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Interim Report IR-00-071/December

Economic co-operation across the Finnish-Russian border - factors of sluggish development and success of enterprises

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December 2000

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Abstract

The post-Cold War era in Europe in the 1990s has caused people to recognize the complexity of economic development and economic co-operation. The opening of borders has not always meant an increase in the cross-border economic activities in general. On the contrary, the adverse socio-economic development of many border areas has been unanticipated. The Finnish-Russian border is one example of this dissonance.

This paper analyses the operation of Finnish companies in economic activities in Russia during the 1990s. The study investigates barriers to the Finnish-Russian trade, economic co-operation and foreign direct investment (FDI). A micro level approach is applied aiming to find out what is the role of institutions, mental boundaries and pure economic factors in this border-crossing development process.

The authors have chosen the mining company Pechenganickel and its employees in two Russian mining towns on the Kola Peninsula, Nikel and Zapolyarnyj, as their case study objects for the research. The employees in Nikel and Pechenga are very conducive to foreign co-operation. Mental barriers are low, at least compared with the outlook of Finns to Russians.

The economic activities of two Finnish companies in Russia have been studied. One of the case study companies, Outokumpu, has operated as a supplier of technological know-how to Russia and has investigated various investment projects there. The strategy has been cautious and no acquisitions or notable FDI have been executed.

Institutionalists blame high bureaucracy and complicated custom regulations for the low level of cross-border trade and co-operation. Are there more important causes beyond those factors? Is it just lacking demand and the disadvantageous location of economic activities, which matter in border areas? Such argument can be supported as well. This is illustrated by the success of the Baltic Beverage Holding AB (BBH). This beer producer has a market share of 23 per cent in Russia and 40-50 per cent in the Baltic States, and the growth continues. BBH's success proves that in certain fields and markets there are no insuperable institutional barriers for foreign companies in the economies of those countries.

The study concludes that the main causes for sluggish development in many sectors seem to be demand-driven and structural (and spatio-structural). The collapse of the former economic system brought about such a deep and unanticipated decline that not all the companies could properly cope with. Nevertheless, the study shows that there is potential for trade and FDI to Russia in the future.

Acknowledgments

This report has been written within the cross-border co-operation framework of the Economic Transition and Integration Project at IIASA. The interest within the project for economic interactions between the EU countries and Russia made this study possible. We would like to express our gratitude to those who have contributed to the completion of this paper. These are ETI project leader, János Gács and Vesa's colleague at IIASA, Guzel Tulegenova. We are also grateful to the other persons who have given their time and effort to assist us in concluding this study.

This study is a part of the project "The impact of intelligent mining technology on regional structures, housing and family-life", financed by the Academy of Finland, decisions 60201, 46372, 64510.

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1. Introduction

1.1 Transition and border

During the Soviet era the economic activities between Finland and the Soviet Union were strictly controlled by the governments. Cross-border trade was handled by a clearing system, and unlike most Western countries Finland continued to maintain this kind of bilateral trade until the collapse of the Soviet Union. The trade between Finland and the Soviet Union was notable, especially for Finland (25 per cent of the foreign trade in 1982-1983), but individuals and entrepreneurs had very few direct cross-border contacts. After the collapse of the Soviet Union in 1991 Russia was re-established, and at the end of the same year president Yeltsin announced that the government would start its radical reform which was going to transfer Russia from a centrally managed economy to a market economy. President Yeltsin also promised to reduce the power of central hierarchy in Moscow in a favor of regions. These statements by Yeltsin raised vast hopes for genuine cross-border co-operation, for example, in Finland, which has a 1269 kilometers long borderline with Russia.

After the collapse of the Soviet Union the expectations towards newborn eastern markets were overestimated and too hopeful (Ollila 1999, 27). This was the case also in Finland and especially in the border areas (North Karelia, Kainuu and Lapland) which constitute the Finnish outback (or less-favored areas), afflicted by unemployment, lack of investments and business innovations. New eastern market area was hoped to be an answer to many of these structural problems in Finland, at least in the long run. Entrepreneurs, together with the public sector, commenced several new business and education projects to be able to take advantage of the opportunities in the Russian markets. The transition process of Russia to a market economy was hoped to happen in a few years time.

Following the collapse of the communist system in 1989-1991 the emergence of new states in Europe and simultaneously the enlargement of the European Union has not been an unproblematic process. Political crises, even wars, in Europe in the 1990s have proven the complexity of human territoriality. The opening of borders has not, in many cases, meant, for example, increase in cross-border social or economic activities (such as trade, flows of people and capital or foreign direct investments). On the

contrary, in many border areas socio-economic development has been unexpectedly slow and even for the worse. Except for the transit traffic and its positive spin-offs in the Southeast, the situation on the Finnish-Russian border is one example of this kind of sluggish economic relations. For example, in spite of the high hopes the share of enterprises in Northern Finland which has managed to create stabilized business relations to Russia is less that 5 per cent (Ollila 1999, 51).

Currently, there are in Europe 49 independent countries and several economic and political regions, which means that Europe is full of both new and old borders. The post-Cold War era has led to various attempts to lower the formal barriers of trade created by borders. These attempts have originated from economic aims, but if a state or trade border vanishes, what will happen to mental and social boundaries? The Finnish-Soviet border was one example of the deep ideological and economic divides between the East and West. During the 1990s, the political environment changed and direct business contacts between enterprises increased. The Soviet legacy, however, still remained. Russian companies succeed to export only raw materials, as they did in the Soviet time. This has led to the concentration of trade into a few companies. For example, between the Republic of Karelia and Finland in 1995 half of the export from Karelia was by three enterprises (Statistic Finland 3/98, 29).

Borders are often results of wars and turmoil, and they do not vanish at once, as it is the case in the Finnish-Russian border. All places and regions, as well as their borders, are very much human constructs. That is, places are constructed out of particular interactions and mutual articulations of social relations, experiences and understandings (Massey 1993, 67). Social processes produce various types of borders, and people perceive these borders differently. This emergence of socially constructed borders has also taken place in communities along the Finnish-Russian border. The border question has thus a strong mental dimension. How does it influence the development potential of the border areas? Does it explain sluggish development?

1.2 Aims of this paper

Our purpose in this paper is to analyze how the recent economic interaction (trade, FDI and co-operation between enterprises) between Finland and Russia has developed and how this co-operation has succeeded. In addition, we will analyze the development of the Finnish/Nordic enterprises in the Russian business environment and the problems of Russian enterprises in the light of possible co-operation. A special focus is on the problems of sluggish development in the border area.

The argumentation is based on two types of reasoning. First, the sluggish development of the economic co-operation in areas, such as Karelia and the Murmansk Oblast, is explained by differences in formal institutions and past socio-economic structures. For example, foreign enterprises in Russia still have no trust in legislation (especially in the enforcement of it) or in taxation. Several studies have proved that institutional and political reasons play an important role in explaining the trends of trade, business co-operation and FDI between Finland and Russia (Sutela 1996; Kosonen 1997). Ambiguous legislation was considered as the most important obstacle to cross-border co-operation among entrepreneurs in Lapland (Granberg & Ollila 1998). Nevertheless, this explanation is not exhaustive. Are there any more important causes beyond the experienced bureaucracy? Is it just lacking demand and the disadvantageous

location of economic activities which matter. Such argument can be supported as well. This is illustrated by the success of Baltic Beverage Holding AB (BBH). The reader will see that one of the case studies to be presented below show that a foreign owned firm, the BBH, has successfully developed business in Russia, despite the usual institutional and regulatory impediments.

Second, if formal institutions are a cause, what about the people? What are their attitudes to economic co-operation? Does the border matter and to whom? Do the attitudes of employees reflect institutional barriers and to what extent? To answer these questions, this research investigates the attitudes of employees of the Pechenganickel mining company which operates in two towns of the Murmansk Oblast, Nikel and Zapolyarnyj, in the vicinity of the Norwegian-Russian border.

The economic development on the both sides of the border has not corresponded either to the expectations of entrepreneurs, or to the theories of economic interaction, such as the growth triangle theory (Kivikari & Lindström 1999), the theories of globalization (Dunning 1997), or the integration theory (Dunning & Robson 1988). There is not much support from models of industrial (re)location and development, either (Chapman & Walker 1992). As a theoretical aim our purpose in this study is to find out the reasons for this mismatch between such theories and the evidence.

The Russian conditions of development have been difficult to conceptualize empirically compared with the conditions in market economies, and to study within the framework of theoretical models of economics and economic geography. This study is grounded on the case-study approach and the amalgamation of several single studies. Some simple statistical analyses have been applied. The focus is on the role of behavior and institutions at the micro level.

1.3 Nikel and Zapolyarnyj and the Finnish-Russian border

Zapolyarnyj and Nikel (see Fig. 1) are industrial towns near the Russian-Norwegian border in Murmansk Oblast. The industrial base of these towns consists of nickel production operated by the Kola Metallurgical and Mining Company (KMMC), which is a subsidiary of the large multilocal mining company of RAO Norilsk Nickel in Russia. Norilsk Nickel is the largest nickel and palladium producer, as well as the second largest platinum producer in the world. KMMC consists of two large companies on the Kola Peninsula, Pechenganickel and Severonickel. The latter is located in Monchegorsk. In the early 2000, the conglomerate employed 93 000, of which 75 000 were in Norilsk, 7 500 in Zapolyarnyj and Nikel, 7 000 in Monchegorsk and a few thousand in Olenegorsk and St. Petersburg.

Administratively the towns of Nikel and Zapolyarnyj belong to the Pechenga District (Fig.1). Currently these mining towns are facing restructuring problems - there are too much labour force, and the industrial capital equipment dates back several decades. Foreign partnership and collaboration have been considered as one alternative for relieving restructuring problems. These restructuring problems have brought to light the importance of international co-operation, foreign companies and borders.

