value to shareholders are the core of the company's productivity, Abdulmalik et al. (2014). Operating performance measures, like sales growth and increase market share, provide an overarching definition of performance, focusing on factors which eventually lead to economic performance.

Quality assessment depends on the measuring device knowledge and the instruments used. According to Tudose (2012), return on investment (ROI), debt, capital expenditure, liquidity, cash flow, inventory turnover and the turnover ratio for receivables were classical metrics used in financial analysis to assess performance. The company's goal can influence the choice of alternatives to evaluate its success. An evaluation focused on non-financial metrics that reflect management efficiency, organizational culture, efficacy of the management rewards policies, consistency of the shareholder relations program, etc. will supplement the assessment of

company performance by financial indicators. There is already a movement to measure value-based success that is explained by Tudose's (2012) sustainable development objective.

Depending on what the organization chooses, the efficiency of a business can be calculated in different ways. For example, as described by Malm & Roslund (2013), the output of individual company divisions or of the entire business can be calculated.

I will concentrate in this study on aggregate output measures for the entire organization. This report will however research the company's positive financial results.

2.2 Internationalization

2.2.1 Internationalization, definition

The objective of the research is to study the financing of the internationalization of a firm. We have already discussed about the capital structure, then, let's give a definition of internationalization. A review of the literature shows that currently there is no agreed definition of internationalization. The origin of the process stems in the 1960s, when Simmonds and Smith identified internationalization as a successful route to increase exports (McAuley, 2001). This work became formalized into models of export behavior, mainly by a number of Swedish researchers including Johanson, Olson and Wiedersheim-Paul (1978) who stated that "internationalization usually refers to either an attitude of the firm towards foreign activities or to the actual carrying out activities abroad". For them it was the interaction of these attitudes and actual behavior which describe the internationalization process (McAuley, 2001).

Even if there is no agreed definition, we can view internationalization as "the process of increasing involvement in international operations" (Welch & Luostarinen, 1988). Another definition given by Calof and Beamish (1995) says internationalization is "the process of adapting firms' operations (strategy, structure, resources) to international environments". Based on dictionary definitions it can be generalized that the internationalization is the process of planning, designing and implementing products and services so that they can easily be adapted to specific local demand, languages and cultures.

2.2.2 Internationalization approaches

Some researches (Jones, 1999; Collinson and Houlden, 2005) noticed that there were changes in the internationalization process of the small and medium enterprises (SMEs).

Glückler (2006, p.369) states that "firm internationalization has become a more complex phenomenon than the initially theorized in the mainstream approaches". He mentioned two reasons of it. First, firm's international expansion has not only grown in traditional manufacturing-based businesses, but also in services (especially in knowledge-intensive services). Second reason is that firm's internationalization is no longer relates to only large firms, but also to medium, small and micro firms.

SMEs often have limited amount of resources and low brand recognition that makes the process of entering in new markets more complicated for them. A failure in the new market can be fatal

for SMEs, because investments that firms have to make to enter in new markets are often high in comparison with the firm's available resources (Buckley et al., 2004). Most of the researches were based on the cases of multinational enterprises and several authors were not sure that it is possible to use these researches for SMEs (Jones, 1999; Collinson and Houlden, 2005; Glückler, 2006). That was the reason why were created new theoretical approaches, applicable for internationalization process of SMEs: Born Global, Network theory and Uppsala model. Let's discuss these approaches in details.

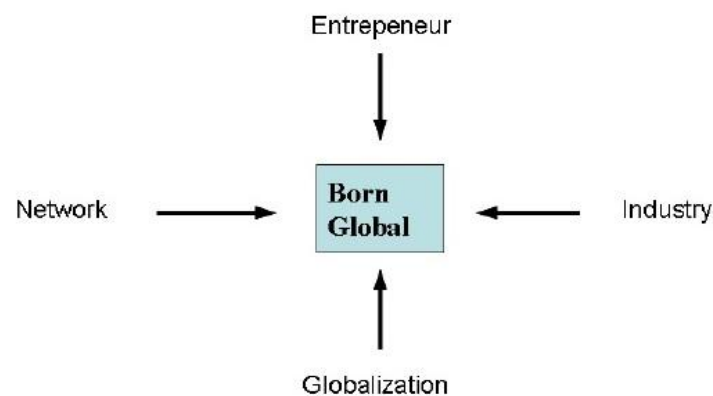
2.2.2.1 Born Global

Kalinic (2009) defines Born Global businesses as organizations with international management of their operations. In a few years, these businesses will achieve a certain degree of internationalization. Some researchers concluded that internationalizing from the time it was created can take just two years (Mckinsey, 1993), while other researchers report that up to three years are needed (Knight and Cavusgil, 2004). The last study community describes the internationalization cycle for businesses as eight years (McDougal and Oviatt 1994). Various researchers suggest over time that the business will have to internationalize, but all writers accept that Born Global companies reach new markets by being a leader market or regional niche target, and sometimes forget their domestic economy (Bell, 1995; Coviello and Munro, 1995).

Loane & Bell (2006) pointed out that Born Global companies view the world as a field for their company operations and seize opportunities on multiple markets regardless of their geographical and psychological distances.

A conceptual framework has been developed by Andersson and Wictor (2003) which identifies variables which influence Born Global 's development. Figure 2 illustrates this framework on the next page.

FIGURE 2: Born Global conceptual framework



Source: Andersson and Wictor 2003, p.254

As can be seen in this diagram, the researchers categorized into four main categories, entrepreneurs, industry, networks and globalization, factors that influence Born Global firms.

1. One of the main attributes of Born Global companies is the creative, ambitious and risk-taking personal characteristics of their **entrepreneur**/owner or company manager, such as global mentality (Mort and Weerawardena, 2006). Oviatt and McDougall (1997) found this member should have a great amount of past international experience as well. If the company's manager/owner already has authentic experience of other countries, so the Born Global business has a tremendous potential to compete very easily in new markets (Madsen and Servais 1997).
2. **Industry** characteristics play a significant part in determining the Born Global industries' international growth. Madsen and Servais (1997) have observed that these companies tend to be niche-oriented rather than other companies.
3. For Born Global companies, **network** features also play an important role. Since the company was founded, every organization needs to build and contribute its connections to suppliers, investors and clients (Andersson and Wictor, 2003).
4. According to Andersson and Wictor, **globalization** is the last factor influencing Born Global companies. It produces technological advancements in communication, shipping and the reduction in trade barriers.

Chetty and Campbell-Hunt (2003) assume that Born Global companies tend to be founded with open economies and modern technology in small countries. They may also have restricted national demand for products and may encourage companies to export from the point they are founded (Knight and Cavusgil, 2004). The example of these countries can be referred to as Finland, Sweden, Denmark, Israel, Australia and New Zealand (Gabrielsson and Kirpalani (2004)).

2.2.2.2 Network theory

During the internationalization process, the theory of the network emphasized the role of company commercial relations. The networks enable companies to succeed by helping them to find new opportunities on the market and gain market knowledge (Coviello and Munro, 1995).

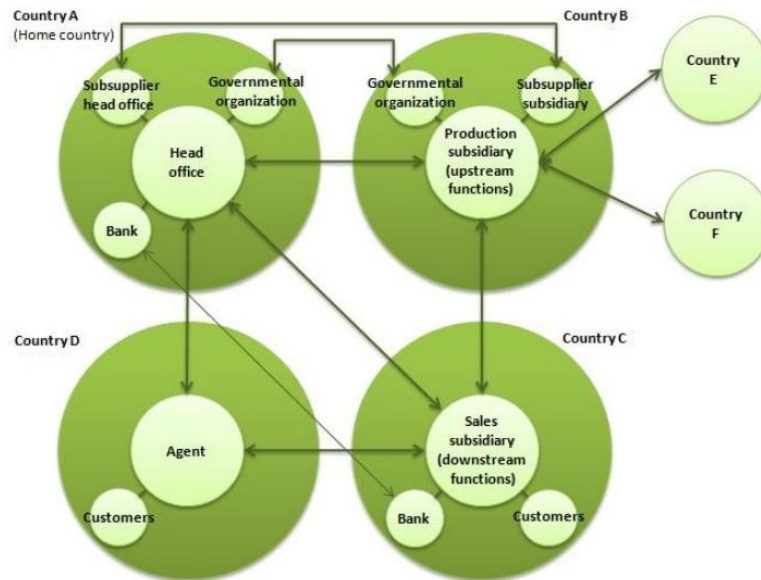
Rundh (2007) describes networks as a series of multiple connected partnerships in interaction. Durrieu and Soldberg (2006) have reported that the networks include independent agents, retailers, local dealers, and customers. Ford (2002) mentioned the most important examples of company networks are suppliers and distribution networks.

Initially, the company has internal market relations and other networks are built on international markets during the internationalization process (Johanson, and Vahlne, 2009). The business will make new network links in a foreign place using domestic networks. Hollensen (2014, p.86) pointed that “a basic assumption in the network model is that the individual firm is dependent on resources controlled by other firms”. Powell et al. (1996) confirm that networks create a path towards creativity because they provide access to information and expertise which can not be accessed without network connections. Coviello and Munro (1995) argue that network links can have various motives, for instance reducing production costs or contributing to the development of new knowledge and skills.

Network relations in the company's international entry into the market is extremely important, since its network partners influence the company's decisions regarding entry and choice of market (Coviello and Munro 1995). Another result of action made by the company 's partner could be the entrance of a foreign market. Mtigwe (2006) suggests that the internationalization of the organization is recent and separate but is a consequence of networking. The company's position in the network is considered to be strategic value by Glückler (2006) and gradually an immaterial resource.

Figure 3 shows linkages between the various network agents in the country and the new country.

FIGURE 3: An example of an international network



Source: Hollensen 2014, p. 87

Figure 3, Country A is the company homeland. In its country of origin, the organization has a subsupplier. In Country B, the subsupplier has established a subsidiary in Country B, as the partnership between the subsidiary and the client is easily used rather than new connections in other countries. Hollensen (2014, p.87) uses this example to show that "a company can utilize its relationships in a domestic network as bridges to other networks in other countries." Mtigwe (2006) assumes that the networking mechanism is accelerating the process of internationalization, because each network within the company has high benefit and very quickly offers the required information about the new market than without a networking connection.

Johanson and Mattson (1988) see internationalization as a phase in which the company builds, constantly creates and embraces new partnerships with foreign partners in order to attain its own international growth.

2.2.2.3 Uppsala Model

The Uppsala model is another path and it is one of the world's most popular examples of internationalization. Johanson & Vahlne created U-model in 1977 and empirical data were obtained by Swedish medium-sized manufacturers. In some sectors, the U-model is still applicable and is partly connected with the internationalization model partner-based by Vahvaselkä 2009.

It is in the cultural or geographical close markets that international activity normally starts (Johanson and Valne, 1977). The businesses seek to start with an entry mode that does not limit their activity. This gives you the chance to return to business only if foreign business is not profitable on the domestic markets. This is why foreign agents are normally exported or used early on. (Johanson and Valne 1977)

In a short time, a business can take the next step and expand its internationalization speed once it gathers knowledge, experience and networking by exporting. An organization that implements the U-model encourages shipping in the international world by an individual sales manager, who is sometimes considered as an agent. The next move is to set up your own selling office or a subsidiary in the target nation. The final step is to set up a plant or manufacturing center in one of the countries concerned. The objective of the U-Model is connections and interactions to be improved at any level. (Johanson&Valhne 1977)

Äijö (2001) wrote about slow international expansion. The company begins to put money and resources in internationalization at the development stage. Collaboration with international partners and likely a regional office within the target market are specific templates for maximizing global transactions. When the investment amount increases and the company concentrates greater power to grow abroad, the volume of trade is rapidly increasing, but the ultimate results of foreign market operations are many times problematic. A high growth rate is typical of the development stage. Business made outside of our own country could be profitable at this stage, even if liquidity is usually relatively low. The firm continuously invests in and enter locations that are attractive for industry. The company has some experience at this stage and knowledge of certain markets.

Äijö (2001) pointed out that the best way to begin internationalizations is, first, to reach into neighboring countries that are geographically and mentally near and need little investment and where, as in the Uppsala model, there are reduced cultural barriers between countries.

