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**Global Business Competition
and its Impact on
International Production**

by

SUSAN FORESTER, B.A.

A thesis submitted to
the Faculty of Graduate Studies and Research
in partial fulfillment of
the requirements for the degree of

Master of Arts

Department of International Affairs

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The undersigned hereby recommend to the Faculty of Graduate Studies and Research acceptance of this thesis submitted by SUSAN EUNICE FORESTER, in partial fulfilment of the requirements for the degree of Master of Arts.

Maureen Appel Molot, Director
The Norman Paterson School
of International Affairs

Professor M. Rudner, Supervisor

Abstract

International business competition among multinational corporations (MNCs) around the world intensified during the 1980's. While the ramifications of this intensified competition are still being enumerated, MNCs have begun the search for new competitive advantages.

In this paper the author investigates the effects of international competition and the adoption of new competitive strategies on the foreign direct investment plans of major Western MNCs in Asia. The hypothesis is that MNCs are adopting new investment patterns to enhance marketing and sales efforts, rather than the efficiency-oriented production strategies widely advocated in the business strategy literature.

Four MNCs with regional headquarters in Singapore were interviewed for this paper - Inco PT, Thompson Television, Matsushita Electric Works and Victron. Through qualitative interviews, results suggesting that these multinationals are not moving towards radically new production strategies and are emphasizing market development in tandem with their production initiatives in Southeast Asia were attained.

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Global Business Competition and its Impact on International Production

Introduction

The dynamic interface between the internationalization of business enterprises and the environment in which they are a part...is a difficult, even a messy, subject to get to grips with, partly because it inevitably crosses disciplinary boundaries and partly because it is unamenable to our tried and tested analytical techniques. But a series of dramatic events in the global economic scenario since the mid-1980s have forced researchers to give more attention to the way in which these events have affected not just the growth and form of foreign production, but the very path or trajectory of the internationalization process itself.¹

In the late 1980's and into the 1990's, globe-girdling multinational corporations (MNCs) were most often characterized in the public press as being under siege. By the mid-1990's, after an unusually difficult business period, such MNCs were attributing their survival to a willingness to reinvent themselves and to change their approach to their main lines of business. Siemens, Whirlpool, IBM, and Volkswagen head the long list of those that made the headlines with their corporate woes in the 1980's and early 1990's, yet today are on the road to recovery.

¹ Dunning, John H., *The Globalization of Business*, Routledge, New York, 1993a, pg. 51.

This paper concerns itself with this older generation of MNCs and delves into the issues surrounding their renewal. What really spurred their global resurrection? Less than a decade ago, a number experienced such difficulties that they were not expected to be in business today. It is the nature of the upheavals these firms faced, and how it spurred old dinosaurs to reinvent themselves that is the starting point of this investigation.

The Lingering Business Crisis

The headlines are everywhere - "For a Pink Slip, press 2", "The World Turned Upside Down", "Time to Wake up and Get Real", "If You Don't Change You're Dead"² - and have been since the mid-1980's. Certainly, a voluminous body of literature has emerged to describe how world competition got tougher and how those MNCs that were unprepared for it were simply eliminated. Along with the traditional MNC establishment, hundreds of thousands of jobs - 600,000 in 1993, 450,000 in 1992 and 540,000 in 1991 - disappeared in the US alone. In 1993, IBM shed 13% of its workforce, Eastman Kodak 17%, while Westinghouse reduced its company headcount by 7%, the same as Bethlehem Steel. Staffing levels at Fortune 500 companies in the US have receded to their 1959 standards - just over 10 million people are employed by such firms, down from a high of 15 million in 1979. And of course, employment figures only mirror the sales figures of Fortune 500 companies - having once accounted for upwards of 55% of the US GDP at

² assorted magazines - Forbes, Economist, Business Week.

their peak in the late 1970's, Fortune 500 companies' sales now account for only 35-37% of national GDP.³

How the transformation of mainstream MNCs is shaping up is an interesting question. While prescriptive works advising companies on what to do abound, few serious studies have been undertaken to determine the trends in the transformation. What kind of restructuring have these firms undertaken to return to profitability? Are MNCs revitalizing production methods to move their bottom line into the red? Has the restructuring affected MNC overseas operations? What are the implications of transformation for the global trading system?

The revitalization of MNCs is not only a tale of domestic restructuring. While steep losses in the home market were the trigger for the MNCs reaction, the overseas holdings of these MNCs have played a critical role in the renewal process. Overseas marketing efforts were boosted and foreign production levels increased. In many MNCs, as will be illustrated later in the paper, foreign sales revenues increased substantially as a percentage of the total corporate earnings. A nexus developed between the renewal of MNC business vigour and augmented foreign direct investment (FDI) flows to overseas markets. Thus the changes in corporate structure and strategy have a host of international implications, including balance of trade figures, national development, and international trade policy.

³ Wooldridge, Alan. "Who wants to be a giant?". Survey of Multinationals. *The Economist*, June 24th. 1995.

Hypothesis - Sales vs. Production

This paper addresses the issue of MNC restructuring initiatives and the implications they have for the broader international political economy, where Dunning's definition of an MNC is "an enterprise which engages in foreign value-added activities and internalizes intermediate product markets across national boundaries"⁴. To do this, a review of the nature of global competition which led to the MNCs downfall, a list of the prescriptive theories offered up to MNCs seeking renewal, and an analysis of some real life strategies being implemented are provided. To conclude, theories are contrasted with the reality of MNC activities today.

This paper takes as its starting point the belief that fundamental change in global competition among MNCs has occurred and that MNCs are searching for successful approaches to deal with the new reality. A large body of theoretical works, some of which will be examined in detail in this paper, are emphasizing change in patterns of production, especially with regards to overseas direct capital investment as the preferred form of restructuring. However, too little attention seems to be devoted to restructuring corporations to address the demands of marketing in new global markets. Out of this belief, the author has developed the hypothesis that while MNCs are restructuring their corporate assets on a global basis, it seems unlikely that the efficiency of production is the

⁴ Dunning, *ibid.*, 1993a, pg. 79.

key criterion upon which the restructuring is premised, in spite of the broad attention evident in the business press. Furthermore, in spite of severe global business competition, the adoption of strategies premised on the efficiency of production is restricted by the degree of change in corporate structure such a strategy would demand. Rather, it is the author's contention that MNCs are restructuring their overseas activities to penetrate new markets overseas. This view was supported by the results obtained during field research on the pattern of FDI flows in Southeast Asia, where the author compared theories of FDI to the real investment strategies MNCs were pursuing in that region. The field research results indicate that firms are emphasizing local market development in their foreign production decision-making over efficiency-oriented production considerations.

The linkage between international business competition and international political economy cannot be underestimated. International business has been inextricably linked with broader political and social developments since the turn of the century, when governments began cooperating with businesses to attain their domestic and foreign policy goals. "First there was the use of MNEs as instruments of the territorial extension of government economic and/or political jurisdiction".⁵

⁵ Dunning, *ibid.*, 1993a, pg. 356, quoting Svedberg, P., "Colonial Enforcement of Foreign Direct Investment", *Manchester School of Economic and Social Studies*, Vol.50, 1981, pg. 21-38.

Since that time, governments have come to rely on big business to employ a large proportion of the populace and to contribute to national wealth through taxation. In turn, business needs government to adopt suitable trade policies, maintain stable economic conditions and to train the labour force. Where countries turn to foreign or domestic capital investment to stimulate national economic activity, changes in the international business environment or changes in business strategy can have serious implications for the state. Additionally, changes in the ascendancy of companies indicate upturns/downturns in employment, which has an impact on government budgets. Such shifts further impact government budgets as a trade surplus or deficit, affecting the value of the domestic currency. The success or failure of MNC business strategies plays a key role in the broader international political economy.

The direction that specific business strategies may take are important because the nature of international business is important. Any change in the nature of business strategies is likely to have an effect on the international business environment as a whole. This in turn is likely to have a critical impact on international relations over the coming decades. International business is more global than ever, and as new business practices alter the way global business is done, it will ultimately alter employment patterns, government policy, relations between states and much more.

Key to discovering the impact of new international business trends on the broader international political economy is the issue of MNC investment overseas. As such

patterns evolve, international relations will evolve in response. If, as the international business theory suggests, MNCs are adopting global reorganizations premised on production-related priorities, it is important for national governments to know this and to know how it may impact their domestic concerns. But are the MNC organizational changes really emphasizing production over other business locational decisional factors? And if so, where in the world are such changes being most clearly manifest? These issues, among others, are explored in this paper.

Methodology - Approach to the Issues

To gain access to information relating to the propensity of MNCs to adopt efficiency-related FDI strategies, the research methodology employed was to approach four MNCs active in Southeast Asia who agreed to participate in interviews of a qualitative nature concerning their production arrangements within the region. The participating firms are from distinct industrial groupings. They are also of differing size and structure. Three of the four companies are leaders in their fields in terms of company size according to revenue, but stand in the mainstream in terms of their reputation for innovation and aggressiveness. As the participants are few, it is not possible for their responses to be representative of all international business. Nonetheless, the insights gained while examining the strategies they employ in Southeast Asia can contribute to an understanding of FDI trends in that region of the world.

With the aim of investigating how far companies might be willing to go with the kind of corporate structure suggested by production-driven organizational theories, a selection of firms with their regional headquarters in Singapore was compiled, from which four firms agreed to participate. While the selection can shed no light on the propensity of certain industries over others to adopt production-driven FDI strategies, it does provide a base from which to make initial observations. In order to achieve a more definitive appreciation of the balance between market- and production-driven factors in FDI decision-making for MNCs, it would be necessary to interview firms across the widest possible spectrum of industries, at the highest levels, and ask very sensitive proprietary information about a firm's most basic competitive strategy.

A definitive study, therefore, is a major undertaking and is outside the scope of this research study. What the selective approach taken in this paper has achieved is an exploratory, preliminary research foundation in which interviews with selected companies led to a greater understanding of why they were in Southeast Asia, how the Southeast Asian operations fitted into their global activities, and the balance the firms tried to achieve in their production and marketing aims.

MNCs and the New Competition

As a thorough investigation of developments in global trade as they relate to MNCs over the past four decades would constitute a major study in itself, the following survey of the period is by no means definitive. Rather, it aims to sketch the course of events in order to demonstrate how Western MNCs found themselves in the competitive quandary of the late 1980's and early 1990's. It is important to appreciate the concurrent developments which resulted in Western MNCs sliding into such a relatively weak position vis-à-vis their competitors. Thus, the following historical overview emphasizes those changes which directly impacted the competitive position of Western MNCs in the post-war setting.

Moreover, this paper is a study of how production methods changed, and are still changing, in response to the evolution of the global trading system. Thus the emphasis is placed on production-related elements of change and only brief mention is made of other important changes such as trade treaties, or enhanced transportation infrastructure around the world. Effectively, in the scope of this paper, the author is unable to present a complete study of the evolution of multinational corporations between 1945 and 1990, and thus resorted to highlighting those issues which play a significant role in determining the competitiveness of Western MNCs over the period.

It has been suggested, and reasonably so, that the trigger for the newly intensified global business competition was a broad-based conversion among national governments to liberal economic tenets which led to deregulation and relatively open trade policies in most major economies. It is undeniable that trade liberalization altered the playing field for businesses around the world, be they domestic and international.

As it turned out, globalization exposed the multinationals' weaknesses. Deregulation and lower trade barriers have reduced the value of their carefully cultivated relationships with governments and expensively accumulated knowledge of local regulatory quirks. It is no longer necessary to be a classical multinational to penetrate global markets...⁶

In their recent work "Economic Reform and the Process of Global Integration". Jeffrey Sachs and Andrew Warner set out to chronicle the trade liberalization progress that has been made since World War II and its impact on global norms of conduct, both business and political.⁷ Most importantly, trade liberalization set the stage for the tremendous expansion of MNC business around the world, creating opportunities to enter markets previously protected by import limitations. Thus the most fundamental change to occur in the global trading system after the Second World War, was to enlarge the scope for trade among all countries, making international trade a much bigger field of activity than it might otherwise have been.

⁶ Wooldridge, Allan, *ibid.*, pg. 4.

⁷ Sachs, Jeffrey D., Andrew Warner, "Economic Reform and the Process of Global Integration", *Brookings Papers on Economic Activity*, January 1995, pg. 1-105.

Within this context of a relatively open world market for the exchange of goods, however, there were many conditions which affected the ability of individual MNCs to flourish. Following the global destruction of the Second World War, only American MNCs emerged with sufficient production capacity to be able to meet domestic demand and still have surplus output to sell in international markets. Much of the world's productive capacity at that time had been decimated or rendered obsolete by technological advances born of war-era research and development programs. "The Second World War impelled US industry on an extraordinary surge of growth. Not only was industrial output greatly increased, but wartime needs also created new technologies that transformed industrial products and processes."⁸ Due to the shortage of production capacity in other countries, American exports to global markets burgeoned and resulted in US corporations evolving into the most sophisticated, early multinational corporations (MNCs). Sales and marketing activities overseas were eventually followed by the establishment of offshore production facilities.

As the Marshall Plan was put into effect, manufacturing facilities in Western Europe were rapidly rebuilt, followed by those of Japan. Once reconstructed, these firms regained the upper hand in their respective local markets, and in an effort to reduce trade imbalances, began to produce consumer goods for export. European MNCs quickly emerged, largely following the administrative and production organizational model of American MNCs. Given their common antecedents, European and American MNCs can

⁸ Chandler, Alfred D. Jr., "The Competitive Performance of US Industrial Enterprises since the Second World War", *Business History Review*, Harvard Business School, Spring 1994, pg. 1-72.

be grouped into a loosely defined category of “Western” MNCs, more fully outlined below.

Many characteristics were shared by American and European MNCs. First, they operated in similar regulatory environments. It is also true that many MNCs grew out of family businesses which turned into massive operations - Bertlsmann, Dupont and Ford to name a few. The business worlds of the US and Europe have long been financially linked, each investing in the other's stocks and bonds. At the turn of the century, UK and German investors financed the development of the American railway system, while US investors largely financed the interwar-period of reconstruction on the continent.⁹ Thus, while Western MNCs competed to sell their products to individual customers, they also shared a common business foundation and structure. Such Western MNCs had characteristics, such as domination of their home market, strong managerial/financial cadres, separation from banks (except in the case of Germany), and competitive supply relations in common. During the postwar period, moreover, the fundamental nature of Western MNCs remained generally consistent. Globally, the number of MNCs was relatively stable and predominantly Western in origin.