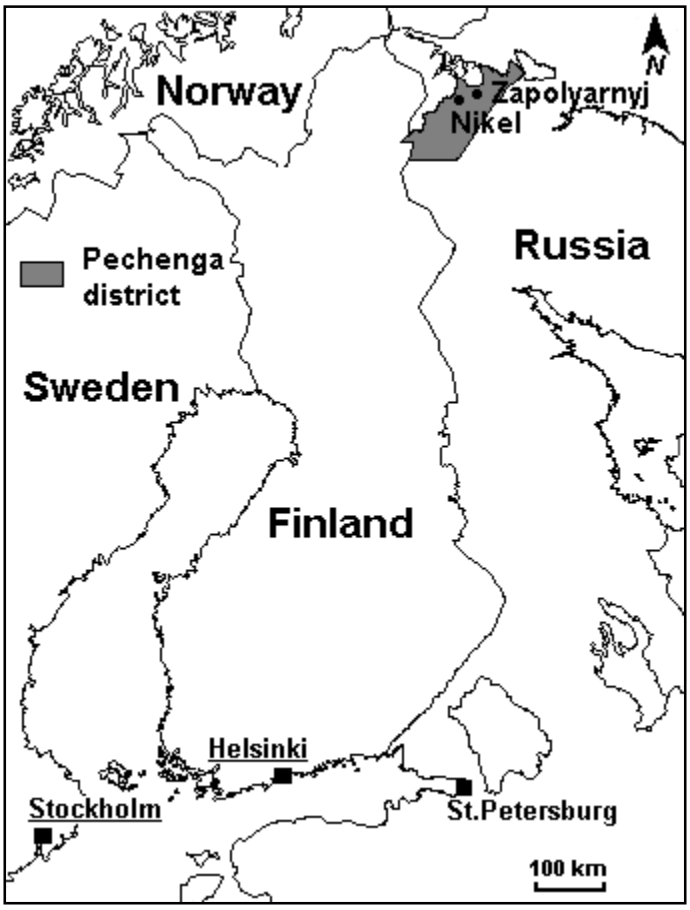


Figure 1. The mining towns Nikel and Zapolyarnyj in Kola Peninsula. Pechenga District in grey.

In the Soviet Union, industry was highly centralized and politically controlled. Industrial production was planned and organized from top to bottom. The goal was to industrialize and urbanize the whole country. Nickel production and the geographical position of the Kola Peninsula were also important from the military point of view. The mining towns in Pechenga district were part of this centrally organized production and defense system.

The regions of Russia opened up administratively in the 1990s. For example, the Murmansk Oblast commenced to practice, at least at some level, its own foreign policy during the 1990s. The Oblast participates in the Barents Region co-operation, which aims to create a common economic and cultural region in the European north. The Barents Region includes northern provinces of Norway, Sweden, Finland, and Russia. In addition, several other countries and the EU are acting as observer members of this regional co-operation. Although the results of this new northern regional co-operation are quite insignificant, it has created direct contacts for the administration of Murmansk with the Nordic countries and Brussels. During the Soviet era, the regions had very few, if any, direct regional foreign co-operations.

1.4 Research methods

The questions listed in Section 1.2 will be examined mainly by case studies from both sides of the border. The empirical work includes case studies among workers in the mining towns and interviews and secondary data obtained from Finnish enterprises that acquired experiences in the Russian business environment during the 1990s. The potential of trade has been analyzed by a concise statistical analysis.

As the main case, the study analyses a survey from two mining communities, Nikel and Zapolyarnyj, on the Kola Peninsula. The survey comprises interviews with 813 mining workers. The main aim of these interviews was to find out attitudes of workers towards international co-operation and globalization. The authors have also included historical and political features to get deeper understanding of the development of the region and interviewed workers' attitudes towards foreign co-operation. In addition, several Russian public sector authorities were interviewed to find out their aims towards international co-operation.

After the collapse of the Soviet Union the residents of Nikel and Zapolyarnyj lost their ties to the central administration and they concretely became dependent on the company. This meant that the only safety net of welfare services was based on the benevolence of the mining company Norilsk Nickel. On the other hand, the mining company is highly dependent on its workers. For example, the company is already worried about getting capable labor force in the future to its peripheral production areas (Kamkin 1998; Kotlyar 1999). Therefore, Norilsk Nickel is behaving as a welfare state within a state. It is offering such social services to its workers that in advanced socio-economic conditions are provided by the public sector and service companies. The company is cautious, for example, with its labor force downsizing policy. Because of this dependency and the costs of labor turnover the social dimension of development is taken into account in the decision making and future planning of the company. Hence, it is important for the company to know about workers' attitudes and expectations towards restructuring and the participation of the company in the increasing globalization which, in part, made it possible for our project to interview people in these single industry towns.

The mining industry in Russia has faced the decline of domestic market and the international competition in the 1990s. During the Soviet era almost the whole ore production was directed to the domestic markets. By contrast, nowadays, for example, Pechenganickel exports more than 90 per cent of its nickel and copper production (Fleming UCB 1999, 3). Consequently, Pechenganickel has to cope with the consequences of the cyclical world markets (Andreev, Rautio and Tykkyläinen 2000). While, in the Soviet era, Pechenganickel was mainly concentrating on increasing its production figures, now the company must cut down production costs to be able to stay in the global mining business. Furthermore, to improve its competitiveness, the company has carried out investment projects and joint ventures with foreign companies. Therefore, we include in our study interviews with mining managers that help to investigate their experiences and aims towards these new contacts.

Experiences of the Finnish companies in the Russian markets have been of great interest for several researchers (for example Hirvensalo 1996, 1999; Salmi 2000; Törnroos and Nieminen 1999). These studies have analyzed, for example, market relationships, the market entry process, and the operational and financial strategies of Finnish companies in Russia and Eastern Europe. The case studies presented in this

paper concern one Nordic company (Baltic Beverage Holding AB) and one Finnish company (Outokumpu Oyj). The latter has a long experience in the Russian markets inasmuch as Outokumpu operated in the Soviet Union. These companies represent two types of co-operation: 1) resource-based heavy industry which was traditionally prioritized during the Soviet time, and 2) the penetration of a foreign company to consumer markets in metropolitan environments.

The level of trade and foreign direct investments between Finland and Russia (especially the neighboring areas) is analyzed by investigating the trends as well as by making comparisons in the trade figures between Finland and the Soviet Union. Although, the Finnish-Soviet trade was bilateral clearing trade and it was highly politicized, the comparison is justified, because Russia is economically the most important state succeeding the USSR. The comparisons are also partly made by applying the gravity model of international trade which is used by several economists to identify especially the trade potential between two countries (for example Holzmann and Zukowska-Gagelmann 1998). However, it is important to notice that to explain the trade to or from Russia by using the gravity model is problematic, for example, because of its abstract nature.

1.5 Theoretical background

According to many standard geographical and economic theories, the differences in costs, profits and the prices of production factors gradually become evened out when the border between two economic systems disappears. As a reaction to the outflow of capital and jobs, high-cost areas develop dynamic competence. However, this assumption of convergence is not obvious and not the only possible scenario. For instance, the relations between USA and Mexico (land border area) and Russia and Japan (sea border area) are examples of different kinds of (un-)development. Even in relatively homogeneous socio-economic conditions (same language, national identity, culture, and similar locational attributes, etc.) the economic convergence takes time as the case of new *Bundesländer* in Germany indicates.

The volume of trade between Finland and Russia has varied in the course of time reflecting political and institutional differences between the countries. Between 1809-1917 Finland was a part of Russia and the trade was boosted by the growth of St. Petersburg and the growth of the Russian economy. Socialism was introduced in the Soviet Union and the political and trade relations between the capitalist Finland and its neighbor were not intense at all. The post World War II interaction was based on bilateral trade agreements, and when the Soviet Union collapsed, trade declined because the Finnish companies did not have the advantage of fixed prices and planned markets brought by former agreements. Figure 2 shows the long cycles of trade reflecting the political eras: 1) integration, 2) separation, 3) co-operation and 4) competition.

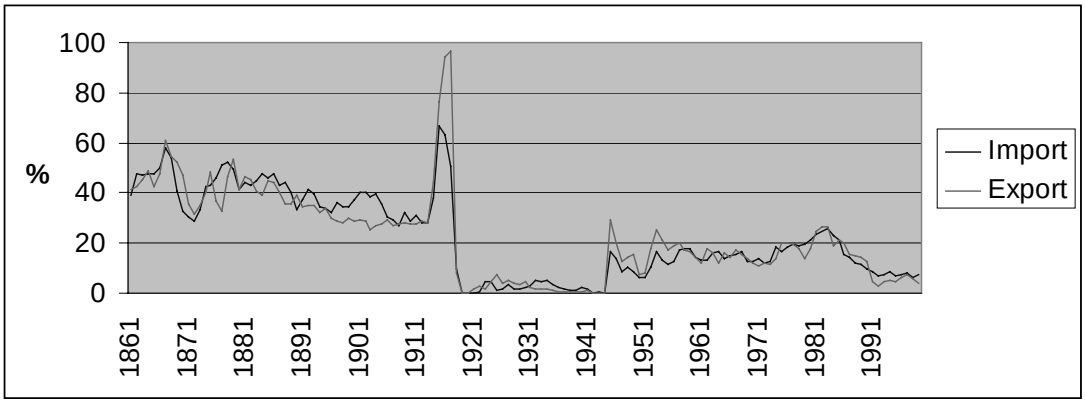


Figure 2. Russia's/Soviet Union's share of Finland's (up to 1917 Finland was Grand Duchy of Russia) import and export in 1861-1999 (Rautava 1998, 6. Updated in 2000).