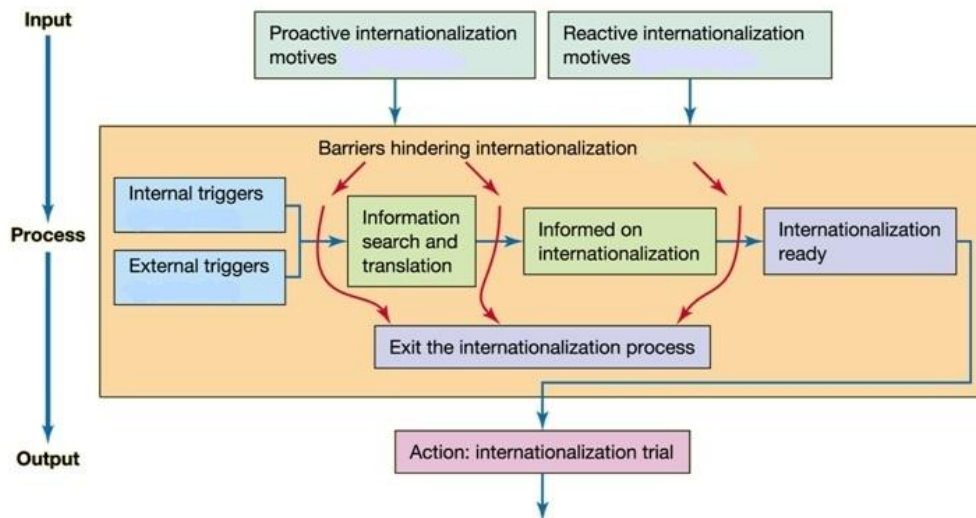
Axinn & Matthyssens (2002) challenge Uppsala-model as a separate component of the company's business portfolio. Furthermore, the Uppsala model has been too strongly developed from the commodity point of view of industry, along with other conventional internationalization theories. Services today form a notable part of international commerce, therefore services and international internet markets which have been subject to change should be given better account for theory supporting it. Worth a note is also that it is not possible to speak to transfer experience and data from a country to another anymore. It is also important to note that experience and data can no longer be transferred from one country to another. Uppsala's internationalization-based model, which evolves and extends step by step, is out of date by Axinn & Matthyssens (2002). The authors can see that the data is already online, and if it is modified from one country to another, the internationalization process will slow down rather than accelerate.

2.2.3 Internationalization motives

Internationalization takes place when a company expands its research and development (R&D), manufacture, sales and other activities to new foreign market. In SMEs, however, internationalization is sometimes a relatively fragmented process where each internationalization project is seen by management as separate and individual (Hollensen, 2014).

In its 2002 report, Freeman point out that SME managers utilize information to gain practical qualifications in pre-internationalization steps to begin an internationalization process. We can see various phases of pre-internationalization in Figure 4. Moreover, in this figure I will discuss every stage more in depth.

FIGURE 4: Pre-internationalization: initiation of SME internationalization



Source: Hollensen 2014, p.53

For most companies, earning money is the principal factor to start internationalization. Just one factor, however, will usually not contribute to the decision to enter foreign industry. It is usually a combination of various factors that affects exports. The internationalization motives were divided into proactive and reactive reasons by Svend Hollensen (2014).

FIGURE 5: Major motives for starting export

Proactive motives	Reactive motives
<ul style="list-style-type: none"> ● Profit and growth goals ● Managerial urge ● Technology competence/unique product ● Foreign market opportunities/market information ● Economies of scale ● Tax benefits 	<ul style="list-style-type: none"> ● Competitive pressures ● Domestic market: small and saturated ● Overproduction/excess capacity ● Unsolicited foreign orders ● Extend sales of seasonal products ● Proximity to international customers/psychological distance

Source: Hollensen 2014, p.54

Proactive motives show incentives to try to switch tactics based on the company's interest in using specific skills or market options (e.g. special technological skills). Reactive motives show that the company reacts in its home or foreign market to stresses or risks by changing its

operations over time and passively adjusting them (Hollensen, 2014). Let's discuss more of every motive for internationalization.

2.2.3.1. Proactive motives

a) Profit and growth goals

In the initial phase of export interest, it is really crucial for small and medium-sized businesses to make short-term profit since it is very motivating to keep going export. The company's desire to grow is also important when the company decides to start exporting. Hollensen (2014, p.54) explains that “the stronger the firm’s motivation to grow, the greater will be the activities it generates, including search activity for new possibilities, in order to find means of fulfilling growth and profit ambitions”.

b) Managerial urge

Managerial urge is the commitment and motivation of the manager that demonstrates a desire and optimism for internationalization. It can reflect the general ambition of entrepreneurship to continue to grow and reach new markets.

c) Technology competence/unique product

If the business has the benefit of using innovative technologies or providing different products or services on the international market, in this situation the organization has a strategic advantage over other firms and can occupy leadership roles in international industry. It will last until the competitors are aware of the technologies. The world market situation is changing quickly since there are so many competitive innovations and a lack of protection from international patents.

d) Foreign market opportunities/market information

A few international markets offer to expansion-oriented firms’ numerous opportunities. The economic successes of South-East Asians countries are their main attraction, whereas the political freedoms and the willingness to develop economic and trade relations with Western Europe, North America and Japan are the root of Eastern Europe markets (Hollensen, 2014). Additional information about the new market in comparison to its rivals give the exporting company an advantage. Business may obtain these information through market research or through special contacts / connections within the new market.

e) Economies of scale

As we know, the price advantage a company gains through expansion are economies of scale (Silvestre, 1987). We can therefore conclude that the company will reduce domestic costs of production by increasing production for the international market. Therefore, the organization has a double benefit.

f) Tax benefits

Hollensen (2014, p.57) describes the US tax mechanism as an example. Global Sales Company (FSC) offers companies some tax delays to allow them to sell their goods in international markets at lower costs or to generate greater profit.

2.2.3.2 Reactive motives

a) Competitive pressures

The behavior of its competitors is a major incentive for a company to start business abroad. As discussed above, companies which manufacture products for the global market profits from economies of scale. It implies that they might set a cheaper price for domestic goods and have a greater market share than companies who do not export and gain market share from export. At the same time, these domestic competitors will lose their domestic market share, as they will be more expensive than their international competitors.

b) Domestic market: small and saturated

When it sees no opportunity for increasing numbers of consumers on the domestic market, a firm begins to develop its export strategy. This can occur if the company manufactures special kinds of goods (for example, industrial products), with few types of consumers in various parts of the world.

An overcrowded home market is another reason for export. As we know, the product life cycle consists of four stages: introduction, growth, maturity and decrease (Kotler and Keller, 2012). So, when the product arrives at the decline stage on the domestic market it can be a situation of internationalization. And “instead of attempting a push-back of the life cycle process, or in addition to such an effort, firms may opt to prolong the product life cycle by expanding the market” (Hollensen, 2014, p.58). In developing countries, usually, the degree of product requirements is much lower (product can be growing in that country) than in developed countries where the same product may be at the phase of decrease. This is how companies use various foreign markets to extend their product life cycle.

c) Overproduction/excess capacity

Sometimes, a company produces more than the domestic demand. We are talking about overproduction in this situation. And starting to sell goods in foreign countries via short-term price reductions can be a response for the company. When domestic demand comes back, international operation could be paused. However, if the company attempts to use this plan afterwards, it can create problems, given that certain international customers are not only interested in short term business and do not want to start working with this company again.

In some cases, there is an excess capacity and new market opportunities need to be developed because demand for products on the home markets has changed. The domestic market has changed to a new product and excess goods, which it has not managed to sell here, will be sold internationally.

d) Unsolicited foreign orders

Hollensen (2014, p.59) explains that “many small companies have become aware of opportunities in export markets, because their products generated enquiries from overseas. These enquiries can result from advertising in trade journals that have worldwide circulation, through exhibitions and by other means. As a result, a large percentage of exporting firms’ initial orders are unsolicited”.

e) Extend sales of seasonal products

Some firms make specific goods for a particular season (for example, farm machinery). These firms may begin exportation throughout all the year to have stable demand for their goods. They will export their goods to countries in the different hemisphere, as seasons are different between the north and the south.

f) Proximity to international customers/psychological distance

Another factor that could affect the company's export activities is physical and psychological accessibility to foreign markets. Many European companies become foreign marketers simply because they are so close to their neighbors. German companies located close to the Austrian border, for example, can view their internationalization process as an augmentation of national activities, while some of their products go over to foreign countries.

Geographical proximity to international markets may not imply close psychological proximity. It varies for different cultural and legal characteristics and organizational standards that may vary considerably. Study demonstrated, for instance, that US companies consider Canada as much closer than Mexico's psychology (Hollensen, 2014).

2.2.4 Internationalization triggers

Hollensen (2014) says that something or someone starts the internationalization process before the company starts this process. The author defines as an internationalization catalyst – an external or internal occurrence to begin the entire cycle. In most cases, Rundh (2007) noted a number of triggers, but not just one stimulus, that impacts the process of internationalization. As mentioned earlier in this paper, external and internal stimuli can be used. Hollensen (2014) suggests that there is a group of external factors including market demand, network partners, competing firms, financing and trade associations and outside experts. Let us talk in detail about each particular trigger.

2.2.4.1 Market demand

Hollensen (2014) noticed that increased demand can be a reason to export some companies' production on international markets. Author provides an example of pharmaceutical firms that managed to reach foreign markets as the demand for their drugs was increasing. Domestic market decline can also be a motive for starting business abroad, particularly for small and medium-sized enterprises, which can generate higher profits and greater sales volumes (Burca, Fletcher and Brown, 2004).

2.2.4.2 Network partners

In this case, network partners are the causes behind the beginning of an internationalization. As mentioned in the previous article, the company can use its external network collaborators as a source of potential information. Vissak et al. (2008) stated that, through distribution channels of its collaborators, the firm can for instance gain access to foreign sales.

2.2.4.3 Competing firms

Hollensen (2014) argues that the firm can initiate internationalization process if the company's members are conscious of the fact that their company does a good business in the special market. Company managers should feel that the competitors in the market could indeed emerge and breach operations of the firm. The fact that rivals can enter into the company's national market and offer better goods to people and lower prices is also a purpose for the internationalization process. When SMEs enter their rival firms' home markets, they call this action a counteroffensive (Burca, Fletcher and Brown, 2004).

2.2.4.4 Financing

The company has to invest in resources to continue its external operations (for instance, demonstrate on world fairs or to make adjustments required within the company to facilitate export practices such as administrative and marketing capability development). The company's willingness to borrow funding from financial firms depend on the ability to have access to financial resources. Subventions from the government can be obtained from the company during the start of the process of internationalization (Hollensen, 2014).

2.2.4.5 Trade associations and outside experts

Formal and informal meetings (such as conferences and business associations) between managers of businesses have been of significance because they will guide the organization to an exporting choice. Based on their combined knowledge, small and medium-sized enterprises can make this decision (Hollensen, 2014).

As other external experts that boost the firm's international expansion, Hollensen identifies export agents, governments, chambers of commerce and banks.

- a) **Export agents** have background of previous international operations, get network abroad and actively reach expected exporters if they analyze that their goods have opportunities in the foreign markets.
- b) **Governments** provide encouragement for firms to start exporting by offering programs for export assistance, making different state policies and laws.
- c) The **chambers of commerce** also seek to motivate businesses to enter new markets. They help producers and suppliers communicate with international companies by offering consumer knowledge and helping them identify financial institutions to support their organization.
- d) **Banks** deliver to their domestic customers, information about business expansion because they want to use their services abroad when domestic customers expand in foreign market.

The internal causes of the internationalization process will be addressed here. Hollensen (2014) assumes that this group includes perceptive management, an internal or external event might lead to internationalization.

2.2.4.6 Perceptive management

Senior executives in international markets are also told of potential business developments. One incentive for executives is foreign business travels that allow them to obtain new insights on

the industry. Information in different languages or involvement in other cultures are other stimuli. The vision of management in the emerging markets is influenced by these factors. Supervisors sometimes emerge to the new company and try to develop their backgrounds in this new company with the experience of exporting activities in past jobs (Hollenden, 2014).

2.2.4.7 Specific internal event

An internationalization trigger may also be a specific event. For example, a new worker who believes that the company should start foreign business and manage to persuade supervisors to attempt it. Overproduction or decreases in national market size can also be an incentive to go abroad (Hollensen, 2014). Forsman et al. (2002) noted that the internationalization decision could also be based on the interest of foreign companies in the local companies' products and services.

2.2.4.8 Inward/outward internationalization

Hollensen (2014) supposes that a successful inward internationalization (import) of the firm can lead to its outward internationalization (export). The natural way for firm's internationalization is to begin to create inward activities, gain relationships and knowledge during this process and then to start with the outward activities (Welch et al., 2001).

Hollensen (2014) says that import activities can be initiated by:

- a) Buyer, who has active international search for foreign sources;
- b) Seller, who has initiation by the foreign suppliers.

