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Relationships in the Russian B-2-B Market: A Macro-level Industry Review

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Abstract: The purpose of this paper is to explore B2B systems within an emerging market and to integrate the existing literature. The importance of studying the Russian market stems from several characteristics such as experiencing transition from a command to a market economy that is seen in its business networks, being the biggest emerging stock market and high potential for business. The "command period", where the government control all aspects of life, has caused the lack of academic research, which makes this study an important addition to the body of knowledge on the Russian market specially the business-to-business market. It becomes an important reference for business practice and a guide for future research.

Key words: relationship marketing; value; wholesale market; Russia; distribution networks
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1. Introduction

One of the most momentous political and economic events of the late twentieth century was the demise of the communist political and centrally planned economic systems in the former Soviet bloc countries. Russia reflects characteristics of an emerging market such as those identified by Dawar and Chattopadyay (2002), they are; low incomes, variability in consumers and infrastructure, and the relative cheapness of labour, which is often substituted for capital. The Russian market also address an important deficiency in the literature on strategies for companies operating in emerging markets as a only few of the companies working in those markets consider strategy development.

This research presents a macro-level industry analysis to the Russian business-to-business market. A macro level industry analysis is based on environmental conditions that affect the industry as a whole without a particular company's strategy, target market, or its role in its industry (Walker, Mullins & Larreche, 2008). As part of Porter's (1980) five forces model, which has been used to analyze industry attractiveness on a macro-level, the bargaining power of buyers and suppliers have been of a particular interest of turning buyer-supplier relationships into a cooperative one where a win-win is achieved rather than a win-lose. To review the current status of Russian buyer-supplier relationships on a macro level current industry data were collected and findings from previous research on Russian business-to-business relationships is reviewed in the light of relationship value in business markets literature. Relationship value in Russian business networks is the centre of this research. How relationship value is created by suppliers and how customers see the value of their supplier's relationships, are some of the main issues explored. Aspects to do with Russia and its transition to a market economy and consequences of this

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transition especially in business to business systems, is also reviewed.

The study of business-to-business system and its relationship structure in macromarketing is supported by Layton (2007). He suggests that the study of marketing systems is central to macromarketing and that the output of a marketing system is an assortment of goods, tangible and intangible, offered in response to customer demand. In defining Marketing systems, Layton (2007) postulates that they are complex webs of interdependencies that require management of relationships within the system (Layton, 2007).

2. Russian Market

The Russian business market is characterized by several unique factors, one is there have been fundamental changes in Russian networks since the transition from central planning to a market economy, which in turn had its effects on businesses and managers (Salmi, 1996). Second the Russian environment is very complex and Russian culture is different from Western culture (Bollinger, 1994; Puffer, 1996a; Holden et al., 1998; Ledeneva, 2001) which makes western marketing strategies not applicable with the Russian market. third the fact that the Russian market continues to perform well and has an impressive gross domestic product (GDP) growth rate of 7 percent and many markets in its large cities remain untapped (A None, 2006), makes it an important potential market that has to be studied and tested for marketing strategies. The fourth unique feature is the result of the communist and command economy era which caused a lack of marketing information and data from research on Russia and Russian market as marketing concepts did not apply within command economies, which calls for more research to contribute to the knowledge of this market. The fifth character is that Russia is considered the biggest emerging market stocks (Schwinder, 2006), which makes it a high potential for investment and raises the need to study its business practices. It is also part of what is called the BRIC countries they are Brazil, Russia, India, and China, which is growing up to eight times faster than the U.S (Zacks research, 2007). All these characteristics identify the Russian business market and makes it unique for the study of business to business relationship value, identifying strategies to work in such a high potential market.

3. The Russian Business to Business Market

To draw a clear picture of how the business to business market is structured it is necessary to discuss the market structure in the planned economy in the pre-transition Russia. The planned economy is mainly characterized by hierarchies (Johanson, 2001). Organizations and enterprises interacted with planners and the planning bodies that meant there was no interaction or relationships between organizations and production budgets were put by planners (Johanson, 2001). To acquire the resources needed for production, producers didn't need a formal relationship with suppliers, which means suppliers were not necessarily known to the producers (Salmi, 2004). Marketing was not needed as where the products are going and to which end-users they are delivered, was pre planned. Networks had a hierarchical and stable nature, created by the anonymity between firms (Johanson, 2001).

