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CAPITAL STRUCTURE OF ENTERPRISES IN THE PROCESS OF INTERNATIONALIZATION

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Purpose: The aim of the article is to define the capital structure in Polish enterprises – in the group of enterprises exporting their products and in the group of enterprises that do not conduct export activities.
Design/methodology/approach: 30 companies representing various sectors of the economy were taken into account for the preliminary research. In the first group of 15 companies that exported their products (the first stage of internationalization), the capital structure was examined, determining the level of financing with equity and foreign capital. The research scheme from the first group was also used in the second examined group – enterprises that do not export their products. Each surveyed group included a company that represented one selected sector. A case study for three Polish listed companies was also used.
Findings: Thus, the view of foreign authors based on the results of their study that, in emerging markets countries, companies that have internationalised their activities have higher levels of indebtedness than companies operating only domestically, should not be considered as confirmed (for the time being on the example of pilot studies).
Originality/value: The results of the preliminary research made it possible to identify the most important differences in the capital structure for companies that exported their products and companies that did not export.

Keywords: capital structure, internationalization, sources of financing.

Category of the paper: Research paper.

1. Introduction

The liberalisation of the world economy is increasing the incentives for companies to internationalise their operations, which is conducive to extending product life cycles, acquiring new technologies and diversifying their sales sphere. In most cases the internationalisation of company is a step-by-step process (following the Upsala model) although there are companies that have found a way to internationalise right form their inception (born global).

Internationalisation of company should be a component of its overall strategy. In turn, capital structure policy is an important element of a company's financial strategy.

The capital structure, its formation and changes occurring in it, have a great impact on the possibilities of financing the enterprises's development, but also directly affects its effectiveness (different capital costs of different sources of financing, the possibility of using tax shield, the limits of acquiring foreging capital, determining the effectiveness of its use). Not only in the scientific literature in Poland, but also in other countries (for example in the English literature), the issue of the relationship between the internationalization of the company and capital structure is quit rarely addressed. Therfore, the aim of this paper is to examine the relationship between capital structure and the internationalisation or non-internationalisation of firms in Poland. The research into the interrelationship between the internationalisation of enterprises and their capital structure commenced in 2021 with pilot studies, the results of which will be presented in this paper. The results of this research should form the basis for the preparation of empirical research, which will be, on a large sample, conducted in 2022. The results of the preliminary research, whose targets were enterprises producing for export, were confronted with the results of the research into the capital structure of enterprises producing for the domestic market. In this way, it is possible to assess whether the internationalisation process influences changes in the capital structure of enterprises under the conditions of the Polish economy. In addition to the survey, three case studies – of companies that have advanced in the internationalisation process - have been prepared on a group of 30 companies.

2. Analysis of existing studies on the internationalisation of enterprises

In reviewing the world literature on internationalisation, it is important to note that studies of the internationalisation processes of companies have largely focused on determining the relationship between internationalisation and the financial performance of the company (Barłożewski, 2017) There have also been studies indicating that profitability declines when the internationalisation process of a company begins – but as foreign direct investment increases and scales, so does the profitability of the company as a whole. The same studies have also shown that exports weaken the relationship between FDI and corporate financial performance, as pursuing a strategy of high exports at the same time as a significant commitment to foreign direct investment (FDI) is less profitable than a strategy of lower exports when the level of FDI is high. Multinational firms often make multiple investments (by forming strategic alliances beforehand) accumulating knowledge and skills – not only in connection with the internationalization of their operations, but also as a result of the cooperation established. A statistical analysis of the overseas expansion decisions made by Japanese manufacturing firms over a period of 35 years showed that the tendency of firms to reinvest in the same host countries was weaker for horizontal investment (i.e. market search), but stronger for vertical investment (i.e. investment to increase efficiency). Research has also been conducted on the links between internationalisation and host country taxes – companies consider the location of their foreign subsidiaries depending on the taxes paid in the host country. The desire for tax savings is related to the relationship between taxes and profitability – the greater the tax savings, the greater the profitability. MNEs can also reduce their tax burden by transferring profits between subsidiaries in different tax jurisdictions/countries through transfer pricing. Research on internationalisation and financial aspects has also raised issues related to defining the stages of corporate internationalisation, namely Johanson and Vahlne's (1977 and 2009) Uppsala model - which assumes a gradual entry of companies into the internationalisation process inspired in part by Aharoni (1966) along with the later concept of Dunning and Lundam (2008). It is noteworthy that other concepts have talked about the possibility of a reversal of this process, i.e. deinternationalization (Welch, Luoristarinen, 1998), as well as the possibility of and Vahlne (2009), Continen, Ojala (2011, 2012). It was also pointed out that there is a need to carry out research to determine the relationship of internationalisation processes with the overall strategy of the company (Frymas, Mellahi, 2011). Some scholars have focused on studying the specifics of this process in emerging markets – which also include Poland, and here it has been pointed out that companies in these countries are trying to reach particular stages of internationalisation more quickly and are mainly aiming to acquire strategic resources and competitive advantages outside the home country (Mathews, 2006; Luo, and Thung, 2007; Hennert, 2012; Kothari, 2013). Research on the relationship between internationalisation and finance also includes studies of the relationship between the foreign investor and the host country, taking into account the motives for internationalisation and incentives used by the host country in relation to the foreign investor, including the theory of special economic zones (Karaszewski, Rymarczyk, Gorynia, Dorożyński), calculating the effectiveness of foreign investment (Różański, Jaworek), the relationship between the progress of internationalisation and the financial performance of enterprises (Barłożewski). There is also a theme of strategies related to international expansion. Some studies explicitly referred to the relationship between capital structure and internationalisation, through:

