THE RISE OF THIRD-WORLD MULTINATIONAL CORPORATIONS

by

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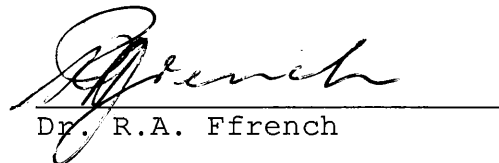

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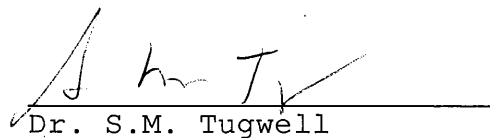

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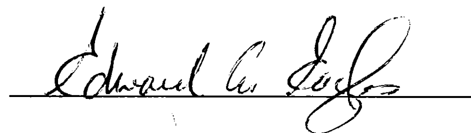

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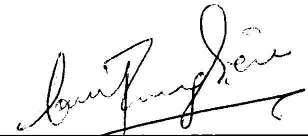

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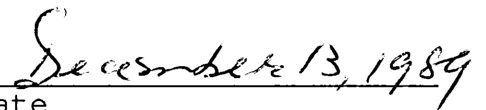

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Abstract

The internationalisation of economic activity has taken many new and dynamic forms in recent years, of which perhaps the most dynamic and least expected has been the emergence of multinational corporations (or MNCs) from the Third-World countries. This study examines the rise of these MNCs and tentatively draws some general conclusions about this phenomenon.

The analysis of this study can be divided into two main areas. The first area involves reviewing some theoretical concepts that were formulated to describe MNCs from developed countries (chapter two); and works of researchers who have applied these concepts to describe MNCs from the Third-World (chapter three). The second area surveys the characteristics of Third-World MNCs with the aim of establishing some consistent behavioural patterns of Third-World MNCs.

The conclusion of this study provides an overview of the competitive advantages which Third-World firms might have in competing with other firms; and factors that motivated Third-World firms to utilise those advantages in the form of foreign

CHAPTER ONE

INTRODUCTION: THE STUDY IN PERSPECTIVE

I) Introduction

Multinational companies operating from and with head offices in developing countries, only yesterday seemed an apparent contradiction in terms, yet they are now a serious force in the developmental process of the world. In the 1950s and 1960s, it would have been difficult to imagine that developing countries could offer the environment that would provide many local firms with competitive advantages sufficient for international competition. Nevertheless, the number of developing countries whose firms now qualify for the label "multinational" has been steadily increasing. More significantly, the total number of overseas projects undertaken by the firms of these countries has been growing at a rapid rate.

While the topic of multinational corporations (or simply MNCs) is always in the forefront of discussions about structural shifts in the world economy, yet many aspects of restructuring have remained relatively unexplored.

of foreign direct investment from the Third-World countries. The purpose of this study is, therefore, to examine the phenomenal emergence of MNCs from developing countries, and to document those characteristics and behaviour common to them. This study will also review some of the existing theories of foreign direct investment as carried out by developed countries, and examine to what extent these theories can explain the emergence of MNCs from the Third-World.

II) Conceptual Clarifications

The study of international business usually involves survey into references that are relatively broad in nature because international business itself involves entrepreneurs, governments and consumers of different countries; and production of various goods and services. Therefore, some conceptual clarifications with regard to the meaning of "multinational corporation" and "developing countries" are necessary so as to avoid unnecessary confusion. The term "multinational corporation" is used here to mean (in a broad sense) all enterprises which control assets- factories, mines and sales offices- in two or more countries. This definition

that the terms "corporation," "firm," "company" and "enterprise" will be used interchangeably so as not to impose any restriction on the meaning and usage of these words.

The term "developing countries" refers to all the non-socialist countries of Africa, Asia and Latin America that are not members of the Organization for Economic Cooperation and Development (OECD). The only region that will not be covered in this thesis is the Middle East. The foreign investments made by these latter countries, because of their distinctive economic and political conditions, constitute a special case. They therefore require a different kind of theoretical and empirical analysis, one that is not possible within the scope of this study.

The term "developing countries" is also used as a synonym for "Third-World countries"- an expression which will appear occasionally throughout this study. Hence, from both definitions, the expression "developing (Third-World) country MNC" refers to a firm that is located in one of the developing nations and owns production or service facilities outside its national boundary.

basically a review of literature. It will draw upon various published studies of Third-World MNCs to derive a composite picture, from which it is hoped inferences can be drawn in terms of the pattern and motivation for direct foreign investment by Third-World nations. The sequence for analysis of these studies is indicated below.

Chapter Two, which is theoretical in orientation, reviews some of the existing theories of foreign direct investment by developed countries. However, as pertaining to this study, references will only be made to the particular theories that are feasible in explaining foreign direct investment from the socialist Third-World nations. Therefore, theories that pertain primarily to developed and communist countries will not be dealt with to any length. Examples of such theories are "Organisation Theory" and "Marxist Economic Theory," which have been used to describe MNCs mainly from developed and communist countries respectively.

Chapter Three provides some historical background to the development of Third-World MNCs. It also reviews studies that have adopted the theories of direct investment by developed countries (theories that will be examined in the preceding

particularly such aspects as investment motives and strategies, and the character of their foreign business operations. This chapter will also look into the relationship between Third-World MNCs and a very important participant of the investment process- the home and host country governments.

Chapter Five gives an overview of the events that have led to a degree of prominence of Third-World MNCs in the world economy. This chapter will conclude with a final effort to seek and offer views that can explain or express adequately the factors underlying the growing trend of Third-World MNCs.

CHAPTER TWO

THEORIES OF THE MULTINATIONAL CORPORATION: DEVELOPED COUNTRIES

I) Introduction

The importance of foreign investment in the world economy has been generally acknowledged, and in particular the MNCs from the developed countries. However, establishing the "fact" that this global phenomenon is important and omnipresent is not sufficient. Further explanation with empirical evidence and theoretical analysis based on explicit concepts is necessary prior to meaningful generalizations.

In undertaking this task, various researchers have offered theories to characterise the operations of MNCs. In this chapter, only three theories of foreign direct investment will be explored. They are the monopolistic theory, first advanced by Hymer in 1960; Vernon's product life cycle theory; and Dunning's eclectic theory of international production. These theories are chosen because of their potential ability in explaining foreign direct investment by developing countries.

conditions and sometimes discriminating national policies of host countries. As a result, for direct investment to take place, the investing firm must have some special advantage, that is monopoly or oligopoly power to counteract the intrinsic disadvantage of foreign operations.

The set of theories that concentrate on identifying the characteristics of monopolistic or oligopolistic MNCs are broadly termed "oligopolistic theories of direct investment". They are drawn from different areas of studies: theory of the firm, monopolistic competition, industrial structure, location and innovation. Quite clearly, they all refer to the condition of an imperfect market structure. Such market structures may have been attributable to economies of scale, governmental influences, innovation and technology developments by the pertinent MNCs.

Hymer, who first advanced this theory in 1960, and Kindleberger, Horst and Caves (1971; 1974a; 1974b) have focussed their research on the domestic market structures in the developed capital-exporting countries. The basic premise underlying their theories is that domestic firms in advanced countries, through mergers and takeovers, have increased the

of access to capital markets, information, advanced technology and maybe even government favours. Together with the market power normally associated with a monopoly or oligopoly, the operations of MNCs usually mean profits and wealth to the investing firms. In this way, the superiority of producing abroad is explained. The exploration expenditure, or the proprietary knowledge, or even the goodwill possessed by the firm is "indivisible," so that its use abroad involves little additional cost to the firm. Through patents, advertising or technological advances, the firm thus tries to prevent other firms from appropriating this monopolistic advantage.