As a result the necessary links and relationships between organizations in the supply chain did not exist (Johanson, 2000). But this formal structure of the Soviet business to business market was not the only one that existed as organizations had to create their own informal exchange networks with other firms, these informal networks are called "blat" (Johanson, 2000; Michailova & Worm, 2002). This resulted in an informal face to the Soviet business network which encouraged the spread of bribery and the grey or black market (Grossman, 1994; Salmi, 2004).

As a result the form of inter-organizational interaction, exchange, and relationships as they existed in the western economies did not exist in Soviet Russia. Only a few organizations that existed during the Soviet era displayed supply chain interaction, relationships and cooperation then. One of these organizations is McDonald's, a multinational company that established itself during the time of Soviet Russia and it has managed to integrate and control its relationships in the local supply chain since then. McDonald's strategy started from the bottom of the supply chain in Russia, by carefully selecting the potato farmers and meat suppliers and educating them.

So how does the old regime affect the current new one in the business to business market? The old hierarchical organizational structure has a big effect on the current one (Salmi, 1995; Salmi, 2004; Shresheva & Tretyak, 2004). After the transition the old structure of organizations broke down but employees who operated these organizations remained with the same mentality running the same organizations or new ones (Salmi, 1995). This gave the new business to business operations two features. First, to do business organizations did not try to establish new relationships with new partners but they resorted to old relationships from their old informal connections (Dolgopiatov, 1994). Second, the one manager way of doing business still takes place, which causes the business to operate through their connections and information (Salmi, 2004).

Evidence for these practices in the current Russian business to business market was provided by three current studies (Linz, 2002; Sheresheva & Tretyak, 2004; Haaparanata et al., 2004), of organizations from different regions of Russia. The results from this study confirm that it is a practice for organizational managers to resort to old connections to borrow funds rather than borrowing from banks. This finding is in line with Hendley (1998) who confirmed from his study of organizations in Russian business to business market that managers resort to old connections rather than choosing to get involved in negotiations with new ones.

Sheresheva and Tretyak (2004), presented a study on Russian supermarkets and their supplier-retailer relationships and one of their findings is that local Russian retailers still consider selling firms as their adversaries not collaborators. This means that their focus is more on creating a successful one-off transaction rather than concentrating on building a long term win-win relationship where both partners benefit. Sheresheva and Tretyak (2004), found similarities between Russian and UK retailers in the bad criticism they both get for unfair dealings with suppliers. Only the UK retailers are governed by laws of fair practice while Russian relationships between retailer and suppliers are developing more impulsively. The main characteristics of UK retailers which makes them different from Russian ones is that the UK retail market is characterized by over supply and stagnant annual growth, which drives retailers to integrate and collaborate more with their supply chain (Hingley & Lindgreen, 2004).

Although the study by Sheresheva and Tretyak (2004), highlight problems in the supplier-retailers relationships which is a result of non comprehension of Russian mangers of how to establish a win-win relationship in the Soviet Russia, but they do not support the idea of using the old network of relationships in the current organizations. They see the network model in the Soviet Russia as hardly useful.

Haaparanata et al. (2004) presented a study of middle sized and large manufacturing companies from several regions in Russia. In their results they found that most of the businesses studied tended to be involved to a great extent in social service provision, which meant that most of them had their own housing or local support for accommodation and employees leisure facilities. This indicated that businesses are playing the same role as before in their local economy, and that the behaviour of the soviet economy still exists.

Huber and Worgotter (1998), distinguish two major types of industrial networks in the new Russian business market; entrepreneurial and survival networks. Both of these networks differ in their view of trade in a market economy or competition in Russia. Survival networks include firms that do not have high expectations for themselves in competitive market conditions; they are created with the clear goal of isolating participants from market competition. The network is basically established on the old connections they had in the pre transitional market. Entrepreneurial networks are completely different from survival networks as they tend to base their operation on market rules and fair competition. Two types of entrepreneurial networks were identified: those that build on old structures and those composed of new structures.

In the new Russia the government no longer creates the plans for firms to carry out, firms have the right to choose who to operate and interact with just as in a mature market economy (Hallen & Johanson, 2004). Some authors (Ledeneva, 1998; Kosova, 1999) believe that the transition to a market economy has changed primarily the way Russians build personal networks and exploit them for business and personal goals, but the study by Linz (2002) discovered that up to 90% of their study sample was paying bribes.