2.2.5 Internationalization barriers and risks

Hollensen (2014) writes that there are many different barriers that can disturb successful export activities. For example, barriers that can hinder the initiation of internationalization process are lack of finances, knowledge, international market connections, foreign distribution channels and increase of the cost. It can be also a barrier, if the firm has incomplete information about potential customers or competitors.

Hollensen (2014) divides barriers that hinder the process of internationalization into three groups: commercial risks (fluctuations of exchange rates, if the contracts are made in a foreign currency, inability to pay of export customers because of bankruptcy or contract disputes, harm of products during shipping or distribution process), political risks (national export policies,

restrictions from foreign governments, big foreign tariffs on imported production, complication of trade documentation, lack of assistance from the government in overcoming export barriers) and general market risks (differences in languages and cultures of different countries, competitors in foreign markets, differences in products usage in specific market, problems to find a good distributor in the foreign market).

Fillis (2002) noticed that the most common problems for firms after entering the new markets are to find a reliable distributor, to promote products and to conform prices of competitors. There are some strategies which management of the company should use to avoid or reduce risks, such as a shunning of doing business in high-risk countries, using of variety of foreign markets, instead of being concentrated on one single and using government support, when it is possible).

2.2.6 Entry modes

The entry mode is described by Root (1987) as an “institutional arrangement that makes possible the entry of a company’s products, technology, human skills, management, or other resources into a foreign country”.

Anderson and Gatignon (1986) have been given a clearer perspective, defining entry mode as “a governance structure that allows a firm to exercise control over its foreign operations” (Sharma & Erramilli, 2004). The influence of control is emphasized in this definition but not all elements such as the asset or capability transaction represent this. Luo (2001) tried to incorporate transaction cost theoretical frameworks with resource-based ideas. His concept says that the internal resources, external goals and volatile environmental factors of the organization should be mixed. In short, the entry mode is a type of governance which changes ownership structures from non-equity modes such as exports to higher liquidity modes, such as investments by capital, plan, environment and some other transactional features, to the point of Mani, Antia & Rindfleisch, 2007.

Companies who want to enter an international market have to choose which entry method they want. The selection of the different entrance modalities according to Dunning is affected by three variables: business equity advantages, advantages of the new market and the incorporation of transactions within the organization internalizations. A business will show its superior assets to help businesses generate income that will offset expenses in order to deal with

host countries on the domestic markets. Its size, foreign knowledge and capacity to produce competitive goods reflect the ownership advantages of one company. The company's size indicates its willingness to pay marketing expenses, to gain volume savings, and thus larger companies will prefer high engagement than low engagement modes. Global exposure also influences the option of entrance. Companies with greater foreign experience prefer to select investment styles because they have more entrepreneurial expertise and social networks to help them pursue a more adventurous path of growth. For companies with the right capabilities to produce differentiated goods, higher control approaches and higher product distinction rates may be more effective (Stopford and Wells, 1972). The advantage of location of the firm has growth opportunity and investment risk, which define the appeal of the growth. In general, businesses prefer, if they can provide long-term rentals, to select investment modes when reaching high market opportunity countries. The benefits of internalization also seem to be contractual risk. On the one side the business will benefit from the size of the actual consumer environment by selecting a low-control entry mode even without taking bureaucratic disadvantages into account. However, in the other hand, in the case where the owner or management team has trouble anticipating potential developments and operating in an uncertain environment or in a scenario where there is no positive opportunity on the market, the company would pay more compared with the combined properties and expertise in the business. Lack of alternatives, the issue of minimal logic and uncertainty will make it useless and expensive for signing and implementing agreements (Andersen and Weitz 1986). In a situation where there are no competitive alternatives and the signing of a contract appears to be an unreasonable choice caused by the lack of potential partners or the existence of risk, it will be easier to prefer such entry modes as exporting or sole venture that would have greater leverage as all the properties would remain inside the business.

2.2.6.1 Exporting

The exports, mutual arrangements, equity joint partnerships and fully owned subsidiaries are usually alternatives that the company has. The first entry mode, the low-engagement one, is exporting. It is a technique to manufacture goods or services in one country and export and deliver them to clients in another. The key distinction between export and other entry types is that, in this situation, a company always avoids the target sector and follows a continuation of the change (Root, 1987). Exports are particularly common among small and medium-sized

enterprises. In a situation where there is minimal selling capacity in the target market, or where there are high target market costs, a firm might prefer exporting.

The effective strategy would also be to export if the political risk is high. A company can take advantage of exports by rising profits, revenue, and scale savings. The benefit is that a organization increases its customer base and reduces reliance on domestic requirements by exporting. A business may also balance variations related to product or service seasonality and economic cycles by exporting them. Exports are also low risk, cost-effective and the fastest way to enter. There is no need for investment in facilities for foreign production. The bulk of export prices will be met by marketing costs. Through the export of a product, an international network can be created. An organization may lose many places by opting to export even if there is a wide range of apparent advantages. For example, if a company wants to grow through exports, it has no power to understand its target market, its consumers and rivals. However, exposure to different trade barriers and variations in tariffs and the exchange rate could generate considerable downside. The firm should understand that growth by export requires company changes; new skills should be gained, and company resources should be changed. Exports can be operated directly and indirectly. Direct exports occur if a home-based corporation either contracts or executes exporting roles with intermediaries, such as dealers and agents based in a foreign country (Sharma and Erramilli 2004). Indirect exportation means selecting export services with intermediaries such as a specialist export processing firm and a trading company in the company's home country. These intermediaries help companies find and receive payment for their customers in a foreign country. Exports are considered the safest way for businesses with already little international presence to enter the global market by Johanson and Wiedersheim-Paul (1975) so that they reduce the burden of foreign operations.

2.2.6.2 Contractual agreements

The Root (1987) describes “long-term non-equity associations between an international company and an equity in a foreign target country that involve the transfer of technology or human skills from the former to the latter” as mutual arrangements covering licenses, franchising and strategic alliances. These partners share ideas and expertise through these agreements. For example, one organization called a licensor allows a licensee to use its intellectual property in return for offsets known as royalty by a licensing arrangement. The concept of one-way transfer of knowledge and know-how is part of licensing and franchising while coalitions correspond to mutual exchanges. A company tends to choose licenses when

faced with import and investment obstacles, or if the target market has a low sales potential. In addition, if a large cultural distinction exists between countries, a company can select licensing, and it is thus better to transfer the license to a foreign business that knows the local environment. A business can check an international demand without investments in resources and consumer expertise by licensing. Another major benefit of licensing is that the licensee is paid an extra fee for production in R&D in the form of royalties. Licensing also strengthens intellectual property rights security. One of the major drawbacks is that an enterprise creates its own rival and, therefore, it gains little experience, because it does not reach foreign customers directly and does not gain experimental information. Therefore, a corporation has no influence over the utilization of resources. The regulation in franchising is similar, but varies in length, quality and incentive. In general, licenses involve the transfer of trademark and operational know-how through trade secrets and intellectual proprietary services (Hoy and Stanworth 2003). The length of franchise licenses appears to be much longer, unlike licensing. In fact, the franchisor has a broader variety of privileges and services. A strategic partnership is a concept which characterizes specific partnership agreements like joint study, structured joint ventures or investment in minority equities (Bartett 2009). The key benefits are minimizing risk, sharing of technology and the integration of the market to create a more innovative consumer commodity. In the other hand, though, there are dangers to strategic collaboration, for example, where either or more participants create an alliance to gain their opponent's technologies to have a competitive advantage in the future. In addition, political partnerships are most established only for a limited period of time.

2.2.6.3 Equity joint venture

The next form of entry is a joint partnership with investors. It is a “particular type of strategic alliance in which two or more firms create, and jointly own, a new independent organization” (Besanko, Dranove, Shanley & Schaefer 2007, p.151). This requires some flexibility and sounds very dangerous mutual mode of entry, suggesting that partnerships will be built on confidence in order to succeed. Possible disputes, policy-making, ethnic gaps and distrust are among the main obstacles. The key feature of this style of entry is that businesses merge capital, technologies, innovations, finances and expertise to succeed.

Compared with other entry forms, wholly owned companies are the riskier. In comparison to others this method involved the highest stake in equity ownership and control (Root, 1987). The controlling stake in equity can be acquired by purchase or the formation of a new company

(Pan & Tse, 2000). It should typically be understood that before selecting the right entry mode, the organization should assess its awareness of the target area, psychological and physical distance, competition, ownership issues in order to determine whether to continue with low-commitment entry modes first or choose more challenging high-commitment modes.

3. Methodology

In this master thesis, we want to look at the internationalization of companies and analyzing their strategy, capital structure, and ownership to understand the link between these parameters and their success. To do so, I have selected four companies with different profiles in terms of strategy, capital structure, ownership or success.

First, I have selected Carrefour and AB-InBev because they are two successful worldwide companies. Indeed, AB-InBev is known as the market leader in the beer industry and Carrefour tries to be a leader in each new market he is entering.

Moreover, I have selected Campari because it is known as a family company and it will be interesting to analyze how a big company like that has succeeded to keep a family ownership whereas AB-InBev is not a family company anymore.

And the last company is Riaktr. It is a smaller and younger company but with this company, we will understand better today's process of internationalization. Moreover, it is a born global company and in today's world, it is more and more common, so it is interesting to have a different point of view.

In order to analyze these companies, I will assess them one by one with only facts, and then compare them and finally try to generalize observations in conclusion. The important information here is that I will compare companies together. Companies have different size, capital and ownership structure; therefore, numbers are not important but the evolution through time is the most important.

I will only analyze the same things for all the companies to compare them. I will begin with the history and strategy of the company's process of internationalization. This will give us a global view of the process to enter a new market, and we will understand the strategy that the company has followed in the process.

In addition, I will analyze the financial data and ownership structure of each company. Three of them are big firms with a lot of financial rounds which makes it difficult to analyze all of them and there are not all related to the internationalization process. That is why I have decided to analyze the last decade (2010-2019) financial and ownership situation. But with the last company, Riaktr, we will have more detailed information about the internationalization process and evolution of financial and ownership structure during this process.

The first analyzed indicator will be the **ownership structure**, this indicator will show us who owns the company. Indeed, as a growing company that wants to enter a foreign market, you

need capital to finance this growth. And, as a company owner, you have a dilemma in front of you, either you ask venture capitalist to invest in your company but in return, they will ask for ownership in your company. Either, you keep all your ownership, but you have to ask loans to banks by convincing them to lend you money even if they do not like risks.

The second indicator will be the **net debt to equity ratio**. I will analyze this indicator because it shows the capital structure and helps us to understand the leverage of the company and the average cost of capital. I have chosen the net debt instead of debt because the net debt is the “non-current and current interest-bearing loans and borrowings and bank overdrafts, minus debt securities and cash.” (AB-InBev annual account) and it is used in all the annual accounts.

The third indicator will be the **EBITDA** (earnings before interest, taxes, depreciation, and amortization) because it is a method that is often used to understand the profitability of companies and the valuation of it. Moreover, even if EBITDA can be manipulated by the company, it is more difficult to do it than net profit because it is not biased by interest, taxes, depreciation, and amortization.

And the last indicator I will analyze is the **share price**. Indeed, investors usually get shares when they are investing in a company. They are receiving annual dividend but when they will sell their share, they want to make a profit and get a return on their investment. Share's price is influenced by a lot of factors and it gives us a better view of the company's performances and speculation about the future of the company.

After going through all the firms, I will compare companies' strategies and performances to find common practices and differences. Moreover, thanks to Pierre Boël, Chief of Operation Organization at Riaktr, I will generalize what is the best internationalization strategy, capital, and ownership structure from a company's point of view. My analysis will be based on the theory we have seen in the literature review, each company case and Pierre Boël's interview. First of all, I will find common characteristics of the strategy and then I will link what we can observe in the practical part and the theory.

Secondly, I will analyze the capital structure of all companies and compare them. I will find a link between capital structure and ownership structure, between capital structure evolution and EBITDA evolution. Then with the theory of the cost of capital and with Pierre Boël's interview, I will understand how a company choose his capital structure during his internationalization process and which mistakes a company can avoid increasing their chance of success.

In conclusion, I will join the strategic part and the capital structure part to make some recommendations about the internationalization process.

4. Internationalization cases

4.1 Carrefour Case

4.1.1 Internationalization process

Carrefour Group is a France-based retail company. It was created in 1959 by Jacques Defforey, Denis Defforey and Marcel Fournier. The first step in their internationalization was the launch of their company in Belgium in 1969. Carrefour became the biggest supermarket company in Europe and the second in the world, right behind Wal-Mart, operating in Europe, Asia and South America, and has grown very quickly in other countries. In the 1970s, after Carrefour joined the CAC40, it has changed into a public company. This decision was very important and transformed Carrefour into a worldwide branch company, one of the first food retail companies to start internationalizing. In terms of economies of scale, market role, customers' trust, exposure to new technologies and diverse raw materials, this move has offered them a competitive advantage. The key reason for the business success of Carrefour in the 80's and 90's was the internationalization process. In the meantime, the company in France continued to open up and strengthen their first position as market leader. During the 2000s, businesses in some eastern countries opened up, with high growth rates and increased buying power.