Western MNCs subsequently came to largely monopolize international trade. “In the early 1950's, the world's production of manufactured goods was still largely confined

⁹ Chernow, Ron. *The House of Morgan*. Simon and Schuster, New York, 1990.

to twenty-four industrialized countries.”¹⁰ They were also chiefly responsible for the formation of the contemporary international system of trade. Significant institutionalization of international rules for the conduct of trade across borders occurred over the period, with the founding of trade bodies like the GATT and OECD. Thus, the basic structure of the global trading system, the MNCs themselves and their exchange and production mechanisms were formed during the late 1940’s and remained effectively unchanged until the mid 1970’s.¹¹

Right through the 1960s and 1970s, the Western MNCs were the main players in international trade. These firms established offshore subsidiaries for a variety of reasons, such as the avoidance of import restrictions, to extract raw materials, or to take advantage of cheaper production costs (largely due to lower labour costs) in some lower income countries. The bulk of production remained firmly rooted in the home market, and all major corporate offices and functions were retained at home market corporate headquarters.

The first shift in the composition of the international business system came with the emergence of truly powerful, productive MNCs from Japan, during the early 1970s. Prior to this, US MNCs were the indisputable leaders of the international economy.

¹⁰ Barnett, Richard J., and John Cavanagh. *Global Dreams: Imperial Corporations and the New World Order*. Simon and Schuster, New York, 1994, pg. 283.

¹¹ Chandler points out in his essay (op. cit.) that a period of intense competition emerged during the early sixties, and that this resulted in significant changes due to large-scale mergers and acquisitions. However, the net result of this turmoil was not a substantially different collection of MNCs, nor were the reigning MNCs challenged in any fundamental way on the basis of their structure or core activities. Thus, I would not consider the 1960s to have been a period of “paradigm shift” as it appears to be today.

supplemented by those European MNCs which emerged from the devastation of the Second World War. Studies of the number of multinational parent companies indicate that just over 7,000 MNCs existed in 1969. By 1990, that figure had jumped to over 37,000 and Japanese MNCs had proliferated among the largest of them.¹²

The first MNCs from outside the traditional Western sphere, the Japanese MNCs had several unique structural differences that set them apart from their Western counterparts. These include a fixed supplier network, permanent employment, stable union relations, unique distribution patterns, significantly different production practices and close inter-company relations, including bank relations. As an alternative to the Western MNC model, Japanese MNCs demonstrated powerful new methods for just about every aspect of international manufacturing.

With their rapid success in traditional Western industries, such as steel and automobiles, Japanese MNCs quickly spread their global reach around the world. By the early 1980s, several Western MNCs were hard pressed to maintain earnings in the face of overwhelming competition. By the early 1990's, many old-line MNCs, such as RCA-Victor, had been driven out of business. At a minimum, many were forced to abandon core business areas, like semi-conductor production. At the same time, Japanese MNCs snapped up bankrupt American corporations for their brand names, including Firestone and Quasar.

¹² United Nations Centre on Transnational Corporations, *World Investment Report 1993: Transnational Corporations and Integrated International Production*, New York, 1993, pg. 19.

Over the same period, economic development and post-war recovery gradually spurred the growth of home-grown businesses within other countries where foreign MNCs were once the only source of advanced goods. Many international firms emerged from the newly industrialized countries of the Pacific Asia region. Firms such as Hyundai, CITIC, Acer and Samsung, reached their maturity in the late 1980's. Samsung challenged the world with its low-cost production of sophisticated processing chips, the basic ingredient of many consumer products; Taiwan-based Acer is beating large US computer manufacturers at their own game of producing high-quality, innovative computer products.

MNCs from these countries also featured unique organizational methods. The success of the Korean *chaebol* and Chinese business networks¹³ presented yet more models of alternative competitive corporate structures which presented a challenge to the formerly dominant Western MNCs. In his edited volume, *Evolution of Asia-Pacific Economics: International Trade and Direct Investment*, Dr. Yamazawa Ippei examines structural change in the Asian economies which enabled domestic firms to grow to a size and competency to compete and win in overseas trade.¹⁴

¹³ for fuller explanation of Chinese business structures, see The East Asia Analytical Unit, *Overseas Chinese Business Networks*, Australia Department of Foreign Affairs and Trade, Canberra, 1995; and Chan Kwok Bun and Claire Chiang, *Stepping Out: The Making of Chinese Entrepreneurs*, Simon & Schuster (Asia) Pte, Singapore, 1994.

¹⁴ Yamazawa, Ippei and Fu-chen Lo, *Evolution of Asia-Pacific Economics: International Trade and Direct Investment*, Asian and Pacific Development Centre, Tokyo, 1988.

Competitive, home-grown industries were able to capitalize on domestic national economic development programs. Mexico, Chile, Singapore, Malaysia, and Hong Kong, among others, formed strong domestic industrial bases, increased national employment and raised gross per capita incomes across the board. Average growth rates in non-OECD countries between 1976-1995 were 4.8%, against OECD growth rates of 2.7%. Between 1965 and 1995, real GNP per capita grew by 3.4% on average annually, compared with 2.5% for OECD countries. And the period during which output per person doubles is constantly shrinking - Brazil needed 18 years, Korea only 11 years and China hit only 10 years between 1977 and 1987.¹⁵

Rising incomes and a strong business sector positioned these countries both as new consumer markets and as competing business centres. Household ownership of TVs among non-OECD countries rose by 219% between 1980-1995. Telephone installation grew exponentially in growing economies, hitting over 1,000% in the Philippines, 250% in Singapore and 175% in Mexico during the past two decades. Old-line MNCs were not quick to appreciate the changes in economic conditions in these markets, though they have since re-evaluated their strategies. In a telling example, US-based automobile manufacturers are only just now recognizing the need to open production facilities in several Asian countries, as these countries become the last frontier for expanded automobile sales.¹⁶

¹⁵ Mobius, Mark. *The Investor's Guide to Emerging Markets*. Irwin, London, 1995, and presentation slides produced by the same author.

¹⁶ Levin, Mike, "Asia: Last Hope for Car Makers". *Asian Business*, May 1994, pg. 50-54 and Frank Gibney, "Detroit Gets into Gear". *Time*, July 15, 1996, pg. 28-34.

At the same time as these dynamic forces were being unleashed, the opposite force was stultifying old-line MNCs in traditional markets. Early competitive pressures created by the entrance of European MNCs after WWII had the effect of driving considerable industrial consolidation, resulting in a fairly stable global oligopoly. While MNCs were also inclined to diversify into new areas of business, as the global economy was still expanding and new technologies made entry into new business sectors feasible, business management techniques during this period largely ossified. They also came to be excessively driven by cost accounting and financial analysis. In a frank discussion of the stagnation in management which evolved in the postwar economy, Alfred Chandler Jr. summarized the developments this way.

Statistical ROI data about performance, profit, and long-term plans were no longer the basis for discussion between corporate and operating management. Instead, ROI became a reality in itself - a target sent down from the corporate office for division managers to meet...Top management was basing decisions on numbers, not on knowledge, a practice that made it all the more difficult for the corporate office to carry out the basic functions of monitoring current operations and allocating resources for future activities and that exacerbated the separation between top and operating management in many companies.¹⁷

Thus, entrenched MNCs and the established international trading system, distracted by their corporate maneuvering and misled by their financial measuring sticks, underestimated the deluge of new business competition unleashed by global market deregulation and economic growth. Of particular surprise was the proliferation of successful models of corporate structures which stood in contrast to those of the Western

¹⁷ Chandler, *ibid.* pg. 21.

MNCs. The best known of these has come to be the Japanese corporate networks called *keiretsu*, although Korean *chaebols* and family networks built by overseas Chinese and Indian organizations also played a role. The unanticipated differences accorded the new entrants competitive advantages, on top of the comparative advantages they possessed at the time which were chiefly low cost labour and low cost business environments.

Sophisticated products began to appear in international markets at a lower cost than could be attained by the older-line MNCs. Because they were made in countries with lower wage costs and simpler social infrastructure, such as Taiwan and Mexico, initially MNCs thought that the problem was a simple comparative advantage dilemma, and they responded with cries of unfair competition. However, Japanese competition was the most fierce and their output presented a particular challenge, as its production was the most sophisticated, regularly surpassing the quality and innovation levels prevailing in Western markets, even though Japanese corporations produced in a relatively similar cost-structure environment.

US and European MNCs suffered mightily from the competitive onslaught, especially in what Chandler has termed “stable-tech” industries. These industries, more mass-marketing oriented, and where it was difficult to move into higher-value categories of production, found themselves against a wall. So competitive were the products from the new competitors, that to Western MNCs it seemed certain that these new competitors must be playing by different rules, rather than the standard practices which had so far

dominated the international trade system up to that time. Although the adoption of entirely new competitive strategies was what resulted in fresh market entrants winning significant market share, Western MNCs were slow to grasp this. Voicing the realizations dawning on Western MNCs, Susan Strange wrote: “The new competition is not so much a contest among the strong and the weak all obeying Queensbury rules: it is now just as much a contest among competing strategies.”¹⁸ Given that the new-comers faced the same global business conditions, from oil shocks to currency fluctuations, MNCs were ultimately forced to look outside the wage-determinant argument for the reasons for the success of their competitors.

MNCs quickly discovered, upon closer investigation, that the lack of innovation in their manufacturing techniques over the past quarter century played a large role in the cost of production differences between themselves and their new competitors. Analysis quickly zeroed in on the antiquated production practices upon which Western MNCs had relied. In fact, manufacturing techniques had little changed since the turn of the century, incrementally evolving from Henry Ford’s assembly line and Alfred Sloan’s task specialization. Not having had any particular incentive to innovate, most MNCs had contented themselves with incremental upgrades to their product lines, distribution mechanisms and assembly techniques over the decades. The production practices in particular were largely carried over from those early production and corporate structures propagated most notably by the US automobile industry.

¹⁸ Strange, Susan and John Stopford, *Rival States, Rival Firms*, Cambridge Press, 1991, pg. 91.

Until the early 1980's, most managers in the United States thought about manufacturing in terms of a paradigm whose roots went back over 100 years. The American system of manufacturing, with its emphasis on mass markets, standard designs, and high-volume production using interchangeable parts, revolutionized manufacturing in the mid-1800s.¹⁹

Western MNCs had come to adopt large-scale production which revolved around the assembly line for most major goods. Assembly lines were characterized by production tasks that were isolated and repetitive, in the belief that such a structure effected the maximum output efficiency. The early production techniques persisted in the post-war production systems, and were evident in the consistent but unimaginative output generated throughout the 1950s and 1960s.

While post-war technological innovation generated a substantial new product range, including televisions and household appliances, the underlying assembly system for making them went unchanged. This system had degenerated into a de-humanizing process which led to labour strife, low productivity and poor quality standards. Maryann Keller's tale of General Motors production process in the 1970's, and more specifically of the prevailing conditions at the GM plant in California which came to be turned around as the NUMMI joint-venture experiment with Toyota, is an eye-opening lesson in the degradation and decay which had ensued among major MNC manufacturers into the 1980's.²⁰

¹⁹ Hayes, Robert H., Gary P. Pisano, "Beyond World Class: The New Manufacturing Strategy", *Harvard Business Review*, January-February 1994, pg. 78.

²⁰ Keller, Maryann, *Collision: GM, Toyota, Volkswagen and the Race to Own the 21st Century*, Currency Doubleday, New York, 1993.

Thus, a significant discrepancy existed at a critical junction in time. Not only were new competitors emerging in large numbers, but the competition exposed weaknesses already prevalent among old-line MNC manufacturers, particularly their vulnerable production processes. Herein lies the justification for Western MNCs to concentrate on remedying their production practices, and for the emphasis placed on production reform in the remedial literature. As the emerging MNCs, led by the Japanese conglomerates, developed organic production methods designed to best take advantage of indigenous labour and material conditions, Western MNCs found themselves facing new entrants offering better products and prices. An entirely new competitive threshold was established.

The Search for Answers

The transformation of the competitive conditions, or changes in the “level playing field” came as a serious jolt to largely complacent Western MNCs and before they could respond effectively, new MNCs had captured significant market share around the world. In fact, the devastating effectiveness of the new competitors resulted in convulsions among Western MNCs, with closures, take-overs, lay-offs and outright business failures. In a stark display of the unbearable reality, a major US documentary, Made in America depicted the process of shuttering or selling one US factory after another, and the devastating impact of the inevitable lay-offs to communities across the country.²¹ With the crumbling of the traditional MNC global oligopoly, businesses around the world came to the understanding that without radical alterations in their marketing and production practices they too were vulnerable to failure.

It quickly became clear that the world trade system had entered in an era of increased participants and new criteria upon which to compete in the international trade environment, an era characterized by the “new competition”. Ultimately, old-line MNCs accepted the need to change, and the search for effective solutions intensified. To respond to changes in the marketplace, Western MNCs exhibited an increased willingness to consider new and irregular organizational structures. A hallmark of these approaches

²¹ Televised documentary, spring 1993, narrated by Robert Reich.

is that they are designed to encompass an unprecedented range of alternative business structures and methods.

For example, Western MNCs have adopted more cooperative approaches in order to get to know the competition. This can be seen in several technical agreements between major Western MNCs and their Japanese counterparts, from Toshiba and Motorola to General Motors and Toyota. New FDI patterns developed in response to the new competition. Texas Instruments took the unusual step of establishing basic R&D facilities outside of its home base in the heart of the Japanese research establishment, Tsukuba Japan. Japanese companies embarked on massive inward FDI to US, purchasing weaker competitors and old brand names. The efforts to learn, change, reinvent and regain market share were marked departures from the static nature of the 1960s and 1970s.

Looking for sources of inspiration and new approaches, the business community turned to academia and the government for support. To provide some context from which to develop solutions, Harvard Business School professor, Michael Porter, outlined the concept of competitive advantage in his seminal work, *The Competitive Advantage of Nations*. This concise term encapsulates all of the factors which firms combine - personnel, equipment, technology, financing, location, political and personal contacts - in order to turn out the most desirable product at the best cost for its customers. The basic

premise of his work is that firms and countries are not restricted by their static natural or comparative advantages, such as geographical proximity to important markets, or natural resource endowments.²²

Comparative advantage was the prevailing basis of competitive analysis through the late 1970's. Porter's conceptualization made clear that companies and nations could create advantage via the manipulation of certain production inputs, supplanting the primacy of comparative advantage in analyzing business competition. In the case of the nation, it was proposed that labour resources could be enhanced via education and the government's human resource policy. Governments could also tinker with the mix of infrastructure, tax policy and the adoption of technological advances to spur competitiveness. All of these actions would alter the nation's competitiveness, and thus the ability of its business community to match or surpass global business standards.