III) Product Life Cycle Theory

Vernon's theory of the product life cycle can be described as an application, or a variant of the oligopolistic theories identified in the preceding section, as exemplified by the experience of U.S.-based MNCs in the past one hundred years (Moran 385). It centres on the role of technological innovation with special rights in new discoveries, such as knowledge, or discovery of a more efficient production function, or a differentiated product.

stage is usually at home because of the availability of production factors, to be near to the market, to cater efficiently to changes in demand, and uncertainties abroad.

At the mature stage, the most efficient production process has emerged and the product form stabilised. The demand for the product, if the product proves successful, also becomes more price-elastic as consumers have better knowledge of the product and cheaper substitutes become available. To keep costs down, output would expand through increasing the scale of production. Firms would also export to other countries when local competition begins to emerge. When foreign demand is established and exports are becoming more difficult because of trade barriers, direct investment overseas will be made so as to market and service the product, and to circumvent the trade barriers impeding exports.

At the standardised stage, the product is completely uniform and non-differentiated, and the production process is commonly known. Competition among firms would then be based mainly on prices. The implication of such competition is that the costs of production has to be further minimized. In such cases, the firm would then seek to locate its production

innovations, exports and investments, with exports serving as a 'feeler' to establish whether it should be backed by investment.

Being basically a behavioural model, there is a certain efficiency in describing the process of foreign investment which has exhibited a regular pattern. During the century or so prior to the development of this theory, the motivation and response of U.S. enterprises with respect to their overseas subsidiaries have reflected these persistent patterns. According to Moran, the product life theory was used effectively to explain the "strong pressures for foreign investment" that he believes so strongly affect "American corporate capitalism" (369).

IV) <u>The Eclectic Theory of International Production</u>

The eclectic theory of international production, increasingly referred to as the 'OLI (organization, location and internalization) paradigm', is proposed by Dunning. He integrates three strands of economic theory- industrial organization, location and market failure theories- to explain the ability and willingness of firms to exploit the advantages

the competitive advantages associated with ownership and location. To summarize briefly, the theory suggests that the propensity for a country's enterprises to engage in foreign direct investment is determined by three conditions. The first condition is the extent to which the enterprises possess or can gain access to assets or rights to assets which its foreign competitors do not possess, or possess to the same degree or on the same terms. The second condition is whether it pays these enterprises to exploit these proprietary advantages themselves, that is, internalize their use; or sell the right to use them to foreign firms (that is externalize their sale). The third condition is whether or not the enterprises choose to locate at least part of the production of the output generated by the advantages outside their home countries. The more a country's enterprises possess ownership-specific advantages, the greater the incentive is to internalize them; and the more these enterprises find it profitable to exploit the advantages outside their national boundaries. By the same token, a country is likely to attract inward investment when the reverse conditions apply. A country's involvement in international direct investment then

nature of these advantages and the conditions under which they are most likely to exist. Some of these are illustrated in table 1. As shown in the table, the presence of (permanent) ownership advantages may be explained by reference to the industrial organization and the extent to which market imperfections create barriers to competition; internalization advantages depend on the extent to which the market mechanism is capable of capturing the full economic rent arising from these advantages; and location advantages depend on relative input (including transport and tariffs) costs, productivity, market characteristics, and government policies of alternative locations.

This approach to explaining international production has been called eclectic for the following reasons. It embraces the three main forms of foreign involvement by enterprises; namely, direct investment, exports, and contractual resource transfers, such as licensing, management contracts, technical service agreements, and provides an explanation as to which path for exploitation is preferred. In all three forms, the possession of ownership advantages is a necessary prerequisite for involvement. However, the possession of internalization

Table 1

The Eclectic Theory of International Production

---

1. Ownership-Specific Advantages (of enterprises of one nationality, or affiliates of same, over those of another).

   a. Which need not arise owing to multinationality. Those owing mainly to size and established position, product or process diversification, ability to take advantage of division of labour and specialization, monopoly power, better resource capacity and usage.

      Proprietary technology, trade marks (protected by patent and other legislation).

      Production, management, organizational, and marketing systems; R&D capacity; "bank" of human capital and experience.

      Exclusive or favoured access to inputs, for example, labour, natural resources, finance, and information.

      Ability to obtain inputs on favoured terms (owing for example, to size or monopsonistic influence).

      Exclusive or favoured access to product markets.

      Government protection (for example, control on market entry).

   b. Which those branch plants of establishment enterprises may enjoy over de novo firms.

      Access to capacity (administrative, managerial, R&D, marketing, and so forth) of parent company at favoured prices.

      Economics of joint supply (not only in production, but purchasing, marketing, and financing arrangements).

   c. Which specifically arise because of multinationality. Multinationality enhances preceding advantages by offering wider opportunities.

      More favoured access to and/or better knowledge about information, inputs, and markets.

Table 1 (continued)

2. Internalization Incentive Advantages (that is, to protect against or exploit market failure).

Avoidance of transaction and negotiating costs.

To avoid costs of enforcing property rights.

Buyer uncertainty (about nature and value of inputs, for example, technology, being sold).

Where market does not permit price discrimination.

Need of seller to protect quality of products.

To capture economies of interdependent activities (see 1b above).

To avoid or exploit government intervention (for example, quotas, tariffs, price controls, tax differences, and so forth).

To control supplies and conditions of sale of inputs (including supplies to competitors).

Where permitted, to be able to engage in practices, for example, cross-subsidization, predatory pricing, and so forth, as a competitive (or anti-competitive) strategy.

3. Location-Specific Variables (may favour home or host countries).

Spatial distribution of inputs and markets.

Input prices, quality, and productivity, for example, labour energy, materials, components, and semi-finished goods.

Transport, communication availability, and costs.

Government intervention.

Control on imports, including new tariff barriers, tax rates, incentives, climate for investment, political stability, and so forth.

Infrastructure (commercial, legal, transportation).

Psychic distance (language, cultural, business, and customs

base. The matrix in figure 1 summarizes the conditions determining those choices.

Figure 1 Conditions Determining the Forms of Foreign Involvement by Enterprises

		Advantages		
		Ownership	Internalization	(Foreign) Location
Route of Servicing Market	Direct foreign investment	Yes	Yes	Yes
	Exports	Yes	Yes	No
	Portfolio resource transfers	Yes	No	No

Source: Dunning, J.H. "Explaining Outward Direct Investment of Developing Countries: In Support of the Eclectic Theory of International Production." Multinationals from Developing Countries. 1981: 4.

In identifying the forces influencing these advantages, economists have found it useful to distinguish three structural characteristics; namely, those which are specific to particular countries, particular types of activities (or industries), and particular enterprises. In other words, the propensity of a particular enterprise to invest overseas will vary according to its home country, the country or countries in which it is proposing to make an investment, the range and the type of products (including intermediate products) it is intending to produce, and its underlying management and organizational strategy. These characteristics are illustrated in table 2. It is worth noting however that they are not always independent of each other. For example, in explaining why different countries' enterprises may have different propensities to invest, one may turn to the industrial composition of such investment, but this is, in part, a reflection of the specific endowments of the countries in question.

By combining the information in tables 1 and 2, one has the nucleus of the eclectic theory of international production. The propensity of each country to engage in direct

Table 2

Some Illustrations of How the Conditions for Foreign Direct Investment May Vary According to Country, Industry, and Firm-Specific Considerations

	Ownership
Country (Home-Host)	Factor endowments (e.g., resources and skilled labour) and market size and character. Government policy toward innovation, protection of proprietary rights, competition, and industrial structure. Government controls on inward direct investment.
Industry	Degree of product or process technological intensity. Nature of innovations. Extent of product differentiation. Production economics (e.g., if there are economies of scale). Importance of favoured access to inputs/markets.
Firm	Size, extent of production, process, or market diversification. Extent to which enterprise is innovatory or marketing-oriented or values security and/or stability, e.g., in sources of inputs, markets, etc.
	Internalization
Country (Home-Host)	Government intervention and extent to which policies encourage MNCs to internalize transactions, e.g., transfer pricing. Government policy toward mergers. Differences in market structures between countries, e.g., with respect to transactions costs, enforcement of contracts, buyer uncertainty, etc. Adequacy of technological, etc. Infrastructure in host countries and ability to absorb portfolio resource transfers.
Industry	Extent to which vertical or horizontal integration is possible/desirable, e.g., need to control sourcing of inputs or markets. Extent to which internalizing advantages can be captured in contractual agreements (see the early and later stages of product cycle). Use made of ownership advantages. See the IBM with Unilever type operation.
Firm	Organizational and control procedures of enterprise.