Carrefour typically penetrates one country through a local alliance because all market, including the under-developed one, have their own local retailers, the only way to reach these countries is to acquire one or two local retailers that don't have to be the most relevant, but having growth potential. For key towns, capitals or very important cities where the population has more buying power, the multinational began with the development of one or two store. After the deployment, the plan is to take the lead or being in the small list of two or three biggest stores in the countries. (Lebreiro, 2014)

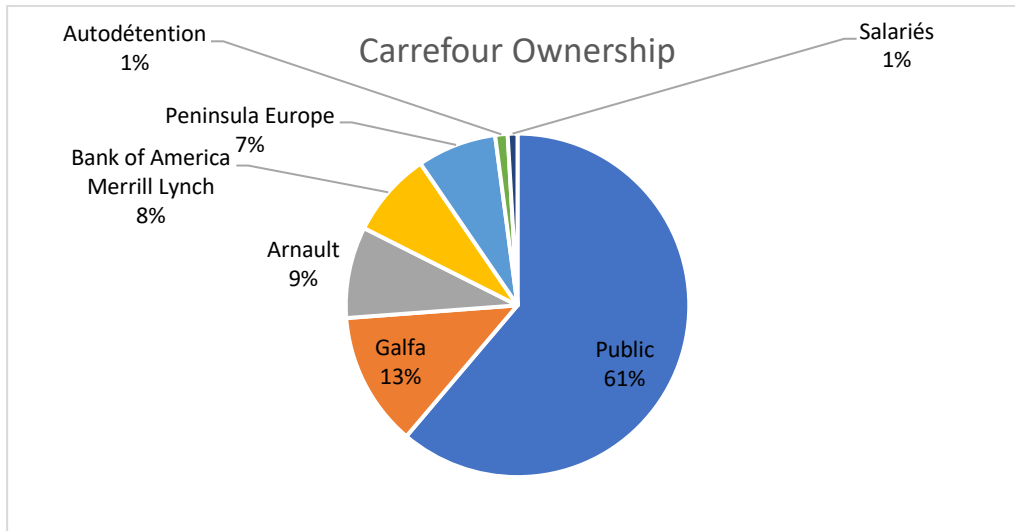
4.1.2 Today's performance and ownership

Now that we have the history of Carrefour's internationalization, we will have a look at Carrefour's performances of the last few years and who really owns the company.

First of all, let's look at the ownership. Indeed, usually when a venture capitalist invests in the company, they are taking some parts of the company (generally proportional to his investments) and in consequences, the first owner of the company loses some ownership. It is not good or bad to lose some ownership, but it has some sides effects, such as you can not take decisions alone anymore (despite you own more than 50% of the company) and you do not receive all

the complete dividend. On the positive side, generally, you have more capital to invest in the company and to grow.

FIGURE 6: Carrefour ownership

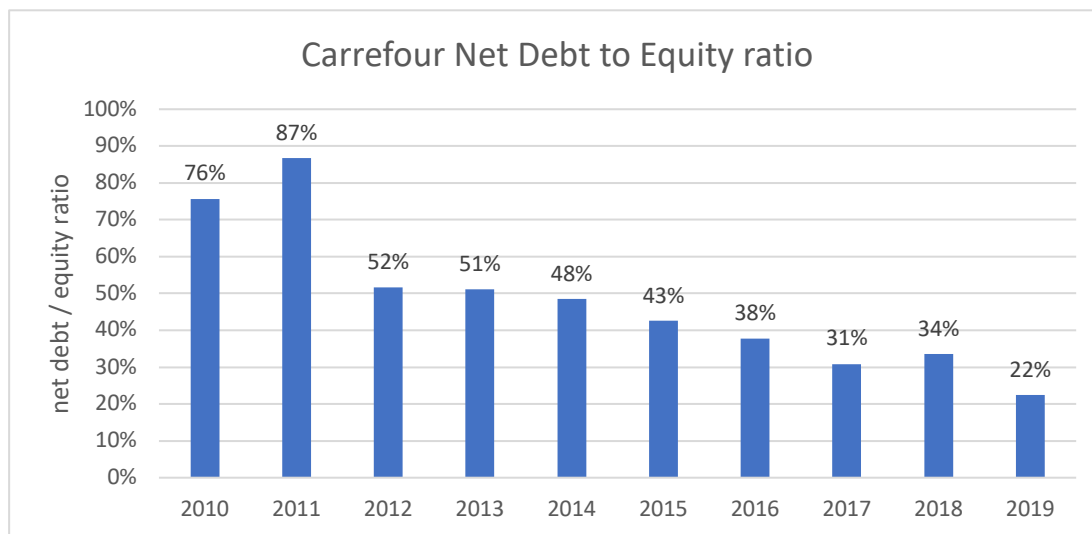


Source: Carrefour website (The structure of the Carrefour shareholder base, <https://www.carrefour.com/en/finance/carrefour-share>)

We can see that Carrefour capital is mostly owned by public shares and that “Autodétention” (which means owning it-self) is only 1% so founders of Carrefour do not own Carrefour anymore.

In terms of Capital Structure, it is relevant to refer that 82.35% of the Equity is free float in CAC Index, which means that Carrefour has a large dependence on the market’s tendencies. The key shareholders with a lower percentage of equity, control the company. (Lebreiro, 2014) Moreover, let’s focus on the net debt to equity ratio to understand how the capital is structured and analyze their cost of capital.

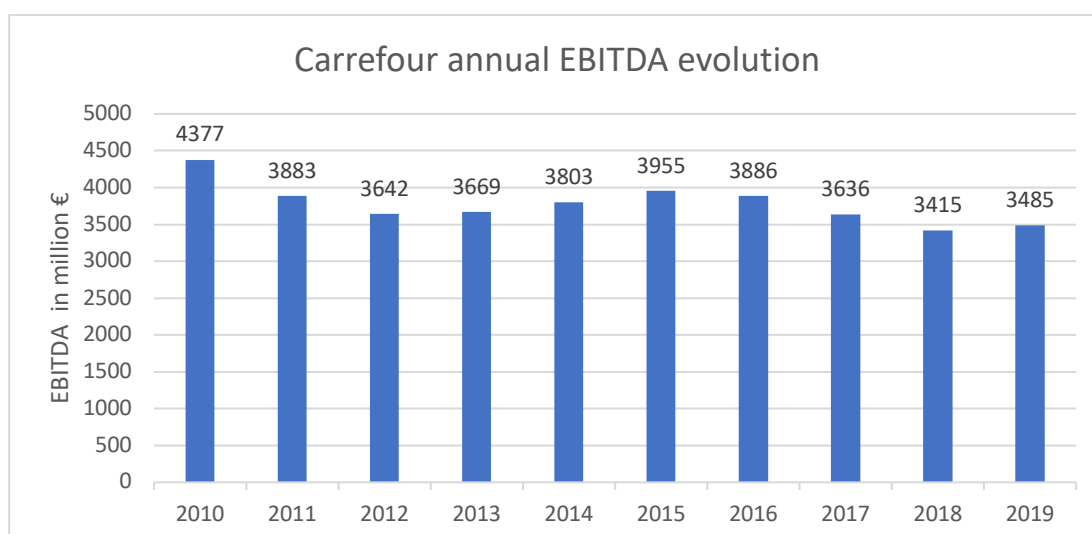
FIGURE 7: Carrefour Net Debt to Equity ratio



Source: Carrefour annual accounts

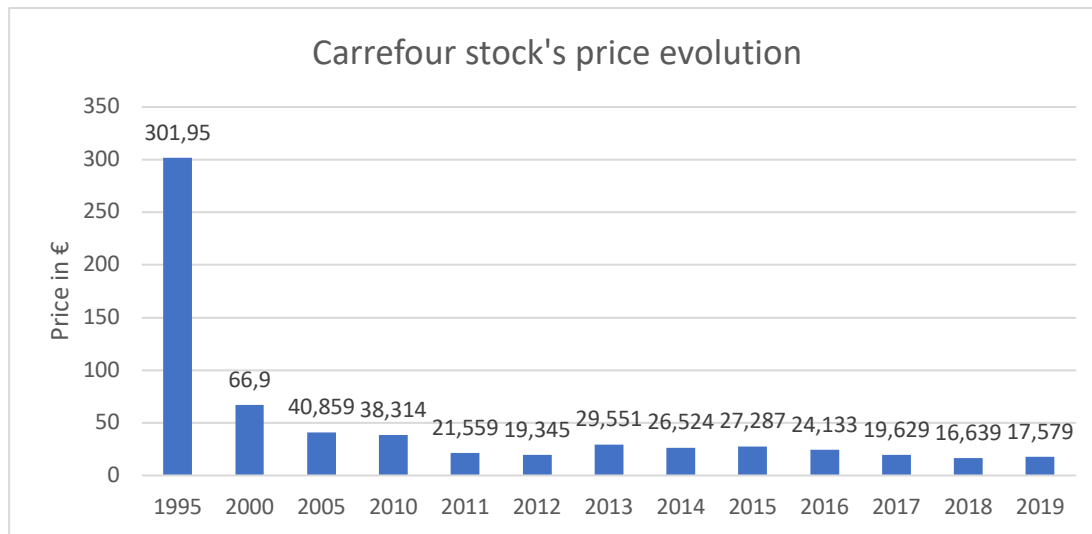
We can see that their net debt to equity ratio decreases over the last decade. We can make a hypothesis that during the 2008 crisis, they had to borrow money because at that time investors did not want to invest in companies. And after the crisis, they tried to reduce the amount of net debt. Or another hypothesis is that they raised more equity during the last decade. And looking at the number in their annual account, both happened, they decreased debt and increased equity. Now, let's have a look at performances, we will have a look at their annual EBITDA and then, we will also focus on the share price evolution to see if it is profitable to buy Carrefour's shares.

FIGURE 8: Carrefour annual EBITDA evolution



Source: Carrefour annual accounts

FIGURE 9: Carrefour stock's price evolution (Price of each year on the 29th of December)



Source: Carrefour website (Share price, <https://www.carrefour.com/en/finance/carrefour-share>)

We see that there was a decrease in Carrefour's annual EBITDA during this decade (-20,38%). There was a decrease between 2010 and 2012, maybe due to the financial crisis. Between 2013 and 2015, there was an increase and then between 2016 and 2018, there was another decrease and a small increase in 2019. This is the same fluctuation of the stocks' price. Indeed, stock price has decreased a lot since 1995 (-92.1% between the 31th of December 1995 and the 31th of December 2019) and in the last decade, there was a drop of 37.76% between the 31th of December 2010 and the 31th of December 2019. Which means that a long-term investment in Carrefour was not profitable.

If we want to link the net debt to equity ratio with the annual EBITDA, we can see that when the ratio decreased between 2013 and 2017, EBITDA increased except for 2017. In 2018, the ratio increased by 6%, and the EBITDA still decreased in 2017 by 6%. And in 2019, the net debt to equity ratio decreased and the EBITDA increased by 2%.

4.2 AB-InBev Case

4.2.1 Internationalization process

AB InBev is an enterprise born in 1987 through a series of mergers and acquisitions. In fact, Artois and Piedboeuf joined and created Interbrew in that year, following decades of strong competition, which in 2004 merged with Ambev to create InBev and in 2008 to create AB-InBev with Anheuser-Busch. The company has always been in operation all the years on the same market, beer, and in recent decades has expanded all over the world.

Today, AB-InBev is the world's largest beer organization. Headquartered in Belgium, the brewing company has established about 151 breweries in 36 countries.

The business has a high degree of popularity both at home and worldwide and that is the outcome of a strong internationalization plan that has been built in accordance with its strategy. All began in 1987 when the Artois beer company headquartered in Leuven merged with its biggest Belgian rival, Piedboeuf. Until then, no company had a coherent strategy: it was only focused on improving itself and its focus was still confined to the Belgian market.

After the fusion of the two firms in 1987, it became obvious that without a strong business plan it could not be further established. A new management plan was introduced in 1989 and a study of internal and external influences affecting the direction of the organization was undertaken. The study found a crowded Belgian market with low profits and return on investment.