When the era of competition (and the opening up of Russia) commenced, there were many expectations of the reconstruction of Russian production systems in co-operation with foreign companies. This led to the expectation of the rapid convergence of Russian and market economies. The convergence of diverse economic systems is possible when barriers to the flow of commodities and capital are lowered. For instance, when a favorable business environment is created: 1) marked differences in wages are anticipated to lead to a flow of industrial capital to a low-cost area (in order to utilize low-wage labor); 2) the opening of a border creates possibilities for investment flows to move to low-cost and natural resources areas; and finally, 3) the out-datedness of industrial capital is expected to lead to replacement investments.

As shown, it is easy to find theoretical arguments for the expectations of increasing interaction between Finland and Russia, and especially at the Finnish-Russian border territories. Nevertheless, no part of this reasoning has been proved to be true. On the contrary, the economic development in the 1990s, in terms of output and employment growth, has been very negative.

The decline of the economies of the Russian North and Northwest indicates that many parts of the resource-based economy there are non-competitive. The restructuring of these industries took place very slowly in the 1990s. Various explanations have been offered as reasons for this economic stagnation in Russia. Institutional and political factors, for example, taxes, custom tariffs and trade regulations, have been regarded as crucial in this decline (Sutela 1996; Kosonen 1997; Tykkyläinen & Jussila 1998; Granberg & Ollila 1998). The structures of economy did not fit in the principles of market economy. As a result, demand declined and the oversupply of needless production prevailed. The extensive use of non-cash modes of payment, massive tax and wage arrears, and the mutual indebtedness of companies led in the 1990s to a very inefficient economy (Gaddy & Ickes 1999). However, the recent development shows that the Russian economy has passed the bottom of depression. The share of barter trade in the Russian economy is declining (Bank of Finland 2000), for example, Norilsk Nickel has managed to get rid of its barter transactions (Fleming UCB 1999, 11).

The problem of a suitable politico-institutional milieu for the economic environment in Russia has impacts on the development of the border areas, such as Murmansk Oblast and Karelian Republic. Although the border between the states is no longer so inaccessible, the socio-economic systems in both countries, i.e. in Finland and

Russia, are still different. From the economic standpoint, although the Russian human capital is well educated, the entire socio-economic system has only few suitable attributes which fit well to a market economy. Thus, the total labor related costs are not as low as the nominal wages indicate. This is especially the case in the Russian North. One may also blame the regulation of the economy, which turns attention again to the issues of institutions within Russian society – the embedded ways of thinking and reasoning. One example of these protectionist regulations in the Russian legislation is the requirement that foreign companies must carry out their projects mainly by using Russian labor and equipment (for example, in the oil business the Russian share must be at least 70 per cent). Nevertheless, these institutionalist and regulation-theoretical perspectives do not fully explain all the development. There are successful cases, despite the existing institutions.

2. Changing Geographies of the Finnish-Russian Border

2.1 Pechenga District

At the beginning of the 20th century the Pechenga, consisting of mountains, a valley, and a fjord, was still so called no man's land in the Russian North. In the Peace Treaty of Tartu in 1920 the Pechenga was annexed by Finland. At the beginning of the Finnish period, Pechenga was seen as an untouched arctic territory which tempted especially artists and researchers for expeditions. However, this romanticized period was ended during the 1930s, when nickel ore was found. Pechenga experienced rapid construction phase which led, of course, to colonization. The number of inhabitants in Pechenga was tripled during the 1930s (Onnela 1999, 105). At that time, the superpowers of Europe, the Soviet Union, Germany, and England, started to express their demands towards the nickel ore of Pechenga. Actually, from the early 1940s Finland had to try balance these demands and to export most of the production, in spite that the domestic demand was sufficient to absorb the production.

The World War II changed again the fate of the Pechenga. During the Winter War (1939-1940) the region was occupied by the Soviet troops, but it was unexpectedly handed over to Finland in the peace agreement. The reason for this action by Stalin was probably the interest of England towards the region (Vahtola 1999, 303). Therefore, Finland was able to continue the interrupted construction work. However, the Continuation war (1941-1944) between Finland (this time together with Germany) and the Soviet Union ended the Finnish period in Pechenga, all the people who had moved to Pechenga earlier were evacuated (Kälkäjä 1999).

After the war massive reconstruction projects were commenced on the Pechenga area. Retreating troops had destroyed industrial premises and dwellings, and now reconstruction was mainly done by soldiers and prisoners (Kiseljov & Kiseljova 1995, 147). After the war, the demand for nickel in the Soviet Union was high which entailed that Pechenga was rebuilt in a few years. At the end of 1945 the town of Nikel had already 7000 inhabitants, and in the middle of the 1950s the new town of Zapolyarnyj was built close to the new ore deposits about 30 kilometers from Nikel (Kiseljov 1999). Russians have constructed industrial premises, houses, roads, railways and an airport within the mining area. Only a couple of dwelling houses were left from the Finnish era.

The Pechenga District, as the whole Murmansk Oblast, can be seen as a product of the Soviet era (Hansen and Tønnessen 1998, 31). Part of its urban network was built for exploitation of the ore reserves and to produce metals and minerals for the needs of the Soviet Union. In addition, the Murmansk Oblast was, and still is, an important military area. Military bases are mainly situated in the northern parts of Murmansk Oblast (Fig. 3). Murmansk is a very important harbor. More than 80 per cent of the inhabitants live in urban agglomerations.

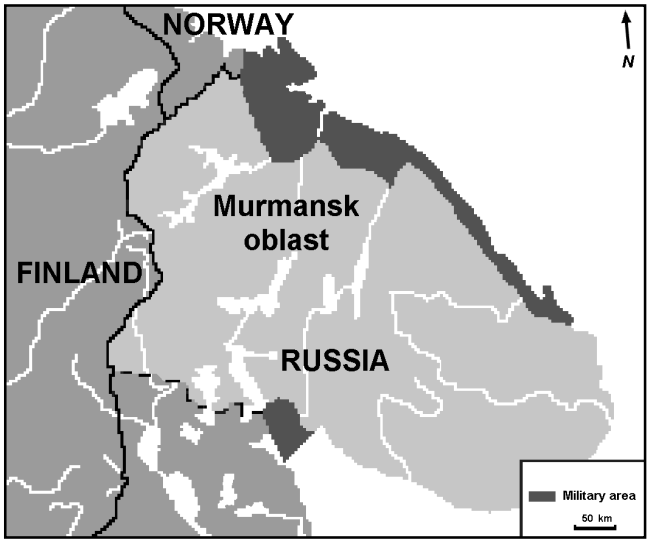


Figure 3. Military areas of the Murmansk Oblast.

The natural environment of Pechenga has been damaged badly, because of the mining industry. Until the end of the 1970s, the annual sulfur oxide emission of the Pechenganickel smelter in the city of Nikel was 400 000 tons, which was subsequently lowered to 250 000 tons (Blatov 1992, 3). In the whole Murmansk oblast an estimated area of 8 100 hectares is damaged beyond rehabilitation, caused by the mining industry (Kotova and Nikitina 1998, 553).

Environmental problems are an important impetus for the modernization of the mining activities from the viewpoint of Finland and Norway. Since the Soviet Union collapsed in 1991 the Pechenga District became accessible via the Storskog crossing point from Norway. The era of closed towns was over. Pechenga became linked to the West.

2.2 Finnish-Soviet trade

After the World War II the Finnish-Soviet economic relations were commenced by reparations and trade. Already at the end of 1940s export from Finland to the Soviet Union was more than 20 per cent of the total exports (Statistic Finland 3/1998, 6). This bilateral clearing trade was balanced by the governments.

Trade was hierarchically handled from top to bottom which supposed that enterprises in Finland had to have a license for the export. This led to a high level of

bureaucracy and trade dominated by large-scale firms. For example, in 1989 the total number of Finnish exporters to the Soviet Union was 1 688, but more than 50 per cent of the total Finnish export to the Soviet Union was handled by the 10 largest export enterprises (Laitila 1995, 107). In the Finnish-Soviet trade the SME sector had mainly the role of subcontractors.

One of the peculiarities of this kind of trade was that there were no cross-border money transfers. The central banks, the Bank of Finland and Gosbank (later VTB and VEB) signed a clearing agreement and through their accounts these organizations kept the trade in balance. Excess exports could be balanced only by increasing imports (Laitila 1995, 75). However, the non-marketable attributes of the Soviet products made it difficult to find products for import. Consequently, Finland was mainly able to import raw materials, energy, and oil. When, for example, the oil prices went down the balance of Finnish-Soviet trade was difficult to achieve. Therefore, for example in the 1980s Finland exported several years consecutively more than imported, which meant that Russia inherited debts from this Finnish-Soviet clearing trade after the collapse of the Soviet Union.

The Finnish-Russian trade was stabilized near to the level of 20 per cent of the total Finnish foreign trade until the beginning of the 1990s. The collapse of the Soviet Union crashed this trade and brought about a severe crisis for various industries in the Finnish economy. At the end of the 1980s the share of the Finnish foreign trade to the Soviet Union was about 15 per cent and suddenly it decreased to around 5 per cent. This brought about the loss of 150 000 jobs and about 2 per cent decline of the total output of Finland (Rautava & Hukkinen 1992, 5). During the 1990s Finnish foreign trade to Russia recovered, but the collapse of rouble in August 1998 caused again difficulties (fig. 4). Immediately after the rouble crisis, in September 1998, the Finnish exports dropped to less than a half, from August, and the bottom was reached in January 1999 (Finnish National Board of Customs, 2000). Concerning the FDI figures, the crisis had even more dramatic consequences.

