

# Czech automobile industry: analysis



In consecutive years 2002-2004, in Europe Czech Republic is one of the country which secured more automotive R&D projects and for accounting 20.2% of manufacturing output, for Czech exports 20.2% in 2007 and in automotive sector there are over 120,000 employees which is half of world's top fifty component manufacturers which is considered as the powerful engine for Czech economy (Czech Business Info, 2009). Furthermore it is given that Skoda combined with Hyundai new plant and Toyota/PSA will be soon producing 1,200,000 cars annually (Czech Invest, 2010). Czech Republic ranked 14th position in EU when compared to central and eastern European countries and its growth rate in automotive parts sector is increased to 7% compared to other segments in Czech (Czech automobile industry, 2010).

By considering the changes and continuous development in automotive parts sector, several factors are interlinked with market entry modes based upon market entry strategy. To evaluate and analyse the complexity associated with the factors through the prism of strengths and weakness in the future prospect of view PESTEL (political, economical, social, technological, legal, competition, currency) analysis is done (Lee & Carter, 2009). PESTEL analysis is a structure of macro environmental factors that will help the firm to know the markets situations in the CZ that are recommending for its international investors (see appendix 1). From the analysis it shows the favourable conditions to invest and also shows the increased growth of production in automotive parts sector in CZ. The economy of CZ is stable and conventional, the country is investing more in high manufacturing and technological sectors which indeed offers excellent potentials due to its rich

heritage and strongly supported by government aid programmes (Czech Invest, 2010). As a member in European Union, its location that is in central Europe, it has highly skilled labour, high quality and innovative technology, advanced infrastructure are the key factors attracting the firms to invest in CZ (Czech economy, 2010).

The choice of entry modes represents one of the most important strategic decisions for foreign MNEs whose desire to enter into emerging economies like Czech Republic. For automotive parts sector high resource commitment and proficiency human knowledge is essential. According to Tallman and Shenker, 1994 nature of market, operating cost and competition should be weighed against the firm's cost integration versus profit which determines the level of risk in CZ automotive part sector control, flexibility and level of involvement (Lee and Carter, 2009). For direct investment factors like level of involvement, speed of entry, flexibility and risk is high but the returns will also be high. The level of risk for shared and controlled MNE's is medium.

### **Corporate objectives and resources:**

Corporate objectives in automobile industry could be met but not easily. Automobile parts sector can be set up in CZ but it involves more investment and high cost.

The factors are evaluated and analysed as follows: Source: Tallman and Shenkar, 1994

### **Level of Involvement:**

Because of the lively environment in automobile sector, the level of control and risk is high. The level of investments and risk is high for the companies

in automotive sector so it is likely to involve in shared and wholly controlled mode.

### **Level of Risk and Control:**

A high resource commitment is required for a firm investing in automotive parts sector. The level of risk is medium for shared and controlled mode. The level of risk is high and investment is more for fully controlled mode.

### **Speed of Entry:**

Automotive sector is highly competitive so it's better to grab the initiative rather than late. The companies must adapt advance technology, must understand the customer's needs according to the market situations.

### **Nature of market, competition etc...**

In Czech in last 10 years maximum investments can be seen in automotive parts sector. The main competitors in automobile industry in Czech are Skoda, Toyota / TPCA, Hyundai and KIA. Market entry modes depend upon the level of competition in automotive parts industry.

### **Market entry mode**

Pay back: The payback period of initial investment in automotive industry is about four years (Czech Invest, 2010). When we compared with jointly owned mode the return of investment would be higher.

### **Flexibility:**

High resource commitments and proficiency knowledge is required in the fields of automotive sector. Choosing CZ will help firm to export to central

and eastern European countries as it is strategically located in central Europe.

### **Investment and market cost:**

The investment and market cost will be high in automotive industry. The firms in automotive industry is more and its makes product differentiation challenging and leads to extra market cost

### **Administrative requirements:**

Some of the administrative requirements in CZ are highly skilled labour, advanced technology, infrastructure and affordable property costs.