Table 2 (continued)

	Location
Country (Home-Host)	Physical and psychic distance between countries. Governments intervention (tariffs, quotas, taxes, etc.). The exchange rate.
Industry	Origin and distribution of immobile resources. Transport costs of intermediate and final good products. Industry-specific tariff and nontariff barriers. Nature of competition between firms in industry. Can functions of activities of industry be split? Significance of "sensitive" locational variables, e.g., tax incentives, percentage of labour in total costs.
Firm	Management strategy toward foreign involvement. Age and experience of foreign involvement. (Position of enterprise in product cycle, etc.). Psychic-distance variables (culture, language, legal and commercial framework). Attitudes toward centralization of certain functions, e.g.. R&D, office and market allocation, etc. Geographic structure of asset portfolio and attitude toward risk diversification.

Source: Dunning, J.H. "Explaining Outward Direct Investment of Developing Countries: In Support of the Eclectic Theory of International Production." Multinationals from Developing Countries. 1981: 5.

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CHAPTER THREE

THE EMERGENCE AND SOME THEORETICAL APPROACHES PERTAINING TO THIRD-WORLD MNCS

I) Historical Development of Third-World MNCs

It may be of interest to note that direct foreign investment from developing countries has existed from as early as the nineteenth century. Alparagats, an Argentine textile manufacturer was the first recorded instance of a Third-World multinational. In 1890, the firm set up an affiliate in Uruguay, to be followed by another in Brazil in 1907. By the 1930s, other Argentine firms, including Siam di Tella (metallurgical products) and Bunge y Born (grain trading, finance and miscellaneous manufacturing activities) had also established branches in other Latin American countries (Lall "The Rise" 618).

These cases apart, the significant growth of direct investment from developing countries actually started in the 1960s and gained momentum in the 1970s. This is attributable to the fact that following the Second World War, many colonial nations were given their independence; and hence emerged as

The 1960s and 1970s witnessed the internationalization of the global system, with innovative changes in the organization and operation of banking, finance, insurance, communications, transport and other services. With trade restrictions imposed by developed countries to safeguard their economy combined with economic control measures imposed by developing countries, these together have provided incentives for foreign direct investment to take place especially within Third-World countries (Vernon 53). Consequently, these factors have contributed to the rise of MNCs from the Third-World.

To elaborate further, in 1960 the first Indian manufacturing investment abroad went into operation; foreign investment by Hong Kong firms also began about the same time. By 1970 India and Hong Kong alone held at least 370 overseas manufacturing subsidiaries. However, a large proportion of the parent firms are concentrated in a few developing countries located in South-East Asia and Latin America; and in large measure from the newly industrialized countries (NICs). By 1980, it was estimated that there were 1,964 overseas subsidiaries and branches established by 963 parent firms of developing countries. Of the 1,964 subsidiaries and branches,

Despite the rapid growth of the Third-World MNCs, the total stock of investment made still remains relatively small when compared to the total stock of investment by developed countries. Nevertheless, the trend for the Third-World MNCs is significant and gaining increasing importance in the world economy.

Numerous studies have been conducted to try to understand the forces motivating firms to invest abroad. Most studies have focused on trying to determine the specific advantages that Third-World MNCs may have in investing abroad; and competing both with local firms of the host countries and with affiliates of other MNCs. Brief references to some of these works were made in the theories examined in chapter two, in an effort to determine their relevancy with respect to Third-World MNCs. Given the fact that this is a relatively new area of research, a review of these studies, based on theories applicable to MNCs of developed countries, would seem as a logical first step to understanding the process of emergence of Third-World MNCs. The rest of this chapter is a review of some of these works.

World MNCs do not possess those monopolistic advantages- particularly 'frontier' technologies and sophisticated marketing networks- which seem to prevail for firms in developed countries.

The innovations of firms from developing countries, which allow them to develop into monopolies, are closely linked to their home-market characteristics (Wells "Foreign" 25). The way in which Third-World MNCs gain advantages in order to be competitive abroad, is to assimilate foreign technologies and modify them to adapt and suit their local market environment. For example, an Indian firm has developed dyes that are less sensitive to intensive sunlight than the dyes generally available from the temperate industrialized countries. The technology used to manufacture the dyes was initially transferred from developed countries (Wells "Foreign" 29).

For foreign technology to be assimilated efficiently into the local market, the special characteristics of the home market will play an important role in generating monopolistic advantages. One of the characteristics of the home market is its small size. Another characteristic is the shortage of many inputs for the production process. Moreover, in most Third-

production processes in developing countries are standardised and labour-intensive (Wells "Foreign" 26-9).

Several studies have concurred with the finding that the proprietary advantages of Third-World MNCs are closely linked to the characteristics of their home country. In his description of Latin American firms, White emphasises that Third-World MNCs have made important contributions to technology based on their research and on internalizing and diffusing new technologies (157). The process of internalizing and diffusing technologies is somewhat unique for the countries of Latin America because the outflow and inflow of intraregional foreign direct investments seem to coincide closely with the different levels of development among the countries in the region. On the other hand, Lecraw and Wells, who based their work mainly on Asian firms, point out the innovativeness of Third-World MNCs in making technologies more flexible and more adaptable to using local materials ("Direct" 445-47; "Foreign" 28). They also emphasize the experience which Third-World MNCs have in using and adopting labour-intensive, small-scale production techniques, to produce at low cost non-differentiated products of low to medium quality.

motivated to make direct investment to preserve its market share, its competitive advantages are derived mainly from the transfer of new technologies of developed countries. If such transfer enables a firm to establish itself 'first' in a particular market, it will give the firm an advantage over others; and this may be exploited in several small markets which the larger MNCs have little interest. This advantage is in turn strengthened by labour-intensive production processes and the small-scale home markets. The characteristics of the home market are often compatible with the factor markets and demand conditions that exist in other developing countries. These similarities would later provide the firm the opportunity and challenge of the kind to which the firm has already responded at home.

III) The Product Life-Cycle Approach

The product life-cycle theory can be described as an application or a variant of the oligopolistic approach as stated in the preceding chapter. According to its premises, firms innovate for their home market, gathering skills and knowledge that, in some cases, are then exploited abroad.

needs of the local conditions. This in turn often calls for standardised and labour-intensive production processes.

Innovation in response to small markets, scarce foreign inputs, and other special characteristics of the developing country fit well into the product life-cycle theory. In the later stages when the modified technology has matured, competition on the local scene begins to intensify. In order to maintain a share of the market, the skills acquired at home by firms can be turned into assets that can be exploited elsewhere.

One may question the ability of these Third-World MNCs to develop such proprietary advantages if technology is diffused and easily imitated. The answer lies in the characteristics of technological progress, namely the 'localization' of technical change.

In his study on the transfer of technology, Lall uses the 'evolutionary' theory of technical change, which suggests that firms only know and understand a very limited range of production techniques ("Developing" 603). To shift to a different production technique would impose considerable cost and effort to the firms. Their technical progress is thus

thus taken cognisant of all the activities related to it. Because of this strong link or (which may be in the form of ownership, control or even passive licensing), technology cannot be efficiently reproduced or transferred even in activities where competitors may possess long-term comparative advantage.