To make the theory more provocative yet, competitive advantages were said to be much harder to replicate - reliant as they were on creativity, human intellect and planning skills - than those inherent in comparative advantage. In a deregulated world, where foreign direct investment was a relatively easy way to obtain various comparative advantages, competitive advantages could be uniquely developed and sustained. Firms

²² Porter, Michael, *The Competitive Advantage of Nations*, Free Press, New York, 1990.

were thus enjoined to maximize their competitive advantage by maximizing the efficient combination of capital, labour and other exogenous inputs.

Today, globalization is making the notion of comparative advantage obsolete. Companies can source low-cost inputs anywhere, and new rapidly emerging technologies can offset disadvantages in the cost of inputs. Facing high labor costs at home, for example, a company can automate away the need for unskilled labor. Facing a shortage of a raw material, a company can find an alternative raw material or create a synthetic one. To overcome high space costs, Japanese companies pioneered just-in-time production and avoided storing inventory on the factory floor. It is no longer enough simply to have resources. Using resources productively is what makes for competitiveness today.²³

Competitive advantage served as a huge encouragement to Western MNCs, as it explicitly eliminated the possibility that the competition was winning on the basis of unreplicable national advantages and that the US and EU were simply, irrevocably moving towards disintegration. This was a notion which haunted the traditionally dominant global powers, and was fed by works such as *The Rise and Fall of the Great Powers* by Paul Kennedy.²⁴ The enunciation and acceptance of competitive advantage theory was also an important turning point because it discouraged firms from pursuing protective strategies, such as lobbying for trade barriers, and offered instead a recipe for matching and even ultimately bettering the business performance of their competitors. As companies came to accept that competitive advantage could be attained by process reengineering to reduce production time and/or resource usage, or by expanding the use of technology to cut down on the size of a production line, they moderated their strategic responses to more constructive, pro-active measures.

²³ Porter, Michael and Claas van der Linde, "Green and Competitive: Ending the Stalemate", *Harvard Business Review*, September-October 1995, pg. 133.

²⁴ Kennedy, Paul, *The Rise and Fall of the Great Powers*, Random House, New York, 1987.

The New Literature and FDI

In recent years, there has been a considerable amount of research on organization practices and arrangements that are network-like in form...One would need to have followed the field of international business, technology strategy, industrial relations, organizational sociology, and the new institutional economics, as well as interdisciplinary work on such themes as cooperation, the embeddedness of economic life in social structure, and the proliferation of small business units to have kept abreast.²⁵

Galvanized by the theory of competitive advantage among companies and nations, business clamoured for and received a mountainous body of research and consulting to teach companies how to nurture (or even discover!) their competitive advantages. Firms were encouraged to reexamine their corporate structure, in order to seek out new competitive advantages that can be gained through the reorganization of corporate assets and practices. While acknowledging that there are pluralistic ways to compete - on the basis of price or quality for example - many analysts advised firms that only fundamental change, corporate reorganization, or "re-engineering" was adequate to meet the challenge. The concurrence with such radical suggestions within the business community was evident in the phenomenal market reception of books like Hammer's *Reengineering the*

²⁵ Harrison, Bennett, *Lean and Mean: The Changing Landscape of Corporate Power in the Age of Flexibility*, Harper Collins Publishers, New York, 1994, pg. 125.

Corporation, and Womack's *Machine that Changed the World*, which grew out of the desire to quantify the competitive advantages of foreign manufacturing.²⁶

As the definitive study, produced by the Automotive Group at Michigan State University led by James Womack, *Machine that Changed the World* set several new standards for competitive manufacturing. Termed "lean production", it required faster product life cycles, shorter production lines, less reliance on inventoried parts, and more responsiveness to customer needs. It presented a specific programme of manufacturing improvements intended to enhance manufacturing competitiveness. This kind of research is emblematic of the material offered to Western MNCs in their quest for competitive solutions.

With the large number of offshore investments managed by the Western MNCs, it is natural that corporate reorganization encompasses foreign assets. Intensifying international competition, combined with the exhortation of analysts, led MNCs to re-evaluate the opportunities created by changing the composition of their international assets. MNCs thus leveraged their international investment as a means of enhancing the firm's overall profitability.

²⁶ Hammer, Michael, James Champy, *Reengineering the Corporation*, Harper Business, New York, 1993 and James P. Womack, *The Machine that Changed the World*, Rawson Associates, New York, 1990.

In the course of developing FDI strategies, attention initially centred on the reduction of labour costs. To some extent, firms used their FDI to lower labour costs, through the relocation of labour intensive processes to lower cost labour sites. American MNCs increased their FDI destined for Mexico, while EU corporations targeted nearby Poland, and today Japanese MNCs are rushing into China. However, urged on by the business theoreticians, firms recognized the need to achieve additional gains through the restructuring of their overseas holdings than were created simply through lower labour costs. The ever-diminishing proportion of total costs represented by wage labour led firms to de-emphasize wage rates among overseas investment criterion and to instead emphasize measures of productivity and quality for more lasting competitive gains.

Among the theoretical works prepared in response to the MNC crisis, there are many that sought solutions in a renovation of production practices, and by extension corporate reorganization at home and abroad. The adoption of best-practice techniques (as opposed to "most-familiar" techniques) was advocated. Foreign direct investment initiatives were largely portrayed as an opportunity to make productivity gains and enhance price competitiveness. Through such advocacy, theoreticians hoped to spur Western MNCs in what they viewed to be a more competitive direction, and to stem the loss of marketshare in traditional markets. To establish a working understanding of how these theories purport to solve the competitive dilemma firms face, a detailed outline of some of the major efficiency production theories follows.

Theories to Invest By

Work done by the United Nations Centre on Transnational Corporations (UNCTC) provided an important quantification of the concept of integrated production, a specific form of international production and corporate reorganization. Integrated production, or IP, refers to the connected networks used to conduct operational functions such as part supply and assembly, administrative functions and markets. The UNCTC, in an attempt to explain shifts in global FDI patterns in its 1993 report in *World Investment Review*, observed that new FDI strategies were being adopted by some MNCs to wring greater efficiencies out of their overseas investments.²⁷

In its report, the UNCTC highlighted a method of arranging international assets to optimize production efficiencies, which they termed integrated production (IP). Investments made consistent with this approach require decisions to be measured against efficiency and cost reductions rather than market or other considerations. Predicated on the principle of responsiveness sought by major MNCs in today's international business environment, IP addresses the need for corporate and particularly production restructuring by proposing the separation or "delinking" of corporate tasks and moving them to overseas locations where the optimal conditions for their execution exist.

²⁷ UNCTC, *World Investment Report 1993 - Transnational Corporations and Integrated International Production*. New York, 1993.

The UNCTC has identified three progressive stages in the method of implementation of IP. These are stand-alone strategies, simple integration strategies and complex integration strategies. Stand-alone affiliates are established by the parent firm as an independent subsidiary in another country. These stand-alone operations coordinate their own production arrangements, such as supplier and distribution networks, and conduct all of their own vertically integrated processes. An example of this kind of expansion strategy is Honda and Honda America. Honda America is very autonomous from the Japanese parent firm and has established its own component production system. The UNCTC suggests that many service firms are likely to employ this strategy of expansion, as services often require significant modification to suit the local market.

The second level of reorganization a firm can undertake is "simple integration". In this model, firms "outsource" some of the operations usually undertaken by a home firm. This is done to take advantage of comparative advantages which exist in other locations for those specific operations. Nike of the United States operates a simple integration system. In the home base, value-added operations such as shoe-design, distribution and marketing are undertaken. Other firm operations, such as financial administration, subcontracting and shoe assembly are undertaken in different locations, principally East Asia.²⁸

²⁸ Chen, Xiangming, "The New Spatial Division of Labour and Commodity Chains in the Greater South China Economic Region", in Gary Gereffi and Miguel Korzeniewicz, eds., *Commodity Chains and Global Capitalism*, Praeger, Connecticut, 1994 and the UNCTC, *ibid*.

The third model, complex integration, recognizes that efficiencies gained from simple integration can be augmented by taking the process much further. Many corporate functions are delinked and distributed around the world, wherever competitive advantage dictates functions can be achieved most productively. Often these functions are ones which the parent company traditionally kept close to the home base. Such functions include finance and treasury management, prototype design, or basic research and development. Affiliates interact often, rather than channelling all materials through the parent firm. IKEA, the Swedish furniture company, and Asea Brown Boveri (ABB) are examples of firms with widespread complex integrated production strategies. according to the UNCTC.

In this model, all units become independent business actors, and are often run by and staffed with people who are the best at their specific function. Due to the organizational separation of each functional group, each operation must make money on its own. The notion of the cost centre in corporate analysis is eliminated. Thus the data-processing "business" of the firm breaks even or turns a profit, the treasury system makes money, and so does the design function. This cost structure is less likely to be achieved by a firm which centres all functions in a single locale because while it may locate in the best geographical spot to accomplish one task, such as automobile assembly, that spot is unlikely to also be the best place in the world to process pay cheques or to make steel.

[Diagram I]

Diagram I

Diagrammatic Representation of Costing in Corporation where Functions have been Delinked

Traditional Structure in which
some departments are cost
centres and some are
profit centres.

IP structure, in which every
department must earn a
profit because it is
independently
operated and
budgeted.

Firms then endeavour to coordinate their FDI to achieve optimal cost structures in finance, administration, product assembly, information systems management, product design and marketing functions to parts of the world known to have the labour and social infrastructure to carry out these tasks most cost effectively. As is made clear in Diagram I, enabling each functional group to operate in a physical location where the activity is optimally conducted permits that group to achieve its objectives at the lowest possible cost with the highest possible level of quality. By attaining a quality/cost ratio that is superior to competitors, functional groups contribute positively to the overall corporate profit scenario. This contribution can be measured either through actual charge-back arrangements among groups or more theoretically through cost-accounting mechanisms.

What is particularly interesting about this theory is that it is applicable to all industries: resource, manufacturing and service sector firms are all able to separate each of the functions intrinsic to its business and undertake these functions where it is most efficient to do so. For example, all three sectors have differing end products, but each has an in-house pay-roll department. This function can be hived off and stand as its own business, which contracts its services to all the business units around the world and possibly to third parties. The same can be said of the in-house marketing group, computer services team, even human resources. Ultimately, every corporate group has a contractual arrangement of some kind with each other for the conduct of business functions, engendering a kind of fraternal client/service-provider relationship.

In summary, there are five basic characteristics of integrated production:

- 1) several stages of the production process are delinked
- 2) many of these production stages are transferred to other sites around the world
- 3) sophisticated technology is utilized to link the disparate sites
- 4) subsidiaries take on a more focused, integral role in the world production strategy
- 5) parent companies do not necessarily take an ownership stake in their affiliates

Using the UNCTC's conceptualization of IP as a foundation, there are other related works which contribute to the body of production theory. Considerable research on this subject is being undertaken by academics at the Uppsala University, including Jan Johanson and Lars Gunnar-Mattson. Research presented by Ghoshal and Bartlett on corporate organization in their book *Managing Across Borders: The Transnational Solution*, addresses this issue. Benett Harrison's *Lean and Mean*, and Gary Gereffi's recent edited volume on international production networks *Commodity Chains in Global Capitalism* both contribute to an understanding of the need for contextualizing FDI under the new competitive situation. They analyze state-of-the-art international production structures, examining both their positive and negative implications.²⁹

²⁹ A paper prepared by Desiree Blankenburg and Jan Johanson, "Managing Network Connections in International Business", *Scandinavian International Business Review*, vol.1 no.1, 1992, addresses this subject as do the books by Benett (ibid.), Sumantra Ghoshal and Christopher A. Bartlett, *Managing Across Borders: The Transnational Solution*, Harvard Business School Press, Boston, 1989 and Gary Gereffi and Miguel Korzeniewicz, eds. *Commodity Chains and Global Capitalism*, Praeger, Connecticut, 1994.

Networked production is a another concept of efficiency production. Benett Harrison in his recent work *Lean and Mean*, best described networked production as a loosely defined theory that refers to coordinated production activity among large and small firms.³⁰ Networked production as described by Harrison is a broad concept, incorporating cutting costs and joint production initiatives between two different companies to achieve efficiency ends.

Ultimately, Harrison sees networked production resolving itself into a “dominant” format of core-ring systems, in which a powerful core firm controls the activities of more dependent smaller firms, generally conducting contracted work for the core firm. The interdependence envisioned among companies as conceived in IP tends to result in a network that is relatively even and flat. Although Harrison admits that his core-ring system looks suspiciously like a Japan-inspired *keiretsu*, with its elaborate hierarchy, he acknowledges that MNCs are themselves moving away from such a structure to relationships that are lighter, more flexible, more international. Strict *keiretsu*, or core-ring systems are recognized not to be in the best interests of firms seeking efficiency gains.

Gereffi's edited volume tackles similar subject matter to Harrison's. However, it goes one step further by incorporating studies of companies perceived as first movers in

³⁰ Harrison, *ibid.*, pg. 127.

the adoption of radically new approaches to their international production strategies. The volume singles out several MNCs, as well as highlighting some FDI locations which specialize in specific production functions. The downside of such structures are discussed equally with their strengths.

In *Managing Across Borders*, Ghoshal and Bartlett present the characteristics of four corporate structures - international, global, multinational and transnational. [TABLE I] These structures represent a kind of evolution in the organizational thinking of MNCs, with the multinational description representative of the kind of subsidiary traditionally established by old-line MNCs, and gradually progressing through to the latest organizational structure, transnational, which in many ways repudiates the characteristics of older models. In characterizing transnational firms as “dispersed, inter-dependent and specialized”. Ghoshal and Bartlett have highlighted structural elements which represent the latest in management thinking about how to connect corporate functional groups around the world most effectively. The adoption of such a structure would necessitate the reorganization of domestic and international assets, from a stand-alone, vertically integrated model, to a more horizontal, functionally-specialized structure.

