

## **INVESTMENT STRATEGIES OF ENTERPRISES, REASONS, FINANCING – AN EMPIRICAL APPROACH**

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**Key words:** investment strategies, investing, reasons, enterprise, financing.

### **A b s t r a c t**

The paper presents the results obtained during the research on investment areas in the enterprises of north-eastern Poland, considering various reasons for investing and sources of financing.

The discussion concerned investment strategies that, on one hand, are directly subordinated to the development of the examined enterprises and, on the other hand, are to ensure the survival of companies or preserve their level of economic stagnation. Investment strategies of enterprises, both in the aspect of development and survival, are presented in the context of reasons underlying investments and of the feasibility of financing. Currently, it is becoming a *"business compulsion"* in the Polish sector of enterprises and a microscale strategic task.

## **STRATEGIE INWESTYCYJNE PRZEDSIĘBIORSTW, PRZESŁANKI, FINANSOWANIE – UJĘCIE EMPIRYCZNE**

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**Słowa kluczowe:** strategie inwestycyjne, inwestowanie, przesłanki, przedsiębiorstwo, finansowanie.

### **A b s t r a k t**

W artykule zaprezentowano wyniki uzyskane w trakcie badań nad obszarami inwestowania w przedsiębiorstwach północno-wschodniej Polski przy różnorodnych przesłankach i źródłach finansowania.

Rozważania dotyczyły inwestycyjnych strategii z jednej strony podporządkowanych jednoznacznie rozwojowi badanych przedsiębiorstw, z drugiej strony natomiast zapewnieniu im

przetwarzania czy utrzymania na poziomie stagnacji gospodarczej. Inwestycyjne strategie przedsiębiorstw zarówno w aspekcie rozwoju, jak i przetrwania zostały wyrażone w kontekście przesłanek inwestowania oraz realności finansowania. Staje się ona obecnie w polskim sektorze przedsiębiorstw „przymusem ekonomicznym” i zadaniem strategicznym w mikroskali.

## Introduction

This paper analyses investment strategies required for companies to develop independently, survive, adapt to changeable environmental conditions and the reality of a market economy and integrate with European structures. The types of reviewed investment strategies all stem from the business practices of enterprises from north-eastern Poland.

The empirical research was based on the following assumptions:

- It was assumed that the analysed investment strategies of enterprises constituted groups of strategies related both to the development of the enterprise and to its survival, and that investment on the micro scale is subordinated to those factors.

Investment undertakings resulted from the domination of particular reasons for investing in the practice of enterprise development. Investment strategies could be in such situations realized by means of (PŁOCICA 1984):

- investments consisting in the construction of new objects, buildings and structures,
- replacement and modernization investments,
- investment consisting in the development of plants and buildings.

Creation of new enterprises and increasing the existing production facilities consisting of the construction of new plants and buildings and in the restructuring of existing ones.

However, functions related to replacement and restructuring of the technical base in the existing enterprises were fulfilled by means of modernization investments.

- Research focused on the independence and the freedom of decisions of investors (entrepreneurs), who invested within the framework of a specific investment activity resulting from running needs or development necessities of enterprises.

This activity was burdened with the so-called feasibility of financing – from modernization, through development to new investments (OLKOWSKA 2003).

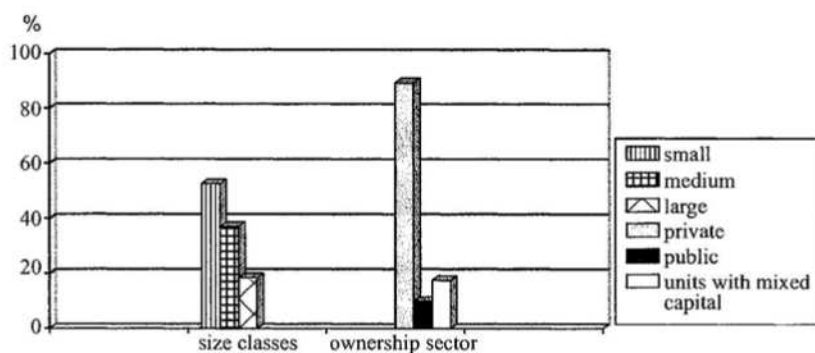
- The main subject of the discussion were manufacturing and service investments related to the developmental aims of enterprises or to those that are to ensure their survival.