Other proprietary advantages of Third-World MNCs might be specific marketing skills, promotion strategies and production of unsophisticated products. In addition, certain firms may be able to meet customer requirements (quality control, product adaptation, after sales services, and so on), and achieve a high degree of managerial and organizational skills. It is also recognised that these advantages may be further strengthened by their ability to function better in the environment of other developing countries, especially those whose cultural, social, economic and political ambitions are similar.

In view of the previous analysis, it seems possible that the oligopolistic theory of direct foreign investment with a few modifications can explain the phenomenon of the emergence of Third-World MNCs. However, the conventional monopolistic

can be traced to such phenomenon as evolutionary and non-transferable technological growth, technical and product adaptation, learning and accumulating unique skills in less-developed countries. These are more aspects of 'minor' technical change and human capital formation, rather than the standard determinants of monopoly or oligopoly in the developed countries.

IV) The Eclectic Theory Approach

Dunning has offered an alternate approach to the understanding of foreign direct investment by Third-World firms with his eclectic theory. He postulates that

> "the propensity of a developing country to engage in direct foreign investment is partly a function of its stage of economic development and partly a function of its particular characteristics of those of its form which make for a unique combination of ownership, location and internalization advantages, whatever its stage of development" ("Explaining Outward" 6).

In particular, Dunning develops a four-stage investment development or cycle, where the stages are identified by the country's gross national product and net outward direct investment, both variables being

Table 3

Inward and Outward Direct Investment and Stages of Economic Development

	Inward Investment		Outward Investment	
Stage 1	Of	Substantial	Od	None
	I	Substantial	I	Not Applicable
	Ld	Few	Lf	Not Applicable
Stage 2	Of	Substantial	Od	Few
	I	Substantial	I	Few
	Ld	Improving	Lf	Few
Stage 3	Of	Declining/ more specialised	Od	Growing
	I	Declining	I	Growing
	Ld	Declining	Lf	Growing
Stage 4	Of	Declining/ more specialised	Od	Increasing
	I	Declining	I	Substantial
	Ld	Declining	Lf	Increasing

Key to symbols: O = ownership advantages
L = location advantages
I = internalization advantages
f = foreign
d = domestic

Source: Dunning, J.H. "Explaining Outward Direct Investment of Developing Countries: In Support of the Eclectic Theory of International Production." Multinationals from Developing Countries. 1981: 8.

is no outward direct investment because the country's own enterprises are generating no ownership-specific advantages. Neither is there any inward direct investment because there is insufficient location-specific advantages to warrant the setting up of affiliates by foreign firms. This may be so because domestic market is not large enough , or because of a lack or inadequate infrastructure and back-up resources (for example, skilled labour) required to make the exploitation of available resources profitable.

In stage 2, inward direct investment begins to rise as the domestic market enlarges (or demand increases) and/or local infrastructure is improved. At the same time, since there still remains insufficient back-up indigenous resources, most capital inflows are likely to be internalized. Outward direct investment still remains negligible because the country's enterprises have not yet established ownership advantages sufficient for them to compete competitively overseas.

In stage 3, net inward investment per capita now starts to fall. This could be so because the ownership advantages of foreign affiliates fall as the indigenous firms, stimulated

mark the beginning of a country's international investment specialization, in which it seeks to attract inward direct investment in those sectors in which its comparative location advantages are strongest but the comparative ownership advantages of its enterprises are weakest. At the same time, its own enterprises will invest abroad in those sectors in which comparative ownership advantages are strongest but their comparative location advantages are weakest.

In Stage 4, a country is a net outward investor, that is its investment flow abroad exceeds that of foreign-owned firms in its own country. This reflects the strong ownership advantages of its firms, and/or an increasing propensity to exploit the advantages from a foreign rather than a domestic location. These advantages could be attributable to the increasing local labour cost (normally associated with high level of economic development); or the need to export resources (including certain types of labour) to help sustain its international competitive position in the world market; or it may be due to increasing tariffs and barriers to trade to the kind of goods exported by these countries.

The investment development cycle just outlined suggests

as outward investors are approaching the third stage (18). He also suggests that at any particular stage of development, countries may differ from each other in their international involvement and structures. These differences can be explained by different country-specific characteristics, which are reflected in the possession of ownership, location, and internalization advantages as outlined in the preceding chapter.

In summarising the eclectic theory with regard to developing countries, a country's net investment position passes through four identifiable development stages. In each stage, the flow of foreign direct investment is determined by ownership, location and internalization advantages that are generated by the specific endowment, market and environmental characteristics of the country. Finally, it can be asserted that the eclectic theory approach is derived from the other theories of direct foreign investment. Ownership advantages are explained by reference to the theory of industrial organization within which oligopolistic theory is significant. The location theory identifies the locational advantages, while internalization advantages stem from the theory of the

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CHAPTER FOUR

BEHAVIOURAL CHARACTERISTICS OF THIRD-WORLD MNCS: A GENERAL SURVEY

I) Introduction

In the previous chapter, the theories of foreign direct investment were discussed with respect to foreign direct investment being made by developing countries. Like all other economic theories, the theories of foreign direct investment were derived by abstracting the "essentials" of the real world economies, incorporating only a small portion of the vast complexities of the internationalization process. As a result, each theory of foreign direct investment has its limitations, and hence, any analysis recognising the recent emergence of Third-World MNCs will be constrained.

In the search for a better understanding of this development, these theories should be complemented with observed or recorded examples that portray the actual behavioural pattern of the Third-World MNCs. In this manner, the theories of foreign direct investment can be tested to see how well each can predict the real world behaviour of Third-

The primary aim of this chapter is to describe the general behavioural pattern of Third-World MNCs. The approach will primarily be to explore some of the common concerns that most of the Third-World MNCs have shared. More specifically, the following concerns of the Third-World MNCs have been identified: the investment motives that underlie their international ventures; the investment strategies that have been pursued by these firms; and the character of their foreign business operations.

Closely related to the above mentioned concerns is another important aspect that must be examined, that is the relationships between the Third-World MNCs and the host and home country governments. Just like all other international ventures, the reactions of the host and home country governments play a major role influencing the decisions of managers of Third-World MNCs (Boarman and Schollhammer 1975).

Another aim of this chapter is, where applicable, to highlight those characteristics of the Third-World MNCs that appear to set them apart from the foreign affiliates headquartered in the advanced countries. However, the characteristics of foreign direct investment by traditional

II) Behavioural Patterns

A) Investment Motives

From the outset, it should be noted that firms, although enjoying cost advantages over their foreign competitors, may not necessarily maximize their opportunities. In some cases, managers have been restricted due to limited information regarding foreign markets, and because additional information would require increased operational expenses. Furthermore, some managers tend to be risk-averse, and if opportunities at home offer satisfactory rewards, they may simply decide to never incur the increased costs associated with gathering information.

Managers who do exploit a competitive advantage in foreign markets are likely to do so first through exports (Lecraw 444; White 168; Diaz-Alejandro 173). Even in the presence of a relatively attractive reward abroad, managers usually prefer to maintain the company's domestic operations; and hence, tend to prefer exporting, which is least disruptive compared to setting up of a foreign subsidiary which would require both managerial and production personnel and financial

profitable. Thus, investment in a plant overseas, or a facility located inside the market is one possible response to overcome such barriers and restrictions. However, defending export markets is not the only motivation for firms going abroad. Firms may also be motivated by the need to reduce risks by diversifying plant locations. Another important motivating factor is the government influence in establishing certain public policy goals.

1) <u>Defending Export Markets</u>

There is considerable evidence to support the proposition that there is a perceived need to protect foreign market positions, which have been developed through export operations (Lecraw 444; White 168; Diaz-Alejandro 173). As shown in table 4, this proposition seem to apply to firms from both advanced as well as developing countries.