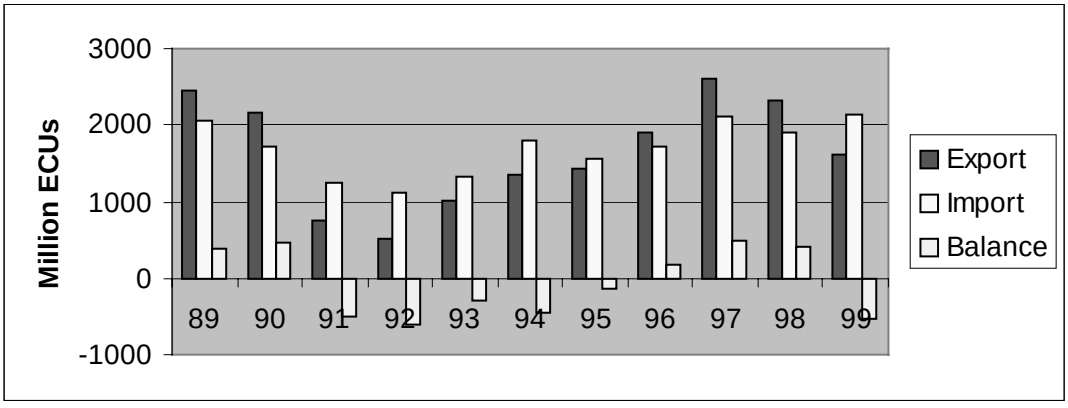


Figure 4. Finnish export and import to Russia/Soviet Union 1989-1999 (Finnish National Board of Customs, 2000).

2.3 East of the Border: Finnish mindscapes and economic opportunities

After World War II the Finnish-Soviet border changed dramatically. In the peace agreement in 1944 Finland lost three regions, Karelia, Salla and Pechenga (Fig. 5). Especially, the Karelian case was, and still is, painful for the Finns. Approximately 420 000 people (11 per cent of the country's population) migrated from the ceded territories to Finland and resettled. A discussion about the restitution of Karelia started after the Cold War. The Northern regions, Salla and Pechenga, have not caused this kind of debate, mainly because those regions were sparsely populated during the Finnish period. In addition, the landscape changes, especially in Pechenga have caused mixed feelings in the former Finnish residents during their visits to the region (Autere 1989).

Figure 5. Areas ceded to the Soviet Union after World War II.

Territories beyond the Russian northern land border with Finland were almost inaccessible before the collapse of the Soviet Union. The Pechenga District was one of these closed regions. What Finns had kept in their minds were nostalgic memories of the ceded Karelia, Salla and Pechenga, propaganda from the war times and talks about Siberia as the pre-1917 destination of convicts. The last-mentioned era consists of reminiscences from the time of Finnish Autonomy, 1809-1917. Russia's image among the Finnish people is not very positive (EVA 1993, 56-80).

The Finnish-Russian border has been the divide between East and West since the World War I, and even for before that (Medvedev 1998). During the Cold War the Russian North and Siberia were tacit and secret territories for laymen, but they constituted an economic area which was economically important for the Finns. The

high-latitude zone of Russia was, and had actually been already before the time of the Soviet Union, a source of raw wood, oil, gas, and minerals. The Finnish companies supplied a great deal of the machinery installed in saw mills, pulp and paper mills, mines and smelters in the northern territories. Those areas were chiefly platforms for all-Union companies – not regions in the European sense. The northern parts of Russia were only mentioned in consignment notes of deliveries to somewhere in Russia.

Everything changed in 1990. Access to Murmansk Oblast, Karelia and Leningrad Oblast was no longer restricted and strictly controlled, and possibilities to do business across the border commenced. Already before *perestroika*, border-trade was conducted in barter form between Finnish and Russian companies, but the volume was small. The openings in the early 1990s made it possible for both companies and individuals to conduct business. State organizations as middlemen disappeared, and no bilateral agreements regulated trade any more. Based on expectations of vast markets and resources on the 'other' side, there was great enthusiasm in Finland not only to visit the Russian border territories, but also to commence business. But when the economic decline continued in Russia, almost the entire 1990s turned out to be an economic disappointment.

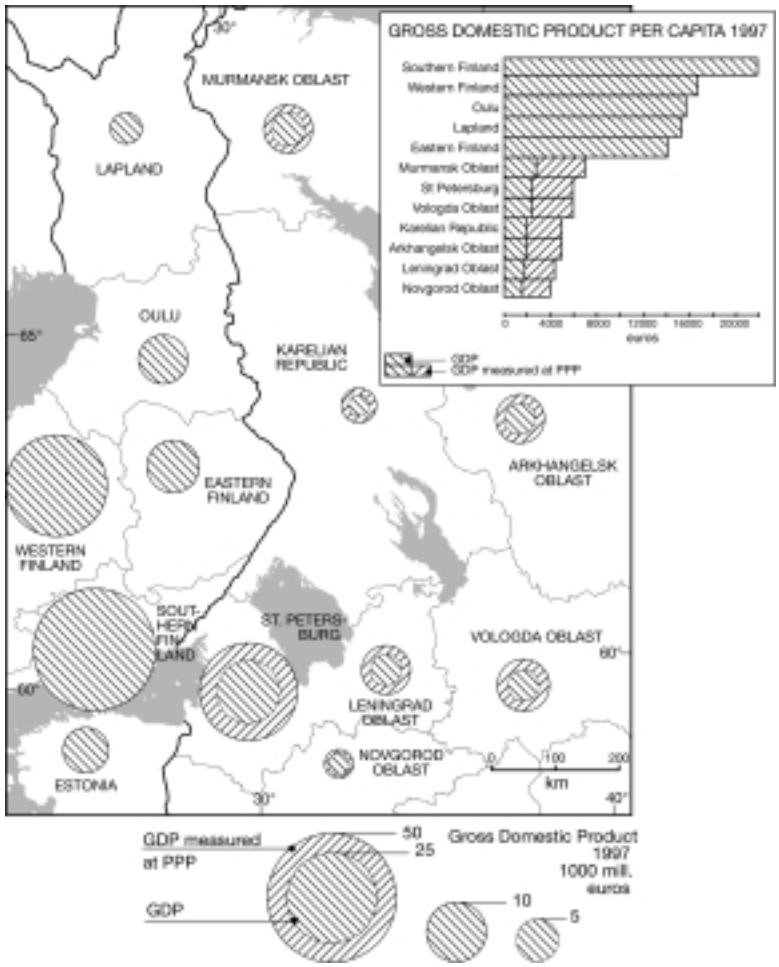
Before 1990, people had even less cross-border contacts on the Soviet side of the border. The border area was strictly controlled and displacements of population in Stalin's Soviet Union braked the former contacts. For example, in the Pechenga District, local people had no contacts to the Finnish side and there are very few signs kept from the Finnish period. The official history of the region does not tell very much about the Finnish period. For example, the local museum only shows that the region was freed from the Nazis by the Soviet troops. Likewise, even the newest brochure of the mining company Norilsk Nickel claims that the region used to be part of Norway (Norilsk Nickel 1999).

During the 1990s cross-border contacts between the northern parts of Finland and Russia have mainly been flows of goods and small-scale tourism. The exports from Murmansk Oblast have been metals to international markets and fish to Norway, while Karelia has exported roundwood and iron ore to Finland. Investments in factories on the Russian side have been negligible. There were expectations that they could partake in the construction of an industrial base in the Russian North and Northwest, but these plans have not been carried through. This has clearly been a disappointment for the companies which delivered machinery to the East as well as for companies which expected that the opening up of the border will boost investments into the border areas.

2.4 Differences between Finland and neighboring regions of Russia

During the Cold War, the borderline between Finland and the Soviet Union was part of the Iron Curtain which separated the East and the West. This borderline separated two worlds which had different economies, culture, politics, language, and hegemonic essence. At the beginning of the 1990s the opening of the Finnish-Russian border made people to realize that this border comprised one of the biggest economic gaps in the relatively limited geographic area of the whole world. During the 1990s this gap became even wider (Fig. 6 and 7). In addition, the gap is not only in GDP per capita, but the difference is huge also in the quality of life. For example, the life expectancy in Leningrad area is about 15 years less than in Finland (Kivikari &

Lindström 1999, 86). In Pechenga District the situation is even worse because of the harsh conditions.



Figures 6 and 7. Gross Domestic Product (GDP) and GDP per capita measured at official exchange rates and Purchasing Power Parity (PPP) by region in 1997. Sources: Statistics Finland (1999, p. 102), and www.stat.fi, Regional Accounts, Table 2.10, December 1999.

One of the reasons for the increase of the gap can be found in the process of transition. The economic turmoil in Russia has meant a huge crisis to the domestic markets which has led to the collapse of output and particularly the industrial production (Fig. 8). One of the transition factors was that in the beginning of the 1990s Russian industry was forced to face global competition which was a new kind of reality to the formerly central controlled and mainly in domestic markets operated industry. It took few years before, for example, the Russian mining industry realized that instead of increasing the production figures they should concentrate to cut the costs and improve the quality of their products to be competitive (Rantanen 2000).