- examining the debt ratio of multinational firms according to agency theory (Chiung-Jung Chen, Chwo-Ming Joseph, 2011) – multinational corporations in emerging economies, defined as firms with at least one foreign subsidiary or some FDI, have higher debt levels than non-multinational corporations, which contrasts with findings for multinational corporations from developed countries;
- studying the impact of foreign investment and export sophistication on capital structure (Chiung-Jung Chen, Chwo-Ming Joseph, 2011);
- determining the degree of internationalisation of a company in the context of agency costs and capital structure (Hitt, 1997);

- study of capital structure among multinational firms (Hughes, 1975; Shapiro, 1978; Michel, and Shaked, 1986; Fatemi, 1988; Lee, and Kwok, 1988);
- a study of the increase in leverage among firms that internationalise their operations (Chen, 1997; Chkir, and Cosset, 2001)

The research also sought to determine the impact of foreign investment and export sophistication on capital structure – the impact is negative, meaning that costs (e.g. agency costs) increase when firms' international operations become overly complex – the firm reaches successive levels of internationalisation of its business. Research on capital structure among multinationals used multiple regression analysis using measures of international activity for firms that internationalise their operations, while comparing them with results for domestic firms. Based on 18,495 observations – 1) multinationals have lower debt-to-equity ratios than domestic firms, 2) in multinational companies, the debt-to-equity ratio is positively related to the degree of internationalisation. In the study of leverage growth among companies that internationalize, an event study was conducted that compared corporate leverage before and after the acquisition of foreign subsidiaries. The level of leverage increases from the first to the third year after the acquisition. It turns out that in addition to such important determinants as size and profitability, debt financing is explained by geographical and industrial diversification effects. The literature also draws attention to the increasing role of technology platforms (knowledge platforms), linking the thread of digitalization to the complementarity of capital and non-capital forms of expansion of foreign transnational corporations (Palulska, Poniatowska-Jaksch, 2021). It is also necessary to point out the appearance of a historical thread relating to the expansion of foreign capital on Polish soil, where the authors indicated that already from the 19th century, through the interwar period, until now (with a clear weakening of this trend in the period of socialist economy in Poland) foreign expansion continued, with sometimes very high amounts of foreign capital (Jaworek, Karaszewski, 2020). Another theme concerns the relationship between international expansion and the type of enterprises, thus supporting development through international expansion and the special role of internationalization of enterprises operating in the area of advanced technologies – on the example of Polish enterprises (Cieślik, 2014). Thus, the role of entrepreneurship and innovation in creating global leaders among Polish enterprises, which have strongly internationalized their activities, is relevant here. Therefore, it was considered purposeful to study the relationship between capital structure and internationalisation also in Polish enterprises.