In the case of Third-World MNCs, researchers have reported that a high percentage of parent enterprises in Latin America had previous export experience abroad before establishing foreign affiliates in those countries (Diaz-Alejandro 173; White 168). The Latin American studies not only

Table 4

Rating of Motivations for Foreign Investment in Thailand by Firms from Advanced and Developing Countries

Motivation	Advanced countries[a]	Developing countries[a]
Threats to existing markets	8	6
Diversification of risk	1	7
High local return	3	6
Investment of accumulated local funds	1	8
Exploit experience with high-technology production	8	1
Exploit experience with labour-intensive technology	1	5
Export capital equipment	2	4
A source of cheap labour	3	1
To export to the developed world	2	1
Use marketing expertise	7	1
Small markets at home	2	6
Circumvent tariff and quotas in developed countries	2	2

Source: Lecraw, D.J. "Direct Investment by Firms from Less Developed Countries." Oxford Economic Papers. 1977: 444.

a. Rating based on scale of 1 to 10, ranging from unimportant

restrictions were factors that led to exports not being a viable format in the longrun.

Asian multinationals have behaved similarly to the Latin American firms. In a study of 23 ASEAN (Association of Southeast Asian Nations) and 177 subsidiaries from advanced countries in Thailand, 19 of the ASEAN subsidiaries had exported to foreign markets before setting up foreign operations in Thailand and other foreign countries (Lecraw 444-45). Thailand is a good representative of the group of less-developed countries in the region because like many others, it followed an import-substitution industrialization path and encouraged foreign direct investment. At the same time, its own manufacturing sector operated behind a moderately high tariff wall.

The link between exports and foreign direct investment can perhaps be best demonstrated by the South Korean firms. The period of 1968 to 1974 was referred to as the export-substitution (ES) period. It was found that about 55 percent of the total value of manufacturing industries in Korea during that period was concentrated in export industries (Sung 59). It was during the ES phase of growth that some of the

served with exports (Sung 73).

Recently, South Korea's "export machine" is facing an uncertain market in the United States (mainly because the policies of the government has been aimed at reducing the increasingly large trade deficit of the United States), and is employing bargain-basement prices to make a concerted drive into the markets of Western Europe. The result is already evident as Korea's trade surplus with Europe jumped 50 percent to U.S.$2.8 billion in 1988. Closely following this diversion in their thrust of exports, three of Korea's largest firms (Goldstar, Daewoo and Saehan Media Corporation) have already committed over U.S.$100 million of foreign direct investment in several European countries (Petersen, Nakarmi and Heard "Korea" 55-6).

Research on Indian investors provides additional support to the link between exports and investment (Wells 69). Table 5 reports the responses by Indian managers of fifty-two different size firms when they were asked why they invested abroad. In small, medium, and large size firms, threats (potential and actual) to export markets provided the principle incentive for investing abroad.

Table 5

Motivations for Foreign Investment by Indian Firms

Motivations	Number of small firms[a]	Number of medium firms[a]	Number of large firms[a]	Total number of responses[b]
Protection of export market	21	10	7	38
Similar technological requirements in host country	19	6	6	31
Host country investment incentive	15	9	6	30
Expansion to new markets	10	4	5	19
Indian domestic growth restrictions	7	7	4	18
Cost advantages	13	3	1	17
Other	2	2	0	4

Source: Wells, L.T. Third-World Multinationals. 1983: 69.

a. Small firms (fixed assets of 1 to 50 million rupees); medium firms (fixed assets of 51 to 100 million rupees); and large firms (fixed assets of 101 million rupees or more).

b. Each of the 52 firms interviewed could answer to more than one kind of motivation.

4, this might not be as important a motivating factor to the firms from the developed countries as compared to firms of the Third-World. In the case of Thailand, foreign investors from developing countries placed greater emphasis on diversification of risk than did their counterparts from advanced countries.

Robock (1971); Kobrin (1979); Rummel and Heenan (1978); and Tallman (1988) have often cited diversification of risk as a determinant for multinational business expansion. But there is a unique element when it is related to Third-World MNCs. The kind of risk that the latter are bent upon avoiding is political risk connected with political instability or threats of adverse political developments at home, a dimension which MNCs from developed countries have less to fear.

In a developing region like Latin America, it is common to see political and economic circumstances changing, with governments shifting periodically from interventionist to conservative policies and vice versa. To a great extent the upsurge of Latin American foreign direct investments in other countries is explained by this factor. This is demonstrated by foreign investments by Argentine firms during the most

been of considerable significance for the activities of Hong Kong (see table 6) and Taiwan investors. The special concerns of businessmen from those two island economies are easy to understand. Past events, like the Macao incident of 1966 and Hong Kong riots of 1967 have served to indicate that Hong Kong's political future is very uncertain and seem to have stimulated investments abroad (Wells 84).

Furthermore, the people of Hong Kong fear that it will cease to be a viable capitalist economy when it is reverted back to the People's Republic of China in 1997 when the British lease expires. Such fear is definitely not exaggerated following the incident in Tiananmen Square (June 1989) in China, which signified a major setback in the quest for democracy. Further, this catastrophic political act by the government of China has definitely shattered the confidence of its future citizens and changed the rest of the world's perceptions toward China's economic reforms. Naturally, the incident has worsened the already uncertain future economic environment of Hong Kong.

The recent events in China demonstrate clearly the link between investment and risk avoidance. Investment capital have

Table 6

Motives for Hong Kong Foreign Direct Investment

Motive	Rank[a]
Higher rates of profits	3
Diversification of risks	5
Lower land costs and rents	7
Lower labour costs	5
Lower capital costs	2
Availability of technical and skilled labour force	1
Availability of management manpower	1
Availability of higher levels of technology	3
Defending the existing market by directly investing there	2
To open new markets by directly investing there	1
To build vertically integrated structure	2
to make use of the outdated machinery in the Hong Kong firm	4
To circumvent tariffs and quotas imposed by developed countries	2
To make fuller use of the technical and production know-how developed or adopted by the Hong Kong firm	5
Availability of raw materials and/or intermediate products	1
To avoid or reduce the pressure of competition from other firms Hong Kong	5
As a means of managing the financial assets of your Hong Kong firm (that is, establishing a subsidiary overseas is similar to investing in the financial markets overseas)	2

In 1949, the government of the Republic of China (ROC) moved to Taiwan following the establishment of a Communist Regime on mainland China. Since its establishment as an independent nation, Taiwan has lived under the threat of a takeover by the People's Republic of China. In fact, the experience of the overseas Chinese throughout Southeast Asia teaches them that every site is potentially unsafe. Overseas Chinese have faced riots or worse in Indonesia and Malaysia, and expulsion from Vietnam (Wells 84). Confronted with uncertainties at home and the insecurity attached to any single overseas site, MNCs from Hong Kong and Taiwan have a special incentive for expanding their interests to a number of other countries.

3) <u>Government Influences</u>

As we have seen, political instability may have pushed investment overseas because firms wish to reduce their business risk. But there are other government influences that have a more "direct" impact. Such governmental measures have been identified as the other common consideration in the decision to invest abroad for both the First-World and Third-

have led to pressures on Third-World MNCs to seek investment abroad (Aggarwal and Weekly 15). Examples of measures of this nature include anti-trust legislation, capacity licensing, or policies that discriminate against large enterprises. The Monopolies and Restrictive Trade Practices of India have restricted domestic expansion by the larger businesses, and consequently, international direct investment have emerged as an alternative outlet for the growth capabilities and aspirations of these companies (Aggarwal and Weekly 19).

Conversely, some home country governments may simply remove existing investment barriers. Taiwan, which previously severely restricted investment to the United States, lifted the investment barriers in July 1987. Taiwan's official tally of approved investment in the United States totalled only $163 million between the years 1959 and 1986. But between July and November in 1987, an additional $67 million of investment was approved in the United States. By 1991, the government predicts that Taiwanese companies will have a total stock value of approximately $2.4 billion of direct investment in the United States alone (Yang "The States" 56).