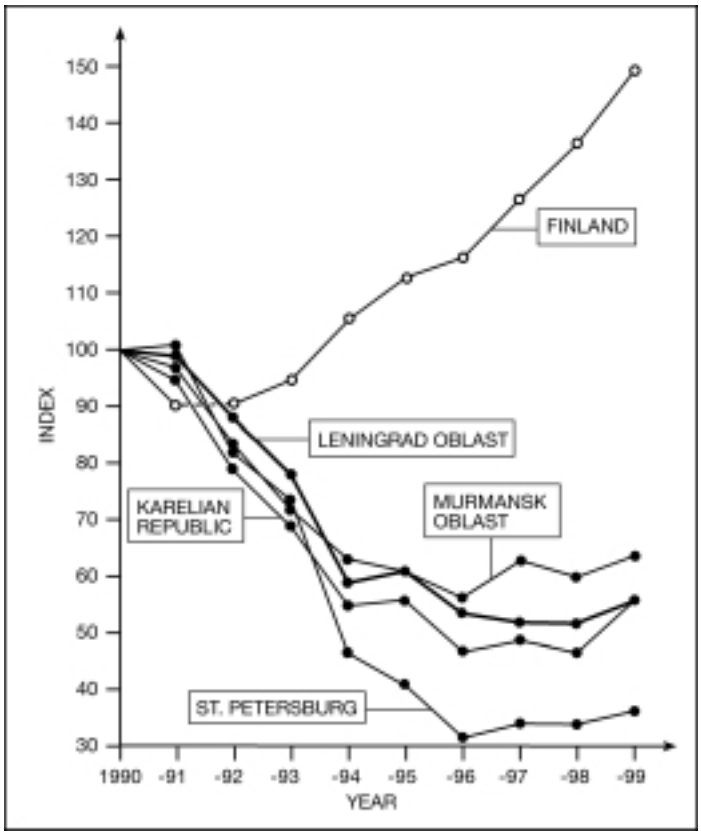


Figure 8. Industrial production (1990=100). Sources: Statistics Finland (2000), *STV*, and unpublished data from Statistics Finland.

The gap in the Gross Domestic Product per capita between a Russian region and the neighboring landregion of another country is the widest in the northernmost land border territories of Russia (Murmansk Oblast, Karelian Republic, and Leningrad Oblast). Table 1 depicts the economic situation in these border territories. As it turns out, the resource-based Karelia and the Murmansk Oblast are relatively wealthy and export-oriented, but unemployment figures indicate that there are structural problems (Table 1; cf. van Selm 1998). Leningrad Oblast and St. Petersburg seem to benefit much more from foreign investments than Karelia and Murmansk Oblast do. Industrial production in all these regions has been recovering after the 1998 devaluation (Table 1).

Table 1. Economic and social indicators in 1997-1999.

Region	Population as percentage of the Russian total	Un-employment, per cent	Monthly, income per earner, USD	Foreign investments per capita (stock), USD	Industrial production, percentage change on a year-by-year basis
Murmansk Oblast					
1997	0.700	18.5	232	3	13
1998	0.691	21.0	105	10	-4
1999	0.682	16.5	150	15	5
Karelian Republic					
1997	0.529	11.9	184	5	1
1998	0.528	16.6	59	6	-3
1999	0.526	15.8	90	21	21
Leningrad Oblast					
1997	1.138	12.8	113	102	-4
1998	1.143	15.0	36	114	-0
1999	1.146	14.5	58	172	8
St. Petersburg					
1997	3.240	9.9	183	49	7
1998	3.228	11.3	59	87	-0
1999	3.223	11.1	114	148	7
Russian Federation					
1997	100	11.8	173	83	2
1998	100	13.3	59	80	-5
1999	100	11.7	59	65	8

Sources: Computed by the author from data in Statistics Finland (2000) and from IBS-service (Statistics Finland); data originate from Goskomstat Rossii.

3. Finnish trade and FDI to Russia

3.1 Finnish-Russian trade

In this section the Finnish-Russian trade potential are estimated by using the gravity model. Two economist, Tinbergen and Pöyhönen developed the gravity model, in the 1960s. The model is applied to predict the potential of trade between two

countries. The equation of the simplest version of the model includes only GDP figures and the distance of two countries. The model assumes that trade is positively related to the level of GDP in both countries and inversely to the physical distance of the countries. More sophisticated versions include more variables like population figures, cultural differences and several other dummies (for example common language region).

The gravity model used in this study is created by Meronen (1997). The structure of this model is simple, but the results and the correlation coefficient (87 per cent) given by more complicated versions (for example the Erkkilä-Widgren (1994) equation) do not differ considerably in the case of Finnish-Russian trade (Partanen 1998). The parameters of the model are based on calculations whose starting-point is the internal trade of EU-countries (Meronen 1997). For the sake of comparison, our investigation includes Sweden and Estonia as two other neighboring countries of Finland.

The potential trade is estimated by following equation:

$$t_{ij} = 5.54 + 0.80 \cdot y_i + 0.82 \cdot y_j - 1.06 \cdot d_{ij}$$

The equation is in logarithmic form and variables are:

t_{ij} = the value of export from country $_i$ to country $_j$,

y_i = the GPD of the exporting country,

y_j = the GPD of the importing country,

d_{ij} = the distance between the respective countries.

Table 2. Values of the variables of the model in 1999.

	Russia	Sweden	Estonia	Finland
Export from Finland to (Million ECUs)*	1 607	3 901	1180	
Distance from Finland to (Kilometers)	381	395	87	
GDP (Billion ECUs)**	214.3	227.84	4.47	135.06

* Finnish National Board of Customs 1999

** OECD 1999

In the model by Meronen the distance is measured by evaluating average of the five biggest cities to find out the theoretical center of the country (Partanen 1998, 9). In this study the distance between Finland and Russia is population weighted average from Helsinki to St.Petersburg/Moscow, because these two cities together with surrounding areas cover more than half of the total import of Russia (Statistic Finland 1999, 75).

Table 3. Model results: Finland's actual and potential export to Russia, Sweden, and Estonia in 1999 (Finnish National Board of Customs, 2000, and own calculations).

Country	Actual (million ECUs)	Potential (million ECUs)	Actual/Potential
Russia	1 607	2 629	61 %
Sweden	3 901	2 649	147 %
Estonia	1 188	525	226 %

Table 3 shows that according to the gravity model, there exists unused Finnish export potential to Russia. On the other hand, Finnish export to Sweden and especially to Estonia is clearly larger than the model predicts. Finland's high export figures to Sweden can be explained by common history and culture, stable and reliable markets, and the two countries' EU membership. Estonia as a market area is tempting for Finland because of the common language area and Estonia's strong efforts to integrate into the EU markets. In addition, a great part of the Finnish-Estonian trade can be explained with dual gateway operations to CIS and Western countries (Kivikari 1997, 310). On the other hand, Russian markets are lacking most of these factors which partly explains the unused trade potential.

3.2 Finnish FDI to Russia

Russia is the biggest country in Europe measured by surface area and population, but as a market area, Russia is only the size of Sweden (based on the value of import). The size of the economy of Russia (i.e. its GDP) is often compared to the Netherlands. The Russian economy has been unstable and the total output declined dramatically in the 1990s. On the other hand, the country has ample natural resources and skilled labor. The seedbed of foreign and joint ventures in Russia is rather unique in economic history.

The ownership of at least 10 per cent of the voting shares of a foreign enterprise is the definition of IMF for foreign direct investment (FDI). In addition, the character of FDI is to make profit for the investment by getting into the decision making process of the target enterprise, for example, by changing business idea or strategy (Hirvensalo 1999, 6). Finnish investors in Russia usually acquire majority share in their direct investment projects.

The long experience from the Finnish-Soviet trade caused expectations that the Finnish enterprises would have ample knowledge of the market and would be eager to invest to Russia. In addition, the deep economic crisis in the beginning of the 1990s in Finland motivated Finnish enterprises to find new markets. Therefore, Russia was seen as a promising market area which could lower the effects of the economic crisis. However, during the last decade Finnish enterprises have mainly concentrated in trade actions in Russia. In spite of the geographical closeness, trade relations, and the long common history Finnish business has been cautious to make investments to Russia. According to the Russian trade statistics in 1997, Finland was among the 10 biggest exporters and importers but not among the biggest investors to Russia (Hirvensalo 1999, 1).

The cautious investment policy of Finnish enterprises in Russia can be explained by internal and external reasons. Finland joined the European Union in 1995 which eased the access to the main European markets. Furthermore, the most rapidly growing industrial sector in Finland has been telecommunication industry whose biggest markets are in Europe, the USA, and Asia. Thus, many Finnish, internationally operating, enterprises have changed their interests from Russia to faster growing and more stable markets. At the same time, the SME sector has increased its share in the Finnish-Russian trade (Komulainen & Taro 1999, 5). However, Finnish direct investments to Russia are still mainly done by large enterprises. For example, in 1997 almost half of the stock of assets were covered by the 5 biggest investment projects (Rautava 1999, 6).

Factors, such as size, legacy, culture and instability, explain the low level of Finnish FDI to Russia. When studying Finnish FDI to the Baltic Sea countries (Fig. 9) it is obvious that Finnish investors have been extremely cautious with Russia.