3. Results of pilot studies conducted in 30 Polish enterprises

A pilot survey was conducted in 2021 to answer the question:
Is there any relationship between an enterprise's capital structure and its openness to foreign markets (or lack thereof) - on the example of Polish enterprises?

30 enterprises were selected, matched in pairs so that one represented a specific manufacturing sector or provided services exclusively to the country, and the other was an established exporter in that sector. The following sectors were selected: manufacture of building materials, manufacture of footwear, metalworking, manufacture of clothing, manufacture of windows and doors, manufacture of textiles, manufacture of electrical engineering products, manufacture of fabricated metal products, manufacture of wood products, manufacture of paper products, agriculture, printing services, transport services. The enterprises represented very different economic sectors. Pairs of enterprises were selected, characterised by similar parameters (size, structure of production or services, history and time of operation), but differing clearly by the feature of export/non-export. In this way the comparability of research objects was ensured. The results of the research will provide an opportunity to design basic research, which will enable confrontation with the results of research teams from outside Poland, undertaking this subject. By performing a collective assessment of the sources of financing of the 30 enterprises studied on a pilot basis, it was found that in 2015-2019, both in enterprises producing for the domestic market and in exporting enterprises, the primary source of financing with equity was retained earnings, and with foreign capital – bank credit and leasing. This is documented in the table below.

Table 1.
Sources of financing for enterprises

Companies	2015	2016	2017	2018	2019
1. Producing for the internal market					
• retained earnings	13	13	13	13	13
• credit	5	5	5	5	5
• lease	6	6	7	6	5
• other own	2	2	3	3	3
2. Exporting companies					
• retained earnings	14	14	14	14	14
• credit	6	6	6	6	6
• lease	6	6	6	5	5
• other own	1	1	1	1	1

Source: survey conducted on behalf of the authors by Biostat.

Thus, we are dealing with a fairly traditional capital structure (retained earnings, bank credit, leasing) that occurs regardless of whether the company exports or produces (services) exclusively for the domestic market.

There were, of course, some differences in funding sources from year to year, for example:

- a company producing and exporting footwear financed itself in 2015-2016 by leasing and in subsequent years by bank credit,
- a company producing windows and doors for export was supported by third-party financing in the form of working capital credit and leasing between 2015 and 2016, and only by leasing from 2017 onwards,
- a company producing metal products for export financed itself through leasing in 2015-2016, in subsequent years it abandoned foreign capital,
- a company exporting food products financed itself with working capital credit and leasing in 2015-2016 and abandoned credit in subsequent years,
- a company operating in the agricultural sector, producing, among others, for export, in 2015 benefited from EU funds, in subsequent years additionally supported by a bank loan.

The existing changes in the financing system of these enterprises, as can easily be seen, were undertaken by exporting enterprises, while enterprises producing or providing services for the domestic market presented virtually unchanged policies for financing their activities. Very mixed responses were given to the question, "What are the plans for the capital structure over the next 5 years?" Of the 30 companies surveyed, the vast majority declared that they did not want to make any changes to the company's financing system, motivating this most often by the uncertainty of the situation, e.g. in relation to pandemics, changes in interest rates, many uncertainties related to future operations. Statistically speaking:

- 8 companies declared that they were afraid to use foreign capital and would continue to use equity,
- 7 companies intend to use credit and 8 companies leasing.

In a few cases it was planned to use:

- financing from liabilities to suppliers – 2 replies,
- EU funding – 2 replies.

As many as 9 respondents declared a complete lack of plans for the future, in terms of shaping the capital structure. It is difficult to find a significant relationship between the sector of economic activity and the company's policy related to the future formation of the capital structure – two companies from the same sector represent a completely different approach – for example, two shoe or clothing companies, the first do not want to plan anything, the second have crystallized views on future financing.