Only a few organizations in Russia comprehend the importance of an organization’s intangible asset, such as the relationship with other organizations, value, loyalty and satisfaction (Shresheva & Tretyak, 2004). The association between these intangible assets and increasing the long term profitability and competitiveness of the organization is still not established in many firms.

In Russia, everyday business practice is characterized by the transition from a command economy to a market economy and the repercussions of the economic breakdown in 1998 (Aslund, 2002). Manevich (2002) conducted a study in the Russian wholesale bottle market. The study detected an increase in the production of glass containers from the year 1998 to 2002 but the market was also dominated by foreign imported products although they were priced high due to their original high price plus the transportation costs they incurred.

The study of glass containers by Manevich (2002) was seen by Wagner (2005) as identifying opportunities and limitations in the Russian business to business markets. In Russia limitations for marketing is seen in shortages in resources and fashionable designs or packages. But Manevich (2002) sees these boundaries as restricted to a few aspects of marketing such as the legal issues of marketing certain products such as tobacco, cigarettes and alcohol as well as financial and insurance services.

The Russian business-to-business markets provide challenges in particular to foreign investors (Wagner, 2005). They can be described by “three Russian cultural traditions” (McCarthy & Puffer, 2002):

(1) Bypass laws and regulations

(2) Little trust, and

(3) Networks of personal relationships

So the opportunity to develop transaction-focused market relationships is restricted due to the institutional infrastructure which existed during the command economy and continues to exert an influence on the current business (Wagner, 2005). Hoskisson et al. (2000) see this institutional deficit being overcome by companies’ commitment to the relationship notion and aspects of business.

Considering consumers in the Russian market, Treadwell and Pridemone (2004) refer to the fact that although they were faced with unfamiliar emerging market economy practices such as unforced legislation and currency fluctuations. The market has experienced a booming consumerism (Belton, 2002; Manrai et al., 2001). The fast growing consumer market has turned Russia into the fastest growing market for many multinationals such as Ikea, L’Oreal, Nestle, Procter and Gamble (Belton, 2002).

3.1 The Wholesale Market in Russia

Research performed at the beginning of the 1990s (Boeva, Dolgopiatova & Shironin, 1992; Predpriytiya &

Pravitel'stvo, 1992) indicated a dramatic loss of importance of the wholesale level and a reduction of the volumes of industrial products sold under brokerage of specialized supply and sales organizations. A number of objective reasons were behind this negative trend. One of the reasons for that was a historically formed artificial monopoly of former state-owned supply and sales organizations (Yakovlev & Kokore, 1994). Liberalization of prices, which significantly eased the problem of shortages, as well as the increase of the trade extra (increases or additional charges made by wholesalers to the original prices from manufacturers) charge to 25% from the previous 7-9% in 1992, resulted in an abrupt reduction of the demand on the services of wholesale enterprises and a decrease in their cargo turnover. Yakovlev (1996) reported a changed in the structure of the wholesale market. In particular, the share of former state-owned wholesale brokerage organizations has significantly reduced and continues to do so.

4. Relationship Marketing and the Network Theory

Arndt (1986) views marketing systems as relational networks. He noted that most transactions are effected not through ad hoc market encounters but in the context of stable relationships within networks. Inter-organizational relationships and relationships between buyers and sellers literature is expanding as is also the case for networks in business markets (Anderson et al., 1994; Achrol, 1997; Achrol & Kotler, 1999; Moller & Halinen, 1999). Different inter-organization models have been developed and applied in different marketing and distribution scenarios (Anderson & Narus, 1990; Morgan & Hunt, 1994; Wilson, 1995).

Of the various approaches/models that explain factors influencing business relationships, the Industrial Marketing and Purchasing (IMP) is the best equipped to deal with the various issues that shape buyer-seller relationships (Metcalf et al., 1992), also the IMP group contributed significantly to the development of literature and research on business networks and relationships (Welch & Wilkinson, 2002).