A large part of governmental interventions appears to

yet subject to such restrictions. During the period of 1967-1970, many textile firms shifted their location of production to Indonesia (Chen 81).

In some cases, import restrictions in the advanced countries led Third-World MNCs to invest in the industrialized countries themselves. Of course, Third-World MNCs that invest in the advanced countries cannot possibly exploit their advantages, such as low-cost of labour, and compete with the local firms. Thus, firms with manufacturing operations in an industrialized country usually undertake most of the steps of the manufacturing process at home, drawing on the cheap labour or other competitive advantages available there, and complete the last stage of fabrication in the advanced country. This type of enterprise is exemplified by a furniture manufacturer from Hong Kong, which has four plants in the United States that do final assembly (Wells 75). For such firms, the possible gains are easy to identify: tariff savings (parts of products are often taxed less heavily than assembled final products); lower transportation costs (shipments of parts are less bulky and less easily damaged); and the foreign assembly operations could serve as an observing base for the local

due to the fact of their home country's inability to import high-quality components needed for their production (Wells 75-6). Hence, the preponderance of these foreign investment were in response to trade restrictions.

The last form of government intervention arises from regional integration programs. Each program is designed for the participation of the respective developing countries in the same political and geographical region. Such programs are usually aimed to promote Third-World solidarity and also to reduce the dependence from outside the region, especially from the advanced countries (Nye 121).

Because of integration among developing countries, a number of Third-World governments have become involved in foreign business ventures, either through state-owned or quasi-public enterprises, or in close collaboration with private firms of their own countries. This sort of joint business-government collaboration is an international undertaking, which constitutes an extension of state-guided approach to economic development, that has been embraced by the majority of the Third-World nations. This approach has been considered by some to be a strong force promoting the

American Free Trade Association (LAFTA), Central American Common Market (CACM), and Economic Cooperation Association of India and Indonesia (BKII) are examples of some regional groupings that have been formed to promote solidarity among Third-World countries.

4) <u>Other Forms of Motives</u>

In addition to those reasons already discussed, firms may set up foreign affiliates in search of lower cost of production (see table 4, 5 and 6). A number of Hong Kong firms went to Macao, Mauritius, the Philippines and Thailand in search of lower land rents, labour, and capital costs (Chen 92). Naturally, a firm in pursuit of a lower cost structure could alternatively seeks location for direct investment where the expected rate of profits is high (see table 4 and 6). Investments abroad could also be prompted by the demand constraints at home. The domestic markets of developing countries are usually quite small, and hence, easily saturated by a few producers (Lecraw 445).

Producers may easily recognise their common interest in limiting output at home (geographical market segmentation) to

investment risk (Wells 88). The predominant proportion of investment by Singapore is concentrated in Malaysia, and the reason given is not only because of their close proximity, but because Singapore was historically a part of Malaysia (Lall 619). Today, the two neighbouring countries still share many similar cultures and common political goals.

B) <u>Foreign Investment Strategies</u>

Another common denominator in the behaviour of Third-World MNCs has to do with their basic strategies in foreign business ventures. Considerable similarities appear in such strategic decision areas as the choice of geographic locale for foreign operations, the organizational and ownership arrangements utilized, and the relationships- functional and managerial- maintained between foreign affiliates and the parent companies.

1) <u>Location</u>

In choosing locations for foreign operations, some Third-World MNCs have shown a preference for investing close to home, frequently in the countries contiguous to their own

heritage.

Latin American firms have also played a significant role in the internationalization process within the same geographical region. During the last two decades, the regional-integration schemes, such as the Latin American Free Trade Association (LAFTA) stimulated awareness of local firms about the possibilities available in the regional market. More broadly, the integration programs also helped to encourage the formation of Latin American multinational enterprises as an effective tool for achieving objectives of common interest in the group (Nye 122).

Some researchers have argued that the availability of a wide regional market is especially important in the case of Latin America's direct investment (Aggarwal and Weekly 15; White 165). The reason is there are significant gaps in terms of industrial modernization and technological capacity among the larger semi-industrialized countries (Argentina, Brazil, and Mexico); the smaller economies with relatively experienced industrial sectors (Chile, Columbia, Peru, and Venezuela); and the rest of the less-developed countries in the region. Such gaps and the corresponding non-synchronism of the

2) Organizational and Ownership Arrangements

With respect to organizational and ownership arrangements, Third-World MNCs have strongly favoured some form of joint venture for their investment in foreign markets. These usually involved partnerships between investors and local firms in the host countries. However, some instances have also been noted in which two or more Third-World companies have combined their resources and efforts to launch business outside their home territories, giving rise to "industrial system constellations" (Perlmutter 139).

The frequency with which investors from developing countries involve local partners in their foreign subsidiaries is striking. Table 7, which reports ownership pattern of foreign firms in Thailand, shows that only 2 percent of Third-World subsidiaries are wholly-owned. As investors, South Korean firms predominantly preferred joint-ventures in the fishing, timbering, mining, manufacturing and construction sectors (see table 8). One plausible explanation for the high propensity to establish joint ventures with local partners is that firms from less-developed countries, including Korean firms, in the production of inexpensive and undifferentiated

Table 7

Ownership Patterns of Foreign Firms in Thailand

	Percentage of foreign ownership				
	100%	99.9-50.1%	50%	49.4-0%	Total
Home country					
Japan	25%	51%	10%	14%	100%
U.S.	10	47	15	28	100
Europe	23	45	12	20	100
LDCs	2	7	5	86	100

Source: Lecraw, D.J. "Direct Investment by Firms from Less Developed Countries." Oxford Economic Papers. 1977: 448.

Note: 25% of the Japanese firms are 100% (Japanese) owned.

Table 8

Ownership Patterns of Overseas Korean Firms (Number of Firms)

Industry	100%	>50%	<50%	Subtotal
Mining	1	-	1	2
Timbering	1	6	-	7
Fishing	1	10	12	23
Manufacturing	2	11	6	19
Construction	5	9	2	16
Transportation and warehousing	4	2	1	7
Trading	134	12	3	149

control. At the same time, the parent firms need local partners to provide knowledge of distribution channels and the economic and political environment (Sung 67-8). Another reason has to do with the government placing restrictions on the ownership structure arising from any direct investment made by a firm from their countries. For example, the Indian government encouraged Indian firms to take minority positions abroad to follow the Indian government's policy toward foreign direct investment (Lecraw 449). On the other hand, ownership pattern of advanced countries based multinationals are usually wholly or majority owned (see table 7).

However, there is strong evidence to indicate that 100 percent equity ownership of overseas multinational subsidiaries is rapidly a thing of the past. In a survey of entry policies for foreign firms in 15 host countries, Robinson found that, in certain cases, it is mandatory for foreign investors to form joint-ventures with local firms. Some host countries have legislation that allowed local partners to own a majority share for various reasons: a) after a specified number of years if incentives were being sought; b) the firm seeks to manufacture new products; c) to locate on

elements in their business strategies. These elements have to do with the degree of managerial control and the kind of interaction that take place between the typical parent firm and its foreign affiliates.

Third-World MNCs by and large have not endeavoured to fuse their affiliates into an integrated or interactive production -distribution system. Instead, they have been content to permit each affiliate to function with considerable autonomy and to confine their sphere of interest to their own local or national markets. Thus, the Third-World MNCs have not for the most part developed the centralised control structure, geocentric managerial philosophy, or unification of subsidiary activities that have to be associated with the true MNC (Aggarwal and Weekly 15).

Such arrangement could be taken as evidence that the concept of global integration does not figure prominently in the long-run strategies of the Third-World MNCs. If global integration was the goal, these firms would appear to be forging, at least in the early stage, those important synergistic advantages and opportunities that flow from such integration. On the other hand, these firms may be realizing a

four out of thirty subsidiaries in Mauritius and the Philippines have indicated that regardless of the market served, capital expenditure decisions were made by the head office; but decisions about operating expenses and personnel policy were almost invariably made at the local level (Wells 113). For the firms serving the domestic market, decisions about prices and sale of products were always made locally. Even decisions about purchasing inputs were not controlled by parent firms.