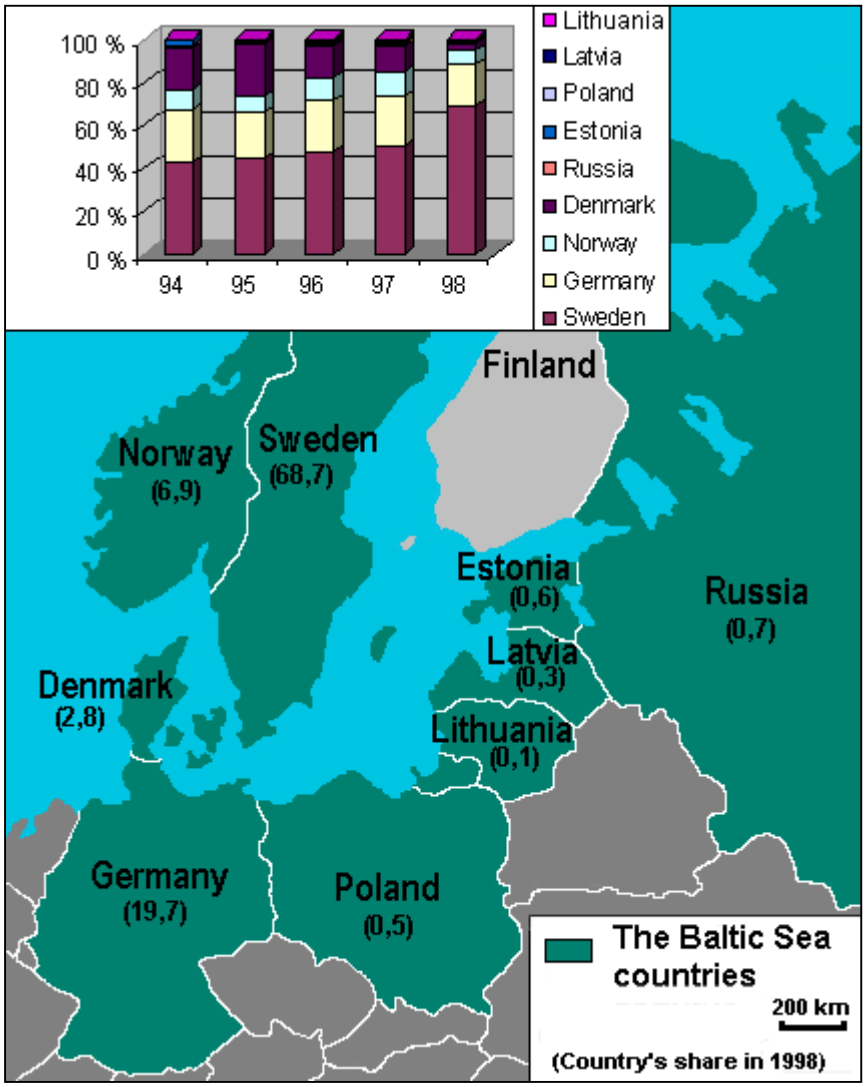


Figure 9. Finnish foreign direct investment to the Baltic Sea countries in 1994-1998. (Country's share of Finland's FDI (stock) to the Baltic Sea region in 1998). (Bank of Finland 1999).

Russia has not been very successful in receiving FDI from foreign countries during the 1990s. Compared to East-European countries like Hungary, Poland, and the Czech Republic all of which have applied the EU membership, Russia is far behind. Finnish investors have been even more cautious with Russia than others. For example, in 1998 Estonia (population 1.4 million) received almost as much Finnish FDI as Russia did (population 147 million). The August 1998 rouble crises caused losses to most of foreign enterprises in Russia. After the collapse of the rouble Finnish FDI to Russia were staunched almost totally (Hirvensalo 1999), but they recovered later.

The geographical distribution of investments indicates that the investments are directed to the main metropolises, especially to Moscow. In the Finnish-Russian border area the focus is in the South, in St. Petersburg and the Leningrad Oblast (Table 1). The resource-based areas have got investments if there is gas and oil industry. Significant investments have been carried out in the regions of Omsk, Tjumen, Tomsk, and Krasnoyarsk. One can find support to the hypothesis, that it is just lacking demand, idle production and production factors located disadvantageously which are the primary causes for low investments in the border area.

3.3 Experiences of Finnish enterprises in the Russian markets

During the Soviet era several Finnish, especially large scale, companies managed to create stable business relations with the Soviet Union which lasted decades. After the collapse of the Soviet Union these former business relations were hoped to help Finnish companies extending their presence in the Russian markets. However, after few years it became evident that the transition process in Russia will take more time than it was expected to.

The principles of co-operation changed as well; the Finnish-Soviet trade used to be part of the foreign policy of states which had given favor to the Finnish companies in the Soviet markets. But the collapse of the Soviet Union opened the Russian markets to every importer or exporter, and the Finnish companies lost their privileges.

To cope with the turmoil in Russian markets has turned out to be extremely challenging. Foreign companies have faced in Russia, for example, groping legislation, unstable taxation, corruption, barter trade, and lack of reliable partners. In the early 1990s, the whole society was unstable and the decision-making structure disorganized. For example, Nokia/ICL Data put lots of effort to a business deal with the Russian army, but after a while it became obvious that no one was able to make the final decision on the Russian side (Salmi 1995). Nokia/ICL Data decided to leave Russia and concentrate on the Baltic markets, because the competition there was not so stiff and the transition process was expected to progress faster, especially in Estonia (Salmi 2000, 11). In spite of all, several Finnish companies have managed to enter successfully the Russian markets. However, many companies have mainly concentrated on trade actions instead of direct investments in production assets.

This study presents two case studies about the companies, Outokumpu and Baltic Beverage Holding AB (BBH). Outokumpu is a mining company which has long experience also from the Soviet era. During the Soviet era Outokumpu operated, for example, in the Pechenga District together with Pechenganickel. On the other hand,

BBH is a Scandinavian joint venture which was founded in 1991 aiming to establish production and marketing networks in Russia and to the Baltic countries.

3.3.1 Outokumpu Company

Outokumpu Company was founded in the firth half of the 20th century to utilize the copper ore deposit found in 1910 in Outokumpu, Eastern Finland. The company expanded, opening several mines and metallurgical plants and developing basic metal technology. A rapid growth period for Outokumpu was the 1980s when the company focused on metal production, mining and technology at a worldwide scale and started several international projects in Europe, South and North America, and Australia.

During the Soviet era Outokumpu mainly sold mining technology and bought raw materials. To carry out this business the company opened a representative office in Moscow in 1981. One part of the internationalization process of Outokumpu was the co-operation with Norilsk Nickel by delivering technology and equipment to Norilsk. Part of the equipment and machinery of Pechenganickel is also made by Outokumpu.

Outokumpu Company showed interest in starting joint ventures in the Soviet Union in the late 1980s. Outokumpu searched enthusiastically for investment projects in Russia, but then Finland was hit by deep depression which lowered the risk taking ability of Outokumpu as well. Following the collapse of the Soviet Union Outokumpu changed its strategy by aiming to open mines of their own in Russia (Hirvensalo 1996, 166). However, this process developed slowly and recently Outokumpu has for the time being frozen these projects. The main reasons for these setbacks have been lack of proper investment projects, and the strategy of Outokumpu to concentrate more on metal production instead of mining projects.

At the beginning of the 1990s Norilsk Nickel was very eager to create joint ventures with Outokumpu. Reasons for this was their lack of own experience in the global metal markets and urgent need to find new customers from the West because of the collapse of domestic markets (Blatov 1998). There was also the need to commence and finance a new underground operation in Pechenga. In addition, managers of Norilsk Nickel realized the need of modernization of their production units and this led to an endeavor to find foreign creditors. Outokumpu was well know from the Soviet era and was considered as a reliable partner.

During the whole of the 1990s Outokumpu was cautious with its business actions in Russia. Outokumpu is still doing successful co-operation with Norilsk Nickel by exporting production technology to Russia and importing raw materials to its own downstream operations. The rouble crisis in August 1998 caused problems to several foreign companies (especially exporters) in Russia, but Outokumpu in a way took advantage from it via Norilsk Nickel. The crisis was of benefit to Norilsk Nickel, because its incomes are mainly denominated in US dollars and costs in roubles. This meant, for example, that tax debts of Norilsk Nickel was cut to the quarter after the rouble started to float (Kotlyar 1999). The rouble crisis, together with higher ore prices, have enabled Norilsk Nickel to start several investments in Siberia and in Pechenga. This recovery of the Russian mining sector has created export opportunities for Outokumpu's technology. So far, Outokumpu has not commenced any joint mining or basic metal project. Nevertheless, the company has small subsidiaries registered in Russia.

The lack of mutual interest and profitable investment projects has prevented deeper co-operation. The economic state of Norilsk Nickel has lately improved because of the higher world market prices, which has meant that the company is able to finance its own investment projects (Rantanen 1999).

The experiences Outokumpu has had from the Russian (the Soviet Union) markets are mainly positive. Outokumpu has managed to create long and reliable business relation with Norilsk Nickel which is one of the most important reasons why Outokumpu is still doing business in Russia (Rantanen 2000). During this co-operation Outokumpu has managed to gain a noticeable amount of experience and know how to do business in the Russian markets. However, Outokumpu is still concentrating on trade actions instead of investments to Russia.

3.3.2 Baltic Beverage Holding AB

Baltic Beverage Holding AB (BBH) is one of the few successful examples of Nordic investment projects in Russia during the 1990s. BBH is owned by the Finnish company Hartwall (50 per cent) and the Swedish-Norwegian company Pripps Ringnes (50 per cent) and it was founded in 1991 to operate in the Baltic and Russian beer markets. After ten years of operations BBH owns twelve breweries and eight malting facilities which are situated in Russia, the Baltic countries, and Ukraine (Table 4).

Table 4. Breweries of BBH in 2000.

Company	Acquired	Owner-ship As %	Production Million liters	Growth Of production	Market share as %	Personnel 21.12. 1999
Russia:						
Baltika	1993	75	633	34	15	2 829
Baltika-Don	1997	83	-	-	-	-
Yarpivo	1996	60	165	26	4	673
Tula Brewing	1997	69	100	20	2	614
Chelyabinskpivo	1999	75	61	-	1	596
Pikra	1999	50	67	-	1	700
Ukraine:						
Slavutich	1996	75	109	40	13	674
Kolos	1998	99	16	-	2	605
The Baltic States:						
Saku (Estonia)	1991	75	52	25	50	256
Aldaris (Latvia)	1992	75	60	23	48	429
Kalnapils (Lith.)	1994	86	44	-5	20	228
Utenos Alus (Lith.)	1997	99	42	-	21	372

Source: Annual Report 1999, Oyj Hartwall Ab.

