Why Do National Firms Become M Essay, Research Paper

Why do national firms become multinational? Critically Discuss.

We must first define between a national firm and one that is multinational. A definition of a national firm could be a firm that s market is mainly in the country it sells into and has no Foreign Direct Investment in any other country apart from the one in which it sells into. A multinational on the other hand is a lot harder to define because over time the very nature of a multinational has changed. For Example in 1958 Maurice Bye began to see and recognise multinational enterprises (MNE s) by the definition Multi-territorial firm indicating that a MNE was purely given the name by the amount of countries a company occupied. By 1960 this had already been updated with David Lilienthal new definition, Multinational Corporation that has become a recent standard definition. Academics see a multinational in greater depth and again the definitions are always slightly different, J.Dunning defines a MNE as an enterprise that engages in Foreign Direct Investment (FDI) and owns or controls value adding activities in more than one country (1992). Dicken on the other hand believes a Trans-national corporation is a firm that has the power to co-ordinate and control operations in more than one country, even if it does not own them. This illustrates the problems of defining a multinational although we can see that there are common themes. We can therefore assume for the purpose of this text that a multinational is” firm that has headquarters in one country, but with bases, manufacturing or assembly plants in others. However Quelch and Klein argue that Any company that establishes a site on the Internet automatically becomes a Multinational corporation. (Internet Encarta) Which would suggest that most large national corporations are in fact multinational because of the very fact that a website makes them Global and open to a foreign market but this is somewhat wrong because it does not fulfil the criteria of FDI in a country.

National firms become multinational for a number of key reasons, to take advantage of overseas resources and factors of production, to be closer to there market, to avoid legislation, to gain tax advantages, to weaken domestic unions, to increase global sales and to gain monopoly power over there competitors. Although multinationals can be defined into three categories, natural resources e.g. Petroleum and Mining, manufacturing e.g. Chemicals and consumer goods and lastly the service industry for example shipping and banking. We will look at the term multinational in its broadest sense because each fragment has its own individual reasons but all of them carry common themes

Many national companies will become in a sense multinational to make use of resources abroad, for example before world war two most foreign operations established themselves abroad to secure sources of raw material, developing countries were usually the recipient of world-wide FDI, mining companies like St John d el Rey set up operations in Brazil so that they could mine gold not only in the US but also in Latin America. You can argue that even today this idea of getting closer to your raw materials has not changed because it reduces overhead costs although it is less of a factor today because increased transport networks have made it increasingly easier to get to your raw materials. Recently what has become more prevalent is that MNE s have taken advantage of the cheaper labour costs of developing countries. For example, In the United States hundreds of corporations from automakers to electronics manufacturers have moved jobs from high-wage US facilities to low-wage plants in Mexico and other Latin American nations. (R.C.Longworth, The New Global Economic Order) What is essential though when companies become transnational is that although there may be cheaper labour in developing countries often they are not as skilled. This can often lead to poorer productivity, for example, labour is X times less than there home country, but at the same time productivity could be X times less. Here it would be pointless ploughing FDI into a new foreign adventure because there is no gain.

As Kenwood and Lougheed would argue there has been an international economic market from the 1820 s but perhaps industrial growth accelerated in the last quarter of the nineteenth century, the consumption of raw materials increased phenomenally. (The growth of the international economy 1820-2000,p11) It is impossible not to argue that with an international economy there will be companies that become transnational, to get closer to there market it is for this reason many national companies become multinational. It enables there product to become internationally available, moreover with premises closer to the market there are other advantages, for example they are able to cut transport costs, thus there product is in line with home competitors and not more expensive. Another key reason why many firms become multinational is that they are able to avoid legislation in there own country which may prevent firms getting too big. (Nancy Wall and Barry Martin) More significantly though firms often become multinational to avoid trade barriers this has been very noticeable with such far east countries who specialise in electronics and automotive products moving into Europe to avoid the Common External Tariff. For a national company who has a large foreign market but does not have other premises abroad there often are a lot of tariffs to pay. The advantage of building factories in other countries here is obvious for two main reasons, first they become more global and second they are able to avoid these tariffs.