Examples of advanced internationalisation of Polish enterprises – KGHM, LPP, Agat – case studies. In addition to companies that have stopped at the first phase (export) in the internationalisation process, there are of course companies that have reached subsequent phases of the process. Three companies were selected which were characterised by varying degrees of progress in the internationalisation process. The company that achieved the most is undoubtedly

Kombinat Górniczo-Hutniczy KGHM SA, which created its own subsidiaries abroad, entered into joint-ventures with foreign entities, took over foreign companies – the scale of these activities was (and is) very large. LPP, in turn, which operates in the clothing industry, has internationalised its activity mainly through a strongly developed distribution network covering many countries of the world (through 25 foreign companies). The Agat company, on the other hand, opened one foreign subsidiary (in Berlin), which can be considered the beginning of a process of further internationalisation. By comparing the capital structures of these three enterprises, which are at different stages of the internationalisation processes, and by comparing these structures with the structures of enterprises that only exported or produced for the domestic market, it is possible to answer the question of whether, under the conditions of the Polish economy, capital structures are in any way related to the internationalisation of the enterprise.

Case: Capital expansion of KGHM Polska Miedź SA

KGHM is a mining and smelting company, which was founded in 1961. Its activities are focused on the production of copper, precious metals and other non-ferrous metals. Since 1991, KGHM has been a joint stock company, and since 1997 it has been listed on the Warsaw Stock Exchange and is included in the WIG 20 index.

It is one of the largest Polish exporters and the main employer in Lower Silesia. It holds shares in over 20 entities, including telecommunications, trade, production, construction, transport, scientific and research companies, etc.

In June 2009 the company KGHM HMS Bergban AG was established in Berlin, in which KGHM holds 75.1% of the shares. The company is engaged in the exploration and exploitation of copper ore deposits and other mines in Europe.

In May 2010, KGHM signed an investment agreement with Vancouver-based Abacus Mining and Exploration Corporation (AMEC) on the joint realisation of a copper and gold mining project in the Canadian province of British Columbia. KGHM contributed USD 37 million to the joint venture formed with Abacus, giving it a 51% stake. KGHM undertook to finance capital expenditures related to the project in the amount of USD 535m. In addition, KGHM purchased 15 million shares in Abacus for USD 4.5 million.

In 2012, KGHM acquired the Canadian company Quadra FNX. Quadra, apart from the copper and silver mines, had mines of molybdenum, platinum, palladium and gold – located in Canada, the US and Chile. The purchase price was PLN 9.5bn. KGHM financed the purchase entirely from its own funds.

Following the addition of the Canadian company, copper production at KGHM increased by 18% compared to 2011. Quadra FNX was transformed into KGHM International. The existing staff was retained, the existing operating plans and their implementation were confirmed, actions were taken to ensure the value of the acquisition (achieving synergies, lowering the unit cost of mining, exchanging best practices) and to ensure control in key areas (cash management, procurement).

A key case in point is the Sierra Gorda mine in Chile – where lowering the unit cost of production is very difficult (high energy costs, lack of workers and lack of water).

KGHM made 40 acquisitions between 2005 and 2015 for a total value of USD 3584.8 million.

Without the purchase of Quadra and access to new deposits, particularly in Chile, it would be difficult for KGHM to achieve further growth.

KGHM is the world's third largest copper mining company in terms of revenue and return on assets (ROA), and fourth in terms of return on equity (ROE). The investment programme for 2014-2020 cost PLN 27bn.

Diversification of activities (e.g. construction of a photovoltaic factory) is to strengthen the company's already strong position on global markets.

Table 2.
The capital structure of the joint-stock company KGHM

Capital structure	2015	2016	2017	2018	2019
Equity	20 211 000	15 772 000	17 694 000	19 133 000	20 110 000
Liabilities and provisions for liabilities	16 350 000	17 531 000	16 337 000	18 012 000	19 207 000
Share of equity in total equity	55%	47%	52%	52%	51%
Share of outside capital in total equity	45%	53%	48%	48%	49%

Source: own compilation based on KGHM's financial reports for the years 2015-2019.

Between 2015 and 2019, KGHM had a fairly balanced capital structure, i.e. the proportion of equity and debt capital was close to a 1:1 ratio, with some predominance of debt capital. This relationship persisted, despite the fact that during this period KGHM pursued an ambitious investment programme (as already mentioned, PLN 27 billion was invested between 2014 and 2020). The very good economic results mean that the majority of capital expenditure is made using equity, which allows the Company to maintain a capital structure similar to the model (1:1). It should be mentioned that the latest investment intention is to participate in an investment involving the construction of small nuclear reactors in Poland, which will strengthen the already very strong position of KGHM not only on the Polish market, but also on global markets.