Therefore, internationalization was seen as one of the key factors of the company's success: it was one of the multinational strategies. The category with most opportunity of international expansion and became the first priority, was the beer. When the decision was taken to focus solely on beer, it was a matter about where to grow. As outlined above, AB-InBev agreed to continue spreading from the unsaturated markets, mostly newly formed Central and Eastern Europe countries, after the merger to become a fully global business. It was a risky move to negotiate the first contract in Hungary, but based on a solid business review, the organization agreed and was built on the implementation of strategy. AB-InBev developed his business also in Asia and South America subsequently between 1995-2007.

The organization started its fast growth in South America in 1999, due to the merger with Ambev. The aim was to improve the foreign presence in various countries and regions by acquisitions of local companies. A good example is the case in Latin America. The decision was to enter a very critical and rapidly changing market when Interbrew combined with Ambev in 1999 to create InBev. Indeed, the number of subsidiaries in South America has risen from that moment to show the company's increasing dedication to the region. Another clear example

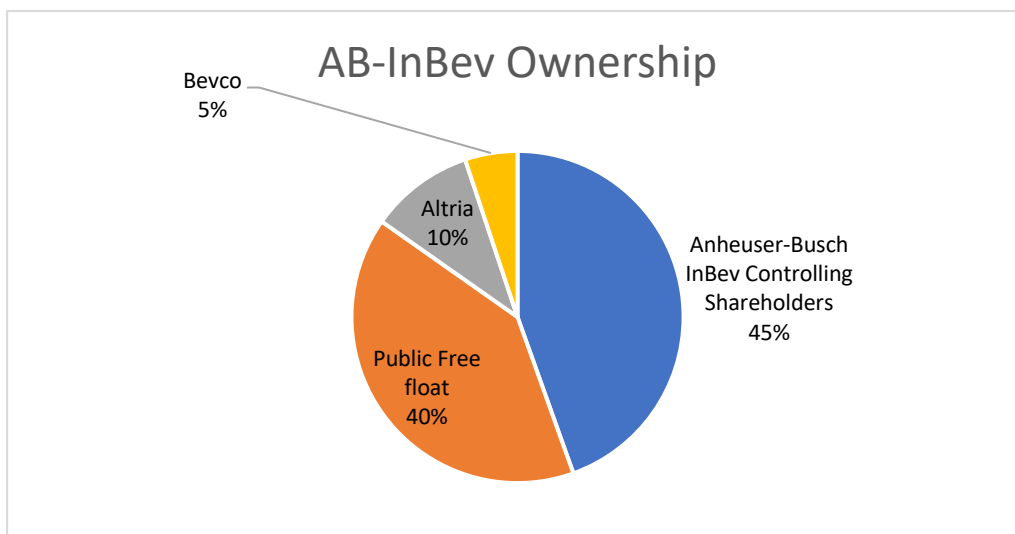
is China: by purchasing K.K and the Zhujiang Brewery, Interbrew strengthened its role within the market in 2002.

AB-InBev grows by gradual measures. It first acquires local companies in part or completely and takes advantage of the market profitability and experience of the target market. This step is followed by a reinforcement of the brands relating to the acquired business, and an increasing dedication to the market. Only later will the multinational brands be introduced, and activities integrated like the rest of the company. (Boiardi and Sleuwaegen, 2010)

4.2.2 Today's performance and ownership

Now that we know the history of AB-InBev's internationalization, let's have a look at AB-InBev's performances of the last few years and who really owns the company, like the Carrefour case, to understand their current capital structure situation and profitability.

FIGURE 10: AB-InBev ownership

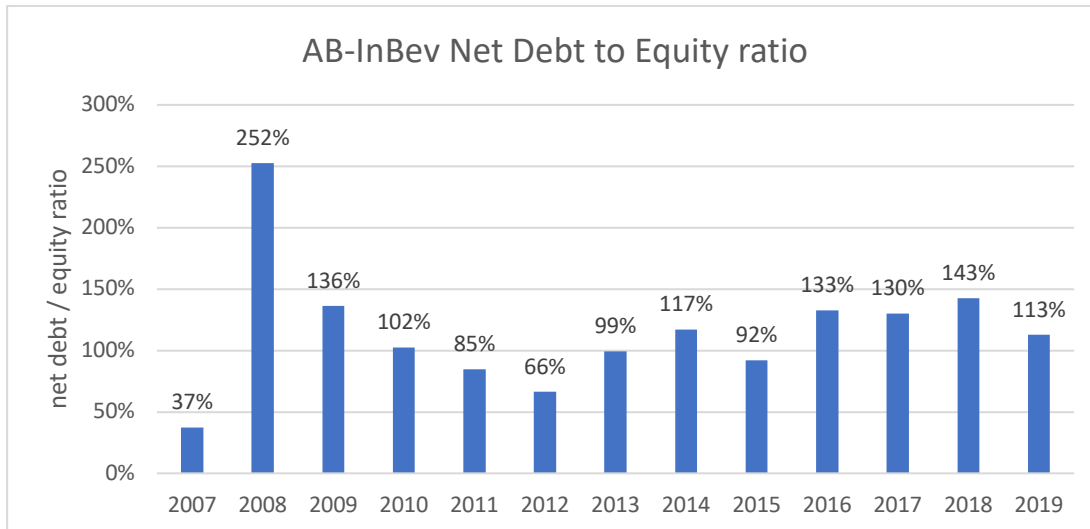


Source: AB-InBev website (Corporate governance, Shareholder Structure, <https://www.ab-inbev.com/investors/corporate-governance/shareholder-structure.html>)

Here we can see that AB-InBev controlling shareholders still own the company. But we have to keep in mind that AB InBev and its subsidiaries Brandbrew, Brandbev and Mexbrew are controlled by Stichting Anheuser-Busch InBev, which is jointly controlled by EPS, EPS Participations & BRC. Moreover, EPS Participations is fully owned by EPS which is not controlled and the ultimate control of BRC is jointly owned by Mr Jorge Paulo Lemann, Carlos Alberto da Veiga Sicupira & Marcel Herrmann Telles.

Regarding the Capital Structure, we can see that like Carrefour, their net debt to equity ratio went up in 2008 and then decreased until 2012 and increased again to be above 100% in 5 out of 7 years (exceptions are 2013 with 99% and 2015 with 92%).

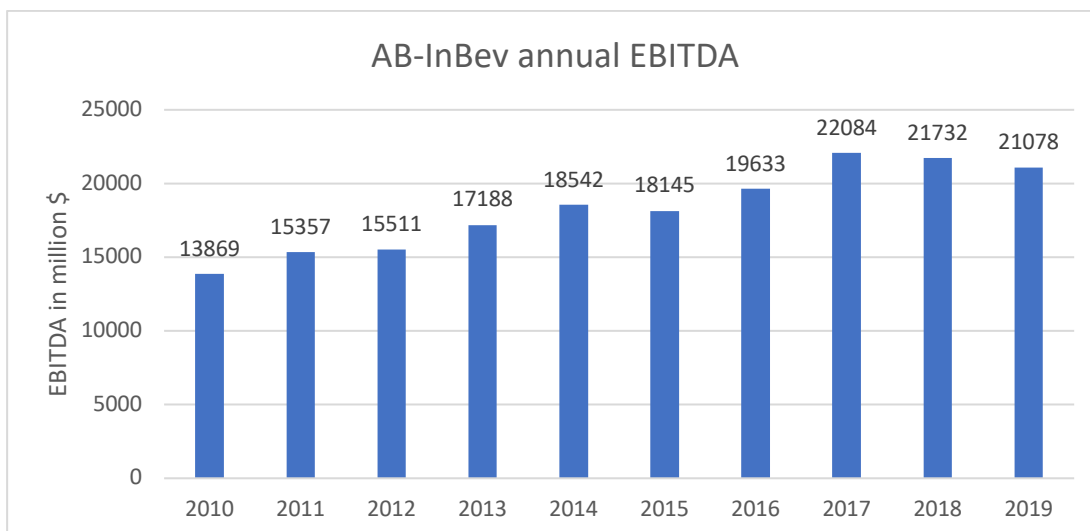
FIGURE 11: AB-InBev Net Debt to Equity ratio (For each year, it is the ratio on the 31st of June)



Source: AB-InBev annual accounts

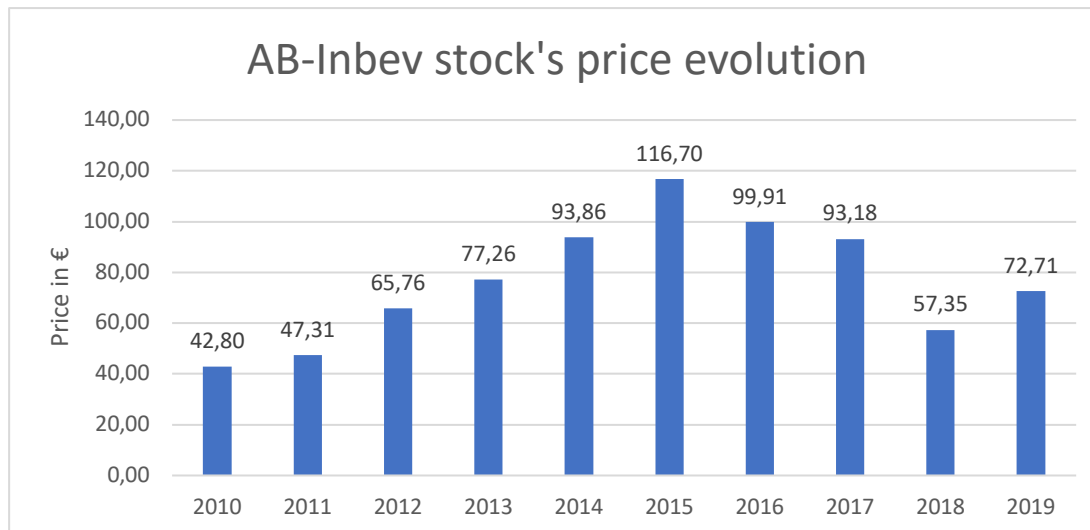
Now that we have information about the capital structure and ownership, let's look at profitability with annual EBITDA and stock's price.

FIGURE 12: AB-InBev annual EBITDA evolution



Source: AB-InBev annual accounts

FIGURE 13: AB-InBev stock's price evolution (Price of each year on the 29th of December)



Source: AB-InBev website (Share information, Stock Monitor, <https://www.ab-inbev.com/investors/share-information.html>)

We can see a small correlation between stock price and annual EBITDA. Looking at stock's prices, we can see that there was a constant increase during the first half of the decade and a constant decrease during the second half of the decade (except in 2019) but in general, there were an increase of 69.88% between the 31th of December 2010 and the 31th of December 2019. Whereas for the annual EBITDA, there was also an increase until 2017 (except in 2015 with a decrease of 2,14% in comparison to 2014) then a slow decrease for the last two years. During this decade, EBITDA increased by nearly 52%. But we have to keep in mind that stock's price is not only linked to the financial situation but to more factors and speculation.

If we compare the figure 11 with the figure 12, we can see that in 2012, net debt to equity ratio is the lowest of the decade and EBITDA increase was only 1%, which was low in comparison to the increase of more than 10% in 2011 and 2013. But we have to keep in mind that in 2012, Europe was hit by the financial crisis and their EBITDA still increased.

We can make the same observation in 2015, when the net debt to equity ratio dropped, EBITDA dropped by 2,14% and also in 2019, when net debt to equity ratio also dropped and the EBITDA decreased by 3,01%.

But it is not always the same trend since in 2018, net debt to equity ratio has increased but EBITDA has still decreased by 1,52%.

4.3 Campari Case

4.3.2 Internationalization process

Campari company has a long history. Beginning with a general overview of the business, founded in Sesto San Giovanni in 1860 and has extended its influence around the world over the years spreading its borders with Italy to the Far East and being the sixth biggest player in the premium spirit industry. The Group has over 50 brands (including Aperol, Skyy, Lemonsoda family) in its portfolio. Today in 19 countries and more than 4,000 staff, Sesto San Giovanni has its own distribution system. (Campari Group website)

In the 1960's, delivery was reaching more than 80 nations, a leader of future generations of businessmen, who pursued and caught up in global markets and achieved outstanding results. The business created enormous positive returns on investments through its forecasting and adaptability, along with good market recognition and brand knowledge. The beverage industry was defined during the second half of the 90s by a powerful M&A trend that led to the development of companies with global size and remarkable portfolio lines. (Campari Group website)

Campari therefore decided to grow from a single brands company into an international company with good and well-donated portfolio that focused on international expansion, not only through organic growth but also through external growth.

Concerning organic growth, it means designing successful frameworks for internal operations that can contribute to core business development.