BBH commenced to buy companies in 1991 when it bought the brewing company Saku in Estonia. The next step was Aldaris in Latvia in 1992 and Baltika, the largest production unit of the company, was acquired in 1993. The company has started its operation in the nearest markets, from the Baltic States and St. Petersburg, and expanded to Ukraine and Siberia. The latest acquisitions have been Chelyabinskpivo in Chelyabinsk and Pikra in Krasnojarsk. The diffusion to new market areas has taken place step by step towards east and southeast (Fig. 10).

The company has been very expansive and profitable. The market share of BBH in Russia is 23 per cent and in the Baltic States about a half of the beer markets. For comparison, Hartwall owns 50 per cent of BBH's shares and sold beer 196 million litres in Finland in 1999 having the market share of 48 per cent. Baltika alone sold 663 million litres of beer in 1999, more than the entire market demand of beer in Finland.

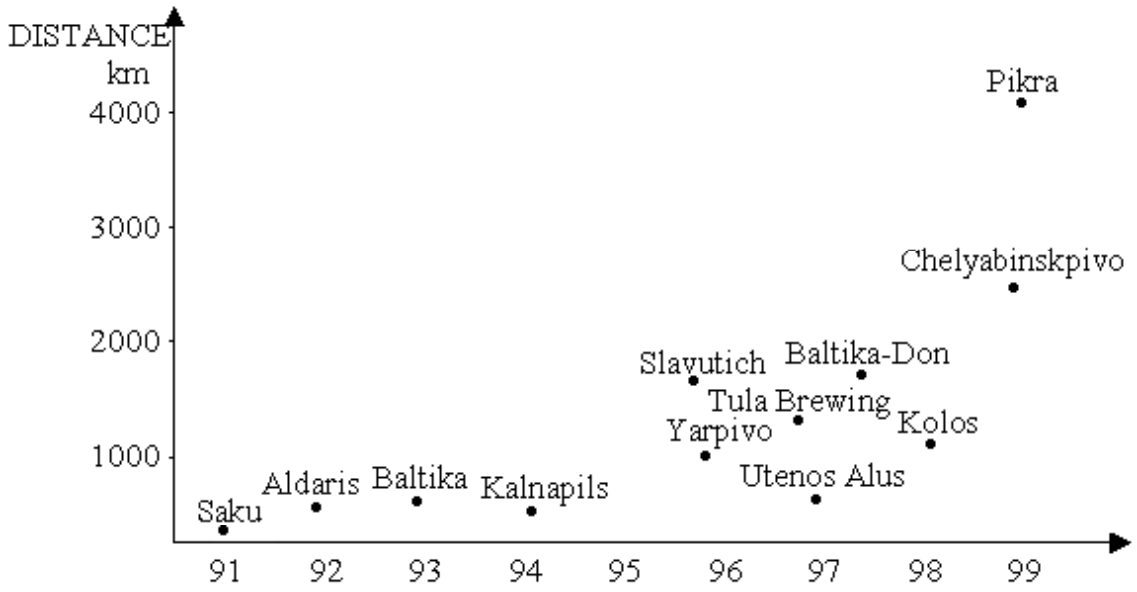


Figure 10. The expansion of the acquisitions of BBH.

The production volume of BBH has developed as follows in million litres: 1991: 14, 1992: 50, 1993: 100, 1994: 160, 1995: 191, 1996: 456, 1997: 676, 1998: 913, 1999: 1278. The figures include the Baltic States, Russia, and Ukraine.

The main business strategy of BBH in the Russian markets was to rely on local workers (including managers) and on local brands. Managers are often made co-owners. In Russia BBH owns more than 50 per cent in every production plant and it is not targeting at total ownership. By partial local ownership BBH aims to attach managers and workers to the company, which has turned out to be a successful strategy. For example, the quality of products has improved up to the western standards which has meant better preservation and therefore wider distribution areas (Hirvensalo 1999, 58). Some of the recent acquisitions are considered beneficial because of the improved and joint logistics. Beer has been a local product in Russia, and Baltika is the first national brand in the country.

Although Russians purchasing power is weak and Russians consume less beer than, for example, Finnish consumers, the Russian beer market has a great potential.

Therefore, BBH has put lots of effort and investments in Russia; in the eastern markets the company achieved success especially in Russia. BBH has already been a market leader for a few years and its market share has grown. Average volume growth of BBH has been 81 per cent a year and they are expecting to do even better in 2000 (Ramm-Schmidt 2000). In addition, in spite of the devaluation of the rouble BBH's profitability has been excellent; this is clear for example, if compared to its parent companies. The company is also a notable taxpayer, for example, in 1998 about 10 per cent of St. Petersburg's budget was covered by alcohol taxes from BBH (Hirvensalo 1999, 58).

The rouble crisis in August 1998 caused serious problems also to BBH. For example, investment plans had to be changed and product prices were raised. However, BBH also took advantage from the crisis because export from the west was almost completely staunched, and local breweries became even cheaper investment objects (Hirvensalo 1999, 61). But even a more serious problem than the rouble crisis has been the lack of suitable subcontractors. BBH has encouraged and even offered long-term contracts to few non-Russian investors, but suspicion towards the Russian business environment is preventing these co-operations (Ramm-Schmidt 2000). In addition, BBH has also faced the hard criminality of the Russian business life: one of the company's top managers was murdered in 1999.

BBH has succeeded very well in the markets of Russia, the Baltic States and Ukraine. Its success is based on the introduction of modern production, logistics and marketing to beer production. It proves that there are certain fields where there are no insuperable institutional barriers for foreign companies in the economies of those countries. The production of BBH is targeting on a growing consumer market and the main population centers. A production niche has been found.

4. Attitudes of the Russian Employees in Pechenga District

What do the Russians think about foreign business partners and foreign investors? Are they eager or reluctant to welcome global economic integration? What sort of seedbed for industrial co-operation exists in the Russian North?

In the mining complex of Nikel-Zapolyarnyj, the main production units in the 10 by 30 kilometer mining area situated in Arctic conditions are three open pits, underground operations, a mill producing nickel concentrate, a roaster plant producing pellets, a sulfuric acid plant and a smelter. When the first interviews were conducted in June 1998, the mines and factories employed 9 000. Retirements and layoffs were seen as an outlet for financial woes. In 1997, 800 employees became redundant; and in 1998 the labor force was further reduced by another 1 100. Layoffs continued in 1999 when the number of employees decreased by 12 000 in the whole combine of Norilsk Nickel.

The Pechenganickel is part of the nickel production chain that processes local nickel ore and ore concentrate from Norilsk, 3 000 kilometers east of the Pechenga District. The nickel produced by the Pechenganickel is further processed in Monchegorsk. The main concern of the Pechenganickel in the late 1990s was lack of competitiveness and profitability. The declining price of nickel did not account for all the losses; the main reasons were raw material problems and inefficient production. During the research interviews, the managers (CEO and executive director of mining) of Pechenganickel voiced concerns about insufficient resources for the necessary

modernization investments (Blatov and Kamkin 1998). However, the recent development of nickel ore price has been favorable for Pechenganickel which has meant that the company is able to extend its lifespan by investments.

Workers were interviewed during the summers of 1998 and 1999. The following analysis is based on these interviews; 813 employees between the ages of 18 and 62 (average age 37 years) were interviewed in Zapolyarnyj and Nikel. Interviews were based on a systematic random sample. Employees were interviewed by Russian research assistants.

The logic of the analysis is based on the causal thinking that local people behave according to the following sequence of reasoning, leading to co-operation with foreign actors: 1) awareness of the economic problems, 2) a need to find ways to restructure the company successfully (relying on existing organizations), 3) a search for advanced technology and ways of implementing it (in this case from the global markets), 4) using foreign technology and capital inputs, and 5) accepting both a foreign company as a shareholder and foreign contract work. This sequence of reasoning ends up with the attitudes of employees toward collaboration with foreign actors, that is, possible acceptance of a foreign company as a shareholder and acceptance of foreign labor.

According to Table 5, the vast majority of employees consider replacement investments and investments in new operations to be necessary: “Mining company urgently needs major modernization investments” is agreed with 4/5 of the employees. Employees do not trust the ability of the management to carry out investments and consider that the management does not think about what is best for the employees (see statements 5, 6 and 9). Employees prefer employees’ ownership more than the participation of local authorities in decision-making (statements 7 and 8).

The logical and concrete starting points for the evaluation of attitudes is found in Pechenganickel: employees recognize that investments are needed, and they are ready to implement the process of modernization (Table 5). The critical issue is how the modernization will be carried out. What sort of mental barriers exist to foreign collaboration? Do the attitudes hinder co-operation?

The employees of the Pechenganickel are very convinced that advanced technology from international suppliers is needed for modernization. The statement “The mining company of this town needs western technology” is supported by 4/5 of the employees. In the interviews only 6 per cent of the employees who intended to continue working in the company denied the crucial importance of imported technology, and only 8 per cent of the employees had at all something negative toward foreign investors. In the case of company restructuring, 7 out of 10 employees would like to continue working in the company. Positive attitudes to western technology (statement 11) are based on past experience. Most of the advanced machinery and equipment of the company have been acquired from world markets during recent decades.

Table 5. Attitudes of the employees of Pechenganickel: from awareness to collaboration. All interviewed employees are considered.

Alternatives: Strongly agree (Sa), Agree (A), Neutral (N), Disagree (D), Strongly disagree (Sd).