Case: Internationalisation of LPP

LPP is a Polish family-owned company involved in designing, manufacturing and distribution of clothing. The company was established in 1991 as a limited liability company and in 1995 it was transformed into a joint stock company. LPP SA Capital Group consists of 5 domestic companies (including the parent company) and 25 foreign companies. Foreign companies of the Group are mostly entities engaged in distribution of products of all brands outside Poland. Currently, the sales network covers the whole of Poland, countries of Central, Eastern and Western Europe, the Balkans and the Middle East. The company does not have its own factories. As a result, individual pieces of the collection are produced in factories specialising in specific types of clothing. According to the company's report for 2019/2020, no single supplier accounted for more than 5% of total purchases. Most orders came from China 36.4%, Bangladesh 31.4%, Turkey 7.1%, Cambodia 6.1%, Myanmar 6.0%. Poland accounts for 2.5% of all orders. Products are offered to customers in stationary and online shops, in a total of 39 countries on 3 continents. The stationary sales network consists of 1,746 shops with a total area of 1,230.9 thousand m2. In its online form, LPP currently operates on 30 markets. Its sales offer includes: clothing, accessories and footwear of five brands: Reserved, Cropp, House, Mohito and Sinsay. Currently LPP operates on 39 markets. The most important location of the company's activity is Gdańsk. The company also has offices in Krakow, Warsaw, Shanghai and Dhaka. The team of employees totals about 25,000 people in offices and sales and distribution structures in Poland, European and Asian countries. The research period covers the years 2015-2019. In connection with the research period of the entire study, an analogous analysis of the LPP company's activity and the most important strategic activities that occurred during that time was conducted. In 2015, the Reserved brand debuted in Egypt, the same year the first shop opened in Qatar and Kuwait. September also saw the launch of new shops in Saudi Arabia. In 2016, the company launched its 1,000th store in Poland and continued to expand in Germany. At the same time, focusing on e-commerce development. At the same time, in Poland all brands of the LPP company have online shops. In 2017. LPP opened a Reserved store in London, Belarus and Serbia. In 2018, the company's founders, in order to ensure its long-term continuity and avoid future fragmentation of LPP's capital, decided to establish a foundation and contribute the shares they hold there (footnote). In 2019. LPP strengthened its position in the Balkans and launched a showroom of its 5 brands in Bosnia and Herzegovina. In October 2019, the company also launched showrooms of its 5 brands in Finland. In 2020, due to the pandemic, LPP transformed its business into an omnichannel organisation[1].

Table 3.

The capital structure of the joint-stock company LPP

Capital structure	2015	2016	2017	2018	2019
Equity	1 889 739	2 134 731	2 443 446	2 860 553	3 247 491
Liabilities and provisions for liabilities	1 675 430	1 543 201	1 763 373	2 520 255	6 358 371
Share of equity in total equity	53%	58%	58%	53%	34%
Share of outside capital in total equity	47%	42%	42%	47%	66%

Source: own compilation based on company financial data for 2015-2019.

Analysing the capital structure of LPP, in 2015-2019 that the company in 2015-2018 recorded a certain predominance of equity over foreign capital, while in 2019 we already have a clear predominance of foreign capital, which is related to the acceleration of the process of development of the distribution network outside Poland.

[1] It is an interaction using a variety of integrated channels between the seller and the customer, guaranteeing multi-channel sales. The use of this business model helps to increase the company's reach. The most important assumption of the omnichannel strategy is the permeation of individual sales channels.

Case: Internationalisation of the Agat Joint Stock Company

The pilot study used more precise data obtained in the enterprise "Agat" S.A. based in Koluszki – to present the relationship between the early phase of internationalization of the enterprise and its capital structure.

The Agat company is a large company operating as a joint stock company specialising in:

- civil engineering works and construction of buildings,
- telecommunications and power lines,
- industrial pipelines and distribution stations,
- roads, motorways, railways and underground railways,
- steerable drilling,
- industrial automation,
- construction of a sewage treatment plant.