External growth in fact, by direct spending, acquisitions or alliances, indicates a globalization cycle and good returns on investments made abroad. (Campari Group website)

The expansion plan of Gruppo Campari sought to incorporate sustainable growth through solid brand development and acquisitions to maximize shareholder value. Spirit was the central activity of the company and concentrated its acquisition activities. The corporate vision of the Company was motivated by a desire in core regional markets to hit or boost critical mass.

Campari 's strategy has been to extend its offer to the market to include complementary segments (spirit industry), covering various segments and objectives (from alcoholic beverages to whiskies and vodka). The clever approach adopted allowed the purchasing of well-known

medium-sized firms, both in terms of the know-how and in the financial sector, into new markets. One more move that should be listed was the identification of funds investing in core and all foreign operations on the Milan Exchange in 2001. (Campari Group website)

Throughout the 1990s, when the world was marked by heavy consolidation strategies and smaller firms being multinationals and organized with a particular brand portfolio, activities leading to transition in the alcoholic beverage industry, the main moment was to turn the single market into a global Market. The core aspect of Campari's community strategy was that businesses had been purchased and left to operate independently: the organization would not centralize its power and ensure that the recently purchased companies' freedoms of operation do not conflict with their principles and goals of the Group.

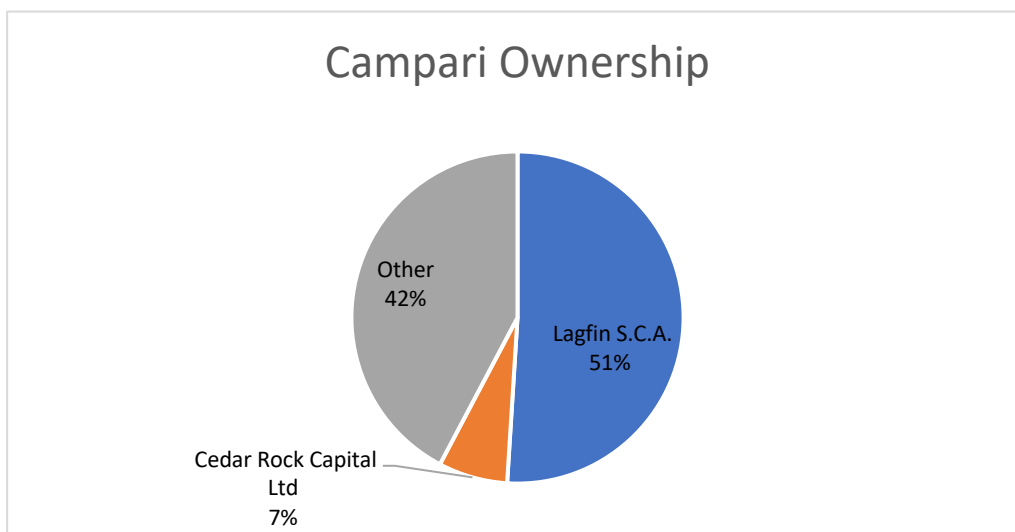
The first acquisition took place in 1995: Dutch BobWessanen group, which has brands such as Crodino, Cynar, Lemonsoda, Biancosarti and Crodo in its portfolio.

This first operation has resulted in a variety of major investments for the entry of various core markets in South America, East Europe, Australia, managing competition such as Aperol and expanding into new commodity categories such as whisky and rum. (Campari Group website)

4.3.2 Today's performance and ownership

Now that we have the history of Campari's internationalization, let's look at Campari's performances of the last few years and who really owns the company like Carrefour and AB-InBev cases to understand their current capital structure situation and profitability.

FIGURE 14: Campari ownership

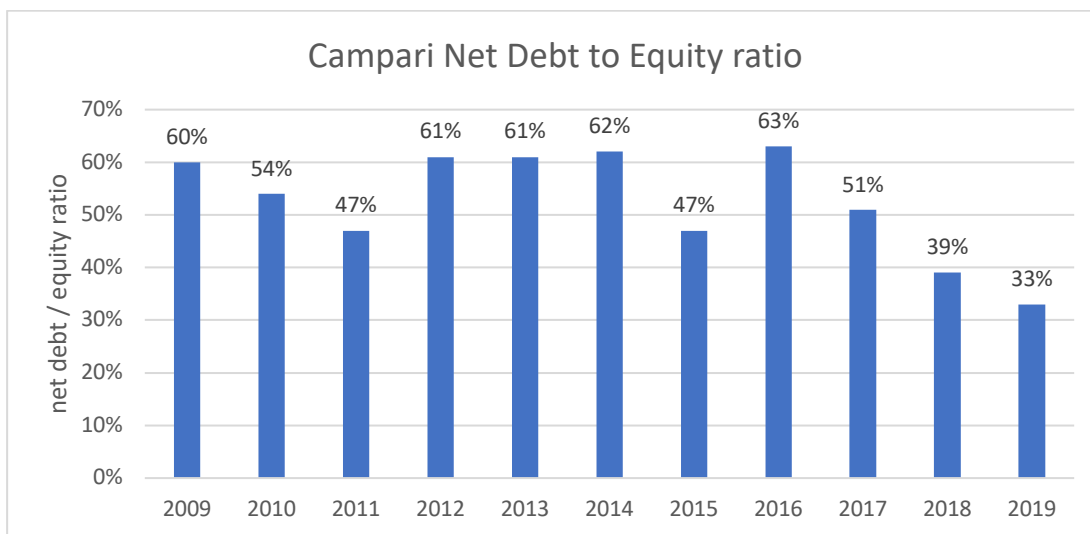


Source: Campari website (Shareholder center, ownership structure, <https://www.camparigroup.com/en/page/investors/shareholder-centre>)

On the Campari website, there are only two major shareholders, Lagfin S.C.A and Cedar Rock Capital Ltd which represent 58% of the shareholders. That is why, I put the rest of the shareholders in “Other” because it should be smaller shareholders or shares that are public. But the main message of this graph is that Lagfin S.C.A owns 51% of the shares and 64.93% of the voting rights, which means it owns Campari and can take all the decisions. Lagfin is the holding company of Davide Campari-Milano.

Regarding the Capital Structure, we can see that unlike Carrefour and AB-InBev, their net debt to equity ratio stayed stable during this decade with a decrease during the last two years (2018-2019).

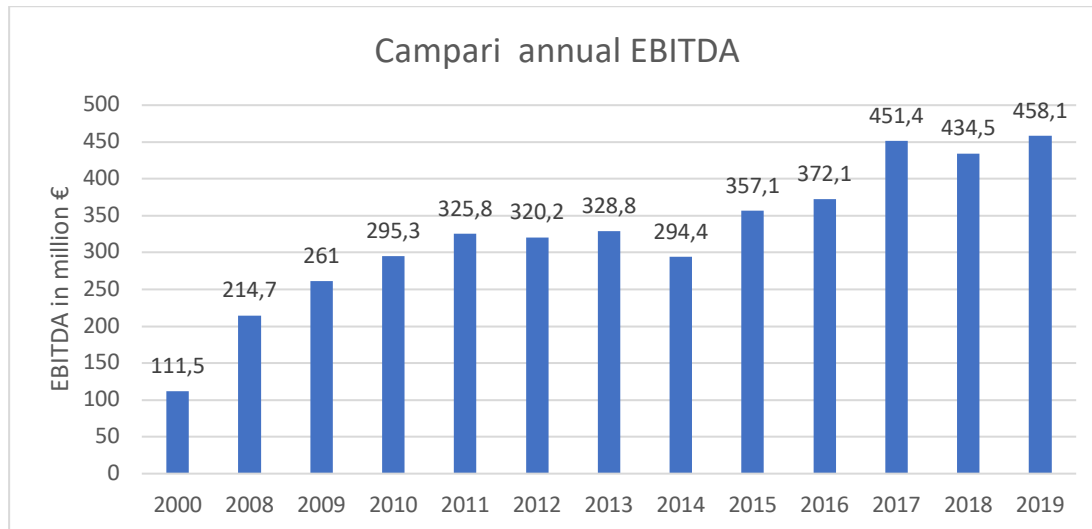
FIGURE 15: Campari Net Debt to Equity ratio (For each year, it is the ratio on the 31st of June)



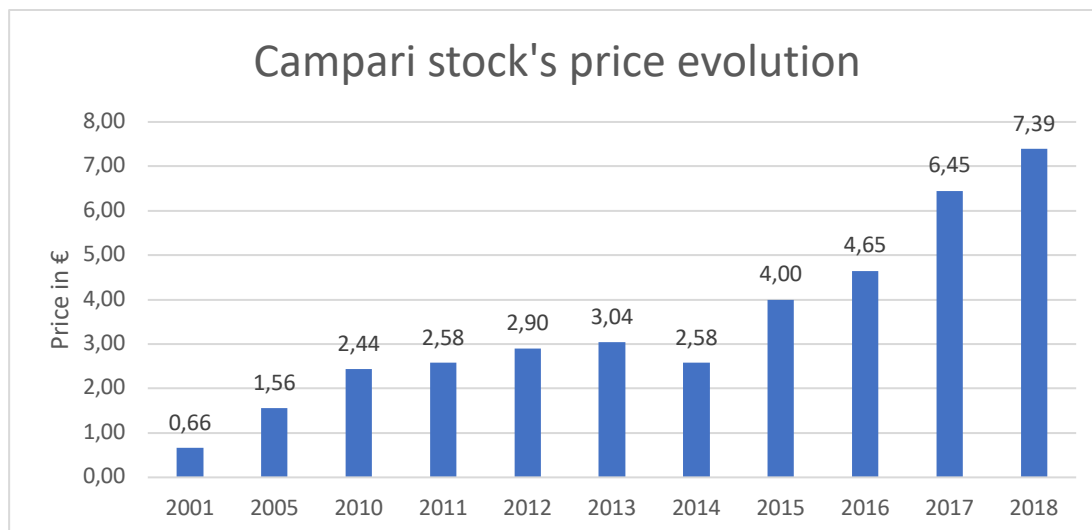
Source: Campari annual accounts

Now that we have information about the capital structure and ownership, let's study the profitability with annual EBITDA and stock's price.

FIGURE 16: Campari annual EBITDA evolution



Source: Campari annual accounts

FIGURE 17: Campari stock's price evolution (Price of each year on the 29th of December)

Source: Campari website (Shareholder center, Historical data,
<https://www.camparigroup.com/en/page/investors/shareholder-centre>)

We can see that their annual EBITDA and stock's price are correlated, Indeed, there was an increase between 2010 and 2013, then a drop in 2014 and directly a higher increase between 2015 and 2018.

Regarding stock's price, we can see that it increased every year (except in 2014) and like the net income, in 2017 and 2018, it went up quickly (38.71% and 58.92% respectively in comparison to 2016). We can safely say that Campari Group was profitable in the last decade.

Regarding the link between net debt to equity ratio and annual EBITDA, we can see that between 2009 and 2011, the ratio decreased, and the EBITDA increased. Moreover in 2012, the ratio increased and stayed stable in 2013 and 2014 and the EBITDA decreased in 2012 and 2014. Then there was a drop of the ratio in 2015, in the same year, EBITDA increased. In 2016, it was a special year since the ratio came back to the same level as 2012 with an increase but the EBITDA still increased. But this increase was low in comparison to 2015 and 2017. Indeed, in 2016, the increase was by 4,2% whereas in 2015 and 2017, there were an increase of more than 20% for both years. And after 2017, EBITDA stabilized itself whereas the net debt to equity ratio decreased.

4.4 Riaktr Case

4.4.1 Internationalization process

Riaktr was founded in 2009 by two entrepreneurs Sébastien Deletaille and Loïc Jacobs. It started as a service company under the name 'Real Impact Analytics'. At the time, Big Data was the new big business, driving important corporate investments. The strategy was and still is to tap into rich telecom data flows to capture their value and turn them into action.

They quickly expanded around the world and gained traction as one of the fastest growing Belgian tech start-ups. And today the company employs more than 60 people around the world. Two years ago, they pivoted from a service to a product company. Indeed, the goal of products is to provide advanced analytics through beautiful and easy-to-use applications. Six of the top ten global telecom groups trust RIAKTR to optimize their Sales & Distribution operations and better prioritize their Network investments, with the help of technical and business consultants who work closely to them.