The transnational approach to firm organization places considerable emphasis on organizational efficiency. Various functions, from those of great complexity and high value-added, to those of low skill requirement and low value-added all have the potential

Table I
Ghoshal and Bartlett's Corporate Structure Model

Organizational Characteristics of the Transnational Firm

<i>Multinational</i>	<i>Global</i>	<i>International</i>	<i>Transnational</i>
nationally self-sufficient	centralized and globally scaled	core area centralized others decentralized	dispersed, inter-dependent, and specialized
exploit local opportunities	implement parent strategies	adapt and leverage parent company competencies	contributions differentiated by national units
knowledge developed and retained within each unit	knowledge developed and retained at the centre	knowledge developed at the centre and transferred to other units	knowledge developed jointly and shared with worldwide units

Source Managing the World Economy: The Transnational Solution, 1989.

to be conducted at locations around the world. The firm achieves maximum productivity by conducting each activity at the site best suited to such activities, reducing costs and increasing productivity on a global basis for the MNC.

The transnational corporate structure is especially flexible in its capacity to accept asymmetrical relationships between the parent and affiliate companies. The transnational structure allows each relationship to be determined on the basis of how to draw out the best/most efficient performance of each component business, as does IP. Examples are as follows:

- Country A has a workforce highly skilled in finance, but maintains strict foreign ownership limitations. The parent firm respects these regulations, but still recognizes the competitive advantages the work force would convey to the firm. The parent firm therefore signs long term service contracts with its affiliates while maintaining an arms-length ownership position.
- Subsidiary A is wholly-owned by the parent company and does advanced research and development. The subsidiary is located in a major market other than that of the parent company and communicates its research findings to the entire corporate organization. It also publishes the research findings for public use. The affiliate is wholly owned, but acts virtually autonomously.

- The parent company holds a token minority share position in Affiliate A. However, over 90% of the affiliate's output is destined for the parent company and is produced to design specifications provided by the parent.

Thus transnational management theory is concerned with broad management issues such as management structure, employee allocation, financing etc., simultaneously endorsing efficiency-seeking investment objectives.

With this review of the literature of FDI locational decision-making, it becomes evident that a new emphasis on investment strategies related to efficiency-seeking investment has emerged. Efficiency-oriented strategies are thought to convey maximum competitiveness in an environment of heightened international competition. FDI decision-making thus takes on a more integral role in the firm's competitive positioning. Overseas divisions are increasingly perceived to be a competitive weapon, intended to convey advantages to the MNC as a whole, not simply to redeploy or replicate the firm's existing ownership advantages.

Uniformly, efficiency-seeking investment strategies emphasize value maximization. Costs are reduced relative to quality output. As a flexible structure, such a strategy also enables management to add or shrink productive capacity with relatively greater ease than traditional investment models. This flexibility corresponds to the needs

highlighted in the competitive global markets characterized by a quicker pace. To summarize the changes, an “old” paradigm, depicted in Diagram II, is contrasted with the features of the “new” paradigm. This paradigm is most applicable to manufacturing MNCs, although it holds some broad relevance for service sector and resource sector MNCs as well.

Examples of the new paradigm structure illustrate its flexibility. Using a contract assembly work force means Nike can very readily respond to market swings by increasing or decreasing the amount of business it contracts out to specific firms. Firms can use the nature of time change to their advantage. One international law firm now wires its case load to its branch in London and then on again to Hong Kong, to receive 24 hour attention. Cases are resolved faster, clients are happier, and the firm has gained a tremendous competitive advantage, simply by using the time differences to its benefit. This is an example of how competitive advantage can be attained through the use of geographical differences. As Powell notes, network forms of organization hold the potential to become the “signature institutional form” of the era, precisely because they offer managers the best working solution to the challenges posed by the increasing need for flexibility.³¹

³¹ Powell as quoted in Harrison, *ibid.*, pg. 132.

Diagram II

Paradigm Shift in the Structure of Overseas Production Facilities

Old Production Paradigm	New Production Paradigm
Features	Features
Overseas production facilities constructed as replica of parent facility	Plants are specialized, to take advantage of local market and workforce conditions
Facilities produce identical output as parent facilities, destined for local market	Instead of making the entire production range of the parent company, overseas facilities receive mandate for global supply of a single product line, such as VCRs
Each overseas facility is responsible for all functions related to its market area	Some offshore sites are responsible for a global function, such as car design, and their output will be utilized by facilities around the world
Production guidelines and standards set by headoffice, but local manager has complete authority for their implementation	Greater autonomy in setting objectives, but global functions mean integration and mutual cooperation levels are higher
New technologies are slow to be adopted and are rarely shared across different facilities	Utilization of technology is flexible, but is encouraged to facilitate cross-border communication Also encouraged to adopt best-practice standards in all facilities

Drawbacks to the New Theories

While the literature is very emphatic on the gains to be made from efficiency-oriented corporate structures, it is important to note the strain of negativity that also emerges as a result of the “side-effects” of such strategies. There are a number of daunting tasks associated with efficiency-seeking investment as described above, which deserve attention. They are serious enough to bring into question the speed or even realizability of what is otherwise a good theory.

Most noteworthy is the challenge of managerially encompassing a global organization. The responsibilities are tremendous. It is necessary to have a fundamental understanding of several countries at once, including tax law, labour law, social norms, hiring practices, resource availability. In a recent study, Morrison, Ricks and Roth came to the conclusion that “global” firms were not ready to face a truly global business environment chiefly because their managers were not able to take in all that was necessary to cope with and adapt to widely divergent business areas. The authors felt that at best managers could cope with regionally-based issues.³² As colourfully quoted in Harrison, “Unfortunately...the reforms made to date have involved pushing the traditional...system to its limits under pressure, rather than fundamentally changing the

³² Morrison, Allen J., David A. Ricks, and Kendall Roth, “Globalization Versus Regionalization: Which Way for the Multinationals”, *Organizational Dynamics*, Winter 1991, pg. 17.

way the system works...Everyone knows the words of the new song, but few can hold the tune.”³³

Another challenge is the effective use of time and technology to maintain optimal coordination. The car seat manufacturer in Nagoya must send its inputs to Ingersoll Ontario on time, or the entire automobile assembly process ceases. Such coordination requires significant investment in computer technology to coordinate production schedules, reliable transport links and accurate planning. The potential for disruption at any point is great, and demands networked production structures to maintain once unimaginable, and still challenging, quality standards.

Yet another drawback to networked forms of corporate structure is that it is very difficult in practice to evaluate the competitive advantage of the location, and to select optimal sites. Competitive advantages are not always easy to assess, and different combinations will result in different outcomes. The crux of the issue is not, for example, should a firm use the world's best labour pool, the question is how to evaluate the labour pool of several countries, and make the right choice. Of course, management consultants capitalize on their ability to assist companies in this process, but there is no denying its complexity or the need for constant reevaluation.

³³ Harrison, *ibid.*, pg. 181.

In his book, Harrison spends considerable time on the “dark side” of flexible production, which he considers to be the vast numbers of employees who are no longer sheltered by a large company with a traditional policy of secure employment and good benefits. He sees the erosion of workers’ living standards and the polarization of wages in the US as evidence of how new production strategies which involve outsourcing and contracted production will undermine the working class.

With a truly networked company, the question of “what is home” becomes particularly acute. Imagine a company which has its data-processing and payroll administered in Ireland, has its product design group based in Italy and its marketing department in New York, raises funds from a Japanese-yen bond issue, settles its corporate executives in Hong Kong and is legally domiciled in Bermuda. Such a decentralized structure affects the definition of “home base”, upon which most corporate legislation is predicated. It certainly becomes more difficult to tax such MNCs, because many of their assets are overseas. Transfer pricing becomes a bigger concern too.³⁴ Harrison poses the question “how to regulate businesses whose organizational boundaries (and as a consequence, legal liabilities) are becoming increasingly fuzzy?”³⁵ This aspect of networked corporate structures need not have intrinsic moral implications, either good

³⁴ Transfer pricing is the practice of valuing a component good for the purchase by an affiliated firm at a cost which differs from that which would be received in the commercial market. It is a problem, because it reduces the total value of sales from an affiliate, resulting in a reduced tax base. Accusations have long been levelled at MNCs that they drastically undervalue intra-firm component transfers. See Lorraine Eden, *Taxing Multinationals: Transfer Pricing and Corporate Income Taxation in North America*, Ontario Fair Tax Commission Research Series, The University of Toronto Press, Toronto, 1994.

³⁵ Harrison, *ibid.*, pg. 34.

or bad, but it is critical that national policies keep up with and account for the nature of the changes occurring within the business sector.

Robert Reich, current Labour Secretary of the United States, and former Harvard business professor, in his book *The Work of Nations*, addressed this issue of legislating “global” firms. He questions how governments should alter policy in order to cope with the new corporate structures engendered by networked production and the expansion in overseas investment. In response, he proposes that the concept of home base should be considered obsolete and that governments should adjust their system of incentives, taxation, lobbying, and labour policy accordingly. Highlighting in his book the uncomfortable contrast between Honda America, a company which has more employees and more production in the US than in its “domestic” residence of Japan, and companies like IBM which employ more people overseas than at home, Reich demonstrates how unreasonable it is to continue to defend IBM internationally and to put up barriers to Honda. Reich takes the position that the government should employ policy for the benefit of the labour force, regardless of who hires them.³⁶ Harrison concurs, cautioning industrial and technology policy planners to place less emphasis on “which companies are ours and which are theirs”,³⁷ and to concentrate instead on developing a constructive business environment *in situ* for everyone. Thus we can see the critical implications of new corporate structures on national political and economic policies.

³⁶ Reich, Robert. *The Work of Nations*. Vintage Books, New York. 1992.

³⁷ Harrison, *ibid.*, pg. 29.

From the points raised above, it is clear that the theoretical gains to be made from efficiency production are inextricably linked to their side-effects. While seductive, corporate structures premised largely on efficiency gains in fact represent a dramatic shift away from traditional MNC organizational structures and while it is theoretically a superior logic around which to structure FDI, compared to market or resource driven investment, production-centred strategies are fraught with their own difficulties. Furthermore, it would seem that MNCs themselves are disinclined to move away from market driven investment in the short run, and perhaps also in the long run. This is due to a need to generate noticeable, significant financial gains from restructuring in the short-run. In the long-run, the need to diffuse a whole new way of thinking throughout the corporation proves discouraging. Thus, while efficiency production theories are alluring, and some firms have made a commitment to give such theories greater precedence in their restructuring agenda, in the final analysis, it seems questionable that old-line MNCs will be able to (a) abandon the traditional logic of market- or resource-seeking FDI practices and (b) muster the internal resources they need to fully implement such radical changes, even in the face of dire global competition.

MNCs and the Investment Response

The ability of firms to manage and organize a system of quite complex cross-border innovatory, production and transactional relations in one, both along and between value-added chains will become an increasingly important competitive advantage of MNEs in the 1990s and beyond.³⁸

Considerable analysis has been done to establish why firms make overseas investments, resulting in the identification of four major objectives associated with overseas investment, as developed by Eden and Dunning.³⁹ These include resource, market, efficiency and strategic acquisition reasons.

According to the Dunning model, the earliest variety of global investment was resource-seeking in nature. Global investment was predicated on the desire of a firm to obtain natural resources unavailable in its home market, either to sell them to domestic customers, or use them as inputs for the firm's own production. Resource-seeking investment predominated during the 19th century, as firms and governments pursued colonial/imperialistic expansionist policies to obtain foreign resources. This pattern of investment eventually evolved into a vertical integration strategy pursued by large firms which wanted to have assured/controlled access to critical raw materials. An example of

³⁸ Dunning, *ibid.*, 1993a, pg. 293, referring to the beliefs of several international strategy experts, such as Ghoshal and Bartlett, Hedlund and Casson.

³⁹ Eden, Lorraine, *Locational Decisions of Multinational Corporations*, Investment Canada, Ottawa, 1991 and John H. Dunning, *Multinational Enterprises and the Global Economy*, Addison-Wesley Publishing Company, London and Cambridge MA, 1993b.

such investment is the Alcan investment in bauxite plants in Jamaica, with the bauxite utilized in aluminum production.

Resource-seeking investment was largely intended to be extractive - that is, advanced processing capabilities were not integrated into the extraction site, with the resources obtained at these sites more commonly being shipped elsewhere for further downstream production. Common among former colonies, resource-seeking investment built on a long tradition of coerced resource extraction. Due to its unsavoury past, such resource-seeking investment was deeply resented by domestic constituencies, and led to extreme confrontations such as demonstrations, riots, expropriation, and even revolutions.

A subsequent development in MNC foreign investment patterns, was "market-seeking" investment, in which MNCs looked to foreign markets for customers to whom they could sell domestically produced goods, expanding their sales base and increasing the size of their manufacturing activities. However, to gain access to foreign customers, firms often had to jump national trade barriers. To achieve this, they invested in overseas manufacturing subsidiaries, which were located inside the trade barriers, and were even better able to penetrate domestic markets and further expand firm business than was possible via exports. This is the genesis of today's MNC and predominated from 1950-1979. The study by Morrison, Ricks and Roth (1990) used the example of General Electric, which purchased Westinghouse's Canadian operations, merged them with GE

Canada operations and created a facility producing a wide range of consumer appliances for the Canadian market, which was at that time protected by relatively high tariff barriers of 12%.⁴⁰

Two other kinds of foreign investment remain - strategic acquisition and efficiency-seeking. Both have as an investment objective making the firm more competitive and able to produce a better product through international investment. Through overseas investment, the firm "acquires" competitiveness by capturing the advantages present in another location. In light of the preceding discussion on new competitive pressures, it should come as no surprise that these two forms of investment are gaining increasing attention. Strategic acquisition and its derivatives, alliances and joint ventures, are variations on ownership that bring new skills in-house. In the case of strategic acquisitions, a firm is bought outright by the MNC in order to obtain certain strategic assets or knowledge such as patents. Alliances are partnerships in which the target firm and the MNC retain independent ownership, but have defined an area of exploration in which they will share the results. Joint ventures require the establishment of a third firm, whose ownership is shared by a partner firm and the MNC, and whose returns will be shared according to the terms of the joint venture agreement by the shareholders. Each approach is a means for the MNC to obtain services it could not otherwise develop in-house within a reasonable period of time.

⁴⁰ Morrison, Ricks and Roth. *ibid.*, pg. 19.