To be sure, the allocation by most firms of a wide range of decisions to the subsidiaries does not mean that decisions are made by nationals of the host country. The large number of expatriates in the subsidiaries certainly suggests a strong foreign influence (Wells 114). Nevertheless, the autonomy of subsidiaries and the frequency with which parent firms from developing countries share ownership with local partners suggest that decisions made at the subsidiary level are likely to be consistent with the interests of the local owners of the subsidiary.

C) <u>Characteristics of Foreign Operations</u>

The products that comprise the "bread-and-butter" lines of the Third-World MNCs can be characterised as relatively simple, standardized products of the sort that would appeal to less-sophisticated buyers. In addition, the Third-World MNCs operate in industries with low advertising intensity, and engage in low research and development (R & D) activities and market promotion.

The typical strategy adopted is supported by Wells' findings in his study of Third-World MNCs. His results are presented in tables 9 and 10, which have shown that the Third-World MNCs have been reluctant to spend extensively on R & D and advertising respectively. Further evidence can be gathered from other sources of comparative studies. In one such study, Lecraw (1981) used 20 firms from developing countries and 130 from the advanced countries and found that multinationals from the industrialized nations spent, on the average, significantly more on advertising than the multinationals from developing countries (45).

Not surprisingly, little effort or attention is accorded to product differentiation, and consequently non-price competition has a minimal role in the marketing programs of

Table 9

Manufacturing Subsidiaries in all Locations, by R & D Expenditures and Nationality of Investors

Industries' expenditure on R & D as percentage of sales	Subsidiaries from developing countries		Subsidiaries from U.S.		Subsidiaries from other advanced countries	
	Number	%	Number	%	Number	%
Low (less than 1%)	537	57.6	2540	30.2	2189	35.6
Med. (1% to less than 2.5%)	148	15.9	1286	15.3	795	12.9
High (2.5%)	247	26.5	4573	54.5	3166	51.5

Source: Wells, L.T. Third-World Multinationals. 1983: 47.

Table 10

Advertising Expenditure of Manufacturing Subsidiaries in all Locations

Industries' expenditure on advertising as percentage of sales	Subsidiaries of developing country investors		Subsidiaries of U.S. investors		Subsidiaries of other industrialized country investors	
	Number	%	Number	%	Number	%
Low (less than 1%)	785	84.2	6196	73.8	4926	80.1
Med. (1% but less than 2%)	122	13.1	1183	14.1	728	11.8
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Table 11

Emphasis of Marketing Strategy of Subsidiaries of Parents from other Developing Countries in Mauritius and the Philippines (1970-1978)

Elements of marketing	Number of firms serving primarily export markets (24 firms)	Number of firms serving mix of local and export markets (24 firms)
Price	20	7
Distribution		
Reliable, timely delivery	7	2
Availability of parts and sales service	1	0
Effective use of distribution network	0	1
Product		
High quality	2	2
Width of product line	1	2
Promotion		
Advertising and brand name	0	3

Source: Wells, L.T. Third-World Multinationals. 1983: 59.

Note: Since firms may emphasize more than one element of the marketing mix, column totals may exceed number of firms in sample.

emphasized greatly the role of price competition in their marketing strategy.

Since price competition is the central theme of marketing, cost minimisation would then dictate the design and selection of production techniques. As mentioned earlier in this thesis, production techniques employed by firms of developing countries would likely mean the choice of labour-intensive and small-scale production processes. The capital stock employed would likely be regarded as technologically obsolete by the First-World firms; in fact, much of the equipment utilized by the Third-World affiliates is acquired secondhand, either through direct transfer from the parent firm, or through purchase from prior owners or used equipment dealers. The Third-World MNCs emphasis on minimizing costs can also be perceived in the buildings and office facilities that they occupy, and in the salaries to affiliate managers and technicians, all of which tend to be quite modest by western standards (Aggarwal and Weekly 16).

Because the Third-World MNCs' affiliates are very often serving markets that are constrained by physical or legal barriers, sparse populations, and meagre purchasing power,

countries. They have been very adept in transferring that experience to their affiliate operations and in adapting the technology, with which they are familiar, to the markets for which their affiliates are producing. This combination of experience and adaptability has been an important source of the competitive strength that the Third-World MNCs have displayed vis-a-vis both First-World MNCs and local competitors of the host countries (Aggarwal and Weekly 16).

D) <u>Relationships Between Firms And Governments</u>

There is little evidence in the way of official pronouncements, or legal case histories to reveal the attitudes of governments toward Third-World foreign direct investment. In most instances, bureaucrats will never reveal their true intentions for designating procedures that may encourage or discourage investment. Consequently, the inferences made from governments' reactions toward Third-World investment about their attitudes are purely conjectural. What is known about the nature and behaviour of these companies has been juxtaposed with what are commonly known to be the guiding interests and aims of national political authorities.

Third-World MNCs are apt to receive a considerably warmer welcome from developing host countries than would be accorded to investors of developed countries. This greater cordiality seems to be based to a large extent upon the notion of economic and cultural kinship assumed to exist between parties who share a common Third-World background. This expectation may also be linked, however, to some of the organizational features of the Third-World MNCs that were noted previously, such as their penchant for involvement with local firms, the local market orientation of their affiliates, and the polycentric nature of their managerial approach (Perlmutter 143). These attributes are deemed to be conducive to favourable relationships with host governments as they provide for beneficial participation by local nationals in the activities of the Third-World MNCs' affiliates while lessening the aura of foreign control that surrounds the more tightly integrated and outward looking affiliates of First-World MNCs.

Further support for the assertion that developing country host governments will be more favourably disposed toward the Third-World MNCs comes from a version of the appropriate technology concept. The argument used is that the technology

techniques of the Third-World MNCs' affiliates and the reduction or elimination of the foreign exchange burden associated with continuing royalty payments for more advanced technology (Wells 136).

In spite of the attractiveness mentioned above, foreign direct investment does raise several sensitive economic and political questions, such as transfer pricing, effects on local entrepreneurship and fear of domination by others. Not wanting to display their intention explicitly, these concerns are, however, reflected by the bureaucratic procedures of host governments. Cumbersome administrative steps for investment, that require much time and expenses from applicants, hit particularly hard on small investors which are usually from developing countries.

2) Home Governments

Speculation about Third-World MNCs and government relationships has also been directed toward the home governments of these companies. As mentioned previously, Third-World governments have encouraged and supported specifically the foreign direct investment ventures of MNCs

through world-wide expansion of industrial empires based in and identified with particular countries.

Again there is the seemingly negative view or opposition to foreign investment by the investing countries' own local firms. A common reason given for such resistance is that foreign direct investment implied a willingness to have capital and technology transferred out of their domestic economies.

3) Governments Of Advanced Country

The attitudes of governments of advanced countries as host countries are somewhat harder to infer, because Third-World firms by their very nature already find it hard to establish a subsidiary inside the market of the advanced countries. Nevertheless, some insights can be gained from their perception of the potential effects of Third-World MNCs in their economies.

Being host to Third-World MNCs will usually impact positively on the development process of the parent countries, which is a matter of concern to the rich nations. But since foreign investors from developing countries are a new source

of product differentiation, as contrasted to price in the domestic market and the converse in the developing countries' market. With the emergence of Third-World MNCs, the latter group is able to offer greater competition to MNCs from the developed countries in the price-sensitive segment of the markets.

On the other hand, Third-World MNCs may provide some positive opportunity for certain MNCs from the advanced countries. Third-World MNCs could serve as attractive partners for projects in a third country. In fact, such possibilities have already been established (Wells 150).