## Methods and description of the analysed group

The analysis aimed at identification of types of investment strategies of enterprises with particular reasons for investing, as well as of the feasibility of their financing. Empirical research was addressed to local companies, operating in the north-eastern region of Poland. They helped to find the answer to questions regarding types of investment strategies directly related to the aims of the enterprise, connected rather to the reasons for investments than to particular types of investments (TOWARNICKA 1986).

Empirical research was conducted by way of a pilot survey in two stages at the turn of 2002 and 2003, and 2005 and 2006. The first stage included a group of 70 business units, and the second one – 40. In the description of the examined group, it was assumed that the size classes of enterprises, affiliation to ownership sectors and sections would make it possible to objectively and exhaustively present the examined objects. The examined group consisted of 110 enterprises. Classification of enterprises according to the employment level showed that small units, employing up to 50 people, constituted 58% (64 companies) of the total examined group. Medium enterprises (up to 250 employees) constituted 30% (33 business units), and large enterprises (more than 250 employees) constituted 12% (13 business units) of all examined business entities (*The Business...* 1999).

The analysis of the examined enterprises, as regards their classification into ownership sectors, showed that 85.7% of the examined units belonged to the private sector. Only 4.3% of enterprises belonged to the public sector, while the remaining 10% were units with mixed capital. The structure of the examined business units according to size classes and classification into ownership sectors is presented in Figure 1.



**Fig. 1.** Structure of the examined business entities according to size classes and ownership sectors

Source: Compilation on the basis of own research.

Taking into consideration the selection criteria, the largest percentage rate of investing enterprises was identified in the trade section (26% responses). The following activities were also found: industrial (20% responses), transport (16% responses), and construction engineering (13% responses). On the other hand, 4.5 % respondents, on average, pointed to hotel activity with restaurants and cafes. Among trade, transport and construction companies, the majority were small units, however, in industrial activities the majority were large enterprises.

The criteria of unit selection, as well as the structure of surveys to conduct the research, were identical. In the second stage of research, a deliberate selection of business units was used, by eliminating enterprises that had been already surveyed. As part of the description of the examined groups, the respondents were asked to choose the types of investment strategies in the aspect of development and survival in the light of the reasons for investing and sources of financing investments for the periods 2000–2002 and 2003–2005.

## Results

The first step in the empirical research was the presentation of the need for realization of various types of investments, taking into consideration their proper selection, depending on the various aims of the enterprises, under various conditions of financing (Table 1).

**Table 1**

Realization of investment strategies in the aspect of development or survival of enterprises from north-eastern Poland in the period of 2000–2005 (% responses)

| Types of investments<br>in development strategies<br>of enterprises              | Percentage of investing enterprises<br>in individual size classes |  |                                 |
|--|---|--|---------------------------------|
|  | small: up to 49<br>employees                                      | medium: between<br>50 and 249<br>employees | large: 250 or<br>more employees |
| New investments, consisting of the construction of plants, buildings, structures | 49  | 58   | 84                              |
| Replacement and modernization investments  | 27  | 40   | 45                              |
| Investments consisting of the development of plants and buildings                | 16  | 24   | 28                              |

Source: Compiled on the basis of own research.

The above mentioned types of investment aimed both at the attainment of specified manufacturing and service results for enterprises as the so-called main aim of investments, as well as their survival, i.e. maintaining the enterprise at the level of economic stagnation.

While indicating types of investment strategies, the respondents most frequently mentioned new investments, in all size classes of enterprises, (between 49% and 84% indications) (Table 1). They involved the purchase of land, construction of modern manufacturing and service facilities or technical infrastructure equipment.

At this point, one can suppose that the examined enterprises, most of all from private sectors, in the years of 2000-2005 directed their investment expenditures toward activities that were to strengthen their market position. However, as a general rule, those were capital consuming investments, characterized by a long payback period (OLKOWSKA 2004). In second place were modernization investment strategies of enterprises, fulfilling the process of reproduction of fixed assets, functions of replacement and modernization of the existing technical base (between 27% and 45% responses). On average, every fourth investing entrepreneur in the small-enterprises size class, and every second in medium- and large-size classes replaced and modernized fixed assets. This indicated a direct process of aging of the existing fixed assets, particularly in small enterprises. On the other hand, investments consisting of the modernization of plants and buildings represented the smallest percentage (between 16% and 28% responses).