Strategic investment also holds potential as an alternative source of OLI reconfiguration, (the confluence of organizational, locational and internalization advantages) without requiring significant restructuring of the original corporate entity. Dunning states four reasons why alliances have become so attractive in business circles. He cites the escalating costs of R&D, the need to quickly introduce new product lines, access to new markets, and to advance their competitive position in general.⁴¹ The operative point here is that alliances allow all of the above to be done quickly, extending a firm's reach without concomitantly stretching its resources, by drawing on the resources of its business allies.

However, such alliances, while apparently expedient, are not absolute solutions. They are often temporary or partial solutions to the competitive issue. For example, Ford formed an alliance with Mazda of Japan to build and sell compact cars during the mid-1980's, before Ford could develop the internal capability to produce such cars itself. Yet Ford was not satisfied with this arrangement, in spite of its commercial success, as full knowledge benefits were not accruing to Ford. While Ford maintains its alliance with Mazda today, and has in fact now taken an ownership position in Mazda, it has also proceeded to develop its own internal capacity to build a compact car.⁴²

⁴¹ Dunning, *ibid.*, 1993a, pg. 293.

⁴² Barnett and Cavanagh, *ibid.*, pg.259-281.

Efficiency-seeking investment stands as the fourth category of investment rationale. Where the goal of the investment is to gain production advantages conveyed by locating in a selected geographical setting. The traditional example of such investment is the MNC which opens an assembly plant in a low wage labour locale, with the intention of reducing costs relative to the home base. Today efficiency-seeking investment is more likely to emphasize a productivity standard, with the aim of achieving the optimal cost/quality ratio. The emphasis in the literature on efficiency production was outlined earlier, and included a review of the drawbacks for MNCs of adopting such an approach to international production and investment.

Where the literature on FDI is strangely quiet is on the continuing relevance of markets to Western MNCs. Certainly market barriers have been falling rapidly, removing a major impetus for market-oriented investment. But are there other reasons to continue emphasizing market-oriented investment? What seems clear is that whole new consumer markets are emerging where once living standards were too low to justify sales efforts. In spite of the Asian economic boom, Western MNCs have been notoriously slow in addressing this segment of the global marketplace. Is this because of a propensity to implement efficiency-seeking investment strategies in Asia? If not, in what way is the literature diverging from the real-life experiences of MNCs in Asia? The following field research results will address these issues.

The Southeast Asian Investigation

With the idea of investigating a firm's propensity to implement efficiency production strategies for global expansion, Asia was selected as the target region for this paper as it is experiencing intense foreign direct investment (FDI). Where once the bulk of global investment was exchanged among the major Western trading partners, today US\$77.9 billion is annually heading directly towards lower-income countries of which over US\$42.7 billion (or 55%) of the total is moving into East Asia.⁴³ With developing countries already receiving 40% of global FDI, the World Bank forecasts this figure to move towards 50-50 by 2010.⁴⁴

The rate of change in FDI flows to lower-income countries is felt most keenly in Asia. [Table II] Rising from a negligible US\$300 million in 1970, Asia now hosts almost US\$43 billion in foreign direct investment from sources around the world. In 1994, Japan's FDI directed to Asia expanded, increasing 47% on levels attained in 1993.⁴⁵ The value of 1994 FDI hit US\$9.7 billion, topping 1989's earlier record of US\$8.7 billion. Analysts predict such levels are to be maintained throughout 1995, in response to the strong yen and declining Japanese competitiveness.⁴⁶ The burgeoning US

⁴³ World Bank. *World Debt Tables*. Washington D.C., pg. 192-194: figures are for net foreign direct investment inflows, 1994 projected totals.

⁴⁴ World Bank. *Global Economic Prospects and the Developing Countries*. Washington. 1995, pg. 60.

⁴⁵ Asian Wall Street Journal, "Japanese Investments In Rest of Asia Rose by 47% in Fiscal Year". May 17th 1995, pg. 5: referring to the Japanese fiscal year ending March 31st, 1995.

⁴⁶ Japan External Trade Organization. *Jetro White Paper on Foreign Direct Investment 1994*. Tokyo, 1994.

Table II
Investment Flows to Asia

Capital Flows to East Asia

Year	Value
	(US\$bil)
1970	0.30
1975	1.00
1980	1.30
1985	3.20
1990	11.00
1991	14.00
1992	20.90
1993	36.50
1994e	42.70

Source: *Managing Capital Flows*, World Bank, 1994

Capital Flows refers to both foreign direct and portfolio investment

Sources of FDI in Asia, 1994

	Amount	Percent of Total National Investment from one Source Country (%)				
	Invested					
	(US\$bil)	China	Indonesia	Malaysia	Philippines	Thailand
NIEs*	32.1	70.9	25.1	37.7	17.9	35.4
Japan	11.7	10.2	17.6	22.2	26.4	35.6
US	6.9	8	6.8	10.8	36.9	13.6
EC	6.5	4.4	16.1	19.6	11.7	11
Australia	1	0.6	0.8	4.6	2	0.9
ASEAN	1.1	0.8	0.5	5.4	0.5	0.5
Total	59.3	94.9	66.9	100.3	95.4	97

Source: Osamu Kawaguchi, in *Managing Capital Flows*, World Bank, 1994

* - includes Taiwan, Hong Kong, Singapore and Korea

N.B. - Totals in each chart are not consistent with those which appear in the text nor with each other, as they are from different sources within the same publication.

interest in Asia is also evident. A *Time* magazine coverstory headlined plans of the Big Three automakers for Asian investment. *The Far Eastern Economic Review* ran an eight page focus section on US investment in Asia. And Whirlpool's rapid-fire Asian investments were applauded by *Institutional Investor* magazine. Asia's share of US foreign direct investment rose to 17.7% in 1994, up from 13.6% in 1982.⁴⁷ US investment in the Philippines represents 37% of that country's total inward investment, while Japan accounts for 36% of Thailand's inward FDI. Flows of FDI within the region are also strong, representing the increasing economic sophistication of local enterprises.

Accelerated FDI flows are associated with the enhanced awareness of Asian countries as major customers and effective production/export platforms. Statistics presented in Table III speak for themselves, illustrating the high savings rates, strong economic growth, rising per capita income and the wealth accumulated by the state in the form of foreign currency reserves. Inflation remains in check in most countries, and excess capital is being channelled into the stock market to fuel further economic expansion.

In a recent Asian Wall Street Journal article, the important role that formerly lower-income economies are playing in the US economic recovery was highlighted.

⁴⁷ Far Eastern Economic Review, "Counter-Attack: Corporate America enlarges its role in Asia's economic boom", May 9, 1996, pg. 42.

Table III
Key Indicators on Asian Economic Growth

	China	Hong Kong	Indonesia	Korea	Malaysia	Philippines	Singapore	Taiwan	Thailand
Real GDP Growth (%)									
1994	11.8	5.4	7.3	8.4	9.2	4.3	10.1	6.5	8.5
1995	9.5	4.9	8.0	9.0	9.5	6.0	8.5	7.0	8.5
1996	8.5	5.5	7.0	7.5	8.5	6.5	7.5	7.0	8.0
Per Capita GDP (nominal, US\$)									
1994	425	21,607	909	8,558	3,500	1,002	23,509	11,558	2,343
1995	539	23,730	na	10,062	4,100	1,125	27,709	12,678	2,628
1996	648	27,188	na	11,651	4,400	1,200	33,090	13,433	3,007
Inflation (%)									
1994	21.7	8.1	8.6	6.2	3.7	9.1	3.6	4.1	5.4
1995	17.0	4.6	9.5	5.0	3.5	7.0	2.0	4.0	6.0
1996	9.0	9.0	8.0	4.5	3.5	7.5	1.5	4.0	5.5
Savings Ratio (% of GDP)									
1994	41.4	33.9	35.3	35.5	37.6	14.9	51.3	25.8	35.2
1995	42.2	34.5	36.0	37.0	37.2	14.7	55.6	26.3	34.2
1996	40.2	33.7	37.4	37.1	37.5	16.1	55.9	26.6	35.0
Foreign Exchange Reserves (US\$billion)									
1994	51.6	na	12.1	25.6	25.2	6.0	58.2	92.5	29.3
1995	66.0	na	13.0	29.0	28.0	7.0	66.5	100.0	33.0
1996	72.0	na	14.5	31.5	30.0	7.5	75.0	103.0	34.0
Stock Market Capitalization (US\$billion)									
1989	2.4**	76.9	3.6	118.4	57.7	15.6**	52.6**	96.2**	59.9**
1994	4.8	270.7	51.2	193	199	56.8	156.4	245.7	134.3

Sources: Merrill Lynch, SBC Warburg, Hoare Govette Asia and the Asian Development Bank, 1996

** mkt cap in 1992

Figures for 1996 are forecast only

According to a recent IMF report cited in the Asian Wall Street story, “developing nations are importing more than they are exporting to industrialized countries...running a large and expanding trade deficit...imports of US\$1.04 trillion exceeded the US\$890 billion of exports last year.” Within this framework, Asian countries are coming to represent an increasingly large market for Western MNC manufacturers. “People want consumer goods, fashions and services, and the prestige names are in the advanced countries. Couple that with infrastructure projects...and you see why companies ranging from Citicorp to Caterpillar to Nestle SA are targeting the booming places, especially Asia.”⁴⁸ The justification for undertaking research on MNC investment in Asia is strong. It is a major production centre and consumer market in its own right, which is also gaining increasing relevance as a target for foreign direct investment.

The next step was to decide how to approach the field work problem of determining a firm's strategy. Several business magazines have recently begun to examine MNC FDI in Asia, but much of the work was too generic. There was a need to have first hand interviews with senior company officials, in order to determine the real perspective from which they approached their FDI and the internal corporate goals to be achieved through the overseas activity. Due to the size of this paper and the exploratory nature⁴⁹ of its investigation, however, it was recognized from the outset that a full-scale

⁴⁸ Asian Wall Street Journal, “The Outlook”, July 8th, 1996, taken from the AWSJ home page.”

⁴⁹ Yin, Robert. *Case Studies Research*. Applied Social Research Study Series, Sage Publications, London, 1989.

investigation with definitive conclusions could not be undertaken at this time. Thus a small selection of companies were interviewed in order to obtain suggestive impressions of their activities and to point in a direction for future research.

During research in Singapore, four multinational companies were directly interviewed, and the interviews were supplemented with an informal set of questions regarding FDI locational decision-making. All of the firms interviewed had operations in more than one Asian country. In fact, many had divided their Asian business into Northeast, Southeast and South Asian divisions. Singapore was usually the seat of their Southeast Asian executive offices, but their manufacturing, administration, transportation and other functions were carried out in several countries across the region.

Of a selection of major MNCs based in Singapore and with operations throughout Asia, four firms agreed to be interviewed. They represented several countries and several industries.

- Thompson Television, a French consumer electronics manufacturer
- Matsushita Industries, a Japanese industrial electronic component manufacturer
- Victron, a Dutch components distributor
- Inco, a Canadian nickel mining and smelting conglomerate

In each case, a senior executive based in Singapore agreed to be interviewed. These executives were familiar with how their operation fit into the global activities of the main company and were also responsible for all of the firm's operations in Southeast Asia, or were integrally linked into it, from their office in Singapore.

This explains why Singapore was selected as the base for this exploratory research. Over the past years, Singapore has actively courted FDI, attracting, through specific national incentive programmes, manufacturing and administrative activities to Singapore. They have also been successful in attracting the regional head offices of MNCs. Singapore is therefore a suitable setting from which to investigate the investment strategies of MNCs throughout Southeast Asia.

The interviews were conducted over a three month period, while the author was based in Singapore as a research associate at the Institute for South East Asian Studies (ISEAS). During that time, supplemental interviews were conducted with various governmental agencies concerned with investment practices, to determine general investment patterns to bolster the impressions created by the individual interviewing process. Significant assistance was also obtained from the National University of Singapore Business School, through Dr. Singh and Dr. Lim, and via several ISEAS sponsored regional conferences, attended by members of the Asian business and

academic communities. All of this combined to generate a broader picture of MNC investment patterns than was possible with four corporate interviews.

The interview process was divided into two parts. To begin, questions were posed to establish the broad characteristics of the firms for comparison purposes. The objective was to establish the relative size of the firm according to staff and revenue, ownership structure, the role of the firm within the overall MNE organizational structure and to provide an overview of locational decision-making, based on a set of 14 criteria. The criteria were not systematically or comprehensively selected, as they were intended only to point towards issues which could be taken up during the in-depth personal interview.

These specific questions were followed by personal interviews of at least one hour. Twelve questions were posed concerning the organization of the MNC's production capacity in Asia. These questions were developed in accordance with the theories of efficiency-seeking investment outlined earlier in the paper and were designed to elicit responses which clarify the company's rationale for being in Asia, and how their objectives are being achieved through the adoption of a particular corporate structure. A copy of the questions presented can be found in Appendix One.

Below is an introduction to the companies which agreed to participate in the field research. A general overview of their business will be presented, progressing to a closer

examination of their Asian operations. All participants permitted their names and corporate details to be used for attribution. Table IV illustrates their general characteristics.

As is evident from the table, each firm is headquartered in a different country, with two from Europe, one from Asia and one based in North America. They operate in different lines of business. Consumer goods, intermediate goods, high technology and natural resources are all represented. All firms have manufacturing capacity in Asia, and manufacturing is their main line of business. Service firms have not been included in this sampling because their efficiency objectives differ significantly from those of the manufacturing sector.

Each firm can be classified as a multinational corporation (MNC), where MNC status is defined by the fact that each firm has business activities and staff posted in more than two overseas locations. Each firm has a substantial ratio of overseas employees to domestic employees. Victron is perhaps the exception here, just barely qualifying as an MNC, but its experiences as an smaller enterprise (SME) overseas are instructive and warrant inclusion. Victron's experiences allow the formation of impressions on the predisposition among SMEs, who are said to be more flexible and innovative, to adopt new investment strategies more readily than the bigger players, with long established vested interests and practices.