While it is important to bear in mind the tentative and conjectural nature of the views of governments/Third-World MNCs relations, the inferences made are under very probable premises. There is no doubt that they play a vital part in the intricate expansion process of the business enterprises.

III) Summary

This chapter has endeavoured to identify and examine the basic features of the Third-World MNCs and their relations with both the host and home governments. In summarizing this

First-World and Third-World MNCs are motivated to make foreign investment.

There are however, notable differences in the motives. This can be seen from their respective emphasis on reducing risk through diversification. Third-World firms are more inclined to invest abroad because of political instability at home as compared to firms from developed countries. Another difference is that joint-ventures and government involvement in international business are more frequently encountered than in developed countries. However, as Robinson noted, the disparity in the frequency of joint-ventures might not be that pronounced between the MNCs from the First and Third-World in the near future (320).

In terms of investment strategies, most Third-World MNCs seemed to invest most heavily in other developing countries that are geographically (and in most cases culturally) close to the home country. In addition, Third-World MNCs tend to form joint-ventures with either local nationals or other MNCs for most of their overseas investments. Finally, foreign subsidiaries of Third-World MNCs are permitted to operate with a great deal of autonomy.

cost, labour-intensive, smaller-scale operations using mostly intermediate level technology and often serving markets which are smaller and/or more hostile than those that would be attractive to MNCs from developed countries.

Lastly, the attitudes of the host and home governments can be inferred from the their bureaucratic policies. Based upon the latter, the attitudes seem to be quite diverse among host and home country governments, ranging from total support to outright measures of deterrence. It is however the reactionary behaviour of governments that reflect their assessments on international business transactions as to whether they will contribute positively or negatively to the economy.

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CHAPTER FIVE

CONCLUSIONS

I) Why Third-World Firms Invest?

Hymer's monopolistic theory and Vernon's product cycle theory are both considered to be contemporary theories of multinational enterprises; and are based on the assumption that MNCs operate and thrive under conditions of imperfect competition. The focus of research with regard to Third-World MNCs, therefore, has been on the identification of these monopolistic or oligopolistic (also known as ownership-specific) advantages that enable a firm to compete with other firms abroad.

From the discussions in earlier chapters, the prevalent view of Third-World MNCs is that their sources of competitive strength come from acquiring and developing labour-intensive, small-scale, and flexible operating technologies. Such technologies often use locally available inputs, and hence are more efficiently adapted in other developing countries with similar resource endowment. In addition, the product technology is usually low cost and simple, which means that

quickly to the environment of host developing countries.

These ownership-specific advantages by themselves do not explain why a firm seeks to exploit them through direct investment rather than through licensing, or the sale of technology. In an attempt to answer the question posed, Dunning has added several location-specific and internalization variables in his eclectic theory. For example, high transportation costs, appropriate levels and structures of resource endowments, prevailing low wages in many countries, and favourable government policies have often provided incentives to a firm for investing in another country. Dunning also suggests that a country's propensity to engage in foreign direct investment, or to accept investment is closely linked to its stage of development. He argues that it is reasonable to think of a four-stage investment-development process or cycle; and that Third-World countries now emerging as net outward investors are approaching the third stage.

The final part of the analysis was the exploration of such characteristics as investment motives, strategies, and operations of affiliates of Third-World firms. First, it was

culturally close to the home country, and form joint-ventures with local firms or firms from a third country. Third, most foreign operations of Third-World affiliates emphasize low cost, labour-intensive and small-scale operations to serve markets that would be considered too small or hostile in most cases for a developed country MNCs. Finally, governments of both home and host country of affiliates have been observed to play an active role influencing the outflow and inflow of direct investments.

In summary, these observed behavioural attributes of Third-World MNCs are complementary to the theoretical concepts outlined earlier. Together, they have provided some insights into the competitive edge which firms from the Third-World might possess, and the subsequent exploitation of those advantages abroad.

II) Criticisms Of The Theories

Just like other models in the social sciences, the proposed theories for direct investment by firms of the Third-World counties also have some deficiencies in their propositions. The monopolistic and product cycle theory have

Hence, his work merely tackles the question of 'how' and 'why'; whereas Vernon's product cycle has tackled an additional question of 'when'. Furthermore, in the formulation of these theories, they have relied almost exclusively on U.S.-based corporate activity as an archetype, and have excluded all forms of multinational activity in the service sector.

Although the eclectic theory can explain many more situations of Third-World corporate activity, it is often criticised on the grounds of it being seemingly too all encompassing in nature (Taylor and Thrift 8). Specifically, it is said that the theory is only a list of factors likely to be important in the explanation of the growth of Third-World MNCs, rather than being an explanation itself.

Admittedly, these criticisms against the theories seem valid, but the shortcomings of a model may not be necessarily serious. It is often said that no economic model can describe fully the events of the real world; and if it can predict some aspects of an economic process, then it can be considered a 'good' model. From the previous analysis, it would be hard to dispute that the theories put forward to explain foreign

advantages have provided a strong proposition for the growth of Third-World MNCs over the last two decades. However, it would be unwise to assume or generalise that these advantages will allow Third-World firms to compete in the international market indefinitely.

The competition among MNCs in the international market is becoming more and more intense, and hence there is no reason to expect that the underlying forces that propelled the growth of Third-World MNCs over the last twenty years will continue to do so in the future. This, however does not imply the ultimate demise of Third-World MNCs; or that foreign direct investments by developing countries will continue, but with individual firms competing abroad on a very short-term basis only. Third-World foreign subsidiaries are continuously being replaced by new aspirants because they lack monopolistic advantages to sustain their competitiveness.

On the contrary, Third-World MNCs will continue to grow and be able to meet new challenges for several reasons. First, some Third-World MNCs do possess unique technological advantages, which are based on 'minor innovations'. Such innovations may be derived from finding the right materials

always replenish their technological stock, where their own efforts are inadequate, by licensing technologies from developed countries or entering into joint-ventures with their MNCs.

Perhaps, the best indication that such optimism is warranted is the presence of the following newly industrialising countries (NICs): Hong Kong; Singapore; South Korea; and Taiwan. These countries have grown in such proportions that it is no longer possible to regard them as 'less-developed' countries. They have been characterised by rapid growth in the level and share of industrial employment, expansion of export market shares and real per capita income levels which are approaching those of some of the advanced industrial countries (LaPalombara and Blank 124).

One result of the improvements achieved by the NICs is that these countries now have better access to international finance and developed nations' economies (Chao 88). In particular, countries such as Taiwan, Republic of Korea, Hong Kong and Singapore are well positioned to take advantage of the access to developed economies. For these countries, financial resources no longer serve as a major impediment to

countries (Lall 626).

Unfortunately, the closing of the gap between NICs and the developed countries is paralleled by the widening of the gap between the NICs and the poorer developing countries. As a result, this has put some strain on the unity of developing countries and increased the tension between the poorer developing countries and the rich industrialised nations. Much of the tension arises out of the dependency felt by the poor countries when they must turn to the rich for assets critical to their progress. However, it has been proposed that internationalising Third-World firms will help to reduce the tension with the rich countries (Wells 161). By investing among developing countries, or forming joint-ventures with firms from rich countries, Third-World firms can reduce the dependency on assets owned by the rich and subsequently the tension existing between them. At the same time, such endeavours have enabled poor developing countries to close the gap with the NICs. Of course, before such endeavours can actually take place, the governments of these poor countries must improve their infrastructures and global communications, and the leaders must be commited to developing an effective

MNCs from developing countries are not likely to perish in the near future. It can be further speculated that MNCs of NICs will have an increasingly significant role to play in international production if these countries continue to grow at their present rate. At the same time, with improved cooperation, planning and management, MNCs from other poorer developing countries will continue to grow. There might come a time when Third-World MNCs must be considered as the same potent force as First-World MNCs in the international business economy.

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