Firms whose desire is to invest in automobile industry sector can use Eclectic theory because of selection of location. Further more in detailed can be explained by considering the example of Volks Wagon a Germany company took the control over Skoda in CZ in the year 2001(presentation on Skoda). For exporting their products to eastern and central Europe VW used eclectic theory. They gained ownership advantage due to 100% acquisition but also by maintaining good technology, quality, financial and marketing variables. By considering these factors they gained local advantage and positioned subsidiaries in a place which is ready for automobile market such as Central and Eastern Europe.

## **Principal Market Entry Modes:**

**Market oriented**

**Contractual**

**Shared Owned and Controlled**

**Wholly Owned and Fully controlled**

Direct Exporting

Agents

Distributors

E commerce

E business

Interactive TV

Licensing

Contract Manufacture

Franchising

Alliance

Management service

Contracts

Joint ventures

Partial mergers and acquisitions

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Subsidiaries

Representatives

Assembly

Indirect Exporting

Via domestic

Organisation

Trading companies

Export houses

Piggy Backing

Low Level of involvement high

Low Level of Risk and Control high

Source: Lee & Carter, 2009

The firms whose desire to invest in automotive parts sector in CZ will be appropriate in adapting towards wholly owned and fully control of subsidiaries than the representatives of every other entry modes. For any MEMs, during the selection of entry mode, it is necessary to briefly review the preeminent role of control that may best suits to them. It is advised to companies which invest in automotive industry to be operated in full control because in fully control mode the level of involvement of resources will be high and it will go through high levels of risk and allows it to gain high

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returns on investment. Especially to entering into automotive parts industry into emerging markets like CZ these forms of entry modes are suitable to sell with in the country and to central and eastern European countries. Market entry modes varies depending upon the operations in specific countries for instance, VWs shared ownership make to take over the operations in Prague thereby signalling switch towards wholly and fully controlled mode (See Appendix 2).

According dunning (2000) firms in automotive parts sector in CZ market they will adopt Bargaining power and Eclectic theory. In bargaining power the level of investment and commitment of resources are high and it also involves high level of risk and return on investment is high (Dunning, 2000). Firms adapting bargaining power approach, the government of the host country provide subsidies in form of tax reductions, location of plant, the riskiness of investment etc. According to Taylor, Zou and Osland (2000) explained that BP starts from the premise that firm preferred for a high control market entry mode because it is the desirable outcome in terms of firms long term ability to dominate a foreign market.

### **Culture Issues while Doing Business In Czech:**

Interesting cross cultures challenges occurs when a firm desires to do business with and in foreign countries. Cultural issues vary from country to country and a firm has to be very careful while investing in foreign countries. For instance consider the example such as business deals go wrong because of over culturally insensitive actions. In international business context a firm can maximize its potentials by adapting appropriate culture of that particular



country such as appreciating a country cultural nuances, protocol etc (Czech Business, 2010).

Czech Republic needs to be viewed as transitional economy which in process the economy is moving from state controlled centrally planned economy to more Anglo style capitalist model. One of the strongest legacies of the former Soviet-style system is in the area of trust in the business environment (Semerak, 2010). Czech business culture mainly focuses or emphasise on developing deep levels of trust within business relationship. According Czech people the distrust in business starts when they engage with in new contact and the mistrust can be broken through time and proving a trust worthy associate. From the above the key message while doing business in Czech is needed to be patience and trying to do much quickly, faster will result in counterproductive(Czech Business, 2010).

The key issue in Czech business environment is people from different generations where we can expect different attitudes to business issues. Older generation people are mainly influenced by soviet style system whereas younger generation who are well educated, come into work after many changes are influenced by western business methods(Czech Business, 2010). Czech are considered to be cautious while getting into new business deals and the main intention of the initial business meetings is to know each other and reserved culture of Czech initially perceived to be cold but they are actually warm and hospitable people.

Some of the tips to while setting up a business in Czech Republic

The Czech Republic is an economy which is still on a journey which is running towards a free market approach. But it is still on progress. The business environment still suffers from the legacy of the old system.