First of all, let's focus on the internationalization process. In the beginning, Riaktr was a born global company. Indeed, it is a Belgian company, founded by Belgian entrepreneurs, but the first client was an African multinational telecommunication company, MTN. As their strategy was to analyze the market in real-time at a micro level, they decided to implement their solution

in growing countries with different behaviors in the same country. That is why they chosen to start in Africa. The first step with MTN in Africa worked well and they have decided to extend their solution in other continents. They have entered a new phase of super expansion to reach new markets such as Brazil, Asia, Middle East. The strategy of this expansion was entering in a new continent by being physically on-field and directly selling the solution. Then when the first contract was signed, the word of mouth was the best solution to sell in other countries and other telecom operators. Indeed, in growing countries, chiefs of operator in one country, speak a lot with chiefs of the same company in other countries and they share information. Moreover, it is common for a chief to switch from one operator to another, so it is easier to have a foot in another operator in the same continent.

With this super expansion phase, they faced some difficulties, and now they start their third phase, the rationalization one. They are more focusing on Africa to enter new countries with the same operator and try to reach other operators.

4.4.2 Today's performance and ownership

I had the chance to have an interview with the Chief Operating Officer, Pierre Boël. We had a very nice conversation and I really thank him for all the information he provided about Riaktr and his point of view about the internationalization process and financial structure.

We will do the same structure as the previous companies (ownership structure, net debt to equity ratio, and EBITDA evolution since they are not on the stock market, there is no stock price evolution). I do not have exact numbers due to confidentiality, but Pierre Boël explained to me the evolution of the different indicators and reasons they made some choices.

Let's begin with the ownership structure. During the interview, we went through the ownership structure evolution which gave us more information than just today's ownership picture like with the other companies.

In the beginning, they were two founders and they shared the company's ownership more or less in two (50-50). After some time, 8 external people joined the company as co-founders, who gained 40% and the two founders kept 60% (30% each). At that time, they did not need capital because it was a service company and they just needed some cash for the working capital.

In 2016, they decided to switch as a software company. This transition changes a lot of things because becoming a software company means becoming a product company. This involves a lot of costs such as research and development and production. With this increase in costs, they

decided to raise 12 million euros with three capital ventures: Endeit Capital, Fortino Capital Partners and Gimv. With this significant increase in capital, an important point was the valuation of the company to know how the ownership has changed. The group of 10 co-founders (2 founders plus 8 external who joined the company at a very early stage) wanted to keep the decision power and they succeeded to keep the majority at least in the board of directors, where big decisions are taken.

In 2017, they raised more money and the co-founders lost their majority. But they still kept some control because they managed to create two different types of shares. To approve critical decision, the majority is needed in the two different groups of shares and the group of 10 still have the majority in one of the two groups, so they can still block some important decisions if they want.

Regarding the evolution of the net debt to equity ratio, it follows the three internationalization phases. Indeed, in the beginning, as a service firm, they did not have a lot of capital, so they did not need debt, therefore the ratio was approaching 0%. At that time, they only had some short-term debt to cover the working capital.

During the expansion phase, they needed some capital to travel to new countries and continents, so they borrowed money to banks. Indeed, according to their CEO, they should borrow as much money as possible because it was cheap in comparison to equity, they kept their ownership and finally, they trusted in their success therefore, paying the debt in the future would not a problem because they would have more than enough money to pay back. During the interview, Pierre Boël told me that banks borrow money base on the cash-flow profile. Indeed, there are two components in this concept; timing and risk. To sum up, timing is when cash flows will become positive and risk is the probability that the future cash flows will be indeed positive. At that time, Riaktr was a small company, so the risks were high, and banks borrow more money when risks are low. But during the interview, I learned that they are some public assistance that can guarantee the payback of the debt. Indeed, governments want to support entrepreneurs to grow especially when it concerns trading with foreign countries because they want to increase their exports. This practice really helped Riaktr to get some loans from banks at a low-interest rate. At that time, there was a lot of debt for a small amount of equity.

But they borrowed too much money and they were more and more focused on how they will pay back their loans than their core business. They added a new cost, the cost financial distress.

As said above, in 2016, they raised 12 million euros, so they increased their equity and they re-established balance between net debt and equity.

Now, during the stabilization process, they want to reduce debt to avoid falling in the same situation as before when they borrowed too much debt which was difficult to be paid back.

It is the same story for the EBITDA evolution. Indeed, in the beginning, it was slightly positive. They were a consulting firm, so they did not support a lot of costs and they were earning the margin they were asking clients.

With the switch to a software company, as said before, costs increased a lot and EBITDA became negative by several million. This deficit was mostly explained by the costs of research and development.

In 2018, two years after the switch to a product company, EBITDA became positive and they targeted a controlled growth.

With this case, I really had the chance to explore the journey of a new firm that wants to grow in a foreign market.

5. Analyze

Now that I have explained the internationalization process and analyzed some financial data and ownership for each company, let's compare them to find what's is working or not.

To do so, let's create a summary table to have a better overview of the four companies.

TABLE 1: Summary table

Company	Entry strategy	Ownership	Average net debt to equity ratio (2010-2019)	Evolution net debt to equity ratio (2010-2019)	Evolution EBITDA (2010-2019)	Evolution Stock price (2010-2019)
Carrefour	Acquisitions but enter new market with the Carrefour brand name	Public: 61% Galfa: 13%	48%	-70,41%	-20,38%	-54,12%
AB-InBev	Acquisitions but stay with the old brand name	AB-InBev Controlling Shareholders: 44% Public: 40%	108%	10%	51,98%	69,88%
Campari	Acquisitions but stay with the old brand name	Lagfin: 51% Other: 42%	52%	-38,89%	55,13%	202,87%
Riaktr	Born Global	Investor have control, but co-founders can still block some decisions	Must be around 100% or slightly higher	Decreasing	Increasing	Not relevant

Source: Carrefour website and annual accounts, AB-InBev website and annual accounts, Campari website and annual accounts and interview from Pierre Boël (I do not have numbers due to confidentiality, but I have the trend)

With this table, we have a better view of companies' strategy and KPIs we want to analyze. Indeed, it will help us to compare companies together and find common characteristics for a success or a failure.

Moreover, all these companies are different. Indeed, AB-InBev and Campari have the same entry strategy but their ownership and debt to equity are different. Indeed, looking at the ownership, AB-InBev controlling shareholders do not hold more than 51% of the shares and behind these shareholders, it is not the founder family anymore. Whereas for Campari, the society Lagfin hold 51% of the shares which means that they can take decisions alone. As everyone agrees that Lagfin is a screen company, Campari remains a family business. Moreover, looking at the debt to equity ratio, we can see that Campari tried to decrease it, whereas AB-InBev increased it and its ratio is twice as big as the one of Campari. And to finish with Riaktr, it is a totally different company as it is a new in comparison to the three others. In addition to that, his process was totally different because its strategy was going on the field and presenting their solution to executives.

This analysis will be in two-part, the strategy to enter a foreign market and the debt to equity ratio to finance this strategy. Indeed, they are two keys to the success of internationalization.

5.1 Strategy

Let's begin with the strategy to enter a foreign market. These decisions are very important because a bad strategy can lead to failure even if the financial choices are very good.

As seen in the theoretical part, knowledge and information about the new market is the key. Indeed, in all entry modes, you try to gain as much knowledge as possible to adapt your products or services to the new market behavior. For success, you need a competitive advantage and differentiation, but you have to take into account new customers and competitors' behaviors.

And this is the case for the four companies even if they have adopted different strategies. With the acquisition process, AB-InBev and Campari entered new markets by adding a brand to their portfolio. By doing that, they gained all information and knowledge of the targeted market. Moreover, they did not change the foreign brand name, so that they did not disturb consumers and their behaviors. They may be made some internal changes but from a consumer perspective, in the short-term, nothing changed. In the long-term perspective, maybe AB-InBev, Campari, and all companies that had the same strategy could make some changes but as they owned the

foreign company, they had all the information needed about the new market to make accurate changes and taking into consideration behaviors.

Regarding Carrefour's strategy, it is a bit more complex because they acquired foreign companies to enter a new market, but they wanted to implement the Carrefour's brand in this foreign market. By acting like that, they needed to gain as much knowledge and information as possible to understand new market behaviors because they entered as a new brand in the market and needed to convince consumers to change their behaviors. Indeed, Carrefour's goal was to become a market leader in each country implemented. Even if Carrefour is a big group and tries to get the same level of performance and the same products all around the world, they still need to adapt some products and prices depending on the country.

Regarding Riaktr's strategy, it is totally different because it is a born global company. Indeed, the founders of the company found a solution to improve the performance of telecommunication companies by micro market management. The solution had an impact in countries where behaviors were different depending on the region in the same country and was correct for growing countries. That was why founders went to Africa and traveled to find a first client. By traveling to Africa, they were on the field and it was easier to get information and understand the reality of the field. After the first client, as said before, they made a name for themselves in the industry through word of mouth and that was how they grew in Africa. Moreover, during the interview, Pierre Boël told me that it was not a coincidence if they were performing better in countries where they had an office (South Africa and Brazil). Indeed, being closer to the client also means having a better relationship with them and getting more information about the field.

In conclusion, there is not only one solution for the entry strategy, but they are some factors that are important to take into account. Indeed, the first one is knowledge of the new market. It is really the key point and you will have more chance of success if you know the market in which you will enter. Acquisition of a company in the targeted market is one good solution because you gain all information, network and you are close to clients, but it is not the only solution. Indeed, the acquisition might be expensive. For that reason, entering a new market can be made by exportation, partnerships with local companies or exploring the new market by yourself and gaining information through direct contact, like Riaktr did.

5.2 Impact of the capital structure

The second part of the analysis will deal with the choice of the capital structure and its influence on the ownership and performance.

As we have seen in the theory, the capital structure is made of debt and equity. Moreover, we have seen that debt is cheaper than equity and in addition to that, you do not lose your ownership. Seen like that, when you need money to finance a growth into a new market, you will finance it only with debt which it is cheaper, and you keep control of your company.

But in reality, it is different; you can not finance all your needs by debt. Indeed, there are some factors to take into account to understand why it is impossible.

First of all, banks will not always accept to lend money to all companies, especially young and small. Indeed, banks take their decision by taking into consideration the risks. They assess all risks and calculate if the company will be able to repay its debt, with some interest rate. Evaluation of risks is based on the expected cash-flows and length of the refund. Banks lend easier money to mature companies with certain cash flows than smaller companies with uncertain cash flows, especially when they enter a new market without being sure that internationalization will work. The second aspect of the risks is the length of the debt. Indeed, the more debt is spread over time, the more risk is high that at a given moment, the company is no longer able to pay back. On the opposite, when companies start a new project like internationalization, costs come first, and then in the future, there is some revenue, therefore companies want more time to repay the debt, but banks prefer the opposite.

For Carrefour, AB-InBev and Campari, today, it is easier to borrow money to banks because there are less risks than companies which would not repay their debt. Indeed, these three companies are well-established with certain future cash-flows, even if Carrefour's EBITDA decreased over the last decade.

Whereas, for smaller companies like Riaktr, it is more difficult to lend money to banks. Indeed, during the interview, Pierre Boël told me that it was very difficult during the "super-expansion phase" to borrow money but as it was the cheapest option, they did all they could to borrow as much money as possible. Indeed, he told me that the government pushed firms to export their products as much as possible to develop the economy. So, for small growing companies, the state subsidizes them or become the guarantor of the debt to reassure the banks. He found that it was a good way to borrow money to banks without paying a higher interest rate. But during this "super-expansion phase" they borrowed too much money (by playing a poker game with

banks by saying that future cash-flows were certain but in reality, they were not) and they were focusing more on how they will repay the debt than the core business. This is called financial distress cost. It is a cost that is not taken into a count for the initial cost of debt but in reality, companies can lose money because of it. That was one reason why Riaktr decided to re-balance the net debt to equity ratio. The other reason was that they needed more money to finance their “super-expansion phase”. Indeed, in the beginning, they borrowed one million euros to a bank and this loan was guaranteed by the European Union. But in 2016, they needed more money and that was why they raised 12 million euros. For banks, it is very different to lend one million or 12 million., as they do not lend too much money.

That was the story for Riaktr but Pierre Boël told me that it was a frequent situation for smaller companies to borrow a lot of money until they could not to pay back anymore and then they were asked to invest in their business and then reduce debt to control it when business was more stable. Indeed, except for AB-InBev, the three other companies reduced their net debt to equity ratio. We can make the hypothesis that with the crisis in 2009, they had to borrow money to face this difficult time. In addition, some investors sold their parts in the business, therefore the ratio went up. And then when the crisis was over, companies tried to reduce debt to control it and to pay less interest rate. Indeed, there was a link between annual EBITDA and debt to equity ratio. For all companies, when EBITDA decreased, generally, the same year the debt to equity ratio went up. We can make the hypothesis that, when companies need some money to face a decrease in earnings, they borrow some money to banks and then, when the situation becomes better, they try to reduce it.