The company started its activities in 1990 as a limited liability company and in 2008 it was transformed into a joint stock company. The company forms a capital group with the following shareholdings:

- Achat Infrastruktur GmbH in Berlin – speciality construction services – company founded in 2015, 100% of Agat shares,
- Agat IT S.A., 74% owned by Agat – in Łódź, company active in the field of IT, telecommunication, industrial automation, logistics and low voltage installations – 74% owned by Agat, active since 2005,
- Przedsiębiorstwo Budownictwa Inżynieryjnego S.A. in Piotrków, construction of industrial buildings, roads and bridges, 55% stake in Agat, founded in 2009,
- Przedsiębiorstwo Inżynierii Środowiska i Melioracji "Piomel " S.A. in Piotrków, "Agat" purchased 100% of shares in 2010,
- KB Pomorze, sp. z. o. o. Gdańsk – construction of fuel tanks and process water pipelines, established in 2003 – 40.32% of shares.

The financial situation of the company is good. Sales revenues have been growing – from over PLN 128 million in 2016 to 148 million in 2019 (only a decrease in the level was recorded in 2017). Stable profits on sales from 2016 PLN 3.6 million to approximately PLN 4.3 million in 2019 (negative result in 2017). Revenue in 2020 – approx. 270 million PLN. It should be pointed out that the structure of the Company's sources of financing is fairly stable between 2015 and 2019. The data is contained in the table below.

Table 4.
The capital structure of the joint-stock company Agat

	2015	2016	2017	2018	2019
Own sources					
retained earnings	6.535	6.557	-3.780	4.311	3.123
redemption fund	1.299	1.437	1.586	1.626	1.847
External sources					
bank loan	6.000	6.000	6.000	6.000	6.000
leasing	2,8	-	-	-	783
share of equity	0,56	0,57	0,21	0,49	0,42
share of outside capital	0,44	0,43	0,79	0,51	0,58

Source: Agat internal materials.

The other items included in the analysis were not filled in, as "Agat" did not use such sources of financing as:

- issue of shares and bonds,
- venture capital and related funds,
- other (for example, grants).

It should be noted that the foreign subsidiary of the Agat enterprise accounts for only about 2% of the total turnover, so its impact on the sources of financing is small, as can be seen by analysing the data in the table. There are two main sources of funding:

- retained earnings (supported by the depreciation fund),
- a revolving overdraft facility, with a fixed limit for its use.

Leasing has been recognised as a complementary source of third-party financing, but it is only from 2019 that this source has been confirmed as an important form of financing for the Company – making it necessary to increase the scale of leasing in future years. In addition, the Agat company does not expect to make any fundamental changes to its capital structure in the next 5 years. Thus, the low degree of internationalisation of Agat's operations – despite the fact that the company owns 100% of shares in a foreign company, so we are already dealing here with a process of internationalisation going further than the classic export of goods and services – means that internationalisation has no impact on the development of the capital structure and will probably continue to do so in the coming years, as the company has announced.

4. Conclusion

The conducted pilot study allowed us to notice the occurrence of certain regularities in the formation of the capital structure of enterprises.

1) Companies producing (or providing services) exclusively for the domestic market are most willing to finance themselves with own capital (retained earnings) sometimes giving up foreign capital altogether (about half of the cases). Other companies use bank

credit, or leasing, or both sources of external financing at the same time. In the case of these companies we are dealing with a very traditional capital structure (retained earnings, credit and leasing), in which, however, external capital plays an important role.

2) Companies producing for export more often use foreign sources of financing, however these are most often also credit and leasing. Only 2 companies in this group did not use foreign capital. Thus a balanced relationship between equity and debt can be observed here, but with a slight predominance of equity.
3) Companies that have moved on to further stages of the internationalisation process also pursue a rather cautious policy related to raising foreign capital, but in most cases trying to maintain a balance between financing their activities with equity and foreign capital. A clear prevalence of foreign capital could only be recorded in 2019 in LPP, and in 2017 in the Company "Agat", but here due to the net loss incurred (clear prevalence of financing with foreign capital).

Noteworthy, in all cases studied, is the high stability of the sources of financing during the period studied. Thus, the view of foreign authors based on the results of their study that, in emerging markets countries, companies that have internationalised their activities have higher levels of indebtedness than companies operating only domestically, should not be considered as confirmed (for the time being on the example of pilot studies). Undoubtedly, extending the time horizon of the research and covering a larger number of enterprises with surveys, interviews and identification of available reporting data will allow for a broader analysis of the explored topic.

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