In Czech society we can find potential generational division, older generation are more influenced by old soviet style whereas younger generation are more open and influenced by entrepreneurial approach. When dealings are made with older generation we can expect to encounter a hierarchical approach where decisions are made at the top of the organizations.

Punctuality is the sign of a serious professional.

Due to the inherent suspicion in Czech Republic, try to keep teams together over long periods of time.

(Source : World business Culture, 2010)

Finally we can say that a firm has to do a careful study on culture and if he follows the above mentioned guidelines while setting up the business in Czech he will be benefited.

## APPENDIX 1

PESTEL Analysis on CZ Automobile parts sector industry

Market Environment

Description

### **Political Factors**

(Czech automobile industry, 2010;

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www. vlada. cz, 2010)

Democratic government combined with steady laws, human rights, protection, value and respect for minorities and one of most advanced new EU members(Czech economy , 2010)

According to CIA Czech is considered as one of most stable and prosperous country of Eastern and Central European countries (CIA, 2010).

Government provides incentives for investments and tax exemptions (Czech automobile industry, 2009).

Job creation, training and retraining grants.

## **Socio – Economic Factors**

(Czech invest, 2010 ; lecture by Anna Klosova, 2010)

Land area is 78, 864 km (Czech invest, 2010).

Population is about 10. 4 million (Czech invest. 2010).

Labour force is about 5. 7 million (Anna Klosova, 2010)

Growth in GDP is 2% (Czech invest, 2010).

Unemployment rate 8. 5% (Czech invest, 2010).

Nationalities in Czech: CZ 81. 2%, Slovak 3. 1%, Polish 0. 6%, Gypsy 0. 3%, Silesian 13% and other 0. 2% (Czech economy, 2010).

Gross wages: 24000 CZK (Anna Klosova, 2010).

Inflation rate of CZ is 1.1% (Czech invest, 2010)

Internet users ('000): 5,970.36 (euro monitor international, 2009)

Highly skilled labour force (Czech invest, 2010)

Good transport system (The Prague Post, 2009)

## **Currency**

(Czech statistical office, 2010)

As per Exchanges rates on July 12th, 2010.

1 GBP = 29.6436 CZK

1 USD = 18.8123 CZK

1 EUR = 24.7629 CZK

(Source: XE – Worlds favourite currency site)

Flexible exchange system.

Czech currency (koruna) is easily convertible. All international transfers are carried out without any delays (factbook.net, 2010)

## **Legal Factors**

(Czech invest, 2010)

Intellectual property protection (Czech invest, 2010)

Foreign legal entities and other states from EU can acquire real estate in CZ without any restrictions where same conditions is applicable to local legal entities (Fact book. net, 2010).

According CZ laws and regulations domestic and foreign entities are treated equally in all parts of the country (Czech economy, 2010)

Laws and regulations are subjected to EU

## **Competition**

(Skoda presentation, 2010; Czech Trade , 2010 )

Strong competition from countries like Poland, Slovakia and Hungary.

Major competitors in Czech automobile industry Skoda 52. 3%, TCSA 13%, Hyundai 10% and Kia 10% (Skoda presentation, 2010).

High number of automobile manufactures (Czech trade, 2010).

## **Technological Factors**

(Automobile Industry in Czech, 2010)

High quality and advanced infra structure (Czech invest, 2010)

Advance technology in automotive industry (Czech automobile industry, 2010)

Increased investments in R&D departments.

## **APPENDIX 2**

MEMs

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Resource

Commitment

Level of

Control

Level of

Involvement

Return on investment

Agency approach (Carney and Gedajlovic, 1991) Uppsala (Stopfort and Wells, 1972)

Exporting

Very low

Very low

Very low

Very low

Industrial network approach (Whitelock, 2002)

joint ventures

Shared Owned and controlled

Medium

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Medium

High

Medium

Medium

High

Medium

Medium

High

Medium

Medium

High

Partial mergers

Shared Owned and controlled

Eclectic theory or Contingency approach (Dunning, 1998)

Acquisitions

Wholly owned and fully controlled