Industrial network literature was developed from earlier work in transaction marketing where the main focus was on single transactions and there was a lack of long-term relationship orientation. The network literature doubted the benefits of transactional marketing in gaining a long term customer satisfaction and providing added value, and started considering relationship marketing instead (Bonoma et al., 1977; Håkansson, 1985). This is where their theories on networks and relationships were developed, and they began looking at relationships between buyers and sellers and taking it further to discuss networks that involve relationships between more than two actors. During the 1990s a number of researchers followed the IMP group which expanded the literature available on networks and relationships (Ford, 1990; Håkansson & Snehota, 1990; Axelsson & Easton, 1992; Blankenburg-Holm et al., 1996; Lehtinen, 1996).

Interactions, relationships and networks have formed the centre of IMP research in business markets. The pillars of their analysis is built on actors, activities and resources (AAR) model, which was introduced by Håkansson and Snehota (1992), as the fundamental dimensions of relationships. The AAR model proposes that networks have a dynamic nature and consist of interdependent and connected actor bonds, activity links and resource ties (Håkansson & Johanson, 1992; Håkansson & Snehota, 1995). The development of network theory has also been influenced by the IMP Group by US, Australian and UK research that analyze inter-firm relationships (Christopher et al., 1991; Young & Wilkinson, 1992; Wilkinson & Mattsson, 1993; Wilkinson & Young, 1994; Perry & Pyatt, 1995; Ford et al., 1995; Wilson & Moller, 1995; Gummesson et al., 1997).

Håkansson and Snehota (1995) have explained, through their AAR model, business networks as consisting of actor, activities and resource, which together produce different layers or types of connections.

Activity links, embrace activities of a technical, administrative and marketing kind. The linkage of each of the activities form activity cycles. Several actors are needed to carry out this cycle, which means that relationships are created in order to realize a transaction chain (Håkansson & Snehota, 1995).

Resource ties include exchanging and sharing resources, which are both tangible such as machines, and intangible such as knowledge (Håkansson & Snehota, 1995).

Actor bonds are created by people who interact and exert influence on each other and form opinions. Actors can be both enterprises and individuals, who are in some way connected within a network. These actors control resources and carry out transactions (Håkansson & Snehota, 1995).

Researchers have used the AAR model to analyze the Russian business to business network (Johanson, 2001; Salmi, 2004). Johanson (2001) used the model to analyze the pre-transition Russian network, which he describes as hierarchical, stable and anonymity. He blames the hierarchy and the stability of the Russian network for actors not gaining experience of dealing within relationships. According to him relationships are transmitters of experience and due to the anonymity that existed in the Russian network; organizations were not able to deal directly with each other. In addition the hierarchy in the network caused the same information to be transmitted over and over again without allowing any room for creativeness. Because of the harsh nature of the Russian networks Johanson (2001) goes to the extent of stating that Russian businesses have to develop a network approach that is suitable for their context which is different from the western context.

While Johanson (2001) used the AAR model to describe the pre transition Russia, Salmi (2004) used it to describe the current Russia. Analyzing relationship resources, the after transition Russia is suffering from outdated equipment and machinery as most of it is from the pre transition time. To update resources investments are needed in the market. But the problem is the lack of investments due to a high rate of capital flight outside Russia; Linz (2002) reasoned this to the lack of property protection which has caused many Russian organizations to invest outside Russia. Low investments in the market are seen as an obstruction to actions. There also seems to be a shortage of new actors for which Salmi (2004) provided reasons such as geographical constraints, more investments, and different adoption from different organizations of new market rules. A study by Kosonen (2002) identified six types of organizations in the Russian market ranging from market economy thinking to socialist thinking; opportunities, neutrals, disputing constructors, constructors, strugglers and reactionaries (p. 202), with constructors as the most adaptive to new market and network ideas.

A buyer seller relationship or the “focal relationship” relies upon connected relations in the network, which may result in a relationship with a third actor (Anderson et al., 1994). Based on a number of related network researches, Moller and Halinen (1999) describe industrial relationships that a network of an organization is built upon. From the organization’s point of view, relationships could be viewed in two ways; horizontally and vertically. Vertically starting from top level suppliers down to the customer’s customer while horizontally, from merging or working together rivalry to partnerships with government units and R&D.