Many large national organisations have tax advantages or grants from overseas governments which encourages them to become multinationals for example the European Union has encouraged overseas investment. If we look to the UK this is apparent with such huge plants as the Nissan factory in Sunderland a recognised black spot in the UK for employment. Nissan had huge grants to build there factory there because it would create jobs thus there would be a domino effect which would create wealth to a depleted area.

In many countries national companies face pressure from Trade Union activity to avoid this companies spread their bases around the world, this in turn weakens domestic unions. In Europe this is noticeable in such countries as Sweden who have strong Trade Unions. Often countries with weak of not even any unions are those in developing countries MNE s have taken advantage of this ploughing large amounts of FDI. For example before WWII the share of FDI going into developing countries was about sixty percent but by the seventies this had dropped to around twenty-five percent, by the mid nineties this had increased once again to around forty percent. This shows the attractiveness of developing countries to multinationals and national firms, partly the reason why national firms become multinational.

National firms become multinational to increase Global Sales, as Drucker has argued we live in the age of Social transformation whereby be have more disposable income. Many smaller national companies have turned multinational to expand production activities abroad, this can account for a number or MNE s originating from developing areas like Hong Kong and South Korea. What has been key to there success is the improvement in technology, transportation, production processes and communications.

So Have the reasons changed over time for national firms to become Multinational? It is possible to argue that firms naturally become multinational from such acquisitions and vertical/backward integration, it is hard for a national firm to become multinational purely from organic growth. Therefore it would be fair to say that firms don t actually mean to become multinational rather it is by accident that they become Global. What is interesting though is that FDI has changed, in the early 20th century it was essentially Spillover investment for example US firms would invest in Mexico and Canada. Post war it was going into developing countries like Japan and South Korea, here we see the greatest growth in FDI, data shows it rose by 251%. Today though most FDI goes into developed countries like much of Europe. However having said that my belief is that the key concepts of becoming multinational are pretty constant over time. For example in the agriculture commodities United Brands, in the 1920 s still wanted to gain from all of the above reasons, e.g. they wanted to be close to their market thus they bought plantations so that they were close to their producers. (Multinational and natural resources, p88)(Integration) Instead of having one central depot where all produce was transported to, it also gave them chance to grow quickly and gain a larger market share so they could be world leaders. This shows the incentives are still the same although where FDI goes is different.

Summary

To conclude as Raymon Vermon argues companies become multinational as the advantages abroad meant, cheaper labour, cheaper raw material and so on which reduces unit costs. Thus you become more competitive and are able to increase sales. This view though is becoming increasingly archaic as Dicken would argue in the Global Shift; this is no longer the sole reason for becoming multinational, it does not take into account the intricate ways in which firms engage in international operations through various collaborative ventures . On the other hand Steven Hymer argues that it must have an advantage over its host firms to become multinational. Essentially though there are three main stages in the evolution to become a multinational. The company must rely on export and expansion of export sales to justify building new plants abroad, a Sony power point presentation found on the internet argued the criteria for a MNE to be A companies whose foreign sales are at least 25%. Secondly foreign production, there must be a limit to foreign sales that is being halted by being a national company. Lastly the company needs to begin planning, organising, co-ordinating, production, R+D, marketing and financing to become multinational. In deciding whether the reasons for becoming multinational have changed, considering the buzz word has only been around for the best part of 40 years it is fair to say that it hasn t. Moreover if we look back to the end of the last century the only real difference is that the huge Petroleum Companies, Gold Miners and Fruit growers only became multinational to get close to there market because the transport of such goods was more difficult than it is today. Thus it was an imperative to become multinational if you were to succeed. Perhaps Richard Longworth in his recent publication, The coming crisis for first world nations, 1998 has got it right with describing multinationals as Global Corporations.