Table IV
Description of Corporate Participants

<i>Company Name</i>	<i>Home Country</i>	<i>Business</i>	<i>Ownership</i>	<i>Overseas Staff*</i>	<i>Revenue</i>	<i>RHQ Status</i>
Matsushita Electric Works (Asia Pacific) Pte. Ltd.	Japan	building supply	100%	10%	US\$671million	yes
Thompson Television Singapore	France	television	100%	na	na	na
Victron UPS (S) Pte. Ltd.	Netherlands	power cables	100%	20%	S\$40million	yes
P.T. International Nickel Indonesia	Canada	nickel mining	58%	1%	US\$192million**	yes

Source: Personal Interviews, annual reports, company documentation

* - Overseas staff as percent of total subsidiary staff

** - 1994 earnings estimate based on first six months reported figures

Each firm is also of a different size. Victron is a European SME, while Matsushita is an Asian conglomerate with over US\$9 billion in sales. Inco dominates world nickel markets, having once accounted for up to 85% of Western nickel output.⁵⁰ The structure of ownership is largely similar in each case, in that all are 100% subsidiaries with the exception of PT Inco (whose parent still holds a majority ownership).

Below is a brief introduction of each company and the issues that it faces in expanding abroad.

T. Teraoka, Deputy Managing Director

Matsushita Electric Works (Asia Pacific) Pte. Ltd.

Matsushita Electric Works Co. (MEW) is a distinct entity from its more famous sister company, the consumer electronics behemoth, Matsushita Electric Co. Both firms own some cross share holdings, but are otherwise entirely separate organizations. MEW is primarily a domestic, Japan-based business, producing a wide range of products for the home building trade. MEW's product lines have been divided into six business groups:

⁵⁰ Chernow, *ibid.*, pg. 598.

lighting (25.8%), wiring (19.5%), building products (27.8%), appliances (11.5%). electrical materials/devices (7.5%), automation controls (8%).⁵¹

The firm achieved annual sales of US\$9.4 billion in 1993, but discovered that it was experiencing fast shrinking profit margins. Net income at MEW peaked in 1991 and dropped precipitously in 1992 and 1993. Profits of Y35 billion (US\$3.2 billion) in 1991 can be contrasted to just Y15 billion (US\$1.4 billion) in 1993.⁵²

To reverse this trend, MEW decided to expand its business activities in Asia to reduce production costs and to find new markets. Currently, world-wide overseas sales account for only 7% of total sales. In its 1993 annual report, the firm set for itself the target of increasing overseas sales to 25% of total sales by 2001, with the intention of increasing offshore production and developing local sales teams to achieve this target.

To realize this goal, MEW is in the process of increasing production facilities and sales operations with the motto 'local production, local sales'. In recent years, economic growth has been particularly rapid in Asia, and the expectations for continued growth in this region are high. MEW is actively working on expansion in this region.⁵³

⁵¹ Annual report, 1993.

⁵² All currency exchanged at prevailing rate of Y109=US\$1. Annual report, 1993.

⁵³ Annual report, 1993, pg. 8.

Already, MEW has a sales or production presence in China, Thailand, Indonesia, and Malaysia. Each business group has dedicated production facilities in a different country: the lighting group controls PT Matsushita Gobel Electric Works Manufacturing in Indonesia; the wiring group runs Siam Matsushita Steel Co. in Thailand; Matsushita Electrical Construction Materials (Taiwan) Ltd. handles the Taiwanese output. Finally, the appliances and automation controls group runs the Matsushita Electric Works (Thailand) Ltd. in Thailand. The firm has only one research and development facility overseas, which is based in California.

Singapore is home to MEW's international purchasing office. Matsushita Electric Works (Asia Pacific) Pte. Ltd., handling international procurement in the Asian region. A Malaysian production facility is also overseen by staff located in the Singapore office.

Steve Grant, General Manager, Victron UPS (S) Pte Ltd.

Victron UPS Singapore Pte Ltd. is the 100% owned subsidiary of Victron BV, based in Groningen, the Netherlands. Their total world-wide sales are S\$40 million (US\$30 million). The firm retains, for now, 100% of its manufacturing in Holland, with some sub-contracting done out of Germany. Victron manufactures an uninterrupted

power supply (UPS) buffer which regulates the supply of power to a computer and is also capable of converting voltage.

The percentage of total company revenue generated out of Asia is 20-25%, and growing, but European sales are generally moving in tandem. All research and development are done in Holland and Switzerland. The company is also about to merge with a Swiss UPS producer that has a complementary line of UPS buffers for use in the infrastructure market, whereas their current product line is primarily computer related.

Although production costs in Europe are falling due to recession, the firm worries about long-term price competitiveness. Victron can see its industry evolving towards lower price, higher volume output - as PCs get smaller, so too do their power needs. "We used to [predominantly] sell UPS products for \$20 000, but now the customer only needs a \$3000 product". And it is concerned that Asian competitors, especially Taiwanese manufacturers, are better positioned to succeed in this environment. Ironically, continued European production together with its ISO 9000 certification, may lend the firm a competitive advantage, given the cachet some buyers attach to Europe, implying higher quality than that of competing Taiwanese products.

In determining its objectives in Asia, Victron set as its first goal to improve sales within the region. The Singapore office is responsible for sales throughout SE Asia (to

Thailand and Vietnam for example). A wholly-owned unit in Hong Kong handles sales in China. Distribution in Vietnam has been underway for 18 months. The firm has a sales director based in Bangkok responsible for sales and regional strategy; regional marketing and product servicing are handled out of Singapore; all sales orders, technical issues and procurement are handled from Holland. The Singapore office is investigating the advantages of attaining RHQ status.

However, Victron now believes that a local production presence and reduced shipping costs would expand their sales in Asia. Victron ultimately sees a need and a reason to produce locally. To this end, Victron is investigating potential production sites in the Philippines, Malaysia, India, and China. The most recent progress in this area is an agreement to establish a joint venture production/distribution facility with a large, well-know Indian company, TVS. Having experimented with joint production two years ago in Malaysia, only to see it fail, Victron is approaching this initiative cautiously, looking for a secure and reliable partner.

Johnny Chan, Managing Director, Thompson Television Singapore

Thompson Electronics, a major MNC based in France, is structured around four worldwide divisions - the tube division, the audio and communications division, video division and the TV division. All but the tube division have operations in Asia. The

Thompson research and development group has three divisions, one each in Europe, US and Asia, although the Asian facility largely supports the work done in the other locations.

With regard to the TV division, it is headquartered in Singapore, and coordinates operations at five T.V. assembly plants in Asia. Two of these plants are in Thailand. One of the Thai plants is a BOI-approved plant, which must export 100% to take full advantage of tax incentives under BOI policy regulations.⁵⁴ The exports are destined 60% for Europe and 40% for the US. The second Thai facility produces black and white televisions for the domestic market. A plant in Shenzhen, China produces for export, while the Singapore operation has a mandate to assemble big screen televisions for Asian markets. In Bataam, Indonesia a plant supplies all the other facilities with remote control units.

As a long time multinational, the reasons for Thompson Electronics to open overseas subsidiaries date back to the 1960s. It began operations in Singapore 19 years ago, after comparing costs in Europe to Singapore. Thompson Singapore has since become the Regional Headquarters (RHQ) for Southeast Asia. Mr. Johnny Chan oversees all of the Asian T.V. production from his base in Singapore. Thompson Singapore markets all of its own output and arranges its own supply network. The

⁵⁴ BOI stands for Board of Investment, the Thai regulatory body which oversees FDI and manages the country's extensive investment incentive programs.

Singapore office is also the purchasing centre for the Asian operations of the additional three Thompson divisions. Mr. Chan made his observations based on his previous work experience with Philips, DEC, Unisys and now Thompson, and as a part-time business studies lecturer from 1978-1988.

In an effort to rationalize its television production arrangements in Asia, Thompson Singapore is looking to open a new plant or expand existing facilities in either Bataam or Shenzhen. It is also reviewing the Thai domestic market production facilities, and is restructuring the Singapore manufacturing arrangements. Thompson's needs are somewhat different than those of the two firms discussed above, as it is in a stage of advanced production throughout the region, and needs to review its maturing business in the region, rather than assess entry tactics.

B. J. Higgins, International Purchasing Representative, P.T. International Nickel Indonesia

Inco Limited is the largest nickel producer in the world, currently supplying 25% of global nickel demand. The parent company owns subsidiaries in the UK, US, Canada, and Indonesia, having recently closed its troubled Chilean operation. As a Canadian company, the firm is headquartered in Coppercliff, Ontario near Sudbury.

PT Inco is the Indonesian subsidiary of Inco Limited, whose role it is to mine and sell nickel to primarily Asian customers. PT Inco celebrated 25 years of operation in 1993. Its initial agreement with the Indonesian government to explore nickel mining potential in Sulawesi province was signed in 1968. Further tests were carried out, and commercial production began in 1978 at the Soroako, Sulawesi site. To date over US\$1 billion has been invested and annual production capacity is now at 45 300 tonnes per year. In half year results from January to June 1994, PT Inco attained almost US\$96 million in sales, with net earnings of just over US\$16 million. In 1988, the Sumitomo Group of Japan bought a 20% stake in PT Inco. Shortly thereafter, in 1990, a 20% share was sold to the public and to employees. Inco Limited retains a 58% ownership stake.

PT Inco exports 78% of its production to Asian, largely Japanese, buyers. "The project was positioned in the world market primarily as a supplier to Japan."⁵⁵ Nickel matte, an intermediate good processed from raw lateritic nickel, is shipped as an intermediate good in order to be able to enter Japan duty free and to be refined into several different products. Human resources consist of 20 people based in Singapore, and 2200 employees in Indonesia of an estimated 8-10 000 staff members worldwide. A further 1500 people, mostly in Indonesia, are employed by contractors to Inco. Less than 1% of the PT Inco workforce is expatriate, i.e. 15 of 2200 workers.

⁵⁵ All figures and quote taken from the 25th Anniversary publication of PT Inco, July 1993.

The Singapore operations were designed (a) to support all supply needs of the Indonesian operations, and (b) to conduct international buying for all Inco operations outside of North America. The Singapore office now processes 60% of international supply orders on a Canadian dollar basis and 100% of PT Inco's daily needs are bought out of Singapore. It was established to take advantage of the advanced communications and transport links that exist in Singapore, in contrast with the comparatively remote mining site in Sulawesi.

With this descriptive background to the participants, it is possible to move into the interview stage of the field research. The questions sought information from company managers on their views as to why locating in Singapore was attractive. With regard to some of these factors, it may be possible to discover if there is a "push" element, in that their own home base has become inefficient relative to world standards as a base for production, or if there are significant "pull" factors in the new host country. By tabulating the numerical value associated with each response, "clusters" of issues emerge. [Table V] The largest value can be attributed to high labour skill, which received an aggregate response of 16. The second set of responses can be grouped into cost factors which received between 9-12 points each. These cost factors include attractive investment incentives, low labour cost relative to skill, and the availability of low cost capital for investment. Included in this group are several "push" factors, such as the

Table V

Table of Responses to Question #3 - Reason(s) subsidiary was established in Singapore

Reason	Matsushita	Thompson	Inco	Victron	Total Score
investment regulation	4	5	na	3	12
incentives	4	3	na	3	10
low labour cost	1	5	4	2	12
high labour skill	4	4	4	4	16
service local market	na*	4	na	5	9
gain market access or knowledge	4	2	na	4	10
new technology access	1	1	na	1	3
offset domestic currency	5	1	na	1	7
domestic labour shortage	4	1	na	1	6
availability of investment capital	3	1	na	1	5
low cost of capital	4	1	na	1	6
offset declining competitiveness	3	1	na	1	5
expand overseas	3	2	na	5	10
follow customer overseas	na	na	na	2	2
other	good transport		transport, power cost	na	

*Note - in Table V, "na" denotes factors the respondents felt were not applicable to their business and to which they felt they could not assign a numerical value.

company's desire to expand overseas in general, domestic labour shortages, and a desire to gain market access and knowledge.

A third group of responses received less than nine points each and is comprised of several miscellaneous factors, such as an interest in the new technology available in the host country, the need to follow customers overseas, and the availability of excess capital for investment. Below each of these response groups is examined more closely, drawing on comments made during the qualitative interview process and used to arrive at some observations on MNC objectives in their Southeast Asian FDI.

High Labour Skill

All interviewees remarked on their satisfaction with the skill level of the labour force available to them in Singapore. Moreover, as most of the interviewed companies controlled their Southeast Asian operations from Singapore, several comments were made regarding skill levels in neighbouring countries like Thailand and Indonesia. Victron was impressed by the high labour skill and felt that it would be able to competitively undertake higher value-added production in Singapore. However, each manager explicitly tied their comments on labour skill to labour cost. Each manager appeared to be making a value, or efficiency judgment.

Mr. Chan remarked on Singapore's labour force and that its skill/cost ratio compared to that of Europe two decades ago are what drew his firm to Singapore initially. He was quick to add that in recent years, inward FDI flows had driven up prices in Singapore, leading to the potential for the cost/skill equation to be imbalanced. He himself was not considering opening another manufacturing facility in Singapore. Mr. Teraoka of Matsushita buttressed Mr. Chan's comments by adding that Singaporean workers were now able to change jobs easily, often increasing their salaries, and that this was clouding the positive image of Singapore's labour pool. Increasingly, Singaporean workers were less devoted to their work and their frequent job hopping resulted in less skill accumulation. Thus, while high labour skill, especially in relation to that available elsewhere in the region scored highly in absolute terms, fuller comment in the course of interviews showed it to be a qualified ratification, a characteristic increasingly open to doubt, and closely linked to productivity.

Cost Factors

As noted above, many participants were concerned with the overall trend in Southeast Asia towards rapid wage increases that were not necessarily accompanied by commensurate advances in labour effectiveness. Thus, costs, including living costs, taxes, and imported material costs were all prominent considerations.

Matsushita's Teraoka felt that costs were rising fast and that Malaysia and Singapore's labour shortage meant that low labour costs alone can't be the sole reason for maintaining operations in Southeast Asia. "This is true of the Southeast Asian region as a whole, Singapore in particular". Because labour costs are changing quickly, Mr. Teraoka suggested that Japanese firms are looking to China for future investment, where it will take time for wages to be driven up uniformly. Interestingly, Mr. Teraoka is of the opinion that increased Chinese investment will not lead to a drain of investment from Southeast Asia. On the contrary, he feels that Japan itself will bear most of the investment brunt. Mr. Chan at Thompson agreed with Mr. Teraoka in his comments regarding the cost structure of labour in Singapore - it is rising and productivity is not necessarily going with it. A factor off-setting rising wages, in his mind, was Singapore's socio-political stability. Singapore's low labour cost as compared to skill level relative to the rest of region was important to Inco as well. So too was the relative sophistication of the business environment, relative to that of the rugged mining site in Sulawesi Indonesia.