	Largest category and its share, %	Agree or strongly agree, %
Awareness of the problems:		
1. Mining company urgently needs major modernization investments	A 46.9	78.3
2. Modernization reduces pollution	A 47.8	63.4
3. Modernization investments are urgently needed to ensure jobs	N 29.1	38.8
4. I believe that in the near future the mining company is going to face major modernization investments	N 41.4	33.9
Human resource policy and participation:		
5. The present company will not pay any attention to the needs of its individual employees	N 36.8	51.0
6. The top management will do whatever is most profitable in the short term, regardless of the long-term interests of the company and its employees	A 39.5	59.4
7. Workers should have a bigger share of stocks in the mining company than they have now	A 40.0	64.6
8. Local authorities should play a larger role in developing the mining Company	N 31.7	49.9
Trust		
9. The present company will do the best it can to look after the welfare of all its employees	N 40.5	32.9
10. The local people at the top do not have the skills to introduce this sort of major changes successfully	N 49.7	35.1
Western technology		
11. The mining company of this town needs western technology	A 55.7	80.3
12. In the long-run, foreign modernization investments will bring prosperity to this town and workers	N 40.3	44.1
Attitudes to foreign partners:		
13. It would be best if investments could be done by a domestic company	Sa 34.4	59.3
14. Foreign mining companies as shareholders of the Pechenga Nikel are welcome	N 36.0	39.4
15. Foreign people (builders, workers, managers etc.) are welcome to this town	D 35.9	22.3

Employees have some experiences from foreign experts and consultation. Non-Russian companies have to some extent installed their machinery and equipment using their own employees in recent decades. Russian experts have often been trained in the West to use new technology. For instance, this happened in the early 1990s when Outokumpu Oyj renewed a mill in Zapolyarnyj. There is also collaboration with foreign partners in everyday operations, such as in blasting.

Domestic technology is not a real alternative because of the widened technology gap between Russia and advanced industrialized countries (Naulapää 2000, 254). Reason for this is mainly the ignorance of production development and research in Russia. However, the employees are not sure whether multinational investments will bring prosperity to the town, as the responses to statement 12 indicate. Benefits may be used, for instance, to cover earlier losses and to pay profits rather than for the benefits of the workers.

Employees clearly would like to keep the control of the company in Russian hands (statement 13). Foreign companies are not very welcome as shareholders (statement 14). This preference for domestic companies is not unanticipated. Similar attitudes are found, for example, in a more international orientated economy like Australia is (Tykkyläinen 1994). Likewise, in Karelia on some economic issues the locals are very nationalistic. For instance, when business school students in Karelia (n=72) were asked for their opinions, 61 per cent agreed to some degree (strongly agreed, agreed or slightly agreed) with the statement that Karelian business should be owned by Russian citizens, and 78 per cent would like to see round wood exports to Finland restricted (Tykkyläinen & Jussila 1998). The latest public opinion poll of 2 338 people in Karelia supports this result (Karelian … 2000). These protectionist attitudes are common when we talk about natural resources and large companies, but not for business in general. Karelian students consider joint ventures very necessary and favor deeper integration with the European Union (Tykkyläinen & Jussila 1998). It is a very common Russian attitude that natural resources are a national, invaluable asset which should be controlled nationally.

Employees face severe reduction of the labor force, which takes place through labor adjustment programs that prefer retirement and a voluntary search for jobs elsewhere. This is certainly an important reason why foreign employees (builders, workers, managers etc.) are not very welcome to Nikel and Zapolyarnyj, as the responses to the respective statement indicate that only a fifth of the employees considers it positive.

In summary, the attitudes of employees to collaboration are well grounded in the context of the socio-economic situation (the need for modernization, labor reduction, etc.) of the mining sector in Nikel and Zapolyarnyj. The results show that attitudes to foreign collaboration are favorable and do not hinder co-operation. As expected, employees defend their own interests and expect that the collaboration will improve the competence of the company and their own position. On the other hand, unrealistically high expectations for improved results may lead to disappointment, resulting in strikes and economic losses, as happened at the paper mill acquired by AssiDoman in Segezha in the late 1990s (Tykkyläinen & Jussila 1998).

5. Conclusion

The collapse of the Soviet Union affected Finland's economy more than any other capitalist country's. However, the Finnish-Russian trade managed to recover relatively quickly. Already in 1993 the growth rate of Finland's export to former Soviet states was higher than any other OECD country's (Kivikari 1997, 271). In addition, the Finnish trade to Russia has increased quite evenly during the 1990s (except after rouble crisis in 1998) in spite of the decline of GDP in Russia. Former, Soviet time, contacts and experiences can partly explain this peculiarity. Even so, the growth rate of the Finnish-Russian trade has not corresponded to expectations of export enterprises (see for example Ollilla, 1999).

Finnish export to Russia managed to recover since the early 1990s and the absolute figure in 1997 was near to the level of the late 1980s. However, Finnish export to Russia collapsed again after the rouble crisis in August 1998. Therefore, the Russian share (4.1 per cent) of Finland's whole export is only about one fourth compared to the Soviet time. As an illustration, the gravity model (Table 3.) shows unused export potential. Reasons to this are, for example, the European markets (EU membership), concentration to the telecommunication industry, the unstable Russian markets, and the increased competition in the Russian market together with the weak purchasing power of the Russians. Finnish exporters increased market orientation to the main EU area during the 1990s (Fig. 11).

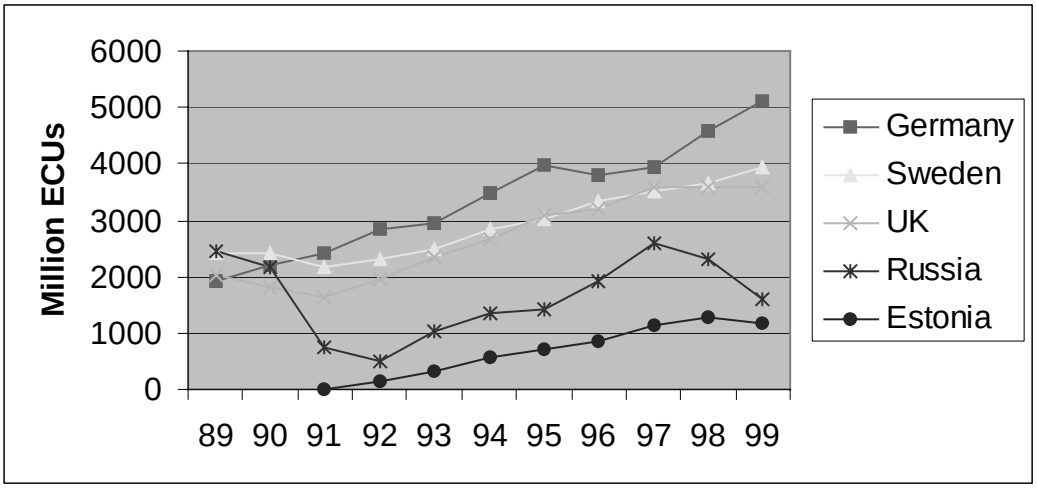


Figure 11. Finnish export to few European countries in 1989-1999 (Finnish Board of Customs 2000).

The Finnish foreign direct investment (FDI) figures show even a clearer orientation to the European Economic Area. For example, in the Baltic Sea region (see Fig. 9) 98 per cent of the Finnish FDI are directed to neighboring EEA-countries (Norway, Sweden, Denmark, and Germany), and only 2 per cent to the former Soviet Union Republics (Russia, Estonia, Latvia, Lithuania) and Poland. In fact, it seems obvious that Finnish enterprises are going to continue cautious investment policy especially towards Russia, because the rouble crises in August 1998 gave an extra

warning to the Western investors. Furthermore, several Finnish enterprises are cautious even with their trade actions by still using the prepayment system.

Many companies in the Russian North and Northwest are the economic victims of the collapsed superpower. At one time, the resource frontier of the forest industry and mining sector shifted to the Russian northern border territories. That period is over, and many of the resources uses are not economically viable in the new economic conditions where global market prices determine the internal prices and where financial support from the state is not possible. The inability to make replacement investments indicates serious structural problems in the resource-based industry of this region. If demand does not recover and companies can not provide marketable products, many factories will gradually be downsized. So far, the Russian economic development has favored consumer goods industry – not heavy industry which has often been linked to the military production.

The Russian northern territories were developed based on the large-scale production and the presence of armed forces, which also determined much of the border relations. This sector represents the currently declining economic sector – formerly prioritized, subsidized and controlled by the core of the Soviet regime. This system collapsed. Opening up the border did not lead to a continuation of the former Soviet trade pattern and to economic growth, and there were no favorable conditions for profitable production. Economic cross-border co-operation did not flourish.

But what about the mental boundary? Is it also a hindrance? People are associated with places and regions, and they easily reject influences from “others”. The strong sympathy towards collaboration with international suppliers indicates that co-operation is considered, in the first place, as an economic option. The outlook toward collaboration is not emotional, affective or political in the sense that Finns think of the ceded part of Karelia. If most people in Russia had been exceedingly nationalistic and unresponsive, they would have denied the importance of imported technology and co-operation with foreign partners – and that was not the case. However, people prefer domestic companies as a local operator and they are suspicious of foreign control and the inflow of labor. Still, in principle, mental barriers are low.

Institutionalists blame bureaucracy and customs. Are there any more important causes beyond those factors? Is it just lack of demand and the disadvantageous location of economic activities which matter in border areas? Such argument can be supported as well. This is illustrated by the success of BBH. This beer producer has penetrated to the markets of the transitional countries rapidly and effectively. BBH's success proves that there are fields and conditions where there are no insuperable institutional barriers for foreign companies in the economies of those countries.

To sum up, development is bound to history and space in Russia, but the actors of development are evolving and finding new solutions. The main causes for sluggish development in many resource-based sectors seem to be demand-driven and structural (and spatio-structural). The collapse of the former economic system brought about such a deep decline with which only few companies could properly cope. Nevertheless, the Russian economy is under reconstruction and recovering. This restructuring seems to happen in a selective way; former socio-economic structures and geography are changing in a way which is not easy to anticipate.

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