Sheresheva and Tretyak (2004) report on several studies that confirmed the prevalent integration between organizations in the Russian market (Kuznetsov & Simatchev, 2001; Ernst & Young, 2003). The study by Kuznetsov and Simatchev (2001) reports a tendency for intensified integration including conglomerations and horizontal integration. Another study by the higher school of economics in Russia reported overwhelming vertical integration tendencies. In line with this study, Ernst and Young (2003) reported a growing number of mergers and acquisitions. Also a recent study reported that the 10 top integrated business groups in 2002 provided 39% of manufacturing production and 21% of Russian investment. Sheresheva and Tretyak (2004) reasoned the tendency in the growing vertical integration to the need for more control over suppliers and distributors. The reason behind this need to exert more control is due to “weak enforcements of contracts, low transparency of legal system, persisting corruption and general economic instability” (p. 4), which causes suppliers to behave in an opportunistic way pushing the need of manufactures to have more control on them. These recent integration tendencies give the Russian network a homogeneous structure with defined boundaries (Radygin, 2001).

The role of distributors has also increased in Russian as many manufacturers have hardly any direct contact with the end-users of their products, but instead they have major relationships with industrial distributor companies, that act as intermediaries for them (Gadde & Snehota, 2001). On many occasions it is the distributor that specifies the product for the market not the manufacturer, in which case many distributors develop new product types for their own customers. In this case manufacturers have to comply with distributors’ requirements as they have more experience and are more in touch with the end users (Gadde & Snehota, 2001). A study on the Russian wholesale durable goods by Morch and Persson (1999), reported that distributors play the most important role in the distribution network as the market for consumer durable goods in Russia is dominated by 100% imported goods. As a result the distributors in this market control the import, distribution and sales through retailers. The same study has also reported an underdeveloped distributor-retailer relationship. Another recent study by Tretyak and Sheresheva (2006) in the Russian fresh fruit distribution networks showed that the main role in the fresh fruit supply chain belongs to wholesalers as they are the leading suppliers of retail chains.

5. Conclusion

From the previous review a picture can be drawn of the Russian business network and its evolution through time. Business networks are a mirror image to economic and political factors in the country and that is what makes Russian networks a point of interest. After the transition to a market economy Russia has been changing together with every aspect of life. From the above analysis of the pre transition and after transition in Russia it seems that organizations still hold on to the old ways of doing things in their organizations, and what has really changed is the formal organizational structure only. Managers are coming to understand more and more every day that working in a network is important for both the development of their business and their country in order to catch up with the race in the rest of the world (Sheresheva & Tretyak, 2004).

Several problems in the Russian business to business market have been identified. These problems can be summarized as shortage of supply from local manufacturers compared to of the higher supply of foreign carpets; dominance of foreign suppliers; dominance of black market smuggled goods; shortages of resources in the market including relative investments; a need to change managers ability to build a long-term win-win relationship to be able to keep up with the competition; establishing value added supplier-customer relationship; and having a more integrated supply chain through collaborating with suppliers.

From the review of findings from previous analysis of the network approach and associated research done of the Russian market some conclusions can be drawn:

First, the characteristic of importers is taking over the Russian market, which gives dominance to the role of wholesalers and distributors in the market, and an unsatisfied demand. Second, other wholesale markets in Russia share the same characteristic such as the glass market, consumer durable goods, and the fresh fruit supply, which show the same tendencies

In an effort to promote an integrated network approach for Russian wholesale market, research has analyzed it through the AAR model; actors, there is a lack of new actors in the market, as a result firms resort to old relationships with old suppliers in the market (Linz, 2002; Shresheva & Tretyak, 2004; Haaparanta et al., 2004). Vertical integration is common in Russia as a tool to have control over suppliers (Radygin, 2001; Kuznetsov & Simatchev, 2001; Ernst & Young, 2003). There is a need for new actors to play new roles in the market (Salmi, 2004).

Activities: geographical constraints have put limitation on activities between organizations (Salmi, 2004). Relationships are not the main criterion in Russian business but it is growing in importance and in length as long-term connections prevails more now than they used to (Shresheva & Tretyak, 2004).

Resources: there is a lack of investments in the market which is also a reason for the outdated equipment (Johanson, 2001; Linz, 2002; Salmi, 2004).

In general the Russian wholesale market is lacking management skills and efficiency (Karhunen, Kosonen, Lewonen, 2003); lack of trust between organizations and professionalism (Shresheva & Tretyak, 2006) and an underdeveloped relationship between suppliers and customers (Morch & Persson, 1999). Russian organizations need to develop their relationship with multinational organizations, which will promote learning new business norms and marketing approaches in a network context (Meyer, 1999; Tornroos & Nieminen, 1999).

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