Thus we see companies weighing the efficiencies to be gained from locating in Southeast Asia by carefully monitoring the costs versus the advantages. Part of this effort to weigh costs and advantages is affected by the availability of investment incentives, which can potentially offset increasing labour costs. Matsushita's Teraoka was impressed by the fact that if the Singapore-based subsidiary made dividends, they were not taxable in Singapore - he felt this was a good incentive. Victron and Inco cited the incentive of no import taxes, which helped their trans-regional shipping arrangements based out of

Singapore. Thompson's Johnny Chan cited Bataam's government support in the area of regulation as being conducive to doing business there - he subscribed to the belief that the business "context" is everything and that this is widely influenced by political attitudes. Mr. Chan said, "You can always train people, but if government is intent on creating a beneficial [business] context of cost, regulations, and stability, these are the critical factors."

The other aspect which emerged in these responses was the interest in markets throughout the region. None of the interviewed firms were active in Asia solely for production and export purposes. Each already had, or was in the process of expanding, their capacity to service the local markets of Southeast Asia. Thompson was manufacturing black and white televisions for Thailand, and big screen T.V.'s for the rest of Asia, while Inco was selling nickel to Japan and Indonesia. Victron cited as one of its objectives the aim of enhancing its competitiveness by being close to customers that might otherwise look to a local Taiwanese competitor. Servicing customers with a local market presence was also thought to be useful because shipping costs could be reduced on a bulky, hard to ship item. Victron's Grant made the observation that the Singapore market for customers is "bigger than it looks" as a result of all of the regional headquarters conducting international purchases from Singapore.

Secondary Responses

In the third group of responses, we find that answers which came low in the priority rankings of the respondents generated inconclusive results. The ready availability of investment capital as a general criteria was not so important, nor was the need to offset declining competitiveness at home. Victron was the only firm which explicitly discussed a need to be in Asia to offset declining competitiveness at home, but even Victron qualified the statement by saying that at this time competitiveness is quite good due to the economic downturn which had reduced costs at home. Rather the firm was worried about the future and had decided to act in advance.

A number of respondents cited "other" as reasons for their investment, and within this category uniformly referred to infrastructure as being very important to their presence in Singapore. Transportation costs, convenience of reshipping, good power rates, advanced telecommunications, comfortable living environment - all were cited in support of the decision to be in Singapore. When combined with the tier one factors, the priority accorded to efficiency resulting from a largely productive labour force and effective infrastructure availability is noteworthy.

Overall, it appears that firms do operate out of Singapore specifically and Southeast Asia more generally in order to attain greater cost efficiencies than are otherwise attainable in other countries. These cost efficiencies are a careful blend of costs

and productivity, rather than a bottom line low wage issue. Additionally, their motivation to invest also derived from the appeal of market access and the expansion of sales. This raises the question to what extent are firms willing to forgo some production efficiency in exchange for market access potential.

If that the motivation to be active in Asia is a mix of cost and market related factors, it is necessary to investigate if the cost-related factors involve a move towards network-style organizational structures. To this end, several questions were posed relating to the structure of the Asian subsidiary and its relationship to the main corporation. The balance of the interview questions, posed during meetings of at least one hour in length, allowed the author to develop a fairly detailed appreciation of the structure of the firm and intra-firm relations.

Before advancing to the interview responses, it may be useful to reiterate the main features of network-style organization structures:

- 1) several stages of production process are delinked
- 2) many of the these production stages are transferred to other sites around the world
- 3) sophisticated technology is utilized to link the disparate sites
- 4) subsidiaries take on a more focused, integral role in the world production strategy
- 5) parent companies do not necessarily take an ownership stake in its affiliates.

1) *Several stages of production are delinked*

During the interviews, questions regarding component production and the specialization of any Asian affiliates were posed to draw out the degree to which efficiency concerns were a predatory factor in FDI placement. What emerged was that production functions had not been delinked, but product line specialization had been inaugurated and assigned to certain Asian production facilities. This is known as awarding a “global mandate” to distinct overseas operations. Thompson attempted to divide its Asian operations according to product output, forming a type of specialization. For example, the Thai plant exports 100% of its production runs to global markets, and the Singapore plant has a mandate to produce big screen TV for the Asian markets. However, these are not firm mandates, and plans to shift them are already in the works.

Matsushita allocated certain production facilities to certain product groups, as described previously. In the case of Victron, it too is considering moving towards a global product mandate, with its new Indian joint venture partnership to be allocated production of a single product line for the world markets. Few of the plants of any of the corporations produced components destined for other affiliates. Matsushita's Teraoka said he would like to move in this direction, with Japan producing specific high-tech components for world wide operations, but the firm has not yet formally adopted this strategy. Thompson's remote control production plant in Bataam did supply other

regional operations, but that plant was also able to sell its output on an OEM basis to third parties.

One form of functional specialization which was widely adopted was the procurement and head office administrative function for all of the Asia region. Thompson, and Matsushita had definitely sought out RHQ status for their Singapore subsidiaries, and had been granted international procurement mandates within the MNC organization. As an RHQ, the Singapore offices undertook administration, accounting, shipping, procurement and quality control for Asia. Matsushita also used Singapore as a shipping hub, to which all Asian production plants shipped their output, where it could be rebatched and distributed according to orders that were also processed in Singapore. Inco too, has tried to devolve a functionally specialized role onto the Singapore office, by gradually increasing its responsibility for global purchasing. The Singapore RHQ now executes 60% of Inco's purchasing for operations outside of North America.

2) *Production stages relocated to efficient sites all over the world*

In the interviews, participants were asked how efficient their production in Singapore was compared to the home environment and compared to other areas around the world. The answers given chiefly related to the costs of labour which are rising in Singapore - too fast to be able to sustain it as a manufacturing centre, in the opinion of Matsushita's Teraoka. The participants reiterated many of the concerns previously

highlighted, regarding costs of labour and instead cited other factors influencing their attitude towards the competitiveness of their Singapore operations. Teraoka liked the fact that suppliers were responsive, and “know what to do to survive”. He felt they were able to meet quality and specification demands. Labour throughout the region was also more open to suggestions on improvement compared to other nationalities, such as the US. Inco’s Higgins felt to some extent that internationalized purchasing operations hurt supplier relationships, which undermined the competitiveness of aggregating procurement in Singapore. However, other factors offset this concern, such as labour costs, transport conditions, and cost efficiencies to be gained from bulk orders.

Most of Victron’s approach centred on customers and the market, rather than efficiency gains from locating an office in Singapore. However, Mr. Grant pointed out that as an SME, the firm can not afford to sacrifice efficiency for long, so while their production structures are not radical, Victron has incorporated significant efficiency factors as well. He characterized initial entry into Singapore as being “on the cheap”, with one staff member and an office, until the operation proved itself. Mr. Grant also referred to their joint venture with the Indian firm TVS as an example, saying Victron was willing to “sacrifice some profit margin” for the security of working with a well-established organization that will “get sales immediately”. However, to draw the line, Mr. Grant noted that in spite of the potential evident in the Vietnamese market, Victron will not consider production there.

3) *Sophisticated technology employed to link disparate production sites*

Some firms are considering or initiating automation in production operations to offset rising labour costs. However, as firms initially didn't anticipate the fast rising labour wage rates, there was some resistance to this practice. There was minimal discussion of communication technology or advanced "just-in-time" component coordination that might be suggestive of IP-like production activity. Several respondents cited their satisfaction with the region's telecommunication and transport links, but this had more to do with procurement from third parties than it did with intra-firm transfers of output among the MNC subsidiaries. Inco noted that the level of technology intensity at its extraction operations in Indonesia is equal to that of its Canadian home-base operations. "The degree of technology intensity...is pretty high". Again, however, this technology was not employed to link disparate corporate sites, but rather to enhance local extraction activities.

4) *Subsidiaries have integral role in world production strategy*

Matsushita was the only participant with substantial intra-firm trade. Mr. Teraoka said that production in Southeast Asia was divided, with 30% exported back to Japan as component parts, while the remainder was shipped to final customers or went on to other international affiliates. In the long run, Mr. Teraoka expressed an interest in heading towards a form of international division of labour where Japan, Southeast Asia and China could form a graduated chain of production, with Japan producing high tech inputs

for world wide operations. While this conceptualization is different from IP in certain technical aspects, it is certainly a step closer than the stand-alone product mandates of other MNC subsidiaries. As noted above, however, Matsushita has not made too much progress in moving towards an international networked production structure. Inco had no real intra-firm trade, except for transfer of assets among affiliates, like heavy equipment. With the exception of the Bataam plant's remote controllers, all Thompson plants produced end-goods destined for market.

Another way to get at the issue of the role of subsidiaries is to consider how the affiliates interact. Is there a significant degree of coordination? Is one plant dependent on another for component inputs? Matsushita again is the only participant with any degree of inter-affiliate interaction. The Singapore office is integrally involved in the management of inter-affiliate relations. Mr. Teraoka indicated that all factory managers have annual meetings in which production levels, mix and allocations are decided. Throughout the year, frequent revisions are made. He even has a dedicated internal telephone line to all the plants around the world from which he is able to call anywhere as if it is a local number.

Victron has a more basic structure, in keeping with its smaller size, in which the marketing group reports to a director in Bangkok on sales and regional strategy. Regional marketing and product servicing are handled out of Singapore, while all sales orders.

technical issues and procurement continue to be managed by the Netherlands headoffice. This suggests a beachhead role for the Asian operatives, not a defined long-term niche responsibility. Inco does not encourage a lot of contact among affiliates, and those that exist are largely based on personal relations among staffers. Staff member transfers are discouraged, and Inco prides itself on its "localization" policy at the Indonesian mine. Thompson Television has all of its Asian television production units reporting in to Singapore, so affiliate relations are determined on a regional basis.

The above-noted affiliate relations among Matsushita operations suggest that a significant level of autonomy exists among the plants. Mr. Teraoka himself said that management of his operation is left largely to him, as long as he makes money. Mr. Chan made the same assertion - he has considerable autonomy from France, and bosses in France accept his arguments as long as he supports them with bottom line results. Mr. Chan has the authority to make decisions such as opening and closing plants within his division. While autonomy implies equality, in this case, it is not an equality based on asymmetrical power relations among subsidiaries and mutual interdependence. The global product mandates combine with the relative autonomy of action within Southeast Asia to create instead a type of regional "stand-alone" product structure.

5) *MNC does not necessarily hold ownership stakes in the affiliates*

Table III outlined that of the four subsidiaries we interviewed, all were majority owned by the parent MNC. No variation was found in this situation for the other subsidiaries overseen from Singapore but scattered throughout Southeast Asia. The Singaporean office of Victron was in the process of negotiating a joint venture with an Indian partner, but this is the only example of asymmetrical ownership relations among the participants.

A Summary of the Interview Outcome

Given the foregoing, the interview responses do not suggest any substantive move towards integrated production, or in fact much of a networked production structure at all. This can be better seen in the table below which summarizes the responses, creating a “thumb-nail sketch” of the structure of operations of these four MNCs in Southeast Asia.

[TABLE VI]

It is possible to infer from the above that Thompson Television is interested in a low cost environment. Their work is not divided by function, but rather by product line and market. Significant emphasis has been placed on regional sales and production.

Table VI
Summary of Production Activity*

THOMPSON	MATSUSHITA	INCO
has regional market mandate, except for Thai BOI plant, exporting to US/EC	plants generally have a product mandate	operates as an independent unit
plants don't interact	strong intra-firm relations	plants don't interact
little local R&D	little local R&D	considerable local R&D related to local needs
most of the plants are final goods producers	plants make both intermediate and final goods	intermediate goods producer
high autonomy	high autonomy	high autonomy
little intra-firm trade except Bataam plant	some part supply to home base	inputs sourced globally
low level of technology, corresponding to sophistication of plant site	modest technological intensity	
more efficient/cost effective than if done at home	quite competitive vs. if done at home	competitive with world standards

* - Victron excluded due to lack of production in Asia at this time

rather than global functionality. Little functional specialization except procurement was discovered. If we refer to Ghoshal and Bartlett's matrix (Table I), Thompson's structure looks more like a multinational, one of the traditional formats, not a new structure such as the global or transnational formats.

In the case of Matsushita, the evidence points to a company that has designed well-integrated operations throughout the region, and is equally market and cost oriented in its Asian investment strategy. Inco stands out among these groups because it is the only "stand alone" model plant, where sourcing and marketing are the subsidiary's direct responsibility. From the interviews, it has been explained that Inco is not located in Indonesia because of cheap production opportunities, but rather because it can sell its output in Asia, due to its proximity to the market. Procurement is becoming functionally specialized, but this is an isolated case within the rest of the corporate structure.

What emerges from these interviews is the emphasis placed on the local or regional market for resale of output generated by the Southeast Asian operations. From the interviews, it is possible to develop a picture of MNCs experiencing static growth in their traditional markets, and that to maintain, much less expand, their corporate revenue, overseas subsidiaries are being asked to, and given responsibility for, expanding their sales and marketing efforts in more distant markets. When asked how many were producing for local markets, how many had mixed strategy, and how many for export, it

turned out that Inco was reliant on the regional market, Thompson both exported and sold locally, Victron was almost solely interested in local sales and Matsushita placed the objectives of expanding local production and sales on an equal footing, of equal importance to the company.

This contrasts with the fact that for most Western MNCs prior to the 1990's, Southeast Asia was not even on their marketing horizon. The contribution of this region to corporate earnings was negligible. Yet today, when MNCs emphasize Southeast Asia's cost structure, they speak with equal enthusiasm of the market potential. A change in perspective of this nature could only have occurred as a result of two realizations. The first was a newfound awareness of the danger in relying on traditional markets, now that they had been found to be vulnerable to competitors. Second a new awareness of the rapid growth rate of Asian countries, raised their attractiveness in contrast to the sluggish Western markets. In Asia, a virtuous circle in which increased investment in productive capacity, driven in large part by foreign investors, resulted in expanded national revenues, reinvested in further productive assets such as infrastructure and education, compounding to lead to a rise in income, greater purchasing power, and ultimately the emergence of a consumer market attracts further FDI.