A second observation is a link between ownership and debt to equity ratio. As said above, one advantage of the loan is that you do not lose ownership. And we can see that Riaktr tried as much as possible to keep their ownership and therefore their debt to equity ratio was high. It was the same for AB-InBev, controlling shareholders had 44% of the shares. It was not a family company anymore because they sold shares to Brazilian investors, but it was not a direct new investment, it was selling shares without directly increasing the capital.

For Campari, it was different because one company owned 51% of the shares and the debt to equity ratio was low in comparison to other companies. But the company that had the majority of the shares was, in fact, a screen company. Indeed, it was based in Luxembourg to pay lower tax and add more debt to the “real” company. It was a simple process, Lagfin, the screen

company, borrowed money to some banks and then invested in Campari as equity. Then they earned some dividend from Campari and repaid the loan taken. This was a trick to borrow more money because banks would not lend all money to only one company, but they would accept to borrow the same amount to two different companies, which would pay back certainly their loan more.

And then for Carrefour, the situation was different because their debt to equity ratio was lower, but they did not own the company anymore. They had more equity; therefore, they needed less debt and that was why their ratio was lower, but their ownership was also lower.

In conclusion, the choice of debt or equity to finance growth and more precisely an internationalization is really important. Indeed, you can have a good strategy to enter into a new market but with a bad capital structure, it can affect seriously the performance of the company. In theory, the founders of a company want to keep their ownership and find the cheapest way to finance this growth. That is why debt looks like the best solution but as said before banks do not want to take too many risks so they will not lend too much money. Moreover, the more money banks lend, the more risk there is that the company will not be able to reimburse his debt, therefore, interests' rate will be higher. In addition to that, borrowing too much money will add some other cost such as the financial distress cost.

One solution to borrow more money with low interests' rate is to have help from the government by subsidies or government becomes guarantor to make sure the loan will be repaid by the companies or the government.

When the company arrives at a point where it does not want to borrow more money because it will increase costs (via higher interest rate and side costs) or because banks do not want to lend money, the other solution is to ask money to investors to finance your internationalization process. This is a tricky situation because as an owner of the company, you do not want to lose your ownership and pay too much if you raise too much equity. But in the other hand, if you do not raise enough money, it can lead to the failure of all the internationalization process or a new raise of equity but with less bargaining power and the risk of losing more ownership than expected.

6. Conclusions

This thesis analyzed the impact of capital structure on firm's internationalization process. The main objective of the master thesis was to determine the optimal internationalization process for a growing company from a financial perspective, without forgetting the entry's strategy.

We have started the related literature with the capital structure of a company. We have seen that the optimum capital structure is the financial structure that minimizes the Weighted Average Cost of Capital (WACC) and thereby maximizes the value of the company. On the one hand, the debt capital corresponds to borrowed money by the company and its cost is lower than the cost of other sources of financing. In addition, the tax deduction of interest payments significantly reduces the company's debt costs. On the other hand, equity capital represents the company's investment capital. It is the ultimate money, which can not be removed during the firm's existence. The return on dividends paid by shareholders is the opportunity cost of the remaining earnings.

The second part of the related literature was theories about internationalization. First, firm's internationalization is no longer relates to only large firms, but also to medium, small and micro firms. Therefore, new internationalization approaches were developed such as born global, network theory and the Uppsala model. They all have in common the goal to increase knowledge about the targeted market. Then we have developed some entry modes such as exporting (technique to manufacture goods or services in one country and export and deliver them to clients in another), contractual agreements (partners share ideas and expertise through these agreements) and equity joint venture (strategic alliance in which two or more firms create, and jointly own, a new independent organization).

For the practical part, the case study used four financial indicators including, the ownership of the company, the net debt to equity ratio, annual EBITDA and stock price at the end of each year. These indicators helped to understand their impact on the company and his internationalization process.

Four companies were selected for this case study and one interview was made to understand strategic and financial decisions made during the internationalization process of the company. In order to analyze these companies, I assessed them one by one with only facts, and then compared them and finally tried to generalize observations. Moreover, thanks to Pierre Boël,

Chief of Operation Organization at Riaktr, I generalized what is the best internationalization strategy, capital, and ownership structure from a company's point of view.

The results showed that there is a link between the capital structure and the internationalization process's success. As we have seen in the theory, cost of capital affects companies' performances and each company has to find its optimum WACC which is generally difficult to reach because the amount of debt is limited by banks. There is also a link between capital structure and ownership. Indeed, the more the net debt to equity ratio is high, the more founders keep ownership on their companies. Finally, the results show that knowledge of the targeted new market is the key to succeed in the internationalization process. Indeed, it is not a coincidence if all analyzed big companies' strategy to enter a new market is to acquire foreign firms and for Riaktr, they perform better in countries where they have an office.

The master thesis recommends the company to find the best net debt to equity ratio with the minimum cost to maximize the financial performance. Indeed, an internationalization process is costly, even if the debt is cheaper, the company has to find a good balance between net debt and equity to finance the process. Indeed, usually debt can not be the only way to finance an internationalization because bank will not lend enough money, especially for small companies. One solution to borrow more money is to ask help from the government as a guarantor or with subsidizes. But the firm has to take into consideration that too much debt will lead to an increase in direct costs with an increase in interest rate but also indirect cost such as financial distress cost. Moreover, the company has to take into consideration that an exceed of equity will lead to a loss of ownership and increase the cost of capital. Finally, the company has to raise enough money because, with a lack of fund, the whole internationalization process might be compromised, or they should raise more money but this time with less bargaining power and they would lose more ownership.

With a strategy point of view, the master thesis recommends the company to have as much knowledge as possible of the targeted market and to be as close as possible to the new targeted client by acquisition or being on the field.

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8. Annexes

Here is Pierre Boël, Chief of operation at Riaktr, interview. Again, I would like to thank Pierre Boël for his time and expertise he gave me. The goal of the first part of the interview was to get information about Riaktr to compare it with the other companies.

The purpose of the second part was to understand their choices and to generalist it thanks to the third one.

Because of the COVID-19 crisis, this interview has been done by Google Meets, which made it more difficult to interact. Moreover, due to confidentiality, he did not give me any number about ownership, and he did not know exactly the number for the debt to equity ratio and EBITDA but the goal of this study is not to focus on this number but more the evolution and the link between them.

Question 1: What was Riaktr's internationalization history and strategy?

Pierre Boël: There were three phases of internationalization. The first process took place in Africa with MTN because it is there that Riaktr is born. Indeed, the purpose of Riaktr is to manage in real-time the sales and distribution in emerging countries. So, Sebastien and Loïc (the two founders) took their backpack and when in Africa to explore the market and they found the first client MTN. And it was working well, with some expansion in multiple countries, but still with MTN.

The second phase was to expand in other countries and continent, it was the super expansion phase. Indeed, in the telecommunication sector, especially in emerging markets, chiefs go from one country to another, from one company to another and they talk a lot within the company. So, the impression in one country is very important because with the words to mouth, it can go very fast and the expansion has to follow. During this period, Riaktr wanted to growth outside Africa, therefore we went to South-East Asia and South America. But with hindsight, we are performing in countries where we have an office, in South Africa and Brazil. This observation tells me that it was the right choice to take their backpacks and going on the field to meet potential clients and understand their needs. Indeed, their solution was for emerging markets, but they did not really know how it was because Belgium is not an emerging market.

And the third phase came with the failure in some countries and even continent (South East Asia) and there where a focus on Africa. Moreover, there was also the launch of a new product "Smart Capex" in Europe.

Question 2: What was the evolution of the ownership structure?

Pierre Boël: The ownership structure evolution follows the three internationalization phases, especially the first two phases. In the beginning, Sebastien and Loïc created the company. It was a service company at that time. So, they did not really need some capital. It was more or less 50-50 between them. Then, 8 other people invest in the company, but they were also working in the company (I am part of these 8). Loïc and Sebastien kept 60% for them (30% each) and we got 40%.

In 2016, during the super expansion phase, we switched from a service company to a product company (selling software). This switch required a lot of money. Therefore, you ask money to family and friend to invest in your company and at some point, you need to ask some investors to invest in the company. Fortino, Endeit and Ginv invested 12 million euros in our company. Then the big question was the value of the company to determine the new ownership structure. But what is really important is the power at the board of directors, where big decisions are taken. There we succeeded to get more or less 50%. Fortino and Endeit had one seat each, we (the group of ten co-founders) got two and there was one independent remaining seat.

But in 2017, we needed to raise more money and there, with this increase in equity, we have lost the majority. But we really wanted to keep some control. At that point, there were two types of share. For big decision, you need the majority in both type (even if one type is smaller than the other) and we succeeded to keep a majority in the smaller type of shares.

Question 3: What was the evolution of the net debt to equity ratio?

Pierre Boël: Like the ownership structure, there were three phases of the debt to equity evolution. During the first phase, the beginning, as a service company, we did not need a lot of capital, just for the working capital (because in Africa, clients do not always pay on time), so we had just some debt on the short term. It was not significant. You can say that the ratio was more or less zero.

Then in 2014, during the super expansion phase, we needed money to finance this internationalization. Our CEO, Sebastien wanted as much debt as possible because it was cheap, and he did not want to lose ownership. His point of view was; it is cheap, and we do not care about the future because we will succeed and have enough money to pay back loans. He was very confident. But banks did not see it like that. To accept or decline a loan, banks look at cash flows profile. The two main indicators are timing and risk. The timing is when will your cash flow become positive and the risks are, what is the certainty of this expected cash flows. If you

have good timing (cash flow become positive very quickly) and you are certain of this positive cash flow, banks will lend you money. But for Riaktr, it was the opposite. Indeed, we were going to expand a lot of cash flows will be negative at the beginning and there was a lot of uncertainty because Riaktr was a small company. And banks do not like this configuration.

But one solution was the government. Indeed, they help small companies who try to internationalize because they want to export as much as possible. So, they provide two solutions, either by subsidizes, either by the been guarantor that the loan will be paid back. Riaktr chose the second option and the European Union was the guarantor for the loan of 1 million made to Belfius.

With this strategy, the net debt to equity ratio went up quickly. But at some point, it was too high, and it was difficult to pay it back and we had the financial distress cost. It is a cost when you are more focus on how you will pay banks than your core business. Then we arrive in 2016, were investors came with 12 million to rebalance the ratio.

And now during the third phase, we are trying to reduce the debt because we do not want to come back to the previous situation, with difficulties to pay back the debt.

But in general, that is how it works, when you need money, you increase your debt but when everything is under control, you reduce it because it is still a cost even if it is cheap, you can not reduce equity because you can not remove investors like that.

Question 4: What was the evolution of the EBITDA?

Pierre Boël: Like other indicators, there are three same phases. In the beginning, it was slightly positive. As a service company, we were putting the price where we wanted. So basically, it was to cover all cost plus a small margin.

Then with the expansion phase, and the transition to a product company, the EBITDA was negative by some millions due to the cost of research and development.

And now with the third phase, in 2018 we become positive again (about 1 million euros) and we are targeting a continuous and controlled growth.

Question 5: Why had Riaktr done this choice of capital structure? Is there a targeted ratio?

Pierre Boël: I have answered this question before. Our CEO was optimistic and as said before, for him, it was obvious that we would succeed, so there was no problem to borrow a lot of money because we would make a lot of money after and we would have enough to pay it back.

And it was the cheapest way to get money and with the help of the government, it was easier. But it was a risky choice and we have faced the consequences.

Question 6: What was the strategy of the ownership structure?

Pierre Boël: The goal was, of course, to keep as much ownership as possible. When you create a company, you do not want to lose it because you put plenty of work and emotion in it. You do not want to lose control. But at some point, you have to ask money to investors but again, you play poker and negotiate a lot to keep as much control as possible.

Question 7: From a personal point of view and with your experience, what would be the best capital structure for an internationalization process?

Pierre Boël: Let's start from the beginning, and you will see that for a small company, you do not have a lot of choices.

First, entering a new market demand a lot of money and it is risky. Since you need money, you will ask for to banks because it is the cheapest way. But it is risky and so they do not often follow, and you need help from the government. But it is never enough to finance the whole internationalization. So, you need to ask money to investors. And there, you have to negotiate with them to keep as much control as possible because every founder wants to keep control.

So, from a personal perspective, first, you borrow money to banks, the, when you need more money you search for equity, that is the reality. Then when the process is over and you are profitable, you can reduce the debt because you can not reduce equity like that.

In conclusion, small companies prefer debt because it is cheaper and you keep ownership but it is risky and you can arrive at a point where you can not pay back loans and you need to ask money to investors but you are in a bad position so you will lose a lot of ownership. There is the tricky point.