The examined enterprises were bound by investment strategies, especially as regards investing. The companies under analysis indicated various reasons for investing, both in the aspect of development as well as of survival. The variety and assessment of the significance of reasons underlying investments was assumed to be decisive, important or insignificant (Table 2.). Many among the examined companies indicated several reasons at the same time, indicating the most important one.

On the basis of the data presented in Table 2, one can claim that dominant reasons assessed as decisive and important in all size classes of enterprises were the reasons regarding the nature and requirement of the markets, including the foreign market (between 42% or 61% to 85% indications). Investment strategies of the examined enterprises were realized first of all as new investments and in the form of development of existing production and service facilities. At another stage of this development strategy, an increase in goodwill was also mentioned (between 30% and 69% responses). However, dominant reasons for investments in the form of reducing unit costs and the improvement of production quality, indicated concurrently as decisive and important in the examined size classes of enterprises (between 42% and 71% responses) resulted from the need to modernize fixed assets in existing investment and service enterprises. These were mainly replacement and modernization investments.

Table 2

Assessment of the significance of the reasons for investing in the realization of investment strategy of the examined enterprises (% responses provided by respondents)

| Reasons for investing   | Significance  | Percentage of investing enterprises, according to size classes |                                      |                              |
|---|---------------|--|--------------------------------------|------------------------------|
|   |               | small: up to 49 employees                                      | medium: between 50 and 249 employees | large: 250 or more employees |
| Growth of sales and change of the production profile.             | decisive      | 23   | 12                                   | 23                           |
|   | important     | 41   | 24                                   | 15                           |
|   | insignificant | 38   | 12                                   | 54                           |
| Reduction of unit costs   | decisive      | 19   | 18                                   | 15                           |
|   | important     | 50   | 24                                   | 54                           |
|   | insignificant | 41   | 15                                   | 8                            |
| Improvement of production quality                                 | decisive      | 23   | 24                                   | 54                           |
|   | important     | 48   | 21                                   | 15                           |
|   | insignificant | 27   | 18                                   | 31                           |
| Nature and requirements of domestic and foreign market            | decisive      | 25   | 27                                   | 31                           |
|   | important     | 36   | 15                                   | 54                           |
|   | insignificant | 25   | 33                                   | 15                           |
| Development of the competitiveness in domestic and foreign market | decisive      | 36   | 15                                   | 0                            |
|   | important     | 41   | 21                                   | 23                           |
|   | insignificant | 34   | 18                                   | 38                           |
| Increase in goodwill  | decisive      | 22   | 12                                   | 15                           |
|   | important     | 47   | 18                                   | 46                           |
|   | insignificant | 36   | 42                                   | 15                           |
| High level of asset obsolescence and its high failure frequency   | decisive      | 9  | 21                                   | 23                           |
|   | important     | 20   | 18                                   | 38                           |
|   | insignificant | 34   | 58                                   | 38                           |
| The pace of technological progress                                | decisive      | 19   | 12                                   | 31                           |
|   | important     | 47   | 39                                   | 15                           |
|   | insignificant | 31   | 12                                   | 38                           |
| Other reasons, e.g. company reputation                            | decisive      | 9  | 0                                    | 8                            |
|   | important     | 23   | 0                                    | 0                            |
|   | insignificant | 5  | 0                                    | 0                            |

Source: Compiled on the basis of own research.

The implementation of technical progress was strongly related both to the strategy of development as well as to that of the survival of enterprises. Between 46% and 66% of respondents indicated its significance as decisive and important. The character of investments in these strategies could be characterized as expanded, simple or narrowed reproduction. The investment strategies of enterprises, both in the aspect of development and of that of survival, should be undertaken upon careful examination of the rationality of financial economics of enterprises. This is currently becoming in the Polish sector of enterprises "business compulsion" and a strategic task on a microscale.

Table 3

Internal and external financing of investments in the examined enterprises  
for the period 2000–2002 and 2003–2005 (% responses in size classes)

| Sources and forms<br>of in-vestment<br>financing.                            | Percentage of the examined enterprises in individual size classes |           |   |           |                                  |           |
|--|---|-----------|---|-----------|----------------------------------|-----------|
|  | small: up to 49<br>employ-ees                                     |           | medium: between 50<br>and 249 employees |           | large: 250 or more<br>em-ployees |           |
|  | 2000-2002   | 2003-2005 | 2000-2002                               | 2003-2005 | 2000-2002                        | 2003-2005 |
| <b>1. Internal financing</b>   |   |           |   |           |                                  |           |
| a) Retained profit   | 51  | 49        | 46                                      | 50        | 40                               | 51        |
| b) Depreciation<br>write-offs  | 36  | 36        | 77                                      | 67        | 67                               | 75        |
| <b>2. Own external financing</b>   |   |           |   |           |                                  |           |
| a) Owners' contributions   | 0   | 0         | 5                                       | 9         | 0                                | 25        |
| b) Material<br>contributions – land for<br>construction – transport<br>means | 0 7   | 9 9       | 16 5                                    | 4 0       | 0 0                              | 0 0       |
| c) Targeted governmental<br>subsidies  | 7   | 8         | 5                                       | 8         | 11                               | 25        |
| <b>3. External debt financing</b>  |   |           |   |           |                                  |           |
| a) Investment credits<br>and credits on mortgage                             | 31  | 33        | 39                                      | 44        | 22                               | 25        |
| b) Leasing   | 15  | 18        | 26                                      | 36        | 22                               | 25        |
| c) Others (long-term<br>loans)   | 10  | 14        | 9                                       | 14        | 44                               | 50        |

Source: Compiled on the basis of own research.

As it follows from Table 3, retained profit was a particularly important source of internal financing for two research stages of 2000–2002 and 2003–2005, both for the SME sector, as well as for large enterprises of north-eastern Poland (between 45% to 49% responses). However, depreciation write-offs played a leading role in the examined periods as regards internal financing of medium and large entities (about 70% responses on average). Significantly smaller was their role in financing the development of small enterprises (36% responses). One can suppose that small depreciation write-offs or their lack in this size class resulted from a high level of asset obsolescence or their full depreciation.

Summing up, in the examined group, on average, every other respondent indicated internal sources of financing. For about 50% of the respondents, the lack of own means did not make it possible to carry out development investments, as well as those aiming at the survival of the enterprise.

However, own external financing, including contributions of owners and material contributions, constituted in all classes of the examined enterprises a marginal phenomenon, which did not play in the years 2000–2005 any



larger role in investment financing. Targeted governmental subsidies were not as popular as a domestic instrument of supporting new investments or those that created new jobs. These were trace quantities, involving 1–3 investors – entrepreneurs in the SME sector. These were entrepreneurs from transport, construction and trade sections. As regards the class of large enterprises, two entrepreneurs in the industrial section benefited from subsidies during the analysed period. Those subsidies were allocated for technological innovations related to the implementation of quality and introduction of ISO.

As regards external financing of investments in the examined enterprises from north-eastern Poland in the period of 2000–2005, every third entrepreneur in the SME sector and every fourth in a class of large enterprises, on average, received investment credit or credit on mortgage (Table 3). Most respondents expressed their opinion that investment credit was too expensive and it required complicated procedures, securities or additional documentation of investment activity. However, credit on mortgage was quite popular and investor-entrepreneurs directed their investment expenditures for buildings and constructions aiming at increasing their market value.

Although leasing companies offered a wide range of goods, it was not a popular source used in financing of investments in the SME sector, as regards the entrepreneurs under analysis. Leasing offers were used, on average, by every fifth of the respondents. However, in the class of large enterprises, in the period of 2000–2002, 22% entrepreneurs chose leasing (2000–2002) and in the years of 2003–2005 – 25%.

On the other hand, other forms of financing, such as long-term loans, were more significant than leasing. They were used, on average, by every third entrepreneur-investor from all size classes. The respondents reported them to be a convenient form of involving debt capitals in investments, as they do not involve costs of issuing which would occur while running up a debt by taking out a bond loan on the capital market.

It should be emphasized that the examined group, including 110 enterprises from north-eastern Poland, was not a big sample. It covered 25% of return from over 400 surveys that had been sent. This, however, does not belittle the importance of the examined issue.

## Summary

This paper presents selected issues regarding the investment strategies of enterprises from north-eastern Poland. Discussion focuses on investment decisions, in the aspect of development or the survival of enterprises. Their common feature is the realization of business aims, both running and related to the development of enterprises, as expressed by various reasons and financial conditions for investing.



The obtained results of empirical research show that the development of investment strategies of enterprises is affected by reasons underlying the investments, related to the development aims of enterprises, and the feasibility of financing investment decisions that have been made.

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