The perception of Asia as an important customer base, and the need to establish a market presence to appropriately service the market, is an important factor in MNC

activity in Asia. The attraction for FDI in Asia is customers at least as much as it is production efficiency. This is not say that firms are not more interested in efficiency than ever before, having had their vulnerabilities exposed in the most dramatic fashion when new competitors appeared on the scene. But without the concomitant attraction of markets, it seems unlikely that foreign direct investment would have occurred or will continue to occur on the scale that has been seen to date.

Where firms are restructuring themselves, and allocating productive investment to Southeast Asia, they do not appear to be following the dictates of networked forms of production. The evidence for this is that MNCs really haven't separated out functions from their home base as would be consistent with theories of networked production. We find that it is much more likely for Asian subsidiaries to have global product mandates and/or regional marketing responsibilities. The plant is likely to produce certain product lines, such as Thompson with certain TV lines, or Matsushita with differing product groups, each complete with their own in-house support systems like personnel, administration, finance. In a limited number of instances, functions were divided by location within the region, such as Inco's and Matsushita's purchasing office in Singapore, or the Bataam plant's production of tubes. But this does not represent a company-wide trend and instead appears to be an opportunistic development in light of specific conditions created through incentives offered by the host government. In the case of procurement, the Singapore government has instituted generous tax advantages

and invested in state-of-the-art shipping facilities and procedures to encourage businesses to specialize in this activity.

Firms are prepared to completely reinvent their entire international business network, (i.e. change old suppliers, move into new markets, establish new client relationships, build things a different way, borrow from new institutions) but they are also trying to satisfy multiple objectives, preferably with a shorter time horizon. Increasing sales to a new client base is likely to confer benefits to the firm faster, through rising revenues, while still encouraging change in production standards to satisfy new customer demands.

The firms interviewed, therefore, seem to be adopting medium-term strategies designed to help them compensate for greater competition and concomitant shrinking margins. These strategies appear to be designed to be easier to implement and to generate faster results. Chiefly, these MNCs are widely involved in (a) seeking out new markets and (b) expanding their operations into non-traditional sites. These approaches have more appeal and the potential to be implemented more rapidly and to generate less controversy than restructuring. This suggests that firms may not be ready to entirely restructure their production activities according to the dictates of absolute efficiency, although they have become more accepting of flexible interaction with other organizations to enhance competitiveness.

Implications for International Investment Patterns

An overview of the activities of four multinational regional offices in Southeast Asia does not equate a definitive global study of MNC activity around the world. However, given the relative importance of Southeast Asia in recent years as a destination for international capital investment, and given the range of activities undertaken by the four firms interviewed, it is worth suspending the qualifications for a moment to consider what the answers to the survey may imply about international patterns of investment. were the surveys found to be representative of broader MNC activity.

MNCs seem committed to developing a presence in a wider range of markets for two principal reasons: first, to find new markets with greater growth potential than that offered by their home base, mature economy markets and second, to enhance regional exposure that will allow them to better operate in the global economy. A concomitant goal at the managerial level is to learn more about the nature of the new global competition and figure out ways to psychologically and practically come to terms with it.

This emphasis on markets would suggest an appreciation of the fact that the international business universe has expanded and that MNCs are prepared to embrace this reality. In the move to adapt to reality, however, Western MNCs appear to believe that there are two dimensions to regaining strength under these circumstances and they want to move on both fronts at once. The “supply-side” aspect relates to more efficient production - most corporate literature addresses such issues, especially as early competitive pressures emanating from Japanese business activity was perceived to stem from the superiority of their production processes. However, firms are very conscious of the second dimension, “demand”, which is chiefly concerned with the newly-expanding consumer base. The literature on MNC market development in Asia is much less outspoken on this dimension, but firms seem to be moving ahead on their own, rapidly expanding their local presence and leveraging their productive investments abroad into marketing outposts. It is this picture of MNC activity which was suggested by the results of the qualitative interview process of managers running MNC subsidiaries based in Southeast Asia. Firms seem willing to open production sites which are not optimally efficient, but have the added benefit of creating a “local face” for the MNC organization. The organization can begin by servicing other international clients in the region, while learning about the market environment and establishing a local reputation.

Once investment reaches a certain magnitude, firms discover additional business opportunities in addition to their bread-and-butter exports to traditional customers. With local economic growth, as the annual 8% figures in Asia connote, comes the opportunity

to supply that growth, and this is where MNCs may perceive their long-term opportunity. Rather than look at these countries as cheap labour markets to help the MNC produce goods for its home market at cheaper costs, MNCs are coming to approach these countries as markets in their own right. A local production presence gives the overseas firm the opportunity to learn about the needs of the market. The natural logic of overseas investment, in the long run, is therefore to support growth through the expansion of consumer markets, even if initially these markets do not possess well-developed consumer cultures or the firm does not possess market experience.

Interestingly, this process is apparent in the market segmentation already instituted by the MNCs interviewed. Many have divided Asia into Northeast Asia (China, Hong Kong, Taiwan, South Korea), Japan, and Southeast Asia (encompassing the ASEAN countries of Singapore, Malaysia, Indonesia, Philippines, Thailand, Brunei and Vietnam). If more widely applicable, this process would indicate that MNCs see the region as more than a production outpost. Otherwise firms could more simply divide all of their overseas production among a few countries in Asia, and ship the output to the rest of the world. Because firms have in mind from the beginning the notion of servicing consumer markets, they realize that they must differentiate their Asian strategy according to similar consumer environments, looking at stages of growth and income level. This makes the division between Asian regions reasonable and even shrewd. Thompson's Chan perceptively acknowledged the inherent logic of this development during a conference on regional trade, when he stated that trade liberalization was as important to him as

business deregulation, because MNCs need access to broader markets at least as much as they need more efficient production.

Based on the feedback garnered during the field research, efficiency-seeking is not the primary investment motivator, because firms are equally emphasizing new customer markets. Firms can leverage their early production presence into positive market reputations which enhance their name recognition and can help build sales in the future. In effect, they become Reich's "insiders" - foreign companies so active domestically that they become associated in the mind of national consumers with local business. Investment is predicated on a two-prong strategy of gaining production efficiency and market access. Pure production efficiency makes good theory, but does not reflect the true approach of the multinational corporations interviewed in Southeast Asia when restructuring their overseas assets.

More generally, it seems that where firms do hope that Southeast Asian FDI can reduce their production costs, largely through the lower wage labour rates, they realize that this is a short-term gain at best. All of the firms interviewed recognized that wage labour rates are rising in Southeast Asia, due to the large volume of FDI moving into the area over a short period of time. Moreover rapid economic growth has caused labour shortages, accentuating the pressure on wage labour rates to rise. However, given that wage labour rates represent an increasingly small proportion of production costs and that

low-cost labour sourcing is an easily replicated competitive advantage, there was never really an assumption that efficiency gains from reduced labour costs offered long term competitive advantage from the relocation of production to this area.

As for the lack of interest in networked structures, the complex calculations required to evaluate the optimal investment decisions appear to be a major barrier to their implementation. It would require thinking and training in a manner with which none of the interviewed managers were familiar, nor for that matter, interested. The complexity of the assessment of competitive factors, via internal and external audits, is so complicated that it leads firms to opt for more simplistic reorganizations than are suggested by the theory. Of course, the example set by the success of functional specialization in the case of procurement may lead some firms to experiment more fully with this concept in the future.

From the field research outlined above, therefore, five trends emerge.

1. There is a strong awareness of competition and eroding corporate earnings which MNCs are strenuously attempting to halt.
2. As a result of (1), there is an equal or stronger emphasis placed on market development when making FDI decisions: firms are not looking at each site from the perspective of optimal production efficiency alone.

3. There is a lack of familiarity with the conception of networked production, and no apparent plans to implement such a structure.
4. Where efficiency is considered, complex networked structures had not been selected.
5. Where the conditions exist to implement selected functional specialization, such as procurement, MNCs recognize the efficiency benefits and are willing to develop them further.

These trends beg the question, why does such a discrepancy between the theory and the reality exist? I would suggest that there are two reasons. First, firms are simply unable to manage a fully “global” organizational structure. Second, there is a difference in the level of analysis undertaken by MNCs versus theoreticians - tactical versus strategic.

In the first case, MNCs are predominantly “international”, not “global”. Recognizing their inability to fully cope global consumer demands, they continue to emphasize regional organizational structures. The awareness of Asia as a major market has only recently been fully integrated into MNC planning, leading to a commensurate upgrading of FDI operations in that region.

Additionally, managers with Western MNCs are not yet prepared to operate truly global corporations. In their study, Morrison et al. discovered that management has not psychologically caught up to the potential for their companies of true globalization. As this process would be made more difficult by adding the layer of managing a networked corporate structure, it would appear that MNCs remain satisfied with traditional subsidiary structures until such time as their staffs are adjusted to the global realities.⁵⁶

In the second case, the emphasis on tactical reform is due to the intensified competition described in this paper. Competition has chiefly manifested itself in companies' bottom lines through narrower profit margins and slimmer earnings, even losses. This is evident in the case of Matsushita, whose profit dropped by a third over three years! While at the *strategic* level, it is accepted that major corporate changes need to take place in order to better the position the company relative to its competitors and its customers, the severity of the losses means companies need to adopt short- to medium-term solutions which will remedy their predicament more readily.

Even implementing changes at the tactical level remains a greater struggle than suggested by theories of globalization and competition. Thus, while there may truly be merit in the conception of a transnational corporate structure, or in asymmetrical organizational relations, such theoretically efficient practices stand at odds with systems

⁵⁶ Morrison, Ricks, Roth. *ibid.*

and practices already in place, and with the desire to quickly return the company to profitability. There are also problems with the theory of networked structures, in that global conditions may not yet be ready for them. The tight coordination and constant communication demanded by networked structures is technically possible, but given natural problems like power black-outs or earthquakes, it is possible that the necessary infrastructure is not yet in place. The inability of human capacity to absorb all that is necessary to implement high-efficiency systems and keep them running means that the adoption of alternative corporate structures is as yet impracticable and unappealing to most business people, except as a very long term target.

Tactical level solutions may be less all-encompassing, but have the advantage of relating to the bottom-line more directly. Companies face a logic like this - If one has fewer customers, one needs to get more. Where can one find new customers today? In Asia. If you have less profit, you have less money to reinvest in the company. How can you make those funds stretch? Adopt corporate reforms with low costs and quick results. The calculations are simple. This may be an explanation as to how firms can approach restructuring in a manner that will generate short-, medium- and long-term results by proceeding on several fronts at once.

What are the implications of the suggestion that market access is so important to MNCs in their investment decisions and their global growth plans? First, it would seem

likely that continuing high FDI levels will be linked to expanding local market access. If efficient production was the primary decision-making factor, flows could be expected to continue as long as local factors of production, such as labour, resources, and infrastructure were consistently maintained and steadily upgraded. This is the pattern on which many Southeast Asian governments base their policy decisions.

In fact, because markets are an important consideration to MNCs in their FDI decisions, MNC investment is likely to centre on those target countries where they can combine their productive capacity with local market development, by encouraging consumption, and opening up their local markets to international goods. Traditional consumer markets in North America and Europe have matured and plateaued. With mature markets in the West, MNCs will naturally look to the expanding consumer base of Asian for their corporate sales growth. Those Southeast Asian countries that will continue to be most successful in attracting FDI are those countries which adopted the most liberal trade and import regulations in Asia.

Continuing with the assumption that markets matter to MNCs as much as productivity, trade liberalization is an important factor in any country's efforts to attract MNC investments. The message that other countries can take away from the experience of Southeast Asia is that market liberalization needs as much attention as investment liberalization in national policies.

This realization, in turn, has implications for the long run success of international trade agreements and forums. These forums, as adjudicators of international trade and as bodies within which nations negotiate trade laws, must become a more integral factor in national policy making and receive more attention from the international business community. It also suggests that trade talks should become more progressive in the dismantling of barriers over time, as the links between investment and market access are made clearer. The importance of market access to MNCs also suggest that trade agreements are likely to be of broader scope, and that future trade negotiations, such as AFTA, will aggressively target rapid tariff barrier elimination.

Only four companies were consulted for this paper, but regular reports of MNC activity in Asia bear out the principal conclusions - that (a) firms are reorganizing to better prepare themselves for truly global competition; that (b) they are not moving towards radical organizational structures which have as their main objective the achievement of ever greater production efficiencies; and (c) that in fact, MNC investment decisions are integrally connected to market access concerns. Further studies in greater detail need to be undertaken, but the direction suggested is clear.

Appendix I

MNC Interview Questions

Section A

1. Corporate Structure

- (1a) Nationality of parent _____
- (1b) Ownership of subsidiary _____
- (1c) Size of subsidiary staff _____ revenue _____
- (1d) Role of subsidiary - HQ Distribution Admin Manufacturer Service/Sales

2. Overseas Employment

- (2a) % of total regional staff employed in Singapore _____
- (2b) % of world staff employed in Singapore _____
- (2c) % of world staff employed in Asia region _____

3. Reason subsidiary was established in Singapore

	not important-----very important				
3a. favourable investment regulations	1	2	3	4	5
3b. availability of investment incentives	1	2	3	4	5
3c. low labour cost	1	2	3	4	5
3d. high labour skill	1	2	3	4	5
3e. to service local market	1	2	3	4	5
3f. to gain market access/knowledge	1	2	3	4	5
3g. to gain access to new technology	1	2	3	4	5
3h. offset domestic currency	1	2	3	4	5
3i. domestic labour shortage	1	2	3	4	5
3j. availability of excess investment capital	1	2	3	4	5
3k. low cost of investment capital	1	2	3	4	5
3l. offset declining competitiveness	1	2	3	4	5

3m.	to expand overseas	1	2	3	4	5
3n.	to follow and service customers	1	2	3	4	5
3o.	other (s)					

Section B

1. Why is your company active in Singapore?
2. Does your company have a broader "Asia" strategy?
3. What is the degree of technological intensity in local production?
4. Are the Asian operations intermediate of final good producers?
5. Does the plant have company-wide responsibility for a function?
6. What proportion of the Asian operation's revenue is generated by intra-firm sales?
7. What proportion of inputs for Asian operations are locally sourced?
8. What is the annual value of R&D conducted locally?
9. How much direct contact occurs among MNE affiliates?
10. How much autonomy/independence do the Asian operations have?
11. How competitive are the Singapore operations compared to (a) if done in home country or (b) if done elsewhere in the world?
12. How much of the parent's reason for opening operations here had to do with (a) production efficiency or (b) local market access/service (how much of one is given